One industry, two funds

retirement funds in South Africa

Etienne Vlok speaks to Jan Mablangu, COSATU pension and provident fund coordinator, about the retirement fund industry and issues affecting members of these funds.

***Bulletin:** Why does COSATU need a pension and provident fund coordinator?*

Mablangu: We have this desk because this industry represents the only savings of our members. Also, the retirement fund industry in South Africa is fragmented with many problems. Without a desk in COSATU to deal with these issues, one affiliate will say one thing regarding a policy matter and the other will say another thing. A coordinator ensures that gains are followed up and implemented.

***Bulletin:** Why are retirement funds important?*

Mablangu: It is important that any person who joins the labour market starts thinking about his or her last day of employment - when he or she retires. That person should plan and prepare in such a way that his or her lifestyle does not change when he or she retires. Without the industry, you will have a group of retirees who will have nothing to eat and nowhere to live because they have no income.

***Bulletin:** What is the difference between a pension and provident fund?*

Mablangu: In a defined benefit (or pension) fund the employer promises certain benefits to the members on retirement. If claims increase or there is a shortfall in the fund, the employer has to increase its contribution to continue providing the benefits as promised. Therefore, the risk is with the employer.

In a defined contribution (or provident) fund, what a member gets on retirement is based on contributions into that fund. Hence, an employer would not have to increase its contributions if there was a shortfall. The fund will have to restructure its benefits using the same contribution as before. Therefore, the risk is with the members.

I am not saying defined benefit funds are better than defined contribution funds. We must have a debate about the future of these funds without taking away a member's right to choose a fund. What was right in 1980 cannot be right 20 years on.

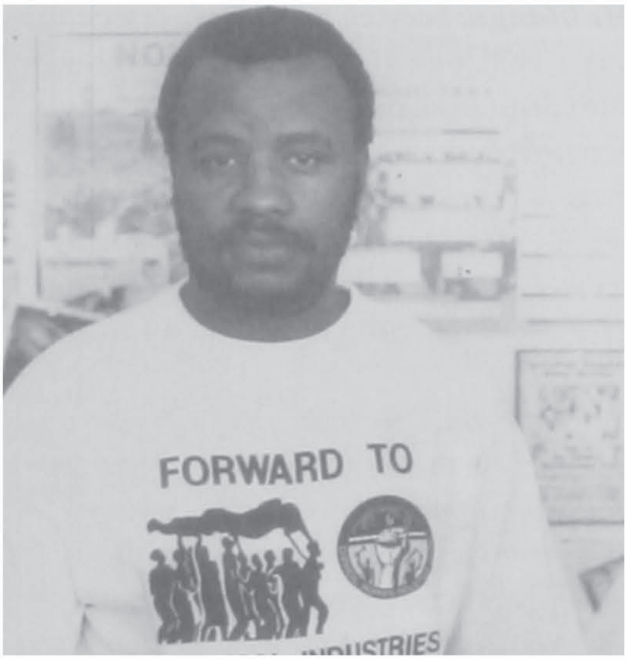
At the end of December 1999, the Financial Services Board (FSB), which regulates the industry, was supervising 16 000 funds. So many funds exist because many employers form their own funds. This fragmentation is not in the interests of the industry or of the funds themselves. The small funds are paying a fortune in administration costs, at the expense of the funds' members. It will be better to integrate all these funds into industry or bargaining council funds. Then each industry will have a defined benefit and a defined contribution fund. This will allow members to decide which fund to join. The privately administered funds can then negotiate better administration costs and, because of their size, all the funds will be able to use their muscles in negotiations with service providers. Workers will be in control of these funds as opposed to the current situation where one union is involved in more than 200 funds.

A number of COSATU unions have their own funds. That is a very strong foundation on which to establish industry funds.

Bulletin:* *Who administers retirement funds?

Mahlangu: A fund can be privately administered or self-administered. For example, NBC administers COSATU's fund. COSATU deducts money from our salaries and pays it into the fund's account. COSATU instructs the administrators to transfer the money to the fund managers, in accordance with our letter of appointment or with our investment strategy. Hence, COSATU's fund is privately administered. The Metal Industry Fund, for instance, is self-administered. That means the industry's bargaining council does its own administration.

Bulletin:* *What is wrong with the Pension Funds Act?



Jan Mahlangu of COSATU.

Mahlangu: The Pension Funds Act is more than 40 years old. We want to amend the whole Act so that it is, firstly, reader-friendly. Secondly, we want to take out old sections of the Act that do not belong in it. One of the changes would be to include a cap on foreign investments, especially as there are no prescribed assets investments. The government spent a lot of time calling for foreign investors. However, we allow our funds to invest offshore. That is a contradiction and a vote of no confidence in our country.

Furthermore, the Pension Funds Act does not compel an employer to form or employee to belong to a fund. This is a shortcoming and, therefore, we have to amend the Act. If all working people belonged to funds, they would have something when they retired. Small employers cannot afford to form their own fund, so they would then join national funds. However, as part of this compulsory provision, we have to set minimum contributions to ensure members are taken care of at retirement age.

Bulletin:* *Who operates in the industry?

Mablangu: Service providers service the industry. For example, Old Mutual provides administration, risk, consulting and actuarial services. You also have fund managers, insurers and a host of other service providers in the industry. Each service provider is employed by the board of trustees depending on which services it needs.

In the last few years, concerns have emerged in the industry. New products are developed purely for business opportunities – funds can live without these products. There is no strategic engagement with member representatives on what will add value to members.

In 1996, the Pension Funds Act was amended to say all funds' management boards must have 50% representatives who are elected by members. We were very happy then. However, I do not think that we are in control yet. If we were in control, we would be able to call fund managers and say 'Can you establish a product that will address what our members want?' We would also be able to give directives regarding investments.

Bulletin: *What is the importance of retirement funds in the local economy?*

Mablangu: It creates a massive amount of jobs. It also provides finance in a number of forms though very limited to members. Whether or not we agree with the manner the resources are used is another issue. The industry has a lot of potential. If only the government could regulate for prescribed assets investments, as COSATU and a number of institutions propose, the industry could play a massive role in the local economy for the betterment of members' lives.

According to the FSB annual report, the retirement fund industry's assets are about R644-billion. That includes private sector, local government, parastatal and government funds. We should use these assets to the advantage of our members and the country.

At the moment, funds can invest the biggest portion of their assets in equities and shares, but this does not create jobs because it is not invested in the productive sectors of our economy or in infrastructural development. In the Scandinavian countries, funds can only invest 40% of their assets in equities. That is what we should be doing as South Africans. It would force us to put more money into government bonds and infrastructural development. (Government bonds are sold by government. It then pays the money back over a period, normally on a fixed interest rate.)

Bulletin: *What are prescribed assets investments?*

Mablangu: We want to amend the Pension Funds Act to prescribe what proportion of each fund's assets to invest in equities, bonds, properties and cash. The idea is gaining ground but it is public knowledge that the ministers linked to the issue, Trade and Industry and Finance, have said government will not go that route. We should start raising it in the meetings of the Alliance. It also needs to be discussed at the economic summit that COSATU is calling for.

It is a dream to say 'Let's have prescribed assets investment, but let's leave it to market forces to decide'. That will never happen.

Some people are very hostile to the suggestion of prescribed investment. This is very interesting because 20 years ago more than 40% of retirement funds' assets were prescribed. This was supposed to oil the apartheid machinery and only benefited a small percentage of South

Without retirement funds, retirees will have very little income.

Africans. We need prescribed investments to benefit the entire country and the owners of the money.

I do not buy this suggestion that prescribed assets investments will scare potential investors. We do not want their monies to be invested in a certain way. We are talking about our own assets. Anyway, who will bring his or her money into South Africa if we do not use the resources that we have.

Bulletin: Can you tell us about the issue of compulsory preservation?

Mahlangu: You cannot say every worker must belong to a fund but not address the issue of compulsory preservation. Compulsory preservation is when funds are compelled by law to preserve benefits. If compulsory preservation is part of the Pension Funds Act, it means that if a member resigns or is dismissed or retrenched, that member will not get his or her benefit. The member will only get it when he or she retires. In the meantime, the money is kept in that fund or transferred to wherever he or she will be employed.

According to the FSB's report regarding withdrawals from funds, R62-billion in benefits were paid in 1999. R62-billion is a lot of benefits to pay out in one year. It is an increase of 0,5%, which is huge. If we can get a breakdown I am sure retrenchments, dismissals and resignations will form the bigger part of this R62-billion. A lot of money is moving out of the industry. For those who retire, it is fine because the money was meant for retirement.

The question of compulsory benefits depends on the restructuring of UIF benefits, basic income grant and other forms of income support during periods of unemployment. It also depends on meaningful progress towards eradicating large-scale structural unemployment.

Workers are not compelled to belong to a fund.

Bulletin: What is the relationship between a union and its fund?

Mablangu: The Act specifies that trustees have an ultimate responsibility in terms of a fund on behalf of members. If a union fund were to decide it wants compulsory preservation, the board of trustees would discuss the issue and take a decision. But what if the fund members are unhappy and say to the union, 'You formed this fund, we want our monies now'? Surely, there is a role for the union's national executive committee (NEC).

When a board of trustees deals with policy decisions, which structure must take those decisions? Surely, a union's constitutional structures have to give policy direction. I know it is a very sensitive situation but you cannot have a board that does not consult. With an important issue, the board of trustees should first take that issue to a structure of the union and then make a final decision.

Bulletin: What is the impact of HIV/AIDS on retirement funds?

Mablangu: This is a major issue. If you look at the claims in funds, death and disability benefits are increasing. HIV/AIDS is contributing to this as people who are HIV positive die because of opportunistic diseases. HIV/AIDS is beginning to bite funds heavily. Insurance companies are saying to some funds, 'Your claim experience is so high that we cannot afford to provide the existing benefits with the current premiums'.

For a fund to provide funeral, disability and death benefits, a company might have to pay a certain percentage of total payroll to the fund. However, because of claim experiences, that company has to increase its contribution to keep on providing the same benefits in the future. If the company cannot afford to pay the premiums anymore, the fund will have to reduce its benefits.

In some funds, employers will decide that they cannot increase premiums, and cap the premiums. Hence, some employers are pushing their employees out of defined benefit funds into defined contribution funds. The risk is then carried by the members. ★