

## IN THE APPEAL BOARD OF THE FINANCIAL SERVICES BOARD

*1. CASE NO: A48 / 2015*

In the matter between:

OLD MUTUAL SUPERFUND DEFINED BENEFIT PENSION FUND	First Appellant
OLD MUTUAL SUPERFUND DEFINED BENEFIT PROVIDENT FUND	Second Appellant
and	
REGISTRAR OF PENSION FUNDS	Respondent

*2. CASE NO: A2 / 2016*

In the matter between

OLD MUTUAL SUPERFUND PENSION FUND	First Appellant
OLD MUTUAL SUPERFUND PROVIDENT FUND	Second Appellant
and	
REGISTRAR OF PENSION FUNDS	Respondent

Appeal panel: LTC Harms (Chair), Mr L Makhubela and Mr J Damons

For the appellant: Adv AE Franklin SC instructed by Walkers Incorporated (Ms B van der Vyfer)

For the respondent: Adv A Cockrell SC

Hearing: 21 June 2016

Judgment: 28 June 2016

Summary: Exemptions under sec 2(5) of the Pension Funds Act 24 of 1956 in respect of sections 15H, 15I, 28, 29 and 30 of the Act in relation to umbrella funds.

## JUDGMENT

- 1 The appellants in both appeals are registered funds in terms of the Pension Funds Act 24 of 1956, and are juristic persons in terms of sec 4B(1) of the Act. They had applied in terms of sec 2(5) for exemption from compliance with the provisions of sections 15H, 15I, 28, 29 and 30 of the Act (subject to proposed conditions). The Registrar of Pension Funds refused the applications and this is an appeal against that decision.
- 2 The appeals were consolidated at the request of the parties because the issues are identical. It will accordingly not be necessary to deal with the appeals or the appellants individually and references in this judgment to “the appellant” should be read as referring to all or any of them.
- 3 Section 2(5)(a) and (aA) of the Act provides as follows:

“(5)(a) The Registrar may, where practicalities impede the strict application of a specific provision of this Act, exempt any fund from, or in respect of, such provision on conditions determined by the Registrar.

(aA) Any exemption in terms of paragraph (a) may apply to funds generally or be limited in its application to a particular fund or kind of fund, which may, for the purposes of this sub-section be defined in relation to either a category or type of fund or in any other manner.”
- 4 The background to the application to the Registrar is this.<sup>1</sup> The appellants are so-called umbrella funds. This means that more than one employer participates in each of the

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<sup>1</sup> Liberal use has been made in this judgment of the heads of argument of both counsel.

appellants, and the assets and liabilities in respect of the members employed by one employer, say X, are maintained separately from the assets and liabilities in respect of the members employed by another employer, say Y (or other employers). The assets and liabilities in respect of X and Y are referred to as a “sub-funds”, and are each notionally ring-fenced in terms of the rules of the appellant. This means that the assets and liabilities of A are ring-fenced from the assets and liabilities in respect of sub-fund Y and vice versa.

- 5 The concept of umbrella and sub-funds is to a very limited extent recognised in sec 15B(12) – the section deals with the apportionment of existing actuarial surplus – and reads as follows:

“Where the Board [of a Fund] satisfies the Registrar that employers which participate in the Fund, on the understanding that their membership, financial position and contribution rates will be determined separately for each employer and communicated to such employer, the Registrar may permit such Board to apply this section to the actuarial surplus in respect of the members employed by a particular participating employer as if the corresponding membership, assets and liabilities constituted a separate fund.”

- 6 Board Notice 36 of 2003 defines, for purposes of the application of sec 15B(12), an umbrella fund as a fund in which:
- (a) More than one employer participates;

(b) The assets and liabilities in respect of the members employed by each participating employer are maintained separately from those in respect of members employed by other participating employers; and

(c) The financial position is determined separately in respect of the members employed by each participating employer.

- 7 However, a sub-fund has no juristic personality under the Act; only the umbrella fund is a juristic person. The effect of this is that the notional ring-fencing of the different sub-funds (although, as said, recognised in sec 15B(12) for a limited purpose) is not otherwise acknowledged by the Act, particularly not in secs 15H and 15I.
- 8 Section 15H(1) provides that, if a fund (in this case the umbrella fund) has credit balances in the member surplus account or the employer surplus account and is found to have a deficit following an actuarial valuation, “such credit balances shall be reduced in the same proportion by the amount of the deficit”. The effect of section 15H is that the credit balances in the member surplus account and the employer surplus account are automatically reduced in order to extinguish the actuarial deficit. See *British American Tobacco Pension Fund v Howie* NO 2016 1 SA 398 (GP) at [37].
- 9 In addition, sec 15I provides that, on liquidation of a fund (once again also an umbrella fund) in terms of section 28 or 29, any credit balances in any reserve accounts, the member surplus account and the employer surplus account “shall be applied” in the “order of priority” prescribed. The “order of priority” in section 15I is triggered under sec 28 in the case of the voluntary dissolution or termination, wholly or in part, of a

fund; and under sec 29 in the event of the winding-up by the court of the whole or any part of the business of a fund.

- 10 The appellant has in spite of these provisions adopted rules to ring-fence the participating sub-funds. The effect of these rules was described by counsel in these terms:

“The [umbrella funds’] master rules provide that each of them is a single juristic person. However, each [umbrella fund] consists of sub-funds as defined (namely, in relation to each participating employer and its employees who are members, or persons who were employees and are now pensioners or deferred pensioners, the assets and liabilities of the Fund that are attributable to such members, pensioners and deferred pensioners, together with any balances in the reserve accounts, participating employer surplus account and member surplus account relating to the relevant participating employer and those members, pensioners and deferred pensioners).

Special rules detailing the benefits and special conditions applicable to each participating employer, its members, pensioners and deferred pensioners, are registered in respect of each sub-fund. The scheme of the [umbrella Funds’] rules is thus to ring-fence the benefits and contributions of each sub-fund from the rest of the [umbrella] Fund, including the other sub-funds within it.

The [umbrella Funds’] master rules make provision for any surpluses arising in a sub-fund, as well as any deficits arising in a sub-fund, to be dealt with separately from the [umbrella] Fund, including the other sub-funds within it.”

- 11 The problem with these rules, which have been accepted by the Registrar, is that they are in conflict with the Act because they ring-fence sub-funds and effectively endow them with legal personality. This much is conceded by the appellants. To legalise the rules, i.e., to bring them in conformity with the Act, the appellant required of the Registrar to grant it exemptions under sec 2(5). As counsel said, the problem facing umbrella funds is that some of their foundational rules are inconsistent with the provisions of the Act, with the result that (despite the rules) a deficit in one sub-fund may in terms of the Act have to be funded by the other sub-funds or the participating employers therein, something which runs counter to the very nature and purpose of an umbrella fund.
- 12 It will be recalled that the Registrar may, “where practicalities impede the strict application of a specific provision” of the Act, exempt any fund from, or in respect of, such provision on conditions determined by the Registrar.
- 13 Counsel explained the case of the Funds in these terms:

The approval by the Registrar of umbrella fund rules of the kind summarised above, and the steps thereafter taken by the Appellants to implement those rules and to implement BN36 and BN22 (that is, to create each sub-fund within the Fund as a separate entity with its own membership, assets and liabilities, its own surpluses – some of which would have been distributed already – and its own deficits), axiomatically impede the strict application of the provisions of the Act requiring cross-subsidisation between the sub-funds in a fund in the event of deficits or shortfalls arising during the course of the Fund’s ongoing operations

or on the liquidation of any or all of the sub-funds in a fund. These are practicalities (involving the practical operation of the Funds) and they impede compliance with particular sections of the Act, as envisaged in section 2(5)(a).

[Underlining added.]

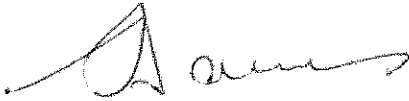
- 14 It was not, and could not, be argued that practicalities impede the strict application of secs 15H and I. Simple bookkeeping entries are all that is required. There is nothing impractical in making those entries.
- 15 There are also no practical difficulties in making the required bookkeeping entries under the ring-fencing rules. The problem is caused by the fact that the rules are ultra vires the Act. In other words, it is not practicalities that impede the strict application of these provisions but the application of the ultra vires rules would be in conflict with the Act. Axiomatically, ultra vires rules cannot override legislation.
- 16 The misalignment between the operation of umbrella funds and the provisions of the Act which contemplate a unitary fund (that is, a single body corporate with a single set of assets and rights, a single set of liabilities and a single set of obligations) is something, as recognised by the Funds, for Parliament to rectify. The Registrar cannot use the power of exemption, which is directed at administrative matters and not matters of substance, to regularise the position of umbrella funds which have sub-funds with deficits or sub-funds which may fall into deficit, pending the consideration by Parliament of amendments to the Act.
- 17 What the Funds are in reality saying (but denying saying it) is that these provisions of the Act are unfair and inequitable if applied to sub-funds administered by umbrella

funds. That may be so but sec 2(5) does not empower the Registrar to grant exemptions on the ground of unfairness.

- 18 It is in the light of the foregoing unnecessary to deal with the other arguments presented.

THE APPEALS ARE DISMISSED WITH COSTS.

Signed on behalf of the panel on 28 June 2016.

A handwritten signature in black ink, appearing to read 'LTC Harms', written in a cursive style.

LTC Harms (Chair)