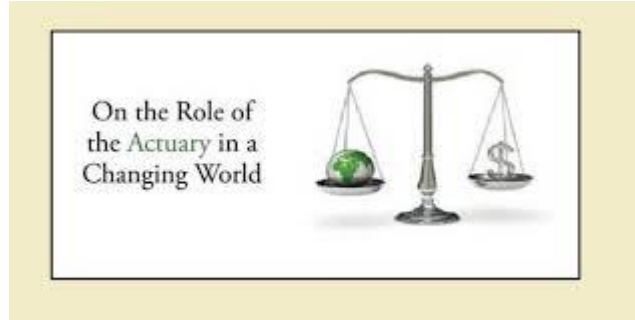




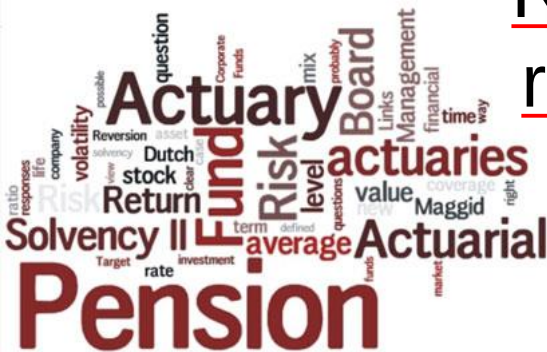
QUANTIFYING RISK, ENABLING OPPORTUNITY

Retirement Fund Matters



“Rules of DC FUNDS and the responsibility of the actuary in approving their financial soundness.”

Gert van der Linde & Pierre Reineck



KEY WORDS

TAKE
PERSONAL
RESPONSIBILITY



- Rules of DC FUNDS
- Responsibility
- Approving
- Financial Soundness.



SOUND FINANCIAL PRINCIPLES

Introduction & Background

1956 Wording:

4. Registration of pension funds

(1) Every pension fund shall apply to the registrar for registration under this Act.

(2) An application under sub-section (1) shall be accompanied by particulars of the name and address of the person charged with the management of the affairs of the fund to which the application relates, and a copy of the rules of such fund, **together with a certificate by a valuator as to the soundness of such rules from a financial point of view** or, if no valuator has been employed, such information regarding their financial soundness as the applicant may possess, and a registration fee of one pound, and, in the case of a fund in existence at the commencement of this Act -

SOUND FINANCIAL PRINCIPLES

Introduction & Background

1956 Wording: continued;

4. Registration of pension funds

(4) If after considering any such application, the registrar is satisfied -
(a) in the case of a fund which is in existence at the commencement of this Act -

(i) that the rules of the fund are not inconsistent with this Act and are based on **sound financial principles**; and

(ii) that the fund is in a **financially sound** condition or that adequate arrangements have been made to bring it into a **financially sound** condition within a period which the registrar considers satisfactory;

SOUND FINANCIAL PRINCIPLES

Introduction & Background

2007 Wording:

4. Registration of pension funds

- (1) Every pension fund shall apply to the registrar for registration under this Act.
- (2) An application under subsection (1) shall be accompanied by the particulars and the fee prescribed by regulation.

[Subs. (2) amended by s. 14 of Act 86/84 and substituted by s. 16 of Act 83/92]

SOUND FINANCIAL PRINCIPLES

Introduction & Background

2007 Wording: continued

4. Registration of pension funds

- (4) If after considering any such application the registrar is satisfied that the fund complies with the **conditions prescribed by regulation**, he shall register such fund and send to the applicant a certificate of registration as well as a copy of the rules of the fund bearing an endorsement of the date of registration.

[Subs. (4) substituted by s. 16 of Act 83/92]

SOUND FINANCIAL PRINCIPLES

Introduction & Background

2007 Wording: continued



REGULATIONS

PART II

DOCUMENTS AND PARTICULARS REQUIRED UNDER SECTION 4 (2) AND CONDITIONS WHICH MUST BE COMPLIED WITH UNDER SECTION 4 (4)

[Heading substituted by GN R2324 of 1993.]

(2) The conditions with which a pension fund shall comply in terms of section 4 (4) shall be as follows:

(a) The rules of the fund shall be consistent with the Act and the regulations; and

(b) the rules shall be based on sound financial principles.

SOUND FINANCIAL PRINCIPLES

Introduction & Background

2014 Wording:

4. Registration of pension funds

(1) Every pension fund shall apply to the registrar for registration under this Act.

(2) An application under subsection (1) shall be accompanied by the **particulars and the fee prescribed.**

[Subs. (2) amended by s. 14 of Act 86/84, substituted by s. 16 of Act 83/92 and amended by s. 17 of Act 22/2008]

SOUND FINANCIAL PRINCIPLES

Introduction & Background

2014 Wording:

4. Registration of pension funds

(4) If after considering any such application the registrar is satisfied that the fund complies with the conditions **prescribed**, he shall register such fund and send to the applicant a certificate of registration as well as a copy of the rules of the fund bearing an endorsement of the date of registration.

[Subs. (4) substituted by s. 16 of Act 83/92 and amended by s. 17 of Act 22/2008]

SOUND FINANCIAL PRINCIPLES

Introduction & Background

2014 Wording:



PROBLEM

“prescribed” means prescribed by the registrar by notice on the official web site, unless notice in the *Gazette* is specifically required by this Act;

[Definition of “prescribed” substituted by s. 1 of Act 11/2007 and s. 1 of Act 45/2013 w.e.f. 28 February 2014]

SOUND FINANCIAL PRINCIPLES

Documents and Particulars Required under Section 4 (2) and Conditions which must be Complied with under Section 4 (4)

Regulation 8 of PFA

(2) The conditions with which a pension fund shall comply in terms of section 4 (4) shall be as follows:

(b) the rules shall be based on

sound financial principles.

SECTION NO LONGER APPLICABLE

SOUND FINANCIAL PRINCIPLES

Section 12(3) & (4) of PFA: Amendment of Fund Rules

- (3) If any such alteration, rescission or addition **may affect the financial condition of the fund**, the principal officer shall also transmit to the registrar a **certificate by the valuator** or, if no valuator has been employed, a statement by the fund, as to its **financial soundness**, having **regard to the rates of contributions by employers and**, if the fund is not in a sound financial condition, what arrangements will be made to bring the fund in a sound financial condition.

SOUND FINANCIAL PRINCIPLES

Section 12(3) & (4) of PFA: Amendment of Fund Rules

- (4) If the registrar finds that any such alteration, rescission or addition is not inconsistent with this Act, and is **satisfied that it is financially sound**, he shall register the alteration, rescission or addition and return a copy of the resolution to the principal officer with the date of registration endorsed thereon, and such alteration, rescission or addition, as the case may be, shall take effect as from the date determined by the fund concerned or, if no date has been so determined, as from the said date of registration.
-

SOUND FINANCIAL PRINCIPLES

MEDICAL AIDS SCHEMES ACT

Section 35. Financial arrangements

- 1) A medical scheme shall at all times maintain its business in a financially sound condition by—
- (a) having assets as contemplated in subsection (3);
 - (b) providing for its liabilities; and
 - (c) generally conducting its business so as to be in a position to meet its liabilities at all times.

SOUND FINANCIAL PRINCIPLES

MEDICAL AIDS SCHEMES ACT

Section 35. Financial arrangements

(2) A medical scheme shall be deemed to have failed to comply with the provisions of subsection (1) if it does not comply with subsection (3), (4), (5), (6) or (7).

(3) A medical scheme shall have assets, the aggregate value of which, on any day, is not less than the aggregate of—

(a) the aggregate value on that day of its liabilities; and

(b) the nett assets as may be prescribed.

SOUND FINANCIAL PRINCIPLES

Long Term Insurance Act 1998

Very similar provisions

No such provisions / guides in

Pension Funds Act

SOUND FINANCIAL PRINCIPLES

“The rules of any fund must be based on sound financial principles and the board of a fund has the obligation to ensure that members' interests are protected (see ss 7C and 7D of the Act on the objects and duties of pension fund boards).”

Ekurhuleni Metropolitan Municipality v Germiston Municipal Retirement Fund 2010 (2) SA 498 (SCA)

SOUND FINANCIAL PRINCIPLES

THE CHALLENGE

“The fund is financially sound if the assets match the liabilities.”

Natal Joint Municipal Pension Fund v Endumeni Municipality (920/2010) [2012] ZASCA 13; [2012] 2 All SA 262 (SCA); 2012 (4) SA 593 (SCA)



HISTORY

DB funds

“financial soundness” relates to the participating employer carrying the balance of Fund costs / liabilities for financial soundness





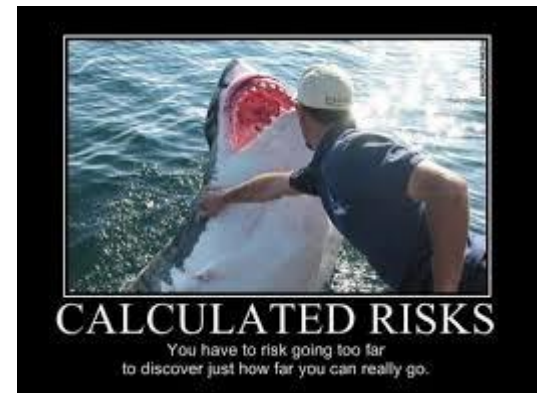
CURRENT

DC funds

“financial soundness”



- = Part Function Accounting
- = Part Function Actuarial
- = Part Function Legal



and members carry all financial risk

PROBLEM

DC funds

FINANCIAL MODEL NOT VALUATION
BASED

MEMBER CARRIES ALL FINANCIAL
LIABILITIES

FINANCIAL LIABILITY CHANGES

Financial soundness no longer quantified
by valuation basis but by legal structure of
rules



FINANCIAL LIABILITY CHANGES

RULES!

1. You SHALL!
2. You WILL!
3. You MUST!

IMPORTANTLY

What the trustees may do with the fund's assets is set forth in the rules. If what they propose to do (or have been ordered to do) is not within the powers conferred upon them by the rules, they may not do it.

Tek Corporation Provident Fund & others v Lorentz 1999 (4) SA 884 (SCA) para 28

Anecdote Regarding Beneficiary Fund

Extract from draft AFS

Assets	R40m
"Contributions received"	R20m
Expenses paid	R4m
Benefits paid	R8m

Rules :

no provision for expenses to be paid

No reference

how expenses be finance

or to "External" agreements

But rules were (probably?):

certified financially sound rules

Rules :

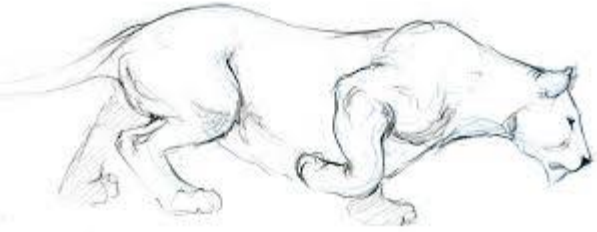
The requirement to certify financial soundness

What does it mean?



an easy automatic signature?

Member Share/ Member Interest



- be able to follow determination of benefits
- as per admin methods
- (at least a reasonable outline)



Common method

- units of portfolios proportioned purchase with
- member retirement contributions; and
- add the new units to the accumulated units etc.
- there may be explicit proportionate deductions for eligible costs
- (Refinements now ignored)
- Value of benefit = number of units x unit price when sold :
(may be 1 or more portfolios)
- Notes: calculation of unit prices, definition of portfolios not discussed



Case study wording in the rules



- Instruction to Rule Drafter(s)
- Purpose to Consolidate Rules plus new statutory requirements
- Admin method: as described (was in previous rules)
- Fund paid substantial fees for calculation of "unit" prices of "portfolios"

Extracts from Rules

“CALCULATION DATE” shall mean the date on which the ADMINISTRATORS, acting in terms of the agreed practice of the FUND, calculate the MEMBER’S benefit on the MEMBER’S retirement, death or his leaving SERVICE in terms of Rule X or in order to transfer the MEMBER’S benefit from the FUND in any of the circumstances contemplated in these RULES.

I do not have a problem with this



Extracts from Rules

“INVESTMENT RETURN” shall mean any income (received or accrued) and capital gains and losses (realised and unrealised) of the FUND, less an allowance for any tax and such expenses (paid or incurred) associated with the acquisition, holding or disposal of the assets of the FUND **as may be determined by the TRUSTEES**, provided that

- (a) such INVESTMENT RETURN may be positive or negative;
- (b) the INVESTMENT RETURN shall be allocated on such equitable basis **as the TRUSTEES** in consultation with the ADMINISTRATOR and in accordance with the agreed practice of the FUND **may determine from time to time**;



Extracts from Rules

"FUND CREDIT" shall mean for each MEMBER at any particular date, the accumulated value of:

- (a) the contributions made by the MEMBER
- (b) the contributions made by the EMPLOYER Plus; ...

less ... any costs ...

and increased or decreased by the INVESTMENT RETURN allocated to the above amounts until the CALCULATION DATE.





"And this is where our ROI became an IOU."

The Challenge



All Seems fine BUT...

Fund Credit = Price of Units X No. of Units

As per admin methods

Rules are wrong / acceptable / ?????

FINANCIAL LIABILITY CHANGES

RULES!

1. You SHALL!
2. You WILL!
3. You MUST!

IMPORTANTLY

What the trustees may do with the fund's assets is set forth in the rules. If what they propose to do (or have been ordered to do) is not within the powers conferred upon them by the rules, they may not do it.

Tek Corporation Provident Fund & others v Lorentz 1999 (4) SA 884 (SCA) para 28

FINANCIAL LIABILITY CHANGES

“Example of Rules approved”

- EMPLOYER'S contributions

10% of the MEMBER'S MONTHLY PENSIONABLE SALARY

- NET EMPLOYER CONTRIBUTIONS

The EMPLOYER'S contributions **minus** the following:

- (i) the expenses in respect of the FUND as described in clause B 1.11;
- (ii) the premiums in respect of the GROUP INSURANCE BENEFITS;
- (iii) the premiums payable in respect of the SEPARATE INSURANCE BENEFITS

FINANCIAL LIABILITY CHANGES

“Example of Rules approved”

**MONTHLY
PENSIONABLE
SALARY**

The basic monthly salary/wage which the MEMBER receives from the EMPLOYER and any other emoluments specified by the EMPLOYER which is deemed to be pensionable; provided that MONTHLY PENSIONABLE SALARY will be determined on joining the FUND and a change in MONTHLY PENSIONABLE SALARY will take effect in the manner set out in the SCHEDULE;

FINANCIAL LIABILITY CHANGES

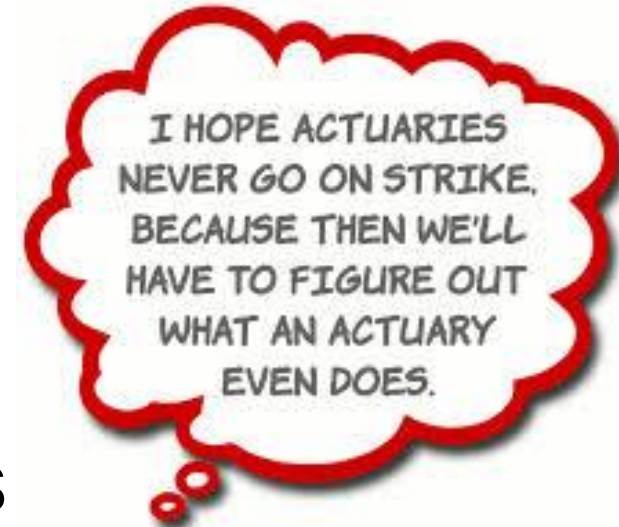
= NO WORK

= NO PAY

= No Administration fees

= No risk benefit premiums

= financial instability



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FUND NOT FINANCIALLY SOUND

FINANCIAL LIABILITY CHANGES

PERSONAL ASSESSMENT

Criteria for financial soundness has moved from valuation basis to legal basis

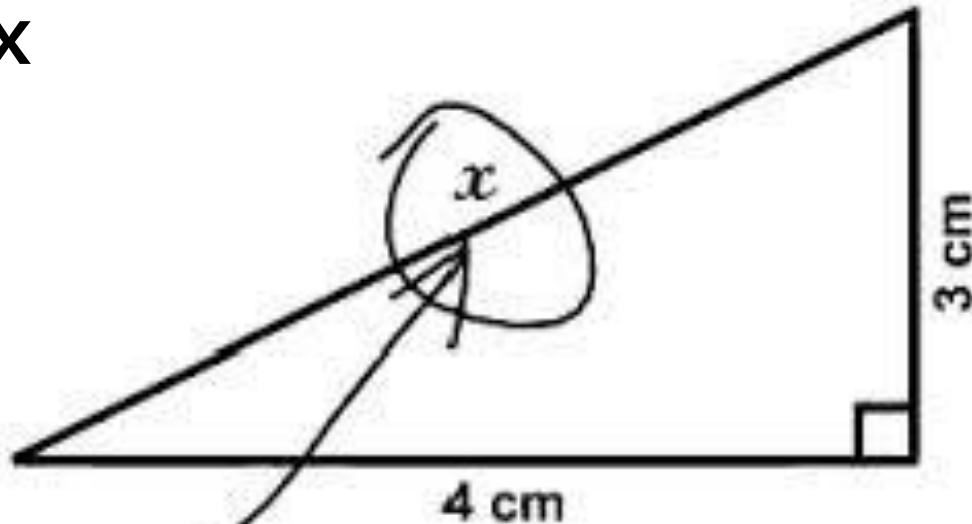
Suggest – legal responsibility NOT responsibility of Actuary

RECOMMENDATION

ASSA issues practice note
regarding the
financial soundness of
DC Funds

LAWYERS & MATHS

Find x



Here it is

The Actuarial Advice Route



Phase I

Board members see the problem..
but they refuse to listen to you



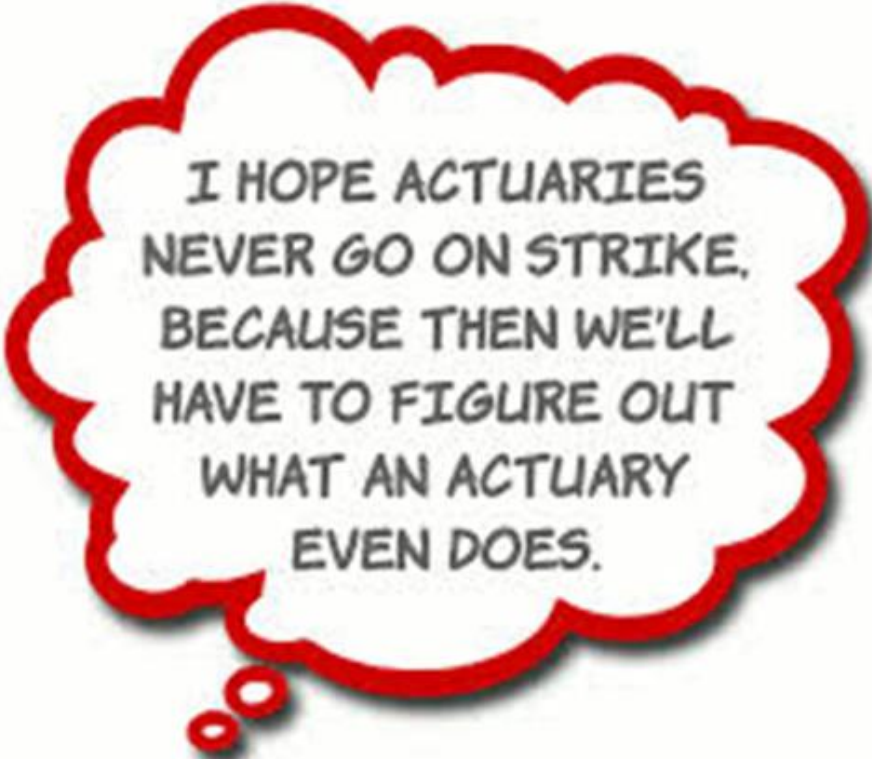
Phase II

Board members are in trouble..
but refuse to see your solution



Phase III

Board members are flabbergasted..
Your recovery plan is accepted
Your advice is rewarded.



I HOPE ACTUARIES
NEVER GO ON STRIKE.
BECAUSE THEN WE'LL
HAVE TO FIGURE OUT
WHAT AN ACTUARY
EVEN DOES.

Thank you