

LEGAL UPDATE 5/2011: Personal liability of board members of pension fund organisations

Board members (trustees) must observe the utmost good faith and exercise proper care and diligence

Section 2 of the Financial Institutions (Protection of Funds) Act provides for the duties of people dealing with funds of, and with trust property controlled by, financial institutions. Trustees are required to:

- observe the utmost good faith and exercise proper care and diligence;
- observe the utmost good faith and exercise the care and diligence required of a trustee in the exercise or discharge of their powers and duties; and
- not gain any improper advantage for themselves to the prejudice of the fund.

“Financial institution” includes any person or institution referred to in the definition of “financial institution” in section 1 of the Financial Services Board Act, which in turn provides for any pension fund organisation registered in terms of the Pension Funds Act. Therefore, section 2 of the Financial Institutions (Protection of Funds) also applies to trustees of pension fund organisations.

Trustees could face fines or imprisonment

Section 10 of the Financial Institutions (Protection of Funds) Act provides that persons who contravene or do not comply with the Act could be found guilty of an offence.

Trustees who do not exercise the utmost good faith, proper care and diligence in the exercise or discharge of their powers and duties could be in contravention of the Financial Institutions (Protection of Funds) Act. Trustees could be found guilty of an offence and on conviction:

- be liable to a fine or imprisonment;
- be ordered to repay any profit made;
- be ordered to pay for any damage suffered; and
- be prevented from serving as directors, members, partners or managers of financial institutions for any period that the court sees necessary.

Trustees must observe the utmost good faith and exercise proper care and diligence

Trustees could face fines, imprisonment, be ordered to repay profit, pay for damages and be prevented from occupying certain positions

The object and duties of trustees in terms of the Pension Funds Act

Section 7C and 7D of the Pension Funds Act provides for the object and duties of the trustees.

The object of the trustees is to:

- direct, control, and oversee operations of the fund in accordance with the applicable laws and the rules;
- ensure interests of members are protected;
- act with due care, diligence and good faith;
- avoid conflicts of interest;
- act impartially.

The object of trustees

The duties of the trustees are to:

- ensure that proper registers, books and records in respect of the operation of the fund are kept. This includes proper minutes of all resolutions passed by the board;
- ensure that proper control systems are put into place;
- ensure that adequate and appropriate information is communicated to the members of the fund informing them of their rights, benefits and duties in terms of the rules;
- take all reasonable steps to ensure that contributions are paid on time to the fund in accordance with the Pension Funds Act;
- obtain expert advice on matters where trustees may lack sufficient expertise;
- ensure that the rules, operation and administration of the fund comply with the Pension Funds Act, the Financial Institutions (Protection of Funds) Act, and all other applicable laws.

The duties of the trustees

Circular PF No. 130: Good governance in respect of retirement funds

The Financial Services Board issued Circular PF No.130 which provides guidelines and principles for the good governance of retirement funds. Under PF No. 130, the board should act with the utmost good faith and in the best interest of all members. The board must always give full and proper effect to the rules of the fund. The board must deal with matters according to their fiduciary duties, fairly and with respect.

Trustees may collectively and individually be held liable for any breach of governance which results in any loss to the fund, members or beneficiaries. The board should adhere to the rules of the fund and should institute disciplinary measures in the event of an alleged breach by a board member. Member and beneficiaries may request the Pension Funds Adjudicator or court of law, to determine the liability of the trustees.

PF 130: Good Governance – The board can be held collectively and individually liable

Court cases and Pension Funds Adjudicator complaints

In the complaint between Knight and Mitchell Cotts Pension Fund, the complainant, a pensioner elected trustee, lodged a complaint against the fund because the trustees decided not to give him certain information of members and pensioners of the fund.

Knight v Mitchell Cotts

The complainant requested the principal officer to provide him with a list of active members, including each member's name, address, date of becoming a member of the fund and their pension amounts as well as a list of pensioners, including the pensioner's full name, address, date of becoming a pensioner and the current value of their pension. The principal officer refused the request and the matter was referred to the first meeting of the board of trustees. There it was decided that the information requested would not be supplied.

**Pension Fund:
giving
information**

The fund argued that the key issue for determination was the balancing of the duties of the trustees of a fund with their needs to obtain information (in order that they may perform their duties) as opposed to a pension fund member's right to privacy. It further contended that the right to disclose information only exists if the information is reasonably required to protect or enforce an existing right. It alleged that the complainant's request for information was not based on his duty to act as a trustee or to protect the rights of the fund's members.

The Pension Fund Adjudicator stated that any person who administers "any funds" of a financial institution must observe utmost good faith and exercise proper care and diligence. If trustees breach these duties, and the fund or any beneficiaries suffer loss as a result of the breach, the trustees may be held personally liable. If a trustee fails to comply with their duties it may result in adverse consequences for a trustee in their personal capacity. The Adjudicator found that in this instance the complainant required the specific information in order to comply with his duties set out in the rules of the fund.

In *Seymour-Smith v Maxam Dantex South Africa (Pty) Ltd*, the applicant was unhappy with the section 37C death benefit distribution of the trustees. The trustees initially agreed to withhold payment until the dispute was resolved. They then refused to withhold payment. The court found that this was unreasonable. An interdict was granted preventing the fund from paying out the benefit in order to allow the applicant an opportunity to start proceedings for the review or setting aside of the award.

**Seymour-Smith
v Maxam Dantex
SA: trustees
ordered to pay
costs as they
acted grossly
unreasonable**

The court found that the trustees in the reasonable exercise of their functions ought to have been aware that the law provides for further adjudication of their decision. They should have been astute in preserving the rights and interests of all claimants. The court stated that they acted not only wrongly, but also grossly unreasonably. The trustees were therefore ordered to pay the applicant's costs for the court case.

In the complaint between *VA Mes and Art Medical Equipment Pension Fund*, the complainant's husband was employed by Art Equipment (Pty) Ltd and was a member of Art Medical Equipment Pension Fund. The sole trustee of the fund was the managing director of the employer. All benefits under the fund were secured by an insurance policy. When the complainant's husband passed away, a death benefit became payable. However, although contributions were deducted from members' salaries no contributions were paid to the fund. The insurance policy had therefore lapsed due to the non-payment of premiums. The employer and the fund had in the interim been liquidated.

**VA Mes v Art
Medical
Equipment
Pension Fund et
al: failure to
exercise proper
care and
diligence**

The Pension Funds Adjudicator stated that this was an appropriate case for holding the trustees of the fund personally liable for the loss suffered by the complainant. The evidence shows that his conduct was grossly negligent, if not dishonest, and that he flagrantly breached his duties.

In the complaint between *Bajikile Sithole and ICS Provident Fund*, the trustees did an investigation to establish the dependents of the deceased member. The trustees determined that there were five dependants: the three children, the surviving spouse (complainant) and the deceased's mother (the grandmother). The grandmother was the sole "nominee". At the time of the deceased's death, all dependants were living

**Bajikile Sithole v
ICS Provident
Fund: breach of
statutory duties**

together with the grandmother. The fund awarded the entire benefit to the grandmother.

The fund advised that in their investigation they were advised that in terms of customary law, in the absence of a male member of the household, the grandmother is regarded as the head of the household. The head of the household is responsible for the support of the other members of the household. On this basis the trustees believed that the benefit should be awarded to the grandmother to assist her in supporting the other dependants.

The complainant was dissatisfied with this decision and alleged that the fund acted negligently by paying the entire benefit to the grandmother to the exclusion of other dependents. The complainant also advised that she did not have any income and could not maintain the three minor children and that the grandmother was not using the benefit to maintain the children and her.

The Pension Funds Adjudicator stated that the trustees who made the decision failed to exercise proper care and diligence when making the distribution. They may be in breach of their statutory duties and could be held personally liable for any damages suffered by the fund or a beneficiary of the fund.

The fund was ordered to pay the complainant and her three children 80% of the benefit.

The Adjudicator stated that the fund could recover the monies from the relevant trustees or the grandmother, to the extent to which she has been unjustifiably enriched.

In the complaint between NA Moabi v Orion Money Purchase Provident Fund, the complainant was dismissed from employment. She advised that she had made numerous enquiries through the years but had not received her fund benefit. The fund had advised that it had not received a withdrawal notification form and therefore could not pay the withdrawal benefit. The employer advised that they had not submitted a withdrawal notification form as the complainant owed the employer money which she stole while working for the company.

The Pension Funds Adjudicator stated that it is essential that the employer complete the withdrawal notification form indicating the cause of termination of employment. This would allow the fund to determine which benefit is payable. The reasons provided by the employer are not sufficient justification for not completing the form.

The Adjudicator also stated that trustees were also partially to blame in this matter. In terms of sections 7C and 7D of the Act, the trustees are required to act with due care, diligence, good faith and impartiality in respect of all members and beneficiaries. The trustees should have compelled the employer to complete the withdrawal notification form. The trustees could have also approached the office of the Adjudicator for an order obliging the employer to complete the form. Instead, the board sat idly by for almost three years to the detriment of the complainant. If the complainant had been legally represented, the Adjudicator would have had no hesitation in making a costs award against the fund or even against the trustees in their personal capacities.

**NA Moabi v
Orion Money
Purchase
Provident Fund:
act with due
care, diligence,
good faith and
impartiality**

Trustees must observe the utmost good faith and exercise proper care and diligence, avoiding conflicts of interests. Trustees found contravening any duty imposed upon them by legislation or the rules of the fund could be found guilty of an offence and held personally liable.

Carlo Subban

Legal Adviser

Momentum BenefitsAtWork

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