Pension power for the people

Nearly a trillion rand is invested in 27 500 local retirement funds, and for most South African workers, pensions are their major form of savings. However, employees are often ignorant of their rights and responsibilities when it comes to administering these funds. Millions of rands and man-hours are currently lost annually through inept or even fraudulent administration.

This situation has the potential to improve as the risk and accountability of trustees (many of whom have come up through the union ranks and now represent thousands of fellow workers) have greatly increased. Trustees increasingly have to show how they have safeguarded the interests of the fund members and fulfilled their duties. Good governance and proper procedures are no longer an option but a legal necessity.

In practice, however, many trustees are ill-prepared for their increasingly onerous duties: a recent Deloitte & Touche report on Retirement Fund Governance in SA showed that only 24% of pension funds provide formal training for trustees, and an average of only 10 hours per year is spent on trustee training.

This inadequate preparation means that investment returns are often negated by poor service, outdated IT systems, fines for late returns, and other administrative problems and costs. This was highlighted by the same Deloitte & Touche report that found:

- Fund administrators' abilities to provide accurate and timely financial information were rated as extremely low.
- Two-thirds of funds surveyed had not submitted their annual financial statements to the Financial Services Board within the prescribed six months.
- 25% of the funds had no signed contracts in place with key service providers, being the administrator and investment manager.
- Over 20% of the funds did not comply with Regulation 28 of the Pension Funds Act.
- One of the three main reasons for funds not offering investment choice to members was because the administrator's systems were inadequate.
- 52% of respondents indicated they would change administrators if a suitable alternative administrator was available and the fund could migrate its data and records to the new administrator with minimal risk exposure and cost.

Such conditions are unacceptable, and it is only a matter of time before consumerism, which has highlighted inadequacies in banking and medical aid services and fees, hits pension funds too. Members of pension funds should keep in mind that they are entitled to request:

- timeous, accurate and complete record keeping at a fund and member level;
- regular valuation of investment records, preferably daily;
- daily reconciliations of bank accounts and member transactions;
- competent financial management;
- valid, accurate and timeous benefit payments;
- effective communication and reporting;
- access to real-time information;
- effective risk management and compliance;
- tried and tested business continuity and disaster recovery plans.

In retirement fund management, the buck starts and stops with the trustees who should not be influenced by factors other than the delivery of an effective and efficient administration service. Trustees have to be clinical in their decisions to ensure that their members' interests are protected and that wealth is created and managed by disciplined and focused role players.

Employers and trustees must beware of selecting an administrator purely on price. It is essential to do your own investigating and interrogating at the administrator's premises. Ahead of the appointment of an administrator, it should be standard practice to review the proposed operating environment. Check that they are not promising more

Finance Minister Trevor Manuel recently called on trade unionists – some of whom are pension fund trustees – to take their roles seriously and ensure pension fund managers are held accountable for how workers' savings are being invested. **Gavin Williams** *and* **Mustaq Parker** *offer practical guidelines on effective retirement fund administration, and outline legislation that is in the offing to provide protection for workers and employers.*

than they can deliver. Obtain a written commitment that all of the proposed services on offer are currently in use by the administrator's existing clients.

Do not appoint an administrator whose proposed service offering depends on new and non-finalised operating systems. This could result in overtime and is bound to result in frustration and delays in or lack of delivery. A pension is usually an employee's biggest asset and must be optimally administered.

Be aware of hidden pension fund costs, which mount up from:

- Regular switching of pension fund investments: While the direct costs of switching investments may be nominal, the cost of chasing performance through regular switching may well result in disappointing performance for pension funds and their members. All too often an increasing number of intermediaries interpose themselves in the decision-making process, without adding any value. In many instances it would be possible to establish appropriate investment strategies without a high level of intermediary involvement.
- Routine annual increases in retirement fund administration fees: While administration fees could rise every year, inefficiencies may also grow because outdated, overburdened IT systems cannot keep up with new requirements for greater member choice and transparency.

Penalties for late entries: The Registrar of Pension Funds 2000 Annual Report showed that 191 self-administered funds (including top corporations, charities and educational institutions) failed to submit financial returns on time. In addition, 43 of the total 256 self-administered funds listed as outstanding in the 1999 report were still in default when the 2000 report was completed. Penalty payments for late returns are deducted from member contributions and it is the employees who pay the price in the end.

- The general ledger should be integrated into the retirement fund administration application to ensure completeness, accuracy and validity of transactional updating, and that financial information is supplied on time.
- Payments to retirement fund trustees: It is becoming more common for trustees to be paid from the fund for time spent administering fund affairs. Trustees may not have the requisite pension fund knowledge and not add value for their fees. Worse still, they may make inappropriate or wrong decisions on fund issues.
- High staff costs: Answering member queries and handling administrative tasks manually adds up to time-consuming, high labour costs. The administration system should instead provide relevant, regularly updated information electronically in a secure manner.
- A lack of investment choice: A one-size-fits-all policy could result in a portfolio that doesn't meet the member's needs and could ultimately cost the member due to the inappropriateness of the strategy. Retirement funds should have the functionality to stratify their membership groups and provide the appropriate risk-profiled investment portfolios to the different lifestage bands.
- Fraudulent administration: During 2000, there were 21 inspections of pension funds and three of fund administrators. The reports revealed 11 cases of employers not paying over contributions deducted from members' salaries as required in terms of section 13A of the Act. Nine of these cases were handed over for prosecution. Two employers were convicted and the other cases were pending at the time of the Registrar of Pension Funds 2000 Annual Report.
  While under-performing funds can be moved to a different fund manager, fraudulent administration could lead to the complete loss of employees' biggest assets.

All agreed procedures, performance

power people

standards and responsibilities must be covered in the administrator's Service Level Agreement. This includes receipt and investment of members' contributions, submission of Annual Financial Statements, payment of Retirement Funds Tax and RSC levies, etc. It is critical to establish the credibility of the people who will be involved in the affairs of the fund before appointing an administrator.

While professional qualifications are no guarantee of a cost-effective delivery, a combination of appropriately qualified persons, industry experience, in-house training, a limited staff turnover and a detailed understanding of the systems that support the retirement fund are bound to have considerable financial impact should problems be experienced. Finally, the agreement must be signed before the mandate commences.

The legal environment in which pension funds operate is also constantly evolving and there are numerous changes currently underway that will impact on employers and employees. Some of the most relevant include:

The Pension Surplus Bill
The bill was promulgated last year, but stakeholders are refining the finer practical details that will drive its implementation. This legislation will have far-reaching implications because any pension fund surplus built up since the early 1980s will have to be redistributed to former and present members within 18 months of the fund's next statutory actuarial valuation. This takes place every three years in the case of defined-benefit schemes. This will increase the workload because trustees will have to reach agreement on how to split the surplus, if there is one, to ensure minimum benefit requirements are met and to track down previous members.

Income tax legislation
If a pension fund member is entitled to a benefit, the fund's administrator had to apply for a tax directive before the benefit could be paid to the member. In practice there were exemptions and frequently there was no need to apply for an assessment. Those whose taxable earnings did not exceed R60 000 were assessed in terms of a blanket tax directive. Under new legislation, every benefit is subject to a directive. This will increase fund administration costs and could delay the payment process.

Transfer of a pension to another retirement fund
Previously, the SA Revenue Services (SARS) was simply informed of the new location of the funds in terms of a Recognition of Transfer procedure. This led to abuse that resulted in benefits escaping the tax net. Now, to prevent any such abuse the administrator must apply for a directive before forwarding the monies. This requirement stands even if there is no tax owing. Again, this adds to costs and time involved.

Retirement funds tax
There are indications that SARS could review the retirement fund tax rate. An announcement was expected in the last Budget, and could be made next year. SARS might revisit the rate of tax on gross interest and net rental income earned by retirement funds, now 25%.

Regulation 28 of the Pension Fund Act
The finalisation of this draft is important because it will prevent pension fund trustees from evading the responsibility of ensuring that an investment strategy is put in place to cater for the varied needs of pension fund members. The regulation moves away from setting specific investment limits and instead lays out the requirement that trustees give careful consideration to investment strategies and member choice. There will also be a greater need for effective communications and greater education to empower employees to make informed choices. Trustees may delegate these tasks, but will have to ensure that this is done efficiently and the necessary controls are in place.

Housing loans
A retirement fund may be asked to provide guarantees to a financial institution for providing housing loans. Who must then assess the value of the property and the risk? Trustees can delegate the responsibility of assessment to the financial institution, but must satisfy themselves that this is done responsibly.

Conclusion
The effective administration of pension funds is an increasingly complex issue, which will require robust IT systems and informed personnel to implement effectively. Handled efficiently by competent administrators, pension funds can be an added bonus for workers; poorly handled, they are a potential minefield for employee discontent. LB

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