

Legal Update

3 of 2021: When is it lawful for a fund to withhold a benefit on request of an employer?

Please read this Legal Update together with Legal Update 6 of 2020.



1. Section 37D(1)(b)(ii) of the Pension Funds Act, 24 of 1956 (the Act) says that funds may deduct any amount due by a member to their employer on the date of their retirement or the date on which they stop being a member of the fund. Such deduction must be in respect of compensation for theft, dishonesty, fraud or misconduct by the member, for which the member has admitted liability in writing to the employer or judgment has been obtained against the member.
2. There have been numerous occasions where our courts have determined that for section 37D(1)(b)(ii) to have effect, it must be understood to confer an implied power on a fund to withhold payment of a benefit pending the determination of the member's liability towards the former employer.
3. The use of the word "may" in section 37D(1)(b)(ii) of the Act means that the board of a fund has the discretion to agree to the withholding of a benefit or not. As a general rule and based on the ruling of the Supreme Court of Appeal in *Highveld Steel and Vanadium Corporation Ltd v Oosthuizen*, the board must ensure that it acts with thorough care when exercising its discretion, while balancing the competing interests of the member and the employer with due regard to the strength of the employer's claim against the member.
4. This means that the board of a fund is not obligated to grant the request of an employer to withhold a benefit, as the facts of each case must be examined. The decision to withhold a benefit requires a careful, independent analysis of all the facts. In this regard, the Financial Services Tribunal held in *NBC Umbrella Retirement Fund and Anax Logistics Services (Pty) Ltd v the Pension Funds Adjudicator and XJ Qubeka* as follows:

"The Fund is not the agent of the employer and is not supposed to act in the interests of the employer and as far as issues between employer and member are concerned, it should act independently."
5. Based on recent Financial Services Tribunal rulings, a fund must ensure that the following requirements are met before it exercises its discretion to withhold a member's benefit:
 - A. If the member did not sign an admission of liability or the employer has not provided a civil judgment, the employer must provide proof that it has instituted a civil court action against the member.**
 1. It has been long-standing practice in the retirement fund industry to interpret the reference to "judgment in any court including a magistrate's court" in section 37D(1)(b)(ii) of the Act to include both a civil court judgment and a criminal court judgment issued under section 300 of the Criminal Procedure Act, 51 of 1977. It has accordingly also been the practice of the FundsAtWork Umbrella Funds to withhold members' benefits on receipt of proof that an employer has instituted (only) criminal proceedings against a member under section 37D(1)(b)(ii).
 2. There have however been recent rulings by the Financial Services Tribunal determining that a criminal court judgment alone can never justify the withholding of and/or deduction from a member's benefit by a fund. In *FundsAtWork Umbrella Provident Fund v EE Ngobeni and Another*, the following was found:

"The section deals with two situations, namely an admission of liability (which does not apply to the facts) and a civil judgment. Highveld Steel and Vanadium Corporation Ltd v Oosthuizen ... dealt with the withholding of payment pending the finalisation of civil proceedings. It did not hold that a Fund is entitled to withhold payment because a criminal case has been opened or even upon conviction. A conviction is not a judgment against a member that quantifies compensation in respect of damage caused, and costs are not awarded against persons convicted."
 3. Before these rulings, the Pension Funds Adjudicator had held in numerous determinations that a fund may withhold members' benefits pending finalisation of not only civil proceedings but also criminal proceedings, subject to employers obtaining a section 300 compensation order.
 4. In light of the above rulings of the Financial Services Tribunal and the views expressed by the Office of the Pension Funds Adjudicator at a recent public forum, in the absence of an interdict, a fund can no longer withhold a benefit if the employer has only instituted criminal charges.

5. It is therefore clear that, based on this interpretation of section 37D(1)(b)(ii) by both the Financial Services Tribunal and the Pension Funds Adjudicator, a fund should only be allowed to withhold a member's benefit if the employer had instituted a civil court action against the member or has obtained an interdict preventing payment.
6. To enable the boards of the FundsAtWork Umbrella Funds to comply with this requirement, the employer must forward a formal withholding request to the Funds. The request must contain, amongst others, the following detailed information:
 - The date on which the employer started its investigation into the member's alleged misconduct
 - A copy of the summons/notice of motion/letters of demand and any other evidence
 - If summons has not yet been issued, reasons for not issuing and the date on which summons will be issued
 - The date on which the member's employment was terminated
7. In terms of the rules of the FundsAtWork Umbrella Funds, the employer's formal withholding request must be made within a reasonable period after the member's termination of service as determined by the board of the Funds, depending on the specific circumstances.

B. The fund must be satisfied that the employer has a prima facie case against the member.

1. In South African Broadcasting Corporation SOC Ltd v South African Broadcasting Corporation Pension Fund and Others, the High Court held that if an employer can prove prima facie that the member might be liable for damages and that the employer has a prima facie right to recover the losses it incurred and which are directly attributable to the member's behaviour, a fund may withhold payment of the benefit.
2. In the Financial Services Tribunal case of Reckitt Benckiser Retirement Fund v BC Gamede and Others, the fund submitted that the allegations of misconduct was sufficient to establish a prima facie right to have the withdrawal benefit withheld and that it thus did not have to be absolutely convinced that the member committed the relevant transgressions for it to withhold the benefit. The Financial Services Tribunal held that although the allegations against the member had to be proven beyond a reasonable doubt, the fund was only required to establish a prima facie case against the member. The board of the fund was only required to exercise reasonable discretion and be satisfied that the employer had made out a prima facie case against the member and that there were reasonable prospects of success. It could therefore never have been envisaged that the fund was required to determine if the allegations of fraud, dishonesty or theft have been proven. However, there must be merit in the case to the extent that the employer had a reasonable prospect of success.

3. In the Financial Services Tribunal case of KPMG Services (Pty) Ltd v Milimo Maseti and 2 Others, the following was found:

"The PFA accordingly found that the trustees exercised their discretion to withhold payment of the complainant's withdrawal benefit without any supporting evidence that the employer had made out a prima facie case against the complainant.

The employer sought to overcome the problem for the first time in "further reasons" filed in the reconsideration application. It now gave the detail of the "crime" and "loss" and said that the evidence was provided verbally to the Fund and "was available from when the request was made to withhold" the funds.

If this was an attempt to apply for the submission of further evidence, it fails not only on procedural grounds. It does not establish that the "trustees" exercised any discretion."

4. Therefore, in summary, the requirement that the fund must be satisfied that the employer has a prima facie case against the member entails that the fund must satisfy itself of the following:
 - That the employer, within a reasonable period from the date of the termination of employment, can show that it has a prima facie case demonstrating that the member is liable for damages
 - That the employer has a right to recover the losses it incurred
 - That the losses are directly attributable to the member's dishonest behaviour.

This does not mean that before exercising its withholding discretion, a fund must be absolutely convinced that the member committed the relevant transgressions and/or determine if the allegations of fraud, dishonesty or theft have been proven. The only onus on a fund is to establish if the employer in its reasonable discretion indeed managed to establish a prima facie case for the withholding of a benefit.

C. The member must be given an opportunity to properly state their case in writing before the fund.

1. In the 2019 High Court case of SA Metal Group (Pty) Ltd v Jetha, Alexander Forbes Retirement Fund and the Pension Funds Adjudicator, the Court held that one can safely assume that the employer's case must be put to the member to afford him the opportunity to respond. This must be done before the fund takes a decision impacting on the rights of the member. The High Court further held that the board of a fund merely being satisfied that the employer has brought allegations that, if true, would show damages arising from dishonest conduct by the member, is not sufficient on its own to withhold a benefit. The duties placed on a board in terms of section 7C of the Act mean careful scrutiny of claims made against benefits by employers. They also mean weighing of the competing interests of the parties after affording the member an opportunity to place their case properly before the fund.

2. In *Rossouw v FundsAtWork Umbrella Pension Fund and Others*, the Pension Funds Adjudicator held that before deciding to withhold, the Fund should have asked the member to provide submissions on whether the benefit should be withheld. Even if the Fund somehow felt that the employer's case was strong, more was required than merely looking at the allegations of the employer. The Fund should have taken facts as set out by the employer, together with any facts set out by the member and which the employer could not dispute, and considered with regard to the inherent probabilities whether the employer could on those facts have obtained final relief at a trial. The facts set up in contradiction by the member should then have been considered. If serious doubt was cast on the case of the employer, it should not have succeeded in its request for withholding, because its prima facie right may have been open to some doubt.

3. In *NBC Umbrella Retirement Fund and Anax Logistics Services (Pty) Ltd v the Pension Funds Adjudicator and XJ Qubeka*, the Financial Services Tribunal held as follows:

“The simple ground on which the determination was based was that the Fund did not comply with the audi alteram partem rule. It did not inform the complainant of the application to freeze his pension pending the finalisation of legal proceedings against him and it did not ask him for his input ...

This Tribunal dealt with the issue in detail in *FundsAtWork Umbrella Pension Fund v EE Ngobeni* case PFA 64/2020. The fact that the applicants do not like the decision is beside the point. The decision did not, nor does the common-law, require a full-blown trial. Failure to comply with the rule cannot be rectified by, as was attempted here, a default judgment sometime in March 2021, or an arbitration award during January 2021.

Unless and until the said decision is set aside by higher authority, it will be applied by this Tribunal.”

4. The *Jeftha* case and the various subsequent Pension Funds Adjudicator (like the *Rossouw* case above) and Financial Services Tribunal decisions (like the *Qubeka* case above) have made it clear that funds are expected to put the employer's case to the member and to hear the member's side before deciding whether to withhold the member's benefit.
5. To ensure compliance with this requirement and for procedural fairness, the FundsAtWork Umbrella Funds have implemented a process to give members the opportunity to properly provide their input or views on the employer's case before the Funds make a decision on whether to withhold the benefit. In some cases – depending on the response provided by the member – the Funds may afford the employer an opportunity to reply to the member's response.

D. The amount that is withheld may not exceed the amount for which the employer is holding the member liable.

1. A fund may only withhold an amount up to the value of the employer's claim. If the alleged loss suffered by the employer does not exceed the value of the member's benefit, it will be unreasonable for a fund to withhold a member's entire benefit.
2. In the Financial Services Tribunal case of *Absa Pension Fund and ACA Employee Benefits (Pty) Ltd v Kgole* and the Pension Funds Adjudicator, the Adjudicator had ruled that the fund had to pay the member compensation in the amount of R1 000 for its unreasonable and unjustifiable conduct in failing to pay her the portion of her benefit that was over and above the amount allegedly lost by the employer, as well as 10% interest. The fund submitted that the benefit was withheld pending the employer's progress report on the case and that the benefit would be released only once the employer failed to effectively resolve the matter. The fund also submitted that the member did not suffer any financial loss as the benefit remained invested in the market and that she received market-related return on the benefit amount. The Tribunal found that the fund not only failed to properly apply its mind to the issue before it but also failed to apply care and lessen the prejudice of the member under the circumstances.
3. The rules of the FundsAtWork Umbrella Funds are aligned with this requirement as they state that the amount withheld may not be higher than the amount that may be deducted from the member's benefit. It is also a requirement that the employer's formal withholding request must contain the estimated amount of the damage suffered by the employer and thus the amount of damage it requires the Funds to withhold.

E. The fund must monitor the progress of the employer's case against the member and ensure that the period of withholding is reasonable.

1. A fund is not allowed to withhold a benefit indefinitely at the request of an employer as members must be protected against any potential prejudice they may suffer as a result of the infringement of their right to be presumed innocent until found guilty. The period of withholding must therefore be reasonable. The Adjudicator held as follows in *Twigg v Orion Money Purchase Pension Fund and Another*:

“However, the power of withholding must also be exercised reasonably and not indefinitely. In the instant matter, within 6 months of the complainant's termination of membership, criminal charges were laid by the employer. A civil claim has also been instituted against the complainant for the recovery of monies. ...The trial in both the matters are about to be conducted. In addition, the proceedings at the CCMA are also pending.

Bearing in mind that the complainant's withdrawal benefit continues to earn interest at the rate of return of the fund and the imminent completion of the aforesaid legal proceedings, I believe it would be prudent to postpone the matter for a further 6 months, allowing the employer further opportunity to pursue its claims in the various courts."

2. In *Mdlalo v Consolidated Retirement Fund for Local Government and Others*, the Adjudicator found that the board of the fund failed to act with due care, diligence and good faith. The failure arose from the fund allowing the employer to sit idly for more than three years from the date of the member's termination of service and not institute legal proceedings against the member. The Adjudicator accordingly found that the period of over three years withholding the member's withdrawal benefit was too long after she was dismissed for fraud.
3. Therefore, if the time taken to finalise a matter is unreasonable and the employer has not taken such further steps to ensure that the matter is finalised, a fund must release the benefit to the member.
4. In *Van Tonder v Motor Industry Provident Fund and Another*, the Pension Funds Adjudicator held as follows:

"This Tribunal notes with concern the passive role played by the board of the first respondent in resolving this matter. The board of the first respondent failed to act with due care, diligence and good faith in dealing with the complainant's withdrawal benefit. This is evidenced by the fact that the first respondent started to enquire about the legal actions taken against the complainant when he lodged a complaint with this Tribunal. There is nothing in the submissions that indicates that the first respondent requested the second respondent to provide it with progress report[s] on the legal actions taken against the complainant. The conduct of the first respondent in this matter is unacceptable and amounts to dereliction of its fiduciary duties."

5. The rules of the FundsAtWork Umbrella Funds are aligned with this requirement. They state that the board may only withhold payment of the benefit if the board members are in their reasonable discretion satisfied that:
 - The employer has instituted or will institute legal proceedings against the member within a reasonable period and
 - The employer has not caused any unreasonable delays in bringing it to finalisation.

F. The fund must ensure that the benefit is protected from poor investment performance during the withholding period.

1. The Pension Funds Adjudicator held as follows in *Dakin v Southern Sun Retirement Fund*:

"In withholding a benefit for legitimate reasons on behalf of a withdrawing member, the fund should afford the member some protection from suffering decline in the value of the benefit during the period it is withheld... The appropriate remedy is to direct the fund to effect an appropriate amendment, with retrospective effect, giving the member the right to divest the benefit at an agreed rate of interest or to hedge the investment performance in some other way."

2. A fund should therefore, if applicable and practical, permit the value of the member's benefit that is being withheld to be isolated, in whatever manner the fund believes appropriate, from the possibility of a decrease in the value as a result of poor investment performance. It must do so by investing the benefit in a suitable investment portfolio.
3. The rules of the FundsAtWork Umbrella Funds are aligned with this requirement. They state that where the Funds decide to withhold the benefit, the benefit will be invested in a portfolio specifically chosen by the board for this purpose (the default investment portfolio) where it will remain until the date of payment by the Funds to the employer or the member. The aim of this default investment portfolio is to protect the benefit from declining markets.