

# Speaker Notes:

## Roles and Responsibilities of Trustees

### FSCA Retirement Funds Supervision Division Workshop - 27 May 2019

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**(Section 26(2) / Independent Trustee)**

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# FIDUCIARY DUTIES & GOVERNANCE

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## Fiduciary duties

1. In terms of the Pension Funds Act (“the Act”), a fund’s trustees, its principal officer and employees are all officers.
2. The common law imposes fiduciary duties of loyalty and care on officers and agents of financial institutions because they control trust property. The Financial Institutions (Protection of Funds) Act (“the FI Act”) expands on these duties by requiring the exercise of the utmost good faith<sup>1</sup>.
3. It must always be borne in mind that those who accept appointment as officers and agents of a fund, do so freely and, upon their appointment, they become obligated to act for the sole benefit of the fund and its members. They must do so in constant pursuance of the objectives and interests of a fund and its members and to the exclusion of the interests of themselves and any other party<sup>2</sup>.
4. It is appropriate to discuss fitness and propriety requirements and standards before venturing into an officer’s obligations because, simply stated, the unfit and improper should not become or allowed remain officers of a fund.
5. There are no published or prescribed fitness and propriety guidelines<sup>3</sup> for officers of pension funds but it is accepted that a fit and proper person would be *financially sound; honest, reputable & reliable; and competent to perform the role in question*. Regard is usually had to both current previous conduct and activities in business of financial matters of the person in question.

## Collective competency

6. Although propriety requirements must be satisfied individually, certain fitness requirements may be satisfied collectively by a Board of Trustees (“BoT”) and must be supplemented by independent professional advice.

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<sup>1</sup> The FI Act also regulates particular actions of officers and agents and I quote section 2 thereof for easy reference: “**2. Duties of persons dealing with funds of, and with trust property controlled by, financial institutions** A director, member, partner, official, employee or agent of a financial institution or of a nominee company who invests, holds, keeps in safe custody, controls, administers or alienates any funds of the financial institution or any trust property - (a) must, with regard to such funds, observe the utmost good faith and exercise proper care and diligence; (b) must, with regard to the trust property and the terms of the instrument or agreement by which the trust or agency in question has been created, observe the utmost good faith and exercise the care and diligence required of a trustee in the exercise or discharge of his or her powers and duties; and (c) may not alienate, invest, pledge, hypothecate or otherwise encumber or make use of the funds or trust property or furnish any guarantee in a manner calculated to gain directly or indirectly any improper advantage for himself or herself or for any other person to the prejudice of the financial institution or principal concerned”.

<sup>2</sup> This is codified in section 7C of the Act and also in sections 2 and 3 of the FI Act.

<sup>3</sup> The term “*fitness and propriety*” has a wide ambit and invariably the insane, the criminal and the financially irresponsible are excluded. Generally speaking a person’s *fitness* relates to his capability, faculties, experience and qualification relevant to the post occupied. Fitness requirements may vary substantially depending on the industry involved. A person’s *propriety* relates to his character, honesty (including whether perjurious or misleading statements have been made), integrity, judgment, diligence and deceitful/questionable/untoward conduct. In this regard a person’s ability for introspection, and ability to act objectively and reasonably may also be taken into account. Regard should also be had to the fact that a person may have been the subject of enquiries (internal or by a regulator). Factors which are typically taken into account in determining fitness (and which also impact on propriety) are as follows: (1) Undisclosed interests (even indirect interests should be disclosed so that they may be managed); (2) Reputation in the industry (has the person ever breached any fiduciary duties, ever been conflicted/reprimanded and/or disciplined?); (3) Obstructive behaviour or the lack of readiness or willingness to comply with prescripts; (4) Knowingly appointing a person who was not fit and proper; (5) Providing false or misleading information; (6) Opposing the maintenance of effective internal control systems; (7) Surreptitious conduct; (8) The passage of time since the event occurred and whether it was isolated or recurring; and (9) Affiliation with companies with governance problems. The reasonability of explanations furnished and commitment to set things right may be taken into account as well.

7. For this “*collective capability*”, a BoT should be constituted of individuals having an appropriate mix of skills and the officers should know what their fellow officers are capable of. Where possible, annual performance reviews should be conducted.

## Good governance

### Fiduciary and other duties

8. Apart from common law (general) fiduciary duties relating to loyalty<sup>4</sup> and care<sup>5</sup>, specific duties are conferred upon trustees in terms of the Act, the rules of a fund and, in the case of trustees appointed in terms of section 26 of the Act, in their letters of appointment<sup>6</sup>.

### Direct, control and oversee

9. The Act stipulates that it is a BoT’s purpose to direct, control and oversee the operations of a fund in accordance with its rules and the law. The sole responsibility for management of a fund vests in its BoT and to discharge its duties, a BoT must:

#### In terms of section 7C of the Act

- (1) Take all reasonable steps to ensure that the interests of members are protected at all times;
- (2) Act with due care, diligence and good faith<sup>7</sup>;
- (3) Avoid conflicts of interest<sup>8</sup>;
- (4) Act with impartiality in respect of all members and beneficiaries<sup>9</sup>;
- (5) Act independently<sup>10</sup>;
- (6) Protect accrued benefits and ensure that the fund is financially sound and is responsibly managed;

Section 7C implies that a code of conduct will be entered into by the officers and adherence thereto monitored.

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<sup>4</sup> This aims to preclude conflicting interests and self-gain. Full candour is required..

<sup>5</sup> *i.e.* like any reasonable, prudent person.

<sup>6</sup> A section 26 BoT’s duty is to take charge of a fund and make its affairs comply with the Act and ensure that a new BoT is correctly constituted in terms of section 7A(1) of the Act. In pursuance of this, the FSCA may require the following of a section 26 BoT: (1) To institute, or defend, any litigation to protect the interests of the fund and its members. (2) To submit quarterly reports, detailing the BoT’s assessment of the state of affairs of the fund and the BoT’s proposed course of action to bring the affairs of the fund into order. (3) To assist the FSCA with any ongoing investigations into the affairs of the fund. (4) To bring statutory reporting and returns up to date. (5) To provide member benefit statements. (6) To recover any arrear contributions. (7) To assess the fund’s records and ensure that they are valid and to take corrective action if they are not. (8) To resolve dysfunctional aspects in the fund. (9) To review the fund’s contractual arrangements. (10) To review the governance documentation and processes in the fund, including its communication policy, risk policy, code of conduct and investment policy statement and to place corrective control measures and procedures in place to ensure good governance. (11) To form a preliminary view as to whether the fund’s previous officers and agents may be liable for any loss the fund may have suffered. (12) To ensure that the fund’s fidelity policy is current and provides appropriate cover. (13) To ascertain if there are complaints and, if so, resolve the complaints.

<sup>7</sup> Section 2 of the FI Act requires the utmost good faith.

<sup>8</sup> If conflicting interests are declared, they can be managed. Invariable there will always be some form of conflicting interests.

<sup>9</sup> This may become problematic in union or sponsored funds.

<sup>10</sup> This may become problematic in union or sponsored funds.

### In terms of section 7D of the Act

- (7) Ensure that proper registers, books and records of the operations of the fund are kept, inclusive of proper minutes of all resolutions passed<sup>11</sup>, a member register, an asset register, a trustee register<sup>12</sup> and so on;
- (8) Ensure that proper control systems are employed by or on behalf of the BoT<sup>13</sup>;
- (9) Ensure that adequate and appropriate information is communicated to the members<sup>14</sup>;
- (10) Take all reasonable steps to ensure that contributions are paid timeously to the Fund<sup>15</sup>;
- (11) Obtain expert advice on matters where board members may lack sufficient expertise<sup>16</sup>;
- (12) Ensure that the rules and the operation and administration of the Fund comply with this Act, the FI Act, and all other applicable laws.
- (13) Comply with any other prescribed requirements (circulars, directives, letter of appointment etc).

### In terms of section 8 & Directive PF No. 5 of the Act

- (14) Appoint a principal officer ("PO") and, if applicable, such officers as may be required for the proper control of the business of the Fund, prescribe the conditions of service of officers of the Fund and engage professional or other assistance for the Fund;
- (15) Inform the FSCA of anything that might adversely affect the status of the PO. This relates to anything that may affect the assessment of a PO as a fit and proper person<sup>17</sup>;

### In terms of the Rules (usual provisions)

- (16) Attend to the receipting of contributions & income;
- (17) Keep record of all necessary particulars of all the members, of all benefit accruals and of all other matters essential to the working of the Fund<sup>18</sup>;
- (18) Ensure that every title deed and other document which proves that the Fund is the owner of a particular investment is kept in an appropriate safe-keeping arrangement;
- (19) Ensure that all investments of the Fund are registered in its name if not held by a nominee company (latter to be approved in terms of section 5 of the Act and be properly authorised by the BoT);
- (20) Ensure that only people who have the authority in terms of a resolution passed by the BoT to sign on behalf of the BoT, sign instructions, contracts or other documents on its behalf;

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<sup>11</sup> The minute book must be maintained in a way that its integrity cannot be doubted. Loose minute pages must be avoided. This also applies to interest declarations. The trustee packs distributed with an agenda should be recorded.

<sup>12</sup> See regulation 31. The trustee register should contain conclusive proof of the appointment of and authority of persons to act as trustees. The FIC Act must also be complied with. Formal upfront interest declarations, as may be updated annually and as may be noted at each meeting, must be incorporated.

<sup>13</sup> Management implies the exercise of control. Compliance can only be measured if there are stated policies and procedures with control measures and procedures. If these are in place, exception reporting should suffice. As administration is usually delegated, trustees must rely on some form of due diligence regarding the competencies of an administrator (see section 13B of the Act; FAIS etc).

<sup>14</sup> A fund's communication policy will provide guidance.

<sup>15</sup> If the Fund's member register is not valid, it will not be possible to monitor this.

<sup>16</sup> Care must be taken to ensure appropriate and independent advice is given. Merely obtaining and relying on advice does not absolve a trustee from liability. This is where collective competency / capability is crucial.

<sup>17</sup> See list in section 8(5)(c) of the Act, discussed more under PO Fitness & Propriety requirements and PO duties.

<sup>18</sup> Out of necessity this is delegated to a benefits administrator. Care must be taken when selecting an administrator and in entering into an agreement. If administration has changed, records must follow. Regular administration reports are crucial.

- (21) Ensure that proper minutes are kept of each meeting and at each BoT meeting, table the minutes of the previous BoT meeting for approval by the chairman;
- (22) Settle and decide upon any claim instituted by or against the Fund and authorise the payment of any claim made against the Fund;
- (23) Check and authorise the payment of benefits;
- (24) Effect fidelity cover insurance to safe-guard the Fund's assets<sup>19</sup>;
- (25) Draw up the Fund's annual financial statements<sup>20</sup>, have the same audited annually by an auditor (appointed by the BoT and whose appointment has been approved by the FSCA) and submit the financial statements to the FSCA within 6 months after its year-end to the FSCA; and
- (26) Appoint an actuary approved by the FSCA to determine the fund's financial soundness and submit reports to the FSCA.

#### General powers conferred upon the BoT

- (27) General discretionary powers of management and investment are conferred upon the BoT to receive, administer and apply the moneys of the Fund and do everything which is incidental or conducive to the attainment of the objectives of the Rules.
- (28) A BoT may only delegate powers to sub-committees or any other person or administrator<sup>21</sup>, if the rules allow subject to condition determined by the BoT<sup>22</sup>. The BoT is not divested or relieved of a function thus delegated and may withdraw the delegation at any time.
- (29) The BoT may authorise and designate any of its trustees and/or officers to sign any contract or other document binding the Fund or any document authorising any act on behalf of the Fund, subject to such conditions as it may impose.
- (30) Establish an investment policy and strategy for the Fund, taking into account the long-term interests of the Fund and its members.
- (31) Provide a housing loan guarantee in respect of a member (section 19(5) of the Act), subject to the rules and such terms and conditions as the BoT and the FSCA may determine from time to time<sup>23</sup>.
- (32) Deal with complaints.
- (33) Effect transfers into and out of the fund.
- (34) Record divorce orders.
- (35) Decide on the disposition of death benefits<sup>24</sup>.

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<sup>19</sup> In effecting such cover, full disclosure is required. Reciprocal provisions must be contained in agreements with service providers.

<sup>20</sup> In assessing the statements, regard must be had to the workingpapers.

<sup>21</sup> The BoT must ensure that an accredited administration system is employed which is suitable for the size, nature and complexity of the administration business. It is best to obtain external assurance from an auditor on the administration system, as prescribed by section 13B. The BoT must ensure that administration services are clearly documented and that service levels and policies relating to benefits disposition are in place, monitored and adhered to.

<sup>22</sup> This is usually set out in administration and investment and consulting agreements. If matters are delegated to sub-committees then there must be a charter or terms of reference, regular reporting, minutes and at least annual review of the sub committee's performance.

<sup>23</sup> Housing loan are prone to abuse. Measures must be in place to ensure that monies are utilised for housing.

<sup>24</sup> The BoT must ensure that: (1) Beneficiary forms are regularly distributed and that mechanisms are in place for members to change their nominations with ease; (2) The Fund has an insurance policy for the provision of risk benefits in place and that claims are made as per the policy and rules of the Fund; (3) Supporting documents for death benefit claims are prepared, facilitating valid decision making; (4) Its deliberations on the disposition of the benefits are in compliance with the Rules and the Act and are properly minuted; (5) Its decisions are given effect to timeously and in full; (6) Any benefits paid to beneficiary trusts in respect of minors are done in accordance with the rules and

## Risk management

10. The risks facing the Fund must be identified and be mitigated through the institution of suitable policies and procedures, including charters setting out the responsibilities of the BoT and its subcommittees, with clear delegation documents and strategic and operational plans.
11. Control measures<sup>25</sup> must be implemented, monitored and reported upon and remedial action must be taken on a continuous basis to address exceptions.
12. Governance literature warns against the dangers of leaving dominant officers unchecked, vesting too much power in chairpersons and not appraising their performance. Sources furthermore stress the importance of balanced and competent boards, proper risk management<sup>26</sup> and the crucial importance of identifying and managing conflicting interests where adequate whistle-blowing procedures should be in place.
13. In this context, competent POs and consultant are required to provide the BoT with guidance on the Fund's affairs, as well as the exercise of their duties. The PO must assist the trustees and the chairperson actively.

## Fit & Proper PO

14. Given the crucial role that a principal officer ("PO") fulfills, section 8(5)(c) of the Act lists characteristics which must be taken into account to determine the fitness and propriety of a PO:
  - (1) Competence and sound judgment for fulfillment of the responsibilities of the particular office and type of fund;
  - (2) The diligence with which the person is likely to fulfill the above responsibility;
  - (3) The previous conduct of the person in business or financial matters; and
  - (4) Evidence of the commissioning of offences; deceitful, prejudicial or otherwise improper business practices; and the taking part in or being associated with business practices which casts doubt on the PO's competence and sound judgment.
15. In terms of PF 130, the PO is appointed by and accountable to the BoT and the role of the PO is vital for the proper performance of the BoT. It is essential that a PO be fit and proper, i.e. be capable, trustworthy and reliable.
16. The PO is required to exercise and participate materially in the executive control over and management of the business and activities of the Fund.
17. The role of the PO within the governance system is central in the proper performance of the BoT and the PO must provide informed and reliable support on strategic, executive, governance and compliance matters. These are briefly discussed below.

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the Act; and (7) Beneficiary trusts are properly monitored in the execution of their mandates. Finally, care must be taken not to follow an allocation formula – each case must be investigated on merit. It is advisable to have decent insurance cover for future claims and determinations that may be made against the fund. Payment of minors' benefits should only be made to a trust if warranted and then care must be taken to select a trust that is reputable.

<sup>25</sup> This entails a proper segregation of duties. In very basic terms this is to ensure that the initiation, recording and execution of financial transactions are done by different people. Policies and procedures record this and a proper delegation of authority framework will govern compliance to the Fund's risk management plans, policies and procedures

<sup>26</sup> Effective controls and procedures, especially risk and assurance management and effective internal and external audit functions, are prerequisites for good governance. The audit committee is the most important sub committee and must be independent.

### Strategic role

18. Typically a PO would guide the BoT on strategy formulation and the implementation thereof and develop and recommend to the BoT the yearly business plans and budgets that support the Fund's long-term strategies

### Executive role

19. The PO forms the nexus of the management & control structure (specifically in reporting to the BoT). The objectives and duties placed on the BoT as per sections 7C & 7D of the Act must, of necessity, be executed by the PO on a daily basis. As such, the duties of the BoT also form part of the duties of the PO and the PO should be in a position to guide the BoT on these issues.
20. However, a PO's duties and the level of accountability remain a factual issue and must be evaluated in the light of the powers conferred upon the PO in terms of the rules, the Act and also *ad hoc* by the BoT in terms of adopted policies & procedures and specifically by powers delegated to the PO<sup>27</sup>.
21. The PO manages the day-to-day business of the Fund and has executive authority over financial management, legal affairs, secretarial services and retirement fund operations. The PO must:
- (1) Ensure that decisions of the BoT are properly recorded and executed;
  - (2) Attend to the daily management of the Fund to ensure it operates efficiently and effectively and meets its objectives and its obligations and furnishing the BoT with reliable management and administration reports on the affairs of the Fund;
  - (3) Monitor and report to the BoT on the Fund's performance and its compliance with policies, procedures and the law; and
  - (4) Establish structures to deliver services, programmes and information beneficial to the members and as specified by the Board of Trustees.

### Governance role

22. The PO must be the guardian of good governance and foster a culture that promotes ethical practices and encourages integrity. Specific duties in this regard include:
- (1) Maintaining proper registers, books and records;
  - (2) Providing secretarial services to the BoT by preparing minutes of meetings and maintaining record of all resolutions passed by the BoT;
  - (3) Ensuring that proper financial and administrative policies, procedures and control systems are developed, monitored and enforced, as directed by the BoT, and advising the BoT on exceptions detected to the controls;
  - (4) Actively monitoring and reporting on the Fund's risks;
  - (5) Liaising on behalf of the BoT with service providers to the Fund (unless direct contact between BoT and service provider);
  - (6) Ensuring that the governance of Fund complies with applicable legislation; and

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<sup>27</sup> By way of example, the PO is equally responsible for safe custody of the assets as are the BoT members. However, the PO may, in certain cases, not be held to be accountable for investment decisions, which is primarily the prerogative of the BoT and such decisions would be taken by a BoT whereas the PO would not have such powers. Conversely, the BoT act on information furnished by and recommendations made by the PO and if a PO should mislead the BoT, accountability will ensue. Whereas a PO may not have the authority to enter into an agreement, ensuring adherence to such agreement and the rules and the law is a responsibility of the PO. Any unauthorised / irregular payment is primarily the responsibility of the PO, if all payments require the PO's approval.

(7) Complying with statutory whistle-blowing duties.

### *Compliance role*

23. A PO has statutory obligations to ensure that all aspects of legislation are complied with and must report directly to the FSCA. The PO is also a protected whistle-blower<sup>28</sup>.
24. Effectively any document to be lodged with the FSCA has to be certified/signed by the PO including all amendments to the Rules<sup>29</sup>, audited financial statements<sup>30</sup> and valuation reports<sup>31</sup>.
25. The PO also has certain statutory reporting duties such as:
  - (1) Informing members of rule amendments within 6 months of fund's financial year end;
  - (2) Sending copies of valuation reports to the employers; and
  - (3) Reporting arrear contributions in terms of section 13A, read with Regulation 33.
26. The importance of the PO in ensuring compliance with the Fund's rules and legislation is emphasised by section 8(6)(b) of the Act and paragraph 7 of Directive PF No. 5 which obligates a PO to inform the FSCA in writing of "*any matter relating to the affairs of the pension fund which, in the opinion of the principal officer, may prejudice the fund or its members*".

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<sup>28</sup> Section 8(6)(a) and para 6 of Directive PF No. 5 – Report to FSCA on perceived reasons for termination of appointment within 21 days of termination of appointment (other than where terminated by FSCA).

<sup>29</sup> Section 12, regulation 24 and circular PF No. 81 – Sign and submit rule amendment (2 copies plus signed certificate) to FSCA within 60 days – together with explanatory statement and applicable fees – accompanied by valuator's certificate or fund statement re: financial soundness of fund (if rule amendment may affect financial condition of fund) –

<sup>30</sup> Section 15 – annual financial statements – sign statement of responsibility re: confirm lodging of all returns, statements, documents and other information required of fund by Pension Funds Act ; or details of non-compliance

<sup>31</sup> Section 16(8) – sign certificate to accompany valuation report submitted to FSCA , stating that information submitted to the valuator was correct and complete