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Today's Trustee

YOUR MONEY YOUR POWER

4 **FIRST WORD**
Were retirement funds to be consumed by prevailing sprits of negativity, they might be tempted as much as possible rapidly to offload SA stocks. They can't and they shouldn't. After the elections, there'll still be life and promising signs do appear.

10 **LITIGATION**
Losses due to the Trilinear debacle have caused a provident fund to sue the FSCA for R70m. A court date for the matter, to be defended, has been set.

14 **PUBLIC INVESTMENT CORPORATION**
While the Mpati commission has its hands full, they could become still fuller. Structural and policy changes must follow.

18 **RESPONSIBLE INVESTMENT**
A strategy for 'alternative' asset allocation is shown by a workers' fund directly to benefit members. It's seen in the launch of truck stops on SA highways.

20 **HOMELOANS**
Another controversy for the PIC and GEPF is in how the payment of a commission was handled. Fortunately, a "mistake" was detected and rectified.

24 **CURRENTS**
Radical review of stewardship codes in UK could resonate in SA; Actuary appeals against R40m damages award; Lila's resignation from EPPF; Nedlac's supposed consensus on social security; Paying for grants and savings; Lessons from the Gamas incident; Court orders needed to reverse erroneous cancellations of fund registrations; Adjudicator disturbed by TCF non-compliance.

April / June 2019

30 **PAIA APPLICATION**
Public servants unhappy with circumstances of PIC loan to Eskom. Questions raised over consultation, documentation and validity. At least the R5bn short-term loan, effectively from the GEPF, has been paid back.

34 **COVER STORY**
There're chinks of light in the ongoing saga of unpaid benefits, in worsening amounts, to members of pension funds. Successful tracing has proved a major problem. But in the list of what's to be done, some institutions are doing it and have ideas for improvement.

41 **ECONOMIC EMPOWERMENT**
A transaction by African Rainbow Capital makes Sanlam Investments the largest asset manager in terms of black-owned criteria. At the same time, Momentum becomes the first of the big life assurers to have achieved a Level 1 B-B BEE ranking.

45 **TRANSFORMATION**
As the amended Financial Sector Code takes hold, here's a guide to help retirement-fund trustees and advisors become familiar with the new set of disclosure requirements.

48 **IMPACT INVESTMENT**
Why it must be the way of the future, and the sooner the better, especially in SA.

52 **SHAREHOLDER ACTIVISM**
What's to prevent asset managers from formal cooperation when they "engage" with investee companies and exercise proxy votes? Might it verge on illegal collusion? Maybe not.

EXPERT OPINIONS

8 SANLAM CORPORATE
on smoothing the ride into the new default regulations.

12 ASHBURTON INVESTMENTS
on the search for yield in private markets.

17 JUST SA
on offering fund members what they can afford.

22 SANLAM INVESTMENTS
on relative downsides in offshore equities;

28 OLD MUTUAL CORPORATE
on the learning curve ahead for fund trustees.

33 RISCURA
on the need for retirement-savings changes to accommodate enhanced longevity;

40 LIBERTY CORPORATE
on better outcomes for fund members.

43 MOMENTUM
on the warts in prescribed assets.

47 FUTUREGROWTH
on tipping points in responsible investment.

56 **GRAVY**
Imbalanced swipe at private-sector funds.

FIRST WORD

Breathe easier

Look at some bright spots. On balance, after the elections the odds are shorter for optimism than pessimism provided that . . .

This pre-elections period is the season of heightened madness. Expect it in vast dollops.

Truths and contexts become casualties, as they invariably do when emotions are let loose on the free-for-all social media. They offer a distorted gauge, as do sound bites from the self-interest of campaign rhetoric, amplifying arguments that stimulate populist response and expectation but belie their capacity for credibility and implementation.

Cool heads risk pollution by hot heads especially within an ANC looking to outflank the Economic Freedom Fighters. With the EFF's eyes set on 'kingmaker' roles in national, provincial and municipal governments, where the ANC might not win outright majorities, some pandering is perhaps strategic for the challenge to be countered. Electoral inflexions are made of dust and return to dust.

There are obviously known unknowns. Particularly amongst them are whether:

- President Cyril Ramaphosa will emerge strengthened or weakened from his "capture" by resolutions of the ANC national elective conference where he scraped into office by a hair's breadth. In two years' time he'll face the ANC national general council when the faction fighting will again play out. Two years is the maximum timescale that he and the country are up against;

- Coalitions with the EFF will be entered for the ANC to hold majorities at any tiers of government and, if so, the likely effects;

- Business confidence is restored. This is essential for him to deliver on promises of increased investment and job creation. At a minimum, it involves the decontamination of state bodies (including the Hawks for obvious reasons) and crucially a turnaround in the electricity chaos. The latter is so severe that Eskom has forced a review of black economic-empowerment policies.

businesses and co-operatives.

• Investigate the introduction of prescribed assets on financial institutions' funds to mobilise funds within a regulatory framework for socially productive investments (including housing, infrastructure for social and economic development and township and village economy) and job creation while considering the risk profiles of the affected entities.

The good, the bad and the ugly

To the extent that the private sector can assist, it must. And it can, not by the continued harping on obstacles but by exploiting opportunities under its control. A case in point is the Financial Sector Code, potentially a game-changer with up to R100bn available for socio-economic objectives. Another is the loads of cash in corporate coffers – unlike the harassed fiscus – awaiting an alert for better use than bank deposits.

It will be a mistake for long-term investors, in SA and from abroad, amongst pension funds and across businesses, to be swayed by the immediate noise. Whilst they can't be deaf to it, they shouldn't succumb to it. There are at least three topical reasons.

First, there're the **commissions of inquiry into corruption** at key state institutions. Cleverly timed by Ramaphosa, for consolidation of his authority and signal of his intent, boils are being lanced. After the elections, his cause to deal with the puss will be the more blatant. Unless this was originally his intention, the exercises will have been pointless and he'll be seen to suffer impotence.

Already having replaced directors at government's dysfunctional agencies and enterprises, the commissions are clearing the way for deepened rooting out of people and practices exposed as useless at best or crooked at worst. Logically, oversight procedures will have to be jacked up so that they actually work. Similarly, criminal prosecutions and civil actions will need to follow.

The process has begun. An antidote to scepticism would be prompt arrests of certain high profile individuals. They know who they are, as does SA at large.

Don't envy Ramaphosa the enormity and complexity of what awaits him, for tentacles from the Zuma years have had a cancerous spread. Their residue remains not only within the power structures of the ANC, including echelons of leadership, but also amongst party appointees within the public sector.

Such is their vested interest in the perpetuation of

nest eggs that they'll be a constraint on the direction of the wind until they perceive it preferable to blow along with it. Opportunism trumps loyalties.

To move, be certain that Ramaphosa will have the ammunition. Be confident that he also has the balls. Be hopeful that no accident, conspired or otherwise, will befall him. Another succession battle is the stuff of nightmares.

Implementation of his programme cannot be instantaneous. Be patient for remedies to the rot whose astonishing depth is gradually being revealed. Brick by brick, myriad structures will have to be rebuilt at a pace allowed by scarcities in financial resources and skilled personnel.

Second, the proposal in the ANC election manifesto that the **introduction of prescribed assets** be investigated is a damp squib. The idea has been around for years – well before the crisis in state-owned enterprises, flaunted by the sorts of ideologues who thought that Hugo Chavez was doing a good job in Venezuela -- and it simply won't eventuate.

There's neither purpose nor need for prescribeds. It survives in the manifesto because, come elections, it can be propagandised as a stick to wield on "financial institutions' funds". Surely the party cannot still be oblivious to the fact that "financial institutions' funds" belong not to the institutions but to the millions of savers – black and white, rich and poor – in a multiplicity of retirement and insurance products.

The concept of prescribeds is laboured with contradictions. As *TT* has argued repeatedly, on each occasion that the ogre has arisen, it's a selective tax; and, at that, a tax by stealth which comes atop the taxes for which fund members are already liable.

Put brutally, it amounts to stealing from people who save; morally tantamount to hacking individuals' private bank accounts, but with the advantage that the skimming of one or two percentage points looks so minimal as not to be worth the bother of protest.

This is the more so when it's supposed to be for the social good, which it isn't. Government cannot on the one hand seek to encourage pension-fund savings, by the plethora of reforms including preservation, while simultaneously on the other hand increase the costs and reduce the benefits by prescribing that they subsidise instruments into which funds wouldn't otherwise invest for uncompetitive returns.

To reduce fund members' benefits by a couple of percentage points annually amounts to huge reductions over the membership's life. Because benefits can increase only by improved investment performance and lowered fund costs, they must be seen in tandem and not as alternatives.

They must also be seen for their likely impact on the pool of national capital essential to fund the fiscus. For individual savers, there's a hard history of withdrawals when employees become nervous over government interventions. For international portfolio managers, heavily exposed to SA government and government-backed bonds, prescribeds send a message of market interference that will discourage their participation.

In essence, prescribeds are a means of replacing voluntary with forced investments. They're voluntary when the risk-return rate is decided by markets and forced when it's dictated by governments. At the same time, in contravention of basic governance principles, they release the bond issuer from the discipline of investors' oversight.

There are predictable consequences: poorer investment performance by domestic pension funds, relative to returns from assets in which they can invest voluntarily, and hence poorer benefits for members; a review by ratings agencies of SA's status as a borrower, rekindling the threat of a downgrade to junk; exits by foreigners, because of their mandates, that can shoot up the overall pattern

of interest rates.

In the case of the latter, to the extent that prescribeds are required for investment at rates below commercial, any advantage will be more than offset. Additionally, the "social discount" is superfluous because the obstacle is not in a shortage of money but in the availability of projects. Little more can be required by the private-sector institutions, in terms of social initiatives, than the commitments enshrined most notably in the gazetted Financial Sector Code.

> *Third, there's land expropriation without compensation. The controversy has been elevated to the most sinister fears and motives by the political point-scoring.*

Fundamentally, introduction of prescribeds will amount to admission of defeat that the corroded state-owned enterprises – Eskom to the fore – cannot be pulled right. Introduce prescribeds and tell the world that SA's market economy is diminished.

Then kiss goodbye to Ramaphosa's ambitious targets for attraction of foreign direct investment. He, most of all, must be aware of the danger.

Third, there's land **expropriation without compensation.** The controversy has been elevated to the most sinister fears and motives by the political point-scoring (*TT* Aug-Oct '18 and Nov '18-Jan '19).

But contrast the impassioned polemic with the actual draft of the Expropriation Bill, to replace the Act that's applied for the past 44 years, published for comment in December. It will be tabled, astutely, only for debate in new parliament.

So far downplayed in the pre-election contest is the draft's modesty. Why a constitutional amendment might be required is obscure. Far from controverting the constitution, the bill offers clarity on the conditions whereby the existing constitutional provision can be invoked; in other words, setting out the grounds for court challenges where the mooted Expropriation Act is contravened.

For example, no expropriation may be done arbitrarily or for anything other than a public purpose or in the public interest. Expropriation may only take place where attempts to reach agreement with the owner on reasonable terms were unsuccessful. Compensation must reflect an equitable balance between the interests of the expropriated owner and the public, having regard to such factors as the current use of the property as well as its history of acquisition and its market value.

It won't make Julius Malema happy, but so what? The unhappier, the better. The size of the EFF's support base is magnified by the airtime given to his endless protests and press conferences. So imaginative are his digs for nationalisation, filled with inflammation but devoid of substance, that they're avoidable potholes on the road being travelled.

Have faith in the direction. It's incontrovertible that, after the backward lurch of the Zuma years, there's a forward leap to attain the sort of society envisaged by the constitution in whose Mandela-inspired compilation Ramaphosa's role was instrumental.

Allan Greenblo,
Editorial Director. ■

Ride smoothly into defaults and Reg 37

Vital checklist for trustees offered by Danie van Zyl, head of Sanlam Smoothed-Bonus Centre of Excellence.

In August 2017, the Minister of Finance signed an amendment to s36 of the Pension Funds Act. This amendment contained the addition of regulations governing conditions for defaults.

Regulation 37, which covers default investment portfolios, applies to pension and provident funds. It excludes retirement annuity funds, beneficiary funds, preservation funds and funds in voluntary liquidation.

The amendments, effective from 1 March 2019, require retirement funds to ensure that they have a suitable default investment portfolio in place for pre-retirement savings. These portfolios must be appropriate, not excessively complex or unreasonably expensive.

Importantly, the board of trustees must be able to demonstrate to the Registrar that its chosen default investment portfolio is appropriate.

Most retirement funds already have a default investment portfolio in place. For the Sanlam 2018 benchmark survey, 62% of funds indicated that they have a default portfolio where members have the option to choose an alternative portfolio should they wish.

The survey also found that a lifestage solution, followed by balanced funds and smoothed-bonus portfolios, are the most popular. Many funds also use a smoothed-bonus portfolio towards the end stage of their lifestage solutions.

As there are many retirement funds that use smoothed-bonus portfolios in their default investment strategy, let's unpack what these funds need to consider and do to demonstrate that they meet the requirements set out in Reg 37.

Demonstrating compliance

The board of trustees should consider adding some or all of the following points as agenda items for their trustee meetings and then include the main points in their minutes. They can then be provided at a later stage if requested by the FSCA.

Default investment portfolio(s) are appropriate for the members who will be automatically enrolled into them.

What is a default investment portfolio?
As defined in Regulation 37, a "default investment portfolio means an investment portfolio in which the retirement funding contributions of a member must be invested unless the fund has been instructed by the member in writing to invest them in another investment portfolio provided in terms of the investment policy statement of the fund or options available to members of the fund".

- Many retirement funds appreciate that smoothed-bonus portfolios provide smooth returns to members, preventing them from experiencing the roller-coaster that members may experience from market-linked portfolios. The guarantees are also valuable to members in a default portfolio as they protect members from potentially losing some of their capital in a portfolio they did not choose. This is particularly relevant to blue-collar members who are risk-averse as well as members close to retirement.

The composition of assets and performance of the default investment portfolio are adequately communicated to members.

- Can members access the latest fund factsheets and quarterly reports? Sanlam provides various forms of communication which contain the asset composition and

Van Zyl . . . comply with defaults

performance of funds e.g. monthly fund factsheets and quarterly reports for our smoothed-bonus portfolios.

Default investment portfolios are reasonably priced and competitive.

- How do the fees compare to other similar portfolios? Sanlam's smoothed-bonus portfolios have competitive investment management fees that reduce as the size of invested assets increases. The guarantee premiums charged are favourable compared to competitor products that provide similar levels of guarantees.

All fees and charges are disclosed.

- Sanlam discloses the fees and charges on all portfolios and provides the portfolio's Total Expense Ratio and Total Investment Costs to clients on request.

No loyalty bonuses or other complex fee structures.

- Do trustees and members understand the underlying fees? The fees charged on the Sanlam smoothed-bonus portfolios are easy to understand and calculate. The portfolios have no loyalty bonuses.

Members are not locked into the default investment portfolio.

- Are there any unreasonable barriers to exiting the portfolio? Members can switch out of the Sanlam smoothed-bonus portfolios at any time. However, should this occur when the portfolios are underfunded, members will receive the lower of book value and market value. Members who leave the portfolio for benefit-payment events (death, disability, retrenchment, retirement, resignation) will always receive book value.

Funds are further required to record their default investment portfolio in their Investment Policy Statements. They are also required to record that the above conditions were considered when the portfolio was chosen. Additionally, trustees are encouraged to include the following:

- Set out in writing how and when the board will review (on a regular basis) the default investment portfolio to ensure it is still compliant with Reg 37;
- The merits of both passive and active investment and reasons for the decision to use either (or a combination of both).

The FSCA released a further standard with conditions that smoothed-bonus portfolios need to meet in order for them to be used as a default investment portfolio. This standard is currently in draft form.

Sanlam, as a leading provider of smoothed-bonus solutions, is engaging with the regulator and is fully supportive of the regulations' aims. Sanlam will keep clients updated with any new developments.

www.sanlam.co.za/institutional

LITIGATION

Full of pep

Battle prepared for landmark case on duty of the regulator to protect retirement-fund investments. R70m claim to be defended.

Like a hand arisen from the grave, the PEP Limited provident fund (PEPF) is holding the Financial Services Board accountable for some R70m in losses it sustained from the Trilinear debacle that's been hanging around for ages.

With the FSB first having inspected Trilinear over a decade ago, matters didn't come to a head even with the "confidential" report of an inspection it concluded years later (*TT* Sept-Nov 2012). In at least one respect, they will now.

Since the PEPF has about zero chance of recovering a cent from Trilinear, it is suing the FSB (effectively the Financial Sector Conduct Authority which has taken over the old FSB's assets and liabilities) for the R70m. The litigation will be heard by the North Gauteng High Court in October.

Defendants are the FSB and its then executive officer Dube Tshidi. PEPF holds them liable for losses allegedly suffered by the fund for them having failed in the performance of their statutory duties; in a nutshell, for not having supervised and enforced compliance with the laws regulating financial institutions and the provision of financial services.

Implicitly, had the PEPF known what the FSB knew, it could have responded to avoid the loss.

PEPF was not alone in its loss. The FSB's damning report of 2011 showed that, as at April 2010, Trilinear had received R467m from funds participating in the Clothing Industry Northern Chamber Provident Fund.

The Trilinear group, which included an investment-management firm (TIM) and an empowerment fund (TEF), had as its "guiding force" one Sam Buthelezi. It had made disastrous investments. For example:

- **Canyon Springs.** Associated with then Economic Development minister Enoch Godongwana, it was lent R91m by TEF. By the time the FSB report was completed, it was in provisional liquidation;

- **Pinnacle Point,** into which TEF had invested R195m from retirement funds, became insolvent.

The essence of PEPF's claim is that the FSB and its executive officer had knowledge of Trilinear's affairs that they didn't disclose to the fund. Their omissions caused the fund's loss.

These were actionable failures in the regulators' duties not only to comply with their own statutory requirements but also in their duty of care and obligation reasonably to prevent harm, amongst them by not having:

- Taken timeous and appropriate action against the Trilinear group, or taken preventative measures at their disposal to divest Trilinear of assets it managed;

Centered on workers

- Notified the fund during August 2009 at the latest that TIM was or appeared to be acting unlawfully;
- Appointed a curator by August 2009 to take control and manage Trilinear's affairs.

For their parts, the FSB and its executive officer deny that they breached any duty of care or that they owed obligations to the PEPF that give rise to civil liability. They further deny that they acted with gross negligence or that "a causal link exists between any of the omissions and the alleged losses".

They add that at all material times the FSB Act provided for the FSB to perform its enforcement function by establishing an enforcement committee to deal with alleged contraventions of the law: "At no material times...(has any) law relating to the enforcement committee conferred any powers on the FSB."

Then they introduce Richard Kawie (purportedly national benefits coordinator of the SA Clothing & Textile Workers Union) as a third defendant. Kawie, they say, was a trustee or alternate trustee of PEPF. As such, he was obliged to act with due care and in good faith, to avoid interest conflicts "and disclose any facts or circumstances known to him which gave rise or may give rise" to interest conflicts.

But according to the FSB, Kawie had failed to disclose to his fellow PEPF trustees that amongst other things:

- He and Buthelezi were influential in decision-making of the TEF (into which TIM was entitled to invest PEPL funds);

Kawie and Buthelezi . . . centered in scandal

- TEF had never been audited;
- An entity to which TEF provided finance, primarily in the form of unsecured loans, was Canyon Springs;
- He exercised effective control over all Canyon Springs' decisions;
- A material reason for him recommending investment in TEF was his expectation of personal financial gain from Canyon Springs.

Had Kawie disclosed such matters to the PEPF, the FSB contends, it would not have granted a private-equity mandate to TIM. Or PEPF would have withdrawn the mandate, reclaimed amounts invested in TEF and made no further investments.

In the event that damages are awarded against the FSB, it urges that the court considers where losses were caused by the PEPF's negligence. Consequently, the amount of damages should be reduced "to the extent that the (PEPF's) losses were caused by (its) own fault".

Having taken eons to reach the civil court, the aftermath must eventually play out in a criminal court. Sleep uneasily, Kawie and Buthelezi. ■

Search for yield in private markets

Isabella Mnisi, the Ashburton Investments chief investment officer for private markets, discusses how SA lags when it shouldn't. Take a close look at where potential advantage lies for the investor and for the country.

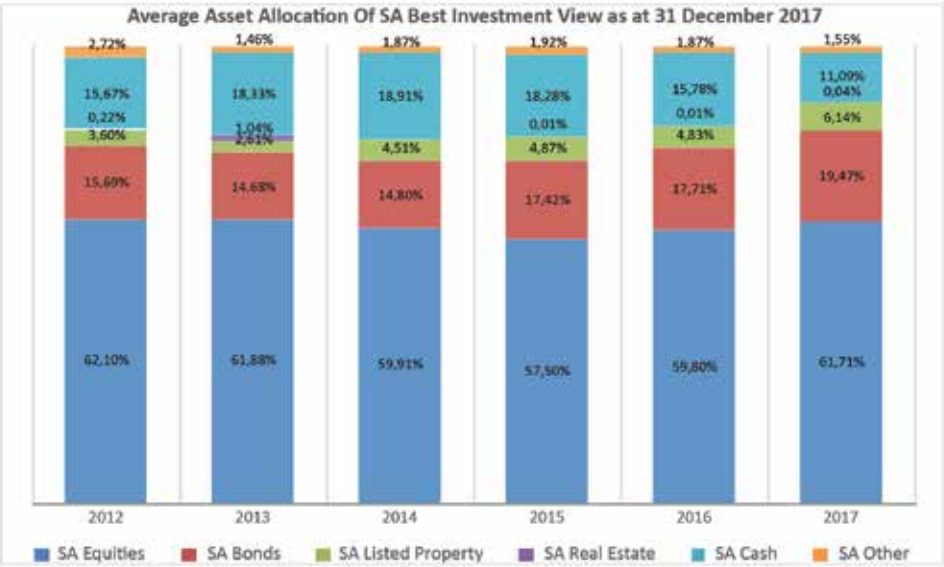
Increasing concerns around the global economy -- the United States/China trade conflict, uncertainty around Brexit and emerging-market risks -- are pushing investors to look for other sources of return. Global growth also seems to have peaked, creating downside risk.

On the domestic front, constrained economic growth projections (albeit in the right direction) – as well as disappointing stock market performance, lack of business confidence and political uncertainty -- are leading investors to look for other sources of return. The market is also not expected to improve substantially in the short term.

Therefore, international factors coupled with local factors have led investors to start looking beyond traditional assets for other sources of returns. Alternative markets still provide attractive valuations and offer the potential for alpha while also offering diversification benefits to traditional assets.

However, SA institutional investors allocate only about 2% of their assets to alternatives. This is extremely low when compared to the developed world (US and Europe) where allocations are generally over 20%.

Below we look at the different alternative-investment options available. Please note that the industry data on alternative assets is not as readily available because this market is not as developed and standardised as for traditional assets.



Source: Alexander Forbes Retirement Fund Survey 2017

Unlisted credit

In SA, more than 80% of companies fund themselves through the banking system (private markets). This means that fewer than 20% of companies use the public-debt capital markets for their funding requirements.

More developed countries have many more companies accessing the debt-capital markets for their debt funding; for example, the US represents the opposite of the SA scenario. The SA phenomenon has resulted in banks having very well-diversified balance sheet portfolios, whereas capital-market investors only have access to limited investment opportunities through the debt-capital markets.

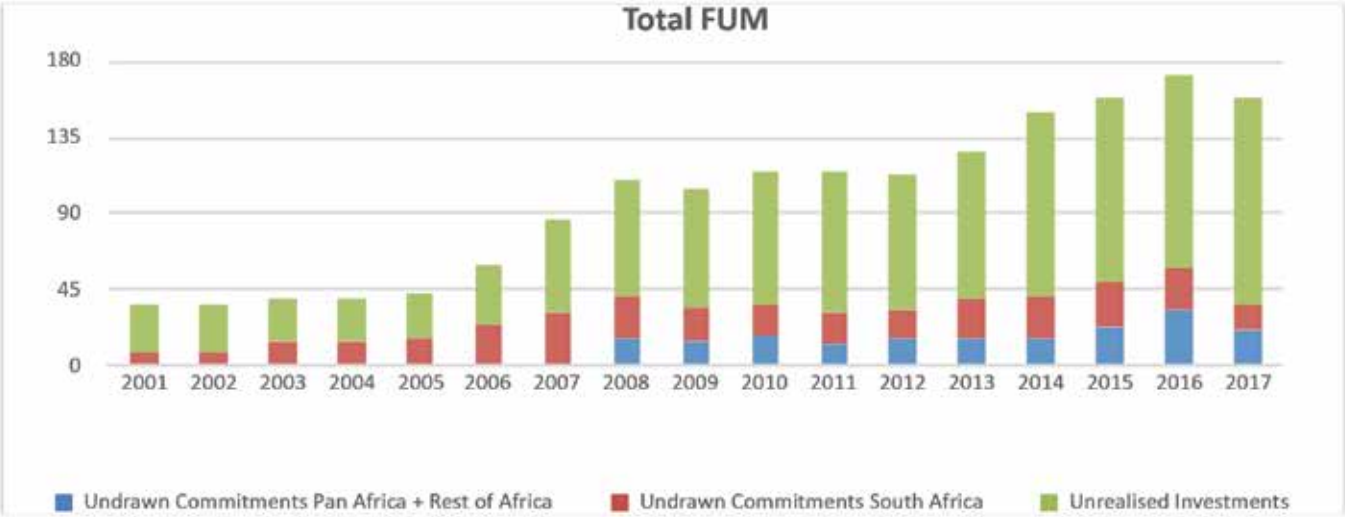
Unlisted credit offerings give investors the opportunity to access diversified pools of assets that are currently not readily available to investors in funds regulated as collective investment schemes.

Yet, in the past few years, we have seen increased interest and demand for unlisted credit from SA institutional investors. Regulation 28 allows for 15% of a pension fund's assets to be invested in unlisted debt instruments. Most pension funds are below this limit.

Private equity

Southern Africa's private equity industry had R158,6bn funds under management as at December 2017. Of funds raised during 2017, 49,9% were from SA sources according to the Southern Africa Venture Capital & Private Equity Association (SAVCA) 2018 Private Equity Industry Survey.

SA institutional investors have been increasing their participation in the private equity market for many years, as can be seen from the above chart. Investors may include mezzanine debt under the private-



Source: SAVCA 2018 Private Equity Industry Survey

equity category depending on the way in which the instrument is structured.

Real assets

Investor participation in real assets will either be through a debt or equity structure. Institutional investor participation in real assets is key, especially for a country like SA with huge infrastructure funding needs.

Real assets offer a great source of inflation hedge for long-term liabilities, particularly for pension funds. These real assets' long duration, predictable cash flow and inherent inflation hedge characteristics are also highly attractive.

Investors have previously participated in toll road and renewable energy infrastructure funding. Some have preferred to participate in the post-construction phase of the transaction due to it being more de-risked. This is mainly because of a lack of understanding of the construction risk phase.

Policy and pricing uncertainty, due to political meddling, have seen investors scaling back from these assets in the SA market. But energy minister Jeff Radebe has moved swiftly to provide some certainty on the funding of renewable energy projects.

We hope that this will lead to increased confidence and funding from institutional investors. Our country's fiscal constraints will require institutional investors to plug the infrastructure-funding gap.

Be meaningful

We believe that any portfolio asset allocation needs to have a meaningful allocation to alternative assets. Alternative investments, when used as part of a multi-asset portfolio to complement traditional investments, can lead to improved long-term risk-adjusted returns.

First-time investors in the alternative markets should focus on the overall benefits that alternative investments could bring to a portfolio.

Mnisi . . . strengthen alternatives

PUBLIC INVESTMENT CORPORATION

When gamekeeper turns poacher

The look into internal workings of the PIC offers a great opportunity for rethink and perhaps restructure. Flaws and failures require resolution for the long term.

The latest annual report of the Public Investment Corporation creates the impression of SA's largest asset manager doing a mighty fine job. But revelations before the commission of inquiry into PIC irregularities reflect precisely the opposite. They cannot both be right.

Whatever the findings ultimately produced by the commission, chaired by retired judge Lex Mpati, things can never be the same again; neither for the PIC itself nor for its major client, the Government Employees Pension Fund. The PIC directly manages almost 90% of the GEPF's R2 trillion investment portfolio.

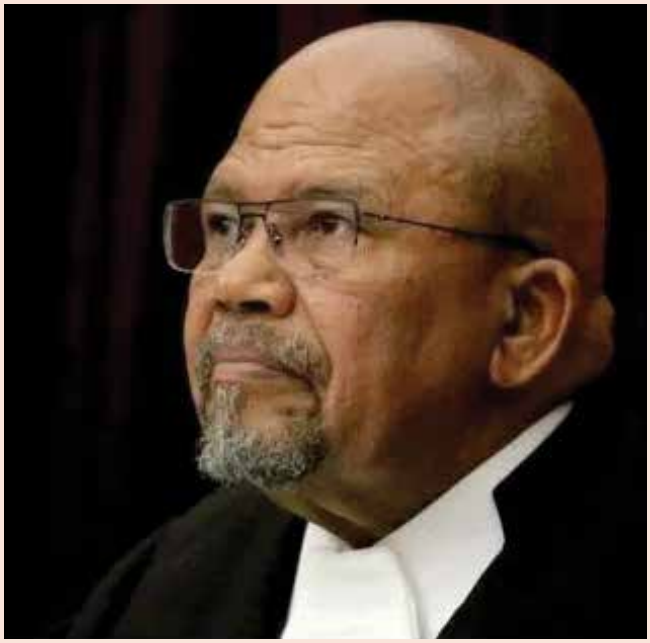
Together, the PIC and GEPF have been presented as the manager-client model for SA retirement funds to emulate. Clearly, the model is flawed. Amidst the alleged shenanigans at the PIC, where was its board to whom the chief executive reported? And where was the GEPF board to ensure that the PIC complied with its mandated responsibilities?

The PIC directors resigned en masse, ostensibly because the evidence before Mpati had made their jobs impossible. Should allegations be proven – there's a long way to go – dismissals in disgrace might seem more appropriate. For their part, the GEPF trustees cannot indefinitely leave their stewardship role unexplained.

It is they who provided the PIC with its investment mandate. It is they who, the GEPF annual report proclaims, govern the fund and are accountable for its investment and administrative performance. They also protect its values, from integrity and transparency to the flag-carrier for stakeholder activism and responsible investment.

Yet, from under the noses of committees and sub-committees, the PIC faces interrogation from the commission for a fundamental tenet of the mandate whereby the GEPF trustees "require global best practice in terms of risk management, monitoring and reporting".

By way of illustration, starting to surface are huge amounts in advisory and other fees paid by the PIC to various black-empowerment entities. Revealed by Sygnia chief executive Magda Wierzycka, from a supposedly 'private and confidential' PIC document,



Mpati . . . evidence accumulates

her comments in a *Business Day* column impact on the reputations of numerous entities "completely unknown" to her although at least one is a service provider in competition with Sygnia.

That the entities are unknown to Wierzycka doesn't necessarily make suspect either them or their transactions with the PIC. The document lists fees paid by the PIC over the period from 2014 to 2018. During this period, the PIC chair was deputy finance minister Mcebesi Jonas. He was subsequently appointed a director of JSE-listed Sygnia Asset Management on whose main board he continues to serve.

Perhaps easier to address is the SA Home Loans instance, small in money but big in principle, of a payment nearly deflected by the PIC from the GEPF to an individual. The "mistake" of then PIC chief executive Dan Matjila was successfully challenged by SAHL (see next article 'Picked out').

Were there occasions when similar "mistakes" had not been detected? It will be for the commission to find out, as it has with such contentious schemes related to investments in Ayo Technologies and Independent Media, bringing with them the important question of how the PIC has selected black-empowerment investees.

Related to it is the criteria, shown only in broad transformational terms, used by the PIC for investment into 123 unlisted companies and support for 785 small-to-medium enterprises. Left to guesswork, except for the Mpati hearings, is where personal or political interventions were possibly at play (*TT* Feb-April '18).

Still undisclosed by the PIC is the identities of the 13 external asset managers it appoints, let alone the sizes of their respective allocations. The PIC merely records the managers by number and shows their BEE levels in an agglomerated table. The GEPF, on the other hand, identifies by name the 18 external managers which it says the PIC has appointed for parts of its portfolio. But it too doesn't set out the sizes of respective allocations.

Why the differences in disclosures, or lack of them, when competition for allocations is fierce and billions of rand in pension monies are at stake? Are appointments made on the basis of objective criteria consistently applied? Once there was trust. Today there isn't.

As the PIC unravels, policy issues arise for consideration. They'd include:

- Whether the PIC should continue in its present form or be rationalised into the GEPF with a view to elimination of duplicated structures. There are talented personnel in both the PIC and GEPF (including highly-regarded board members) whose functions overlap. In its most recent financial year, the GEPF paid R1,1bn to the PIC as management fees while the PIC had R805m in total expenses of which R550m were employee costs;

- Whether, alternatively, the PIC's investment

function cannot be performed entirely by GEPF-appointed external managers under client mandates; or whether the PIC shouldn't be open to competition for GEPF appointments. Such moves would doubtless cause salivation amongst private-sector managers, particularly those with strong BEE credentials, and the potential explosion in the sizes of their assets under management should comfortably invite the absorption of specialist skills from the august bodies;

- If not, whether the PIC's board composition should be solely at government's discretion. By contrast, half of the GEPF's board comprises stakeholder representatives;

- Whether the time has arrived for the GEPF to establish a defined-contribution fund, so that new members can enter it and existing members can choose whether to convert from the present defined-benefit arrangement. A DC fund (prevalent in the private sector) could be to the greater advantage not only of members but also of government (hence taxpayers) which underwrites the DB liabilities.

None of these suggestions can be simplistically argued but they could be seriously contemplated, given the thrust for review generated by changed circumstances. The ostensible situation that's arisen, of the PIC 's unacceptable behaviour and the GEPF's flawed oversight, cannot be resolved by tinkering.

Begin with an examination of the GEPF's investment mandate to the PIC – curiously, not at present in the public domain – for launching a debate on how its objectives can best be attained. Documentation is one thing. Implementation is another.

This might not be within the immediate remit of the Mpati commission. However, it might well be a necessary consequence. ■

Principal officers receive PPEO certification

The Batseta Council of Retirement Funds for SA is proud to announce the latest recipients of the National Certificate for Professional Principal Executive Officer (PPEO). This auspicious qualification is designed especially for principal officers practising within SA's retirement-fund industry.

Nineteen principal officers of retirement funds successfully completed their exams:

Chanka, Sooshiela (ACA Employee Benefits)
Fabre, Penelope (University of CapeTown Retirement Fund)
Fernhout, Genive Ann (Lifesense Group Pension Fund)
Govenden, Rama (PPS Pension Fund)
**Jackson, Alison Jane (Deloitte & Touche Pension & Provident Fund)*
**Mokorosi, Jolly (Independent PO)*
Mphanje, Mavis (University of Johannesburg Pension Fund)
**Ndawana, Leslie (National Fund for Municipal Workers)*
Ntombela, Floyd David (NBC Unclaimed Benefits Pension & Provident Fund)
Ramiah, Devara Krishna (Southern Africa Quantum Beneficiary Fund)
Rollason, John David (Independent PO)
**Sanford, Linda Rose (Mondi Mpact Group Fund)*
Shuping, Bryan Kgosana (Moriting Retirement Fund)
Spence, Roger Mark (Liberty Corporate Selection Umbrella Fund)
Thulo, Aaron Motlalentoa (Hospitality & General Provident Fund)
Van Coller, Hester Natasha (Independent PO)
**Wessels, Wendy Shannon (Alexander Forbes Core Plan & Provident Section)*
**Whittaker, Philip Andrew (Alexander Forbes Retirement Fund)*
**Wingrove-Gibson, Lindy (City of Johannesburg Pension Fund)*

**Denotes with distinction*

The PPEO qualification is an occupational qualification aimed at refining the skills of principal officers. This NQF 7 qualification is the underpinning requirement for the Chartered Principal Executive Officer designation awarded by Batseta. The designation sets the standard of professionalism in the retirement-fund industry for principal officers.

It aims at ensuring that principal officers are able to guide and monitor a fund board's compliance with external legislation as well as implement and monitor fund rules and board-approved policies. In addition, principal officers are equipped to manage the operations of the retirement fund, guide and implement the board's decisions.

More than 50 principal officers from a variety of retirement funds have so far completed the qualification.

For more information, call 011 805 6340 or visit www.batseta.org.za.

Offer members what they can afford

Vital element in default strategies, urges Just SA chief executive Deane Moore.

From 1 March 2019, the board of trustees of every pension and retirement-annuity fund must be able to demonstrate to the Registrar of Pension Funds that it has in place an annuity strategy that is appropriate and suitable for its members, taking account of:

- their level of income;
- inflation and investment risks; and
- income protection for beneficiaries on death of the main member.

A member reaching retirement has two categories of needs:

- basic lifetime needs: a monthly income for life for the member and his/her spouse, which grows with inflation, to pay for essential expenses such as food, medical, accommodation, water, electricity, telephone, transport and insurance;
- lifetime aspirations: flexible income for other expenses, tax planning, or to leave as a legacy for beneficiaries.

In South Africa, most people reaching retirement have insufficient savings to consider aspirations. Their priority is to focus on maximising their incomes for life to cover their basic lifetime needs.

There are two retirement options for providing members with a sustainable income for life, where this is expected to grow with inflation: a living annuity or a guaranteed life annuity.

In a living annuity, members need to decide how to invest their retirement savings and how much income to draw from these savings each year. Income is not guaranteed, but the Financial Sector Conduct Authority has published a table to show what proportion of his/her assets a member can draw at each age to have a 90% probability of sustaining their income for life and increasing this with inflation each year. This table was developed by industry professionals and is currently under consultation.

A with-profit annuity is a type of guaranteed life annuity that provides members with a guaranteed income for life that is targeted to grow with inflation each year.

This table compares the income from a guaranteed life annuity and a living annuity on a consistent set of assumptions.

	Guaranteed Lifetime Income[1]		Living annuity[2]	
Age	Males	Females	Males	Females
55	6,0%	4,5%	4,5%	4,0%
60	6,5%	5,5%	5,0%	4,5%
65	8,0%	6,5%	5,5%	5,0%
70	9,5%	8,0%	5,5%	5,0%
75	12,0%	10,0%	6,0%	5,5%
80	15,5%	12,5%	7,0%	6,0%
85	20,0%	16,5%	8,0%	7,0%

1 *The guaranteed life annuity rates are for the Just Lifetime Income with-profit annuity.*

2 *The maximum sustainable living annuity drawdown rates published for consultation by the Financial Sector Conduct Authority on 7/11/2018 in their Draft Conduct Standard for Living Annuities in a Default Annuity Strategy. If individuals withdraw income at these rates, they have a 90% chance of being able to sustain their income for at least as long as their average life expectancy i.e. their income will keep up with inflation until their expected death.*

In a living annuity, when the main member passes away, his/her beneficiaries will receive any capital that is left in the living annuity.

In a guaranteed life annuity, members can opt for income to continue for the remainder of their spouse's lifetime and until beneficiaries are no longer dependent. This is a death benefit that is specifically focused on the ongoing needs of beneficiaries to meet essential expenses.

In surveys carried out by Just in 2015 and 2018, over 85% of retired people said they would prefer a secure, guaranteed income for life against investing a pool of assets and deciding how much to draw each year.

www.justsa.co.za

JUST.

RETHINK RETIREMENT

RESPONSIBLE INVESTMENT

Truckers' trailblazer

Fund making inroads for its members.
An 'alternative' asset-allocation strategy is put to good use.

When rushing along the Johannesburg- Durban motorway, pause briefly outside Harrismith to take a look at the Highway Junction Truck Stop. It's a fine example of "responsible investment" by a retirement fund – in this case the Transport Sector Retirement Fund – directly to serve the occupational needs of its workforce members.

The project is large and impressive. It's also unique.

"Four years ago we determined that good-quality truck stops are sorely lacking along SA's major routes," says TSRF principal officer Joe Letswalo. "Recognising that the vast majority of our members are truck drivers, and that a major cause of accidents is driver fatigue, we launched a strategy to ensure that our members and the broader transport community would have facilities to park and sleep safely.

"At the same time we wanted them to have access for refuelling and auxiliary services such as restaurants, primary healthcare clinics, recreational and warehouse space."

A multi-brand facility, it is probably one of the busiest truck stops in Africa. Three different petroleum brands – Engen, BP and Total – have their own forecourts. Trucks can park overnight on a reinforced concrete surface with no chance of being stuck in mud. It's purported to be the preferred stopover for about 70% of truck drivers passing through the N3 corridor.

A joint venture with the Deysel family's Highway Group (whose chief executive is Ben Deysel), three years ago the TSRF bought its 50% share of the Harrismith project for R55m. Since then, says Letswalo, a 26% internal rate of return has consistently been achieved.

With introduction of the multi-brand expansion strategy, he expects that it will be revised to 30%.

Now the TSRF Truck Stop Fund is raising around R3bn for development of similar hubs on major routes throughout SA. Sites have already been earmarked near Cape Town, East London, Colesberg and Musina for project completion during 2020-21.

The fund wants a national brand strongly recognisable for safety and cleanliness standards that qualitatively support the transport and logistics industry. The TSRF, says Letswalo, is continually looking for ways to improve members' livelihoods while they are still actively employed.

A non-aligned standalone umbrella fund, TSRF currently has around 3 000 employers which bring its total membership count to about 70 000 individuals. Assets under management are approximately R7,1bn.

The Truck Stop Fund forms part of the TSRF's "alternatives" asset allocation in terms of the Pension Fund Act's Regulation 28. The TSRF has allocated R250m, representing 2,5% of its assets under management, to the Truck Stop project.

• *Formerly the Road Freight & Logistics Industry Provident Fund, in 2017 its name changed to the Transport Sector Retirement Fund when it was opened to the wider transport sector.* ■

HOME LOANS

Picked out

Bank kills attempt by the PIC to avert the GEPF. Vital issues for the Mpati commission to investigate.

To date an attempt by the Public Investment Corporation to play fast and loose with monies of the Government Employees Pension Fund, its major client, is under the radar.

The particular matter, which concerns unlisted company SA Home Loans, begs inquiry by the PIC commission led by retired judge Lex Mpati. The experience at SAHL invites examination into whether there were similarly-curious elements in transactions that might have been avoided had the PIC been required to seek approval from the GEPF trustees.

It further raises broader questions of how the PIC selects black economic empowerment partners to co-invest with the GEPF; and, in this instance, the real motive for a PIC instruction to an investee company that it pay R45m to a third party who'd added zero value to a BEE transaction.

That the R45m claim for payment was eventually negated redounds to the credit of Standard Bank, not to the PIC. The intended beneficiary of the R45m was one Kholofelo Maponya.

For background, the Durban-based SAHL was founded 20 years ago. A specialist provider of mortgages, it's considered a highly competent competitor in the SA home-loans market with national reach and a strong management team.

Until 2015, SAHL was jointly owned by banks JP Morgan Chase and Standard. The former then agreed to sell its 50% stake to the PIC, representing the GEPF, for R300m.

Prior to closure of the sale, the PIC introduced a consortium assembled and controlled by Maponya for half of the PIC's stake to be acquired; in other words, for 25% of SAHL. The PIC lent the Maponya consortium the money for its share of the purchase price.

At the insistence of Standard, which continues to own 50% of SAHL, the GEPF was bound to guarantee the discharge all obligations assumed by the indebted Maponya consortium as a SAHL shareholder. Maponya, it's understood, had told the bank that he and his consortium were selected as the BEE partner because of his personal relationship with then PIC chief executive Dan Matjila.

On the transaction being concluded, the PIC nominated two directors to the SAHL board. Maponya nominated himself to represent his consortium.

The PIC's stated investment purpose was use of SAHL as a vehicle for the channelling of home loans to GEPF members. Consequently, in 2016, the PIC agreed that the GEPF would make available to SAHL up to R9bn for onward lending that provided GEPF members with mortgages.

But before the ink had dried on this contract, Maponya demanded a R45m payment from SAHL ostensibly on the contention that it was his relationship with the PIC that had brought about the loan agreement.

SAHL rejected Maponya's demand on grounds that he had no mandate to represent SAHL. Moreover, he had not been promised any such reward. Neither had he played any role in the initiation, negotiation and conclusion of the loan agreement.

To the surprise of SAHL, Maponya then delivered a letter from the PIC that had been signed by Matjila. The

Matjila . . . curious transaction

letter informed SAHL that the GEPF had ceded to a private Maponya-owned company a claim that the GEPF had to receive R45m from SAHL under the loan agreement. Therefore, said the PIC letter, SAHL should pay the R45m to Maponya's company and not to the GEPF.

The letter was referred by SAHL to Standard in its capacity as a 50% SAHL shareholder. The response of senior bank executives was to inform Matjila that, in all the circumstances, Standard regarded the transfer of a pension fund's assets by cession to a third party – who had provided no value – as possibly irregular if not suspicious.

Accordingly, the bank would oppose any payment in terms of the cession unless and until the PIC had demonstrated that the cession had been approved by the GEPF board.

Shortly thereafter, SAHL received a response from the PIC. In this letter (also signed by Matjila), it was stated that the GEPF owed nothing to Maponya's company. It further stated that the deed of cession should not have been signed (by Matjila). The deed of cession had thus been unilaterally cancelled and in future SAHL should ignore it.

In turn, Maponya informed SAHL that he challenged the lawfulness of the unilateral cancellation. However, he would not push SAHL for payment.

It's believed that the PIC-nominated directors on the SAHL board were fully engaged in this sequence of events but have offered no explanations beyond the contents of the letters. ■

- *This article, by TT editor Allan Greenblo, was first published by FM/BusinessLive on Jan 28.*

Offshore equities not the panacea as

So argue Adam Bulkin, Mark Phillips and Peter Urbani of Sanlam Investments.



Those retirement-fund investors in the accumulation stage need to invest for both real (after-inflation) growth and also to preserve and grow their wealth in hard-currency terms. Over 2018, these objectives were extremely difficult to achieve.

The rand lost close on 14% as measured against the US dollar. As a result, along with the dismal performance of most domestic asset classes for the year, many SA investors suffered significant wealth destruction particularly when measured in dollar terms. Once again, offshore investing is front of mind for South Africans wishing to preserve and grow their real spending power.

Conventional wisdom is to utilise shares in SA-listed companies whose operations and revenues are based offshore (so called "rand-hedge" stocks), or shares directly in offshore jurisdictions, to benefit from and protect against rand weakness.

It makes intuitive sense to follow this strategy, since this should achieve diversification and negative or low correlation with a weakening rand and thus with a major driver of the returns of one's dominant growth asset (domestic, non rand-hedge equities). But are investors following the correct strategy? Does research in fact support it?

The Legae Peresec firm conducted research based on the behaviour and correlations of rand-hedge stocks to the relative strengthening or weakening of the rand during the period 2013 to 2018. It wanted to investigate the hedging power of these rand hedges and the diversification benefits of offshore asset classes.

It found that the relative hedging strength of the rand-hedge stocks seems to vary greatly depending on the magnitude of the currency move and the particular stock, and that the relationship between currency and return is not a direct or linear.

Therefore, the evidence certainly does not support an investment strategy based on a simple, blanket assumption that rand weakness will automatically or necessarily equate to high relative or absolute returns for rand-hedge stocks.

What of other asset classes, such as offshore listed shares? Legae points out that diversification seems to disappear exactly when one needs it most – in extreme events, such as stock market crashes, particularly those brought about by global events. Specifically, it found that local property and global equities provided poor forms of diversification for the local equities market.

However, there were some good diversifiers. US dollar cash and US government bonds, as well as local fixed-income assets, provided protection in global risk-off events when domestic equities sold off.

This research was echoed by Avior Capital Markets. It had analysed the optimal strategic asset allocation needed to achieve the highest probability of outperforming various real return objectives.

Avior concluded that, to achieve the optimal asset allocation for a CPI+5% return objective within Regulation 28 confines, a

SA investors believe

high allocation to domestic bonds (slightly above 40%), about 25% to domestic equity and property and small allocations to gold and African equities (about 5% or less) was optimal.

Interestingly, the balance, allocated to offshore assets was exclusively to fixed-income assets i.e. US government bonds and US high-yield corporate bonds, with no allocation to global equities. Avior's research therefore supports that of Legae with respect to the optimal offshore asset allocation being to fixed income assets.

We conducted our own conditional correlation analysis from January 2013 to December 2018 to examine Legae's and Avior's conclusions. We broke down this period into three regimes:

- January 2013 to January 2016, when the rand depreciated by 47% against the dollar and the JSE gained 37%;
- February 2016 to December 2017 when the rand gained 28,2% and the JSE gained 27,9% cumulatively;
- January 2018 to December 2018, when the rand fell 13,8% and the JSE returned -8.5%.

We found that the behaviour of asset classes is dynamic and affected by myriad factors. Correlations are different in different regimes. Using historical data simplistically, without forward-looking views and insight into the drivers of historical returns, is therefore not an optimal manner in which to make asset-allocation decisions.

That said, from the perspective of correlations, our conditional correlation analysis is broadly in line with the findings of Avior and Legae. US fixed-income assets were a good negative correlator to domestic equities and therefore protected wealth in hard currency.

Our analysis is therefore generally in agreement with Avior and Legae in that the expectation that US fixed-income assets will act as a good diversifier to domestic equities and protectors of wealth in the case of rand weakness.

Moreover, our analysis confirmed that the behaviour of rand-hedge stocks does not display a stable or directionally clear relationship to periods of rand weakness. It would seem that other drivers of returns for these stocks are more significant.

But our research also highlights that, from a longer-term perspective and taking into account the imperative of driving total returns, there is empirical evidence for utilising global equities (US and Japanese in particular).

We also observe that the drivers of returns of any particular asset are extremely complex and diverse. Thoughtful asset allocation needs to apply forward-looking views and judgment to investment decisions, as well as insights into the causes of observed past behaviour. Correlations are not static. There is evidence to suggest that the negative correlation between equities and bonds may be changing.

In short, a simple extrapolation into the future of asset classes' past behaviour -- without considering fundamental drivers of such behaviour and the ways in which they may change -- clearly would be imprudent.

Yet the empirical, historical research (discussed above) supports the contention that a SA investor should be circumspect in the use of both SA-listed rand-hedge stocks and offshore equities to manage the risks of rand weakness and its effect on the returns of domestic equities. Research indicates that assets such as local and global fixed-income assets may be far more effective for risk control.

However, in balancing the requirements of risk and return, global equities have definite merit and should be considered as an element of a well-diversified portfolio.

CURRENTS

Sparks for King from Kingman

Revamp of codes initiated in UK. Radical changes foreseen to prevent 'boilerplate' compliance by fund managers on such matters as ESG in company engagements.

SA's pride and joy on corporate governance is the King code. From its original iteration 17 years ago, it's pretty much marched in lockstep for philosophy and intent with the UK stewardship code. If this happy parallel is to continue, King looks due for a jolt.

As with King, the UK code defines how fund managers hold to account the companies in which they invest. As in SA, fund managers frequently act on behalf of pension funds (and other indirect shareholders) under mandates. Unlike SA, at least for the present, the UK code may be scrapped if planned reforms aren't sufficiently radical.

The re-think has been provoked by a government-sanctioned report of Sir John Kingman, chairman of the Legal & General insurance group. It produced scathing criticisms of the Financial Reporting Council, the regulator of auditors and actuaries.

Kingman wrote: "The government should also consider whether further powers are needed to assess and promote compliance with the (stewardship) code. If the code remains simply a driver of boilerplate reporting, serious consideration should be given to its abolition."

Specifically on auditors, Kingman's view is that they no longer be proposed by the company's board and approved by shareholders. Instead, they should be appointed by an independent body (a new regulator) representing the public interest.

The FRC has begun an overhaul of the stewardship code. The head of responsible investment at the UK's largest private-sector retirement fund, the Universities Superannuation Scheme, believes that it should include a stronger emphasis on engagement over environmental and social issues, corporate ethics and reputational matters.

Andrew Ninian, director of stewardship and corporate governance at the Investment Association which represents managers overseeing £7,7tr, is also quoted in the *FT*: "It's an opportune time for the code to be fully refreshed and refocused on best practice and the activity that goes on between companies and investors day to day."

The FRC consultation is being held simultaneously with discussions on the European Union's shareholder rights directive II. Paul Lee, an advisor to the International Corporate Governance Network, says: "It's an opportunity for the stewardship code to set a higher hurdle that not everyone will be able to leap over."

R40m appeal

SA actuaries will be waiting with bated breath – perhaps anxiety, more likely – for the outcome of the appeal by actuary Viv Cohen against the R40m in damages awarded against him by the Pension Funds Adjudicator for the Amplats Group Provident Fund (*TT* Nov '18-Jan '19).

The Financial Services Tribunal has set down the appeal for hearing on April 16. No actuaries can be more anxious than Cohen himself.

Lila . . . reasons on ice

EPPF's big loss

Sitting down for coffee in Lonehill on a sunny Friday morning, the relaxed demeanour of Nopasika Lila contrasts starkly with the enthusiastic determination evident only a few months earlier on her widely-lauded promotion to principal officer and chief executive of the Eskom Pension & Provident Fund (*TT* Nov '18-Jan '19). Something serious must have happened, seemingly as a bolt from the blue, to have provoked her sudden resignation after less than a year in the hot seat.

One doesn't give up such a powerful position, at SA's second-largest retirement fund which she'd served for nine years, without good reasons. Lila won't pinpoint them. But perhaps there'll be clues in the EPPF annual report due for publication within the next few months.

In the previous annual report, the message from then chief executive was from Sbu Luthuli who'd signed it on March 29 2018. The next day, Lila took over. Watch for what she signs, if anything, at end-March this year. It might be difficult because, although it's formally her departure date, she'll be ice-racing in Finland.

Watch nonetheless for such items in the annual report under substantial or significant matters. There might be clues.

Lila feels that she's left the EPPF in good shape, right down to scenario planning for different levels of reductions in the size of the Eskom workforce. Yet she remains mystified by why the fund has almost R0,5bn in unpaid benefits – "there should be proper records" – and is concerned for sustainability by the propensity of younger members to take all their benefits in cash on withdrawal, leaving annuities for the older to be funded.

Whatever the problems at Eskom, even if the employer can no longer afford to pay contributions, she leaves on the note that all member benefits in the fund are fully protected.

Whatever prompted Lila's resignation, it can be safely assumed that the reasons were hers and hers alone. The best that can happen for the fund is that a successor of similar competence is found, and for the broader industry it's that her presence will continue.

Consensus? What consensus?

In his SONA address, President Cyril Ramaphosa made a statement so dramatic in its implications that it's all the more remarkable for having passed virtually unnoticed.

"We have made significant progress in devising a comprehensive social-security strategy though Nedlac," he said. "The reforms focus on achieving comprehensive social security and retirement reform that is affordable, sustainable and appropriate for all South Africans."

Then he added: "With the assistance of the National Planning Commission, we reached consensus on reforms that include the National Social Security Fund, institutional arrangements, regulatory reforms, improved unemployment benefits, improved social-assistance coverage....We will now incorporate this consensus into a policy framework to guide implementation."

It's fantastic that such consensus has been achieved. Unannounced is how it will be paid for by whom, and whether private-sector representatives at Nedlac are aware that they're committed to this consensus.

In the absence of detail, Ramaphosa could have been jumping the gun. Elections have this sort of effect on politicians.

Or maybe it's because nobody had told him about

the 2019 Budget Review which appears to contradict him: "Government, business, labour and civil society have engaged extensively on the first draft of the comprehensive social-security paper through Nedlac. The process should come to a close in 2019, after which the paper will be revised and released for broader public consultation."

There could be a way to go before consensus is achieved, let alone a guide to implementation.

Subsidised savers

Also revealed in the Budget Review is the increasing extent to which the fiscus is sacrificing revenue in the form of tax deductions for contributions to pension and provident funds and to retirement annuities (see table). What this means, Fasken partner Rosemary Hunter told the annual conference of the Pension Lawyers Association:

- While taxpayers may have funded social grants to approximately 17,6m people in the year to end-March 2018 at a cost of some R170bn (on average R9 659 per person),
- In 2016-17 at least 3,17m taxpayers also received the benefit of almost R73bn in tax revenue foregone by the deductibility of retirement-fund contributions (on average R21 470 per person).

"We should therefore not think of our retirement savings as our alone," Hunter urged. "We should recognise that the state is our co-investor."

So stop complaining. In a society of marked inequalities, it's worth comparing the costs to fiscus of social grants for people who couldn't otherwise afford to eat against tax deductions for those who can.

Mob justice

What social media say can be less important than what binding agreements say. This was discovered by Momentum at reputational cost in the furore over non-payment, then payment, of a death benefit to the widow of murdered policyholder Nathan Gamas.

Eventually the benefit was paid by Momentum, from shareholder funds rather than policy premiums, in response to the public outcry and not in terms of the contract. The emotion focused on the circumstances of Ganas' death, shot while protecting his wife.

Overshadowed has been the crisp issue of fraud. It would have arisen had Ganas been aware, on entering the contract, of serious health problems that he decided not to disclose. But in course of the outrage, details of his situation at time of signature have been withheld from the public discourse.

They could have put a different spin onto the debate that might otherwise have centred less on Ganas' heroism and the insurer's heartlessness than on whether a dishonest intent, if that's what it was, should be rewarded.

The industry had better face this new reality that contractual agreements are no match for social media.

About turn

Whereas previously the FSCA seemed not terribly happy about the cancelled registrations of

Table B.3 Tax expenditure estimates

R million	2013/14	2014/15	2015/16	2016/17
Personal income tax				
Retirement fund contributions[1]	49 418	53 707	58 980	72 991
Pension contributions – employees	*11 999*	*13 019*	*14 363*	*15 579*
Pension contributions – employers	*22 010*	*23 882*	*26 348*	*28 578*
Provident contributions – employees	*–*	*–*	*–*	*3 928*
Provident contributions – employers	*9 297*	*10 087*	*11 129*	*12 071*
Retirement annuity	*6 113*	*6 718*	*7 141*	*12 835*

Source: Tax Expediture Statement, 2019 Budget Review

Makhubela . . . getting tough

'dormant' funds being overturned on applications to court (see *Cover Story*), it's now switched in the opposite direction for the reinstatement of funds that the FSCA (actually, its FSB predecessor) had deregistered.

Where a fund or administrator becomes aware that a cancellation was made in error – as the fund still has members, assets or liabilities – it must immediately:

- Inform the FSCA accordingly;
- Disclose particulars of the error and explain why it had occurred;
- Apply to court for the cancelled registration to be reviewed and set aside. The applications must be made "without delay" and served on the FSCA.

These instructions pertain to cancellations prior to April 1 2018. For cancellations of 'dormant' after this date, the FSCA must immediately be informed of those which have members, assets or liabilities.

The FSCA may undertake supervisory on-site inspections to invoke any legal measures to verify whether funds or administrators are implementing the appropriate process. They must also be "doing the necessary reporting and approaches to the courts where the information justifies such action", warns FSCA divisional executive Olano Makhubela.

Spirit of the TCF

National Treasury has pushed the 'Treating Customers Fairly' principles. They apply to pension funds whose members must be kept appropriately informed before, during and after entering contracts.

Lukhaimane . . . duty to disclose

The point is emphasised in a determination, following a complaint against the Municipal Employees Pension Fund, by Pension Funds Adjudicator Muvhango Lukhaimane: "TCF requires entities to measure themselves as to whether or not in doing business they are dealing fairly with the consumer by... providing them with sufficient and clear information that will enable them to make informed choices when acquiring financial products."

The complainant, C J Modiba, had disputed the computation of his withdrawal benefit. The critical issue, said the Adjudicator, was that the MEPF had failed to inform Modiba that the transfer value had been used to purchase additional pensionable service from the Government Employees Pension Fund.

This issue should have been disclosed to the member when he joined the MEPF so that he'd understand at the point of exit that the amount wouldn't simply be added to his withdrawal benefit. That the information hadn't been disclosed to him, Lukhaimane believed, "has been ruinous to say the least".

On receiving details of the computation from the MEPF, she dismissed the complaint but nonetheless noted that the fund had contravened TCF principles by its disclosure failure. ■

Default regulations' learning curve

Andrew Davison, Head of Advice at Old Mutual Corporate Consultants, summarises what trustees need to know.

On 1 March 2019, the industry saw full implementation of the retirement-fund default regulations. They aim to deliver better retirement outcomes for members by addressing three key areas of retirement savings.

A fund default investment strategy is nothing new. It is unusual for a fund to not have one. Given that many people are invested in their fund's default strategy, the regulations seek to tighten up the requirements that such a default investment strategy should meet.

One of the biggest reasons why people fail to accumulate sufficient savings by the time they reach retirement is that they cash in their savings when changing jobs. The regulations aim to improve preservation of savings by providing cost-effective and easy-to-access methods of preservation. Then, at retirement, the regulations require funds to offer members an annuity or annuities to assist them to convert their accumulated savings into a pension for life.

There are three default regulations to the Pension Funds Act:

- **Reg 37** requires retirement funds to offer a sound default investment strategy;
- **Reg 38** requires that pension and provident funds offer a default preservation strategy;
- **Reg 39** requires funds to have an annuity strategy for members upon their retirement.

All three offerings should be appropriate, simple, cost-effective and transparent to improve members' overall benefits. Members should be provided with suitable communication in relation to the default investment strategy, including fees and performance, on an ongoing basis. They should also be given adequate information and guidance about their options when they leave a fund, either before retirement or at retirement.

The industry has been aware of these changes since they were promulgated on 25 August 2017. They align with the principle of Treating Customers Fairly which governs the way all financial-services providers treat clients.

What are trustees to do?

Even if trustees have already developed and implemented their fund's default solutions, there is still a lot of work to be done. It is essential that they carefully document the process followed and the decisions taken as compliance by boards will need to be evidenced.

The fund's Investment Policy Statement (IPS) must be updated to reflect any changes and specifically to reference Reg 37. The IPS should also refer to the annuity strategy that the fund has put in place and ensure alignment between pre- and post-retirement investment strategies. Trustees should consider drafting an Annuity Policy Statement to document the fund's annuity strategy.

There is also the important issue of communicating the default solutions to members and ensuring that they understand the options and solutions available to them, including any access to retirement benefit counselling. A further note offering interpretation and other guidance in respect of the default regulations was issued by the Financial Sector Conduct Authority (FSCA) on 12 December 2018.

There are two further draft conduct standards that are still to be released. They cover living annuities and smoothed-bonus portfolios.

Funds that utilise smoothed-bonus portfolios for their default investment strategy and those funds that have selected a living annuity as part of their annuity strategy will need to review their solutions to ensure that they comply once the final documents are released. The FSCA has indicated that these will be issued shortly, but with a delayed implementation date.

Challenges for trustees

There will be additional work for trustees. This relates to development of the solutions, selection of service providers, communication to members and then ongoing, regular review of solutions and providers to ensure they remain appropriate. Depending on the type of annuity strategy developed, the levels of administration and oversight will vary.

The default regulations are not a silver bullet. There will still be challenges. An important element is that trustees deal with a group arrangement. It is therefore impossible to build solutions that suit each and every individual member, but trustees need to communicate with members and advise them on how decisions were made in the members' interests and to suit their personal circumstances.

Choosing annuity strategies

Regs 37(2) and 39(2) place an onerous responsibility on trustees when it comes to default investment portfolios and annuity strategies. Education and upskilling of trustees are paramount if they are to implement high-quality solutions that truly address their members' needs.

There are various training providers that are adapting their training to incorporate post-retirement solutions and default regulations. Employee-benefit consultants are also investing in training and building the knowledge of their consultants to advise trustee boards.

Asset consultants are also available to assist trustee boards to navigate this new territory. It is fair to say that this is a learning curve for the entire retirement industry. In the past it has not had to deal with post-retirement issues, especially in the defined-contribution space.

Trustees' key requirement is to justify that they are adhering to the regulations. They should be able to document and demonstrate that they have applied their minds and considered all the available options before selecting the solutions or service providers they have used. Clear objective comparisons will also have to be documented as part of the process.

There are many different types of annuities available in the market. It has proven a challenging exercise for most trustee boards to go about choosing annuities that meet the requirements of Reg 39.

Davison . . . improvements over time

This is exacerbated by the fact that it's a new area of expertise for most trustees. Annuities, particularly with-profit annuities, are not easy to compare because the levels of initial pension for a set amount of capital vary between providers.

Also, over time the bonus histories aren't always comparable and they need to be evaluated in conjunction with the starting pension. This means that it is difficult to assess the likely future performance.

This has undoubtedly been, and will still be, a steep learning curve for trustees and consultants.

Our view is that the institutional default annuity space will evolve over the next few years, both in terms of the products available as well as in terms of the ability to assess and compare the various annuities and providers.

For more information, please contact Andrew on adavison@oldmutual.com, or visit

www.oldmutual.co.za/omcc

OLDMUTUAL

PAIA APPLICATION

In search of truths

Contradictions and clarities revealed in public servants' unhappiness with R5bn loan from PIC to Eskom.

Yet another confrontation has befallen the beleaguered Public Investment Corporation. This time it's been to explain the inner workings of its relationship with the Government Employees Pension Fund, the PIC's major client, specifically over the grant of a R5bn bridging loan from the PIC to Eskom.

The purpose of the loan was to allow Eskom time, through a short-term operational liquidity crunch, to arrange longer-term borrowings from financial institutions. Fundamentally at issue were whether or not:

- The loan, granted in February 2018, was guaranteed by government. (If it wasn't, which is denied, there are at least explanations of how government considers the guarantees take effect.).
- The GEPF was consulted. (The PIC, represented by thenchief executive Dan Matjila, said that it was consulted. The GEPF, represented by principal executive officer Abel Sithole, said that it wasn't.)
- The GEPF board ever discussed the loan either prior or subsequent to it having been granted. (Because the investment mandate of the GEPF to the PIC is kept confidential, respective obligations aren't in the public domain.)

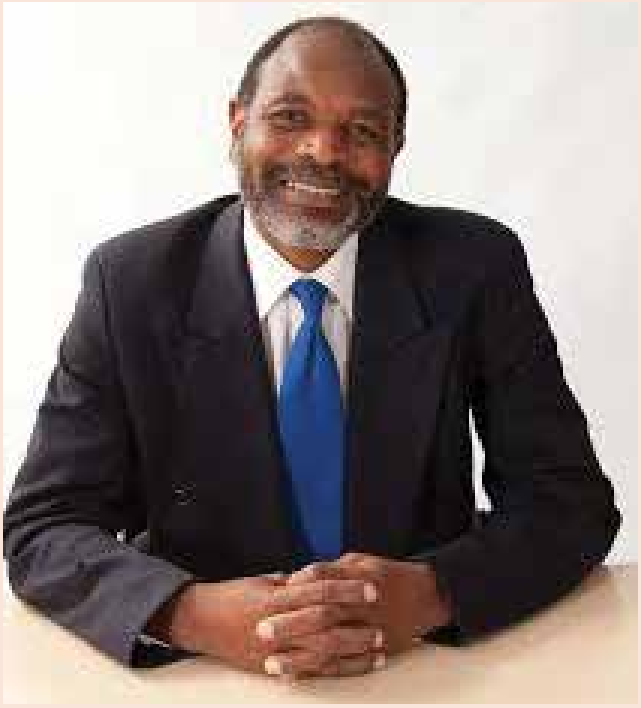
This latest dispute came about because the Public Servants Association, a 230 000-member strong trade union with a seat on the GEPF board, has applied to the North Gauteng High Court under the Promotion of Access to Information Act for disclosures that relate not only to the loan but also to the ministerial appointment of PIC directors.

What happens next? Will witnesses be called, either to the PIC commission of inquiry or to give evidence in court? Both options are debatable.

No date for the PSA hearing has been scheduled. It could be that a hearing is unnecessary because much of the requested information is already revealed in a series of voluminous affidavits. So it would be over to the commission, should it want, for a deeper dig into how the PIC operates.

The affidavits have been deposed by PSA general manager Ivan Fredericks in launching the notice of motion, then by the various respondents: Stadi Mngomezulu of National Treasury for the Minister of Finance, Matjila for the PIC and Sithole for the GEPF. (Incidentally, Mngomezulu is also a GEPF trustee and Sithole is also acting commissioner of the Financial Sector Conduct Authority.)

In essence, the PSA wanted to know how the PIC directors were appointed; for example, whether the Minister had exercised "due regard" to nominations submitted to him by depositors. It turned out that



Sithole . . . no consultation

there were none. The PSA additionally wanted to see documents in support of the PIC's contention that the loan had in fact been guaranteed by government.

On February 5 last year the PIC issued what purported to be a joint announcement by itself and the GEPF. It stated that the PIC, on behalf of the GEPF, had agreed to advance Eskom the bridging loan for the purpose of funding Eskom's operations for the month of February; that the PIC had obtained approval in line with its investment mandate and corporate governance requirements; that the GEPF and PIC board took comfort from the fact that the bridging loan was fully backed by a government guarantee; and that the PIC and GEPF were encouraged by the recent changes in Eskom governance.

A few days later, on February 13, the PIC issued a statement expressing its concern about the "false, misleading information" in the media about the decision by the PIC and GEPF to provide Eskom with the short-term R5bn loan facility. "The decision to advance the bridging loan facility to Eskom was taken in consultation with the GEPF," it said.

In replying to the respondents' answering affidavits, however, Fredericks contends that this PIC statement is directly contradicted by Sithole. Under oath, Sithole now said that the PIC had not submitted an application for the bridging loan to the GEPF; that the application had not been considered by the GEPF, and that the GEPF "did not participate in taking any decisions relevant to the Eskom bridging loan".

Fredericks further insists that National Treasury did not have any records relating to the PIC board request and that, on the Minister's version, there was clearly no valid government guarantee for the loan. Whereas the PIC claimed that the Minister had considered and approved the guarantee, the Minister said "that he did not and that it was not necessary for him to have done so".

In his affidavit for the Minister, Mngomezulu addressed the PSA's concern that the PIC board's media statements – to the effect that there is a guarantee – are untrue: "I can confirm that a guarantee does indeed exist. Part of the guarantee is used towards a Domestic Medium Term Note (DMTN) Programme, which Eskom is proceeding with, under the oversight of the JSE."

He explained that Eskom does not have to request government approval prior to issuing notes under the DMTN programme. Instead, for monitoring purposes, Eskom needs only to notify National Treasury of issuances made against the loan's amount.

"There is thus no loan agreement entered into or discussed with the lenders," the affidavit continues. "There is furthermore no individual guarantee documentation for note holders which is prepared for individual issuances, such as in the case of the R5bn in notes bought by the PIC...I (therefore) submit that the DMTN programme presents no cause for alarm."

The DMTN programme provides for government to issue guarantees, in respect of notes issued by Eskom, so that Eskom is enabled to raise finance for its capital-expenditure programme. No note has been disclosed in relation to the short-term R5bn bridging facility and neither has a guarantee related to this facility been produced.

So far as the GEPF is concerned, Sithole pointed

out that it was not a party to the loan agreement and that the PIC had not submitted to it an application for the bridging loan. The GEPF is a defined-benefit fund and the members' entitlements to benefits "are not in any way affected by any of the investments which it makes," he added.

In any event, said Sithole, the GEPF denied that it had failed to exercise its fiduciary duties. The PSA's allegations had ignored the facts that the so-called bail-out – fully backed by a government guarantee -- was not free because Eskom was obliged to repay the full R5bn plus interest and had done so.

On affidavit for the PIC, Matjila stated that the PSA was aware from the outset that the PIC had not only complied with its requests but also that the documents requested could be obtained from the Minister and/or National Treasury. Unfortunately, he added, the PSA had adopted an unreasonable approach by subjecting the PIC "to this frivolous and unnecessary litigation".

Should the PSA persist with this approach, he warned, the PIC's answering affidavit "serves as a notice to PSA that...the PIC will seek a punitive costs order against the PSA".

Since the PSA now has much of the information it sought, unclear is what's to be done with it. For the contradictions exposed, there's at least clarity on how the guarantees are seen to be valid and on how the PIC works in relation to the GEPF.

Most usefully, the request for information on how the Minister appoints PIC directors appears to have borne fruit. Indications are that in future the PIC board, as with the GEPF board, will include representatives of stakeholders; in other words, presumably, trade unions such as the PSA.

Lawyers in this PAIA application were Fasken Inc (for the PSA), State Attorney (for the Minister), Werksmans Attorneys (for the PIC) and Ndobela Lamola Inc (for the GEPF). ■

A GENERATION OF UNWILLING PENSIONERS

Fran Troskie, Investment Research Analyst, RisCura

As a generation of baby boomers reaches retirement, and as people live longer due to medical advances, an important question is getting more attention globally: What is the right age to retire? Should SA's aging workforce be working – and contributing – for longer?

Particularly in more developed markets, retirement reform has seen the retirement age increase, at times sparking the ire of would-be pensioners. But, there is also a flipside, particularly in countries where pension provisions are inadequate.

Picture a 64-year-old engineer, a year away from being pensioned off. He's grateful to have his health and looks forward to a touch of leisure. Yet, mostly, he's concerned because he knows he only has one year of working left to contribute to a comfortable retirement. Several factors makes this seem like a pipe-dream:

- Past mistakes: Cashing out his retirement savings when he changed jobs 20 years ago, and choosing the lowest contribution rate;
- Present circumstances: Was not offered an in-fund annuity by his employer and did not receive financial education on retirement saving;
- Future prospects: With advances in medicine, he believes his retirement years will last longer than he'd foreseen 20 years ago.

Unfortunately, there isn't much he can do to change the above. But, one thing he could do to improve his financial situation is to keep working – and contributing to his retirement savings. Company policy, however, doesn't necessarily allow him to. It may impose mandatory retirement, with normal retirement age at 65.

In many respects, he believes he's a more valuable employee now than ever before. He has a lifetime of knowledge, learning, and experience. He's the first one in the office in the morning, and the last to leave, since an empty nest means there are fewer responsibilities for him at home.

He is one of thousands of highly-skilled employees facing a financially uncertain future after unwillingly retiring. There is a whole generation of people who believe they are still fully capable of making a meaningful contribution to society – but the current employment system seems to underestimate their value. And, in a country like South Africa with soaring youth unemployment rates, they know that finding gainful employment elsewhere is highly unlikely.

Statistics SA's Q2 Quarterly Labour Force survey released in July 2018 has few positives to report. Compared to last year, the national expanded unemployment rate increased by 0.5 percentage points. The proportion of youth aged 15 to 24 who were not in employment, education or training (NEET) increased by 0.7% over the same period. At 39%, this means that an average of four per ten youths are unemployed, but are not in education or training to become employed. Within this context, the prospects for people of pensionable age are dim.

There are no simple solutions, but the retirement industry and government policymakers should take into account that policies and regulation should encourage trustees and investment consultants to help ensure that:

a) members receive sufficient financial education throughout their working careers;
b) funding models are appropriate (life stage models and asset-liability matching);
c) members are provided with appropriate savings-options at retirement (annuities/in-fund annuities).

Government may need to reconsider how it uses the longer-lived grey workforce. An added emphasis on skills transfer programmes would be laudable – not only in terms of making efficient use of valuable human capital, but also in addressing some of the concerns about youth NEET. Educated and experienced elderly instructors could work in training colleges, even if only on a temporary and substitute basis. Mentorship programmes can also add to the socio-economic impact of such initiatives. And, if such work were to be compensated (potentially partly by revisions to the old age grant system), all the better.

Deciding which interventions are feasible, needs more attention. But, at the very least, it is clear that a generation of unwilling pensioners and a growing grey workforce should not be left in the cold. ■

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COVER STORY

Wake up! Pay up!

Were it only so easy.
Proper thought must be given, and appropriate action taken, over the R50bn of pension assets not being used as they should be.

Terms have meanings, frequently emotive and rarely neutral for conveying an impression.

"Unclaimed benefits" and "unpaid benefits" can be used interchangeably, but they carry different connotations. "Unclaimed" implies that the obligation rests with former members of pension funds that they get off their butts to demand entitlements. "Unpaid" denotes a responsibility on the fund, the employer or the fund administrator to find beneficiaries who're owed payments.

"Unpaid" is preferable because there are at least 4,5m former members and dependents due for some R50bn in pension benefits. Many of them -- including, for example, spouses and minors eligible to receive pay-outs on a member's death -- haven't a clue that monies await them.

When these people are poor, often pitifully so, in urban and rural areas across SA and in neighbouring states, the human destitution is heightened. A few thousand rand in these peoples' pockets is meaningful.

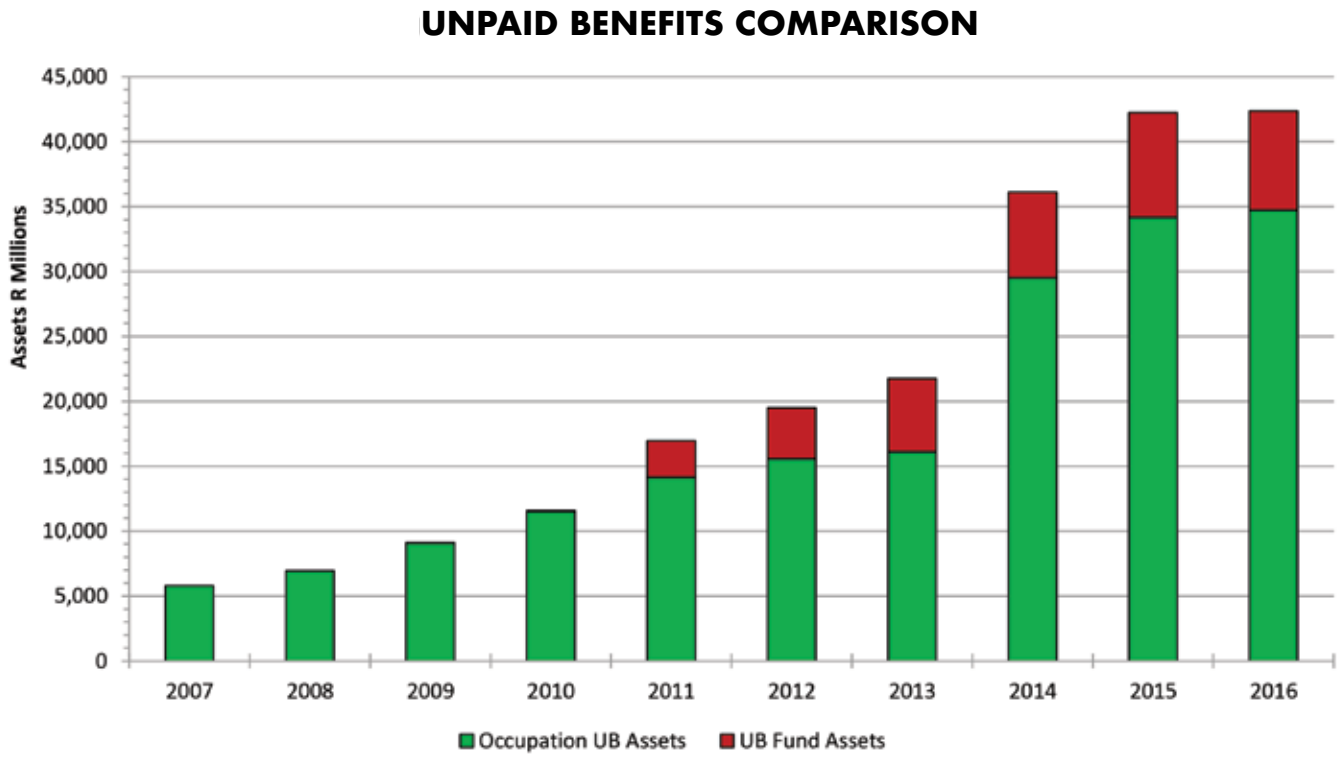
There are facilities to initiate the claims process. But feel for the inquirers, especially of low literacy, who attempt to use the search engine provided on the website of the Financial Sector Conduct Authority; first to know that there is such a facility; second to have the internet tools and skills to use it; third to provide such details as an ID number (of a migrant?), the name of the fund (really?) and the name of the employer (accurately?).

Only then will the database be able to match these details with the central database, and only then to supply the inquirers with contact details for the relevant fund or administrator so that they can follow up. Wish them luck as they try to submit a claim without easy and cheap access to a photocopy machine, a commissioner of oaths and telecommunication facilities.

The fault lies not with the FSCA search engine for it's an honest endeavour to assist members as best it can through the tracing function on its website. By end-June last year, it had received 45 000 enquiries of which 8 000 possible matches were identified to a value of R1,8bn.

The problem has myriad causes. National Treasury has identified several: fund members not being required to supply their funds with the necessary information to facilitate pay-outs once they leave their jobs; employers not providing correct and updated information to the fund; insufficient effort being made to trace beneficiaries, and poor data-management systems at numerous fund administrators.

To this mournful list can be added such other factors as employers failing to inform employees that they're members of retirement funds in terms of



Source: Financial Services Board, Sept 2017

their employment contracts, the names of their funds and the fact that the funds are separate entities that should survive even if the employer folds; let alone for employees being requested to provide details of their beneficiaries in the event of death or disability claims.

So how is a fund or administrator supposed to respond when it hears from a person purporting to be a member but who cannot supply evidence to prove it? Or when the person has a common surname and an identity number or even a birth date that doesn't match records?

Bluntly, there is no single correct answer. Worse, the environment is ripe for fraudulent documentation and phoney offers from crooked operators demanding upfront fees to assist desperate people.

Stark numbers speak for themselves. A 10-year trends analysis by the then Financial Services Board shows that in 2007 there were 3 753 funds with 9,3m members and slightly over R1 trillion in assets. Of these there were 1 859 funds which had 1,06m members owed R5,8bn in unpaid benefits.

By 2016 the picture had deteriorated markedly. There were 2 053 funds with 14,5m members and assets of R2,4 trillion. Of these, there were 1 327 funds which had 4,2m members owed R42,4bn in unpaid benefits.

This isn't the end the sad story. Not only would today's total for unpaid benefits exceed R43bn but they'd be only for those funds supervised by the FSCA. Thus excluded are the huge Government Employee Pension Fund (which alone has reported unpaid benefits of R9,2bn) and the Transnet funds, amongst others.

It's nonsensical, national priorities for new infrastructure projects and social benefits being what they are, that more than R50bn should be left to accumulate in anticipation of the full amount eventually being successfully claimed. This simply won't happen.

A proposal is therefore that the amount across the spectrum of institutional and employer-based unpaid benefit funds (UBFs) be consolidated into a central not-for-profit UBF, supported by a central database into which government departments – such as SA

Revenue Services, Social Security Agency and Home Affairs -- can input relevant identification details. This UBF would be managed jointly as a public-private partnership.

Another proposal is that one of the existing funds, which is effectively already a UBF, be taken over by the state and run as a fund to which closing funds could voluntarily transfer unpaid benefits. Even if the UBF takes all reasonable steps to find and pay all those entitled to the unpaid benefits, it will never be able to find and pay them all.

Then, the argument goes, it could justify holding assets with a value less than the full face value of its liabilities. Particularly if the fund is underwritten by the state, no beneficiary will be deprived of money due.

The balance could be released to finance new development and social programmes. Private-sector participation in governance and oversight is essential, just in case a strained fiscus becomes tempted to fill old holes.

Necessity being the mother of innovation – and necessity being acute – a centralised UBF could offer the further advantage of supervision under the Pension Funds Act requiring that funds supply information by which members can be identified and traced.

Only in 2009 were the regulatory reporting requirements for funds under the Act amended to require all funds to include reports on their unpaid benefits in their annual financial statements. Previously there'd been no provision for them separately to disclose memberships and the assets related to unpaid benefits.

Two years ago, the FSB noted in a September 2017 presentation, it had proposed amendments "to provide for a Central Unclaimed Retirement Benefit Fund to house all unclaimed retirement benefits and possibly be expanded in the future to include other sectors such as insurance companies and banks".

Meanwhile, endemic problems remain. The amount of unpaid benefits due to a fund member is in many cases gradually chipped away by administration, asset-management and tracing fees deducted from individual 'member accounts' rather than from a fund-wide expense account.

Kotze . . . better and better

Not uncommon is that amounts held to provide benefits for people who can never be traced (due to bad records, for example) remain available in an UBF as 'assets under management' until depleted. Instead, they could cover expenses attributable to those who can be traced.

Unacceptable are arrangements that create disincentives to trace. They're suspected to enter the mix usually when relationships between fund trustees and service providers are incestuous.

However, there is a brighter side. Databases are evolving as company records, perhaps as a function of labour legislation, are improving. If only under regulatory pressure, communications with fund members are refining. When a member switches from one employer to another, there's a better chance of the move being recorded for a tracing agency to follow.

Moreover, at least some institutions have become increasingly proactive. A case in point is Liberty, historically the most impacted by the sheer volume of funds it had gathered. Under testing circumstances, where each fund requires examination, Liberty's behaviour on the treatment of UBFs presents an illuminating case study.

Its clean-up started off the back foot with the large number of messy employee benefit (EB) books taken under its wing. Some years ago Liberty bought Capital

Van der Merwe . . . unique usage

Alliance which had previously acquired the EB books of AA Life and Stangen. Then it took over Investec EB which included the Fedsure and Norwich EB businesses. Big size, shooting Liberty to the uppermost range in terms of fund numbers being administered, caused big trouble in terms of flawed records.

When the FSB commenced its 'cancellations project' in 2008, there were more than 6 000 funds which had no boards of trustees. Of these funds, about 80% were on Liberty's books. Some had no assets or liabilities, but others did. Liberty has been painstakingly tracking the latter.

So far it has stood alone in having obtained a High Court order for the cancelled registrations of 25 'dormant' funds to be reversed. Because these funds were discovered to have assets and liabilities, their registrations should not have been cancelled (*TT* Feb-April '18). The Liberty decision voluntarily to commence reversals, by court applications, shortly preceded the landmark Concourt judgment on the FSB's so-called 'cancellations project' (*TT* Nov '18-Jan '19).

That Liberty didn't await this judgment, on the gamble that a different outcome could have averted a legal compulsion on the FSB/FSCA to reverse erroneous cancellations across the board for all administrators, speaks to a moral sensibility.

"Most important is that benefits are paid to members," says Liberty Corporate chief executive Tiaan Kotze. He won't be going to court for reinstatement of other funds possibly deregistered in error but instead "will be working with the regulator to ensure that proper processes are followed".

The processes will be keenly monitored both by Liberty and other administrators of erroneously-cancelled funds as well as the Right2Know Campaign, the Casual Workers Advice Office and the Sebokeng-based Unpaid Benefits Campaign.

It's unclear how the flaws can be remedied without court orders of the type for which Liberty had applied. In fact, on March 4 the FSCA suddenly issued a circular that effectively endorsed the Liberty route. The circular instructs administrators, who'd been responsible for erroneous cancellations before April 1 2018, to apply to court for these cancellations to be set aside (see *Currents*).

Having investigated a sample 500 funds of the 4 600 funds subjected to the FSB's 'cancellations project', KPMG found that the FSB had insufficient information on the disposal of their R2,5bn in assets. In the months since the Concourt judgment last September, remedy appears still to elude finality.

Nonetheless, although the handling of the erroneously-cancelled funds is obviously important, Liberty's R110m so far detected in some 130 'dormant' funds (including the 25 re-registered) is tiny against the private-sector industry's R40bn-plus total for unpaid benefits. Kotze reckons that Liberty's share of unpaid benefits amounts only to around 6% of the industry issue.

As part of its clean-up, Liberty appointed two independent trustees to its UBF. One is a former unionist with extensive retirement-fund experience; the other has long served in asset-management firms. No longer on the UPF board is there a Liberty employee.

Then too, Liberty has re-looked its pricing model. In September 2017 it stopped charging an administration

fee to any member whose benefit is less than R800.

Better processes – which come at significantly increased capacity-building cost, borne by Liberty – mean better ability to pay claims. The tumultuous process involves taking somebody verified by a credit agency and getting the person's dependents to provide documentation that will show the correct benefit for the correct person. The process is supplemented by engagement with community-based organisations and education initiatives.

At the beginning of last year the Liberty UBF had assets of more than R1bn. After investment returns and R175m in payments, it stood at a little more than R900m. Individual balances average less than R10 000 per member, and more than 35% of members have balances under R800. Payment of claims has improved over a year from around 500 to 5 000 people a month.

The major bottleneck is in the ability to trace, Kotze points out: "Of approximately 90 000 members in the UBF, tracing agents are struggling to trace around 27% of them. Where tracing is expensive for the 35% of members with small balances, we've been running sms campaigns with some success."

A curious phenomenon is that, of those successfully traced, roughly 5 000 have declined to submit claim forms. The reasons beg an industry-wide examination to establish, for example, whether members might be fearful of beneficiaries learning about monies due. If this is a factor, then member communications and unpaid benefits have yet another problem.

Also speaking to improved tracing abilities is Fedgroup, pleased with having been awarded the tender by Argen Actuarial Solutions to find unpaid members in the now-liquidated IF umbrella pension and provident funds (*TT* Aug-Oct '18). The funds have about R180m for distribution.

Fedgroup Life chief executive Walter van der Merwe is confident of his division's ability to satisfy the tracing mandate by virtue of its setup for administration of beneficiary funds: "We're merely extending our capability to a similar process of maintaining a relationship with beneficiaries." The

ANOTHER PERSPECTIVE

Michael Prinsloo, head of employee-benefits consulting strategy at Alexander Forbes, comments:

We are not going the Liberty route for the reinstatement of closed funds. Our situation is different from Liberty where closed funds still had assets.

Unclaimed benefit funds, and occupational benefit funds, have typically implemented policies around unclaimed benefits and gone through extensive efforts to trace individuals, then to pay them once traced. Alexander Forbes' funds are no exception.

At this stage it's unclear what more can be done as in many cases much time has elapsed. Some unclaimed records result from surplus allocations dating back to 2001. Funds have run multiple tracing attempts but the problem is that 15 years ago funds did not receive ID and contact numbers etc, so the data on older records is patchy.

The Mines 1970 UBFs have put themselves forward as a success story in terms of finding members and paying them over the past few years (*TT* March-May '17). They have a tighter pool in which to fish, being largely ex-Chamber of Mines employers who were involved, so it is limited.

Given current legislation, in particular default preservation and changes in tax law which set out when a benefit accrues, theoretically in the future we'll have far fewer 'technical unclaimed benefits'. They'll still happen but will be called something else. So the visible problem will shrink but it's uncertain whether the actual problem will go away.

In the surplus-legislation aftermath there were funds that submitted valuations to write down the value of the liabilities associated with these types of benefits and essentially release those assets for other purposes (essentially working on the liability being equal to the fund credit calculated into a probability of payment). This was met with resistance from regulators.

But I do think there is merit in considering an approach where a portion of the money is used for specifically identified cases e.g. social development and impact investments. The trustees of UBFs could conceivably follow such investment strategies today, but many would be too nervous to take on risky investments of this nature.

However, if the liability is reduced it may be more palatable for these trustees to "take risk" with essentially surplus assets.

exercise for beneficiary funds is "vastly different" from pension funds, he suggests, because the latter are mainly concerned with active members.

Van der Merwe explains that Fedgroup's tracing method starts with information available electronically, moves on to databases and continues to inquiries with former employers. Then it proceeds to visiting places or work and last-known home addresses.

The higher the volumes that pass through its systems, the lower the costs to members. There are no fees for unsuccessful traces.

"Unique is not our technology but the way we use it across the spectrum of financial products," he explains. "They all require bank interactions."

Main competitor to Fedgroup in the beneficiary-fund space is Fairheads, necessarily active in tracing, where director David Hurford argues for a centralised administrator of unpaid benefit funds that are separate from fund investment management: "It would charge a modest monthly administration fee, rand-based and not a percentage of the benefit, as well as a termination fee once the member has been traced. The administrator's revenue stream would therefore depend on finding people."

What needs to happen, one way or another, is a centralised database that can draw on multiple sources exclusively for its confidential use. There's a wealth of invaluable contact information held not only in government agencies but also in customer records of retail groups and cellphone operators. Take it as a thought for the FSCA to action, along the lines of the proposals already presented.

Clearly, from what's being done and can be done, the problem of unpaid benefits is not intractable. Not by a long shot, provided that the public and private sectors collaborate for innovation. That R50bn hangs in the air can be justified by neither, and least of all to fund members. ■

LIBERTY
CORPORATE

Behaviour, conversations and relationships

Default regulations highlight their importance. Louis Theron, head of investments and annuity products at Liberty Corporate, explains why.

The default regulations under the Pension Funds Act, now effective, aim to lower charges and improve outcomes for members of retirement funds. All funds must ensure a minimum level of compliance even though the design, detail, extent and execution of the default strategies will differ between funds.

Still to become certain are whether discussions are taking place at the appropriate levels and whether behaviours, conversations and relationships are being considered. These are crucial for a retirement fund to achieve success and advance members' financial freedom. Investment strategies, product selection and financial-services providers are important, but must be considered against the right context related to each retirement fund.

Theron . . . clear objectives

Doubt and scepticism around the regulations will persist due to recent negative investment and market sentiment. Within the SA retirement industry, shorter-term changes and successes will arise with fundamental (appropriate) shifts requiring more time to settle.

Behaviour

Trustees generally have a good idea of the member behaviour in their funds. At Liberty we believe that the default regulations afford the opportunity to clearly articulate the ideal member behaviours that trustees would like to encourage. Identifying initiatives to change members' current behaviours accordingly can then be implemented to facilitate this.

As we are dealing with members, we need to remind ourselves that a one-size-fits-all approach is not possible and not something that the default regulations are trying to drive. Rather, they're about putting into place strategies that are suitable for the average member of the fund. In turn, these represent the main characteristics and preferences of the fund's membership.

They encapsulate the DNA of the fund - what it stands for and to which all intended behaviours should revert. The strategies should be regularly reviewed, monitored and adjusted to accommodate fundamental environmental shifts such as changes in regulations and the fund's membership profile.

Conversations

Stakeholder conversations across the value chain will promote the successful delivery of any strategy promoted and enabled by the default regulations. One example relates to discussions between trustees and their consultants. Another example is member communication around the default strategies.

Regardless of specific conversations, they should be seen as the delivery and support of mechanisms built around the default strategies. These are as important as the actual solutions themselves.

Liberty research has found that pensioners' needs and wants can broadly be grouped mainly into functional and emotional categories. The research also revealed an overarching need for communication and information. The specific communication-related needs of pensioners and those close to retirement are:

- Early career education and engagement opportunities;
- Regular access to knowledgeable advisors;
- Conclusive information that is simple and concise;
- Detailed breakdown of processes and procedures;
- Information in addition to product information, e.g. alternatives ways to save for retirement;
- Stories and testimonials from others.

Communication around a default strategy alone will not achieve the desired outcomes, whereas a conversational approach can be expected more successfully to deliver this.

Partnerships

The definition of a partnership, within a business context, is appropriate for the default-regulations context. As with conversations, different partnerships exist in the delivery of a fund's default strategies. Most obvious would be the partnership between trustees, the product provider and consultants.

If appropriately addressed, the default regulations can introduce a new partnership in the delivery of the default strategies i.e. the partnership between benefits counselling and advice. According to the default regulations, benefits counselling is "the disclosure and explanation, in a clear and understandable language, including risks, costs and charges, of available investment portfolio and annuity options". Most importantly, it is limited to the provision of factual information around the default strategies.

The default regulations have created opportunities for product providers, consultants and advisers to deliver better outcomes for fund members. These enhanced toolkits will not succeed by themselves. They're intentionally associated with setting targeted member behaviours, the strategic enablement offered by member conversations and shared ownership focus from partnerships.

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ECONOMIC EMPOWERMENT

Big and black

With adjustments in shareholding, Sanlam Investments is catching the wave for pension funds' procurement choices.

In a stroke, a deal with African Rainbow Capital **has** shot Sanlam's third-party asset manager to the top of B-B BEE rankings for assets under management. By virtue of its brand and base, Sanlam Investments (SI) moves to a pole position for the attraction of business from pension funds in terms of the Financial Sector Code.

At present, compliance with the code is voluntary but progress will be annually measured by the Financial Sector Transformation Council. A critical metric is that large retirement funds – which implicitly include umbrellas – compile and publish annual scorecards for preferential procurement. So an easy win is to appoint a black-owned asset manager.

The council warns that, if sufficient disclosure by pension funds does not materialise, "consideration will be given to revising this (voluntary) dispensation". In measuring transformation progress, it says, there may be reliance on surveys in the public domain. The only such survey is BEE.conomics (*TT* Nov '18-Jan '19).

In terms of the survey's black-owned definitions, ranking firms by size of assets under management the first is Taquanta (R146bn) followed by Aluwani (R57bn) and Mazi (R48bn). SI will eclipse them all, perhaps soon to have assets under management that will equate double the R410bn size of the top 10 put together. Don't be surprised if at least one additional black-owned firm is soon merged for shares into the restructured SI.

Van Zyl . . . strategic advance

"We're contemplating one or two similar transactions," says ARC joint chief executive Johan van Zyl. "The idea is to have a firm with R800bn of assets under management, which will be at least 60% black-owned, by the second half of this year."

ARC is black-owned and controlled via the Patrice Motsepe-led Ubuntu-Botho Investments, Sanlam's long-standing empowerment partner with cross-shareholdings between ARC and Sanlam. In a R2bn transaction -- ARC buys shares in Sanlam, and Sanlam buys shares in ARC Financial Services -- ARC gains effective economic control of Sanlam Investment Holdings.

"This will position SIH as a leading player in a market segment where B-B BEE credentials will support the strategy to enhance our share of it," Sanlam group chief executive Ian Kirk has explained.

Gaining momentum

Amongst the major insurance groups, first off the mark to a Level 1 rating for broad-based black economic empowerment under the revised Financial Sector Code is MMI. Having spawned black-owned asset manager Aluwani Capital Partners, its brands include Momentum and Metropolitan.

The Level 1 rating applies to all companies within the group. Its transformation focus is on youth employment, by increasing its support for youth-development initiatives, and building strategic partnerships with organisations similarly focused.

Another area is support for small and black-owned businesses, inclusive of empowerment financing and assisting the businesses' access to markets by directing procurement spends. An improvement in MMI's equity ownership also contributed to the Level 1 elevation, says MMI group head of transformation Busisiwe Sithole.

Closely on the heels of MMI to be a Level 1 contributor is Sanlam. Transactions concluded or pending, ARC being one, will increase Sanlam's direct black ownership to more than 18% and combined B-B BEE ownership (direct and indirect) to 35%. In some operating units, Sanlam expects B-B BEE ownership in excess of 51%.

The issue of new shares, in aggregate constituting 5% of Sanlam's enlarged issued ordinary shares (excluding Treasury shares), is to new broad-based groups of empowerment shareholders and Ubuntu-Botho. The new groups, focused on black women and youth as well as Sanlam employees in SA, will participate in 80% of the share issue. Ubuntu-Botho will participate in the 20% balance.

Sithole . . . committed approach

"Institutional clients want to see companies like Sanlam facilitate inclusive wealth creation," says group chief executive Ian Kirk. "While direct B-B BEE ownership at listed-company level is key, increasingly clients want to see B-B BEE in the operating companies with which they do business."

The extent of SIH black ownership, inclusive of the 25% now bought by ARC, will be 30% directly and 52% indirectly. For participation in the BEE.conomics survey, fund managers must be at least 50% owned by blacks (as defined in the codes of good practice) with accompanying voting rights. They must also have a minimum of 50% black directors and 50% black individuals in senior management positions.

SA's larger asset managers would battle to reach the levels required for participation. However, the effect on them of the SIH transaction is probably minimal. SIH's targeted market would be pension funds. Theirs are heavily targeted on retail investors where margins are larger and transformation is advanced.

Are SA black-owned asset managers frightened by the developing SIH colossus? "Not at all," says one. "It's part and parcel of the sector's transformation that we welcome." ■

momentum

ABC of prescribed assets

Momentum Investments head of strategy Rowan Burger believes it's important to distinguish between ANC policy proposals, actual government policy and the regulators tasked with implementation.

When there are tax benefits for investing in retirement vehicles (pension, provident, preservation and retirement-annuity funds), government feels that it is entitled to apply certain restrictions to the underlying investment exposures to ensure their policy intentions are delivered. These are primarily to ensure a long-term investment horizon (no gearing) and diversification (restrictions on the maximum exposure to assets to avoid concentration) to deliver a prudent investment outcome.

Many people will be familiar with these restrictions, often referred to as Regulation 28. A consequence of these restrictions is that government effectively directs investment. It is therefore possible for government to change these investment restrictions to channel pension-fund investment into certain asset classes. This would allow it to direct investment into certain government projects or to help fund ailing state-owned enterprises.

Why does this affect me?

Other than government employees, most South Africans are invested in defined-contribution funds. The retirement benefit is the accumulated value of the fixed contributions to a personal pension account plus investment returns on these contributions. If the restriction was such that a meaningful part of your account had to be invested in prescribed assets, you would retire with a lower benefit. It is reasonable to assume that prescribed assets would only yield a return equal to inflation rather than equities which generally yield 5% to 7% above inflation.

A redirection of 20% of the investment strategy would reduce real returns by (20% x 5%) 1% a year. While this may not sound like much, compounding it over a working lifetime of 40 years leads to an end pension 30% less than what it could have been (or half the value in the case of a lump sum for this period).

Has this been done before?

When SA was a pariah state under the National Party in the mid-1980s and could not enter international capital markets, a large allocation was required of pension funds to invest in government bonds. In those days funds were defined benefit. It meant that the retirement benefit was fixed and corporates had to pay higher contributions to funds to compensate for lower returns.

This situation has now changed. Individuals will bear the consequence of a restricted investment opportunity.

Why is there this proposal?

A number of asset managers have refused to fund certain parastatals, where there have been governance concerns, as well as other infrastructure projects where there are social and environmental concerns. The lack of support and feeling that the private sector would be dictating terms to government is probably a key driver behind the prescribed-assets proposal in the election manifesto.

Is there a lack of support for government initiatives?

No. Existing pension funds have many investments in programmes generating employment and developing the economy. The grievance from managers is a lack of 'bankable projects' that will be delivered on time and within budget.

In fact, ASISA (the industry body representing asset managers and life insurance companies) has committed to actively creating public/private partnerships with government and supporting these with capital to meet the broader employment and development policy objectives. There are many good examples -- such as renewable energy producers, toll roads and student housing --where pension monies have been used to enhance the country and still deliver great returns.

As another example, we are currently working as an industry to find ways to improve water provision using pension monies. Momentum is an active participant in the conversations and investments.

Are prescribed assets likely to be implemented?

The proposal has been ANC policy for some time. In previous manifestos, policy was more strongly worded in terms of directing retirement outcomes with proposals for a compulsory national pension fund. On many occasions, the private-sector industry has engaged with regulators on this matter. General agreement has been that prescribed assets would not be a desirable outcome. As the latest proposal suggests a discussion rather than firm policy, turned down in the past, it is less likely to become a reality.

What would be a better proposal?

It is critical for a country to have large investment pools which can be deployed to fund investment in jobs and the betterment of living standards. Our pension industry could be significantly enhanced if government adopts the proposals – already put to it by the regulators – that will keep money invested in pension funds.

This large pot would create an attractive opportunity set for government to partner with the private sector to build these infrastructure projects. Equally, the levels of oversight of certain investments have led to better outcomes for SA because of the activism that the asset managers apply.

www.momentum.co.za

RI tipping points

Whilst he finds encouraging signs, Futuregrowth's Andrew Canter also notices continued impediments.

Canter . . . more must be done

There are meaningful changes in the world of responsible investment (RI).

Investors have now realised that global warming is real. It may be approaching the point of no return with visibly rising temperatures, melting ice and altered climates. The ability for humanity to make adjustments has dropped from decades to mere years. Investors seem less willing to trade 'ecology' for 'economy'.

Capital is shifting away from carbon emitters to sustainable practices. 'Stranded assets' – the idea that coal or oil in the ground may never be used – is a phrase first coined only a few years ago. But it has quickly become a real factor in company analyses.

More investors are behaving proactively. This may be defensive as global inequality, slow growth and corruption have created political risk. They create unwanted uncertainty. However, RI is also driven by the trend for investors to seek a sense of purpose in their lives and with their money.

As investors move toward 'making money and also being a positive force in the world', they take on a wider role and duty. This leads to more varied analyses and better decision processes.

Investors are finding new tools to be responsible and engaged. These include proxy-voting policies and transparency, direct dialogue with companies and improved reporting on sustainability issues. There is an organised global movement toward requiring more comprehensive and standardised reporting on a range of environmental, social and governance (ESG) factors. Improved information flow on ESG issues is a vital first step for analysts to do their work.

In SA, recent corporate and public sector shenanigans -- plus the rising tide of stewardship codes such as the PRI, CRISA and Reg 28 -- have led investors to contemplate how they can improve governance standards. Tickbox governance assessments are clearly inadequate. The King IV code, for all its merits, is evidently not a panacea.

Governance does not begin and end with the board of directors. A more sophisticated view is that governance is the duty of the board, insiders, capital providers (investors and funders), regulators, auditors, ratings agents, journalists and customers alike.

While there are positive movements in RI, various challenges remain. Some asset managers put a veneer of ESG onto their investment processes, but investors are becoming increasingly savvy in differentiating between 'ESG on the label' versus 'ESG in the product'.

Equity fund managers may also fetishise their benchmarks, in many cases leading them to be 'closet indexers' – reticent to stray too far from benchmark exposures. Thus, a manager with a strong view (either financial or ESG-based) has a difficult time going to zero exposure of a large-cap share. Until their investor clients expect and encourage bolder positions (relative to benchmarks), asset managers will be reticent to act strongly on corporate misbehaviour.

Another challenge is that investment analysts can suffer a range of inappropriate pressures that impair their independence or stifle their public voice. For example, there are corporate bullies ready to punish analysts who make critical comments by excluding them from future conference calls or report-backs.

Likewise, some financial-sector employers are more interested in protecting their corporate relationships than to allow unfettered analysis. SA has seen strong evidence of the benefits of a free press. Investment analysts' independence is equally vital in maintaining accountability and transparency on issuers in public capital markets.

The world of RI has seen clear forward movement; at the least, an understanding that the choices about capital deployment have real-world consequences. To overcome the structural barriers to change, investors should start by recognising that ESG factors actually do impact risk:return considerations.

Value-adding investment processes can be built around this idea.

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TRANSFORMATION

Action stations

Retirement funds must get to grips with a new set of disclosure requirements. Here's help for trustees.

The amended Financial Sector Code (FSC), gazetted and now effective, is at present a voluntary dispensation for compliance by retirement funds. This is because many aspects of the B-B BEE requirements cannot be relevant to them.

For example, the funds have little or no influence over their membership demographics. Neither do they usually have a large number of employees. But they do make decisions, amongst other things, on the appointments of private-sector service providers.

Nonetheless, because the funds hold over R4 trillion in members' savings, the Financial Sector Transformation Council (FSTC) points out that they play a vital role in transformation itself. Accordingly, funds will be measured against particular metrics such as procurement and member education.

Says the Codes of Good Practice at s9(1): "The B-B BEE annual reporting by retirement funds should include a narrative on the B-B BEE score achieved and future plans for improving the score. The (FSTC) will measure transformation on an annual basis. This may include relying on surveys that are available in the public domain. If sufficient disclosure by pension funds does not materialise, then consideration will be given to revising this dispensation."

The FSC document is not the easiest of reads and the schedule on retirement funds isn't either. To help trustees through the detail, *TT* requested that certain terminologies be clarified. Trevor Chandler, special advisor to the Association of Savings & Investment SA (ASISA) and the FSTC, was happy to oblige.

***TT*: For compliance, what is the approximate dividing line between "large retirement funds" and funds not considered sufficiently large?**

Chandler: We include the top 100 funds measured by assets. The definition includes all types of funds including umbrellas but excluding retirement annuities.

Where does "management control" reside in a fund? Presuming it to be in a fund's board, then how does it reconcile with the right of members to elect up to 50% of board members e.g. if no trustees elected by members are black, or if there are no black candidates for election? Will the fund be penalised for not being adequately transformed and, if so, how will it be penalised?

Management control vests mainly with the board, but also with the principal officer and other employed executives in the few instances that this exists. Funds are penalised only through the allocation of fewer points on the management-control scorecard. You're correct that the fund does not have control of the people that either the member or the employer puts forward. Principal officers will need to sensitise trade unions, employers and others to this dynamic.

Chandler . . . key terms explained

Is the fund's principal officer included or excluded under the definition of "management control"?

The principal officer would be seen as equivalent to the chief executive officer in a corporate.

When it comes to amounts spent on "approved training" and "member education", what if no amounts are spent by the fund itself for these purposes e.g. where trustees and/or members attend courses offered by service providers who pay for them? Will the fund be expected to report on these and be credited/penalised accordingly?

Funds are not scored on their skills-development spend for staff or financial education of members. They simply need to disclose information on training that was provided. This could include sponsored training.

They are not penalised in any way if they do not spend. Of course, rules of the Financial Sector Conduct Authority around gratuitous support must be considered. But this is beyond the scope of the Code.

Do funds usually record the racial profiles of their members? If not, any advice on how they might cost-effectively go about creating records that separate black from non-black members and men from women?

No, funds don't usually record such profiles. But the data is often available from employers. Again, this is merely a disclosure requirement and not something that's scored.

On "preferential procurement", specifically on funds' allocations of assets for management, would only the 48 asset managers listed in the latest 27four BEE.conomics survey qualify as "black-owned"? For reference, which other surveys are available in the public domain?

There are no other surveys of which I'm aware. However, the FSC rules are based on the FSC level and not only on ownership. There are many asset managers with good broad-based statuses e.g. Level 2 or Level 3. B-B BEE is about a wide range of balanced scorecard measures.

The FSTC says that, if "sufficient disclosure" by pension funds does not materialise, then a revision of the voluntary dispensation will be considered. Some guidelines of "sufficient"? Some indications of possible revisions?

It's too early to comment. Now that the Batseta Council of Retirement Funds is a formal part of the FSTC, it would have to agree on compulsion. Decision-making at the FSTC is by consensus. ■

EDUCATION GUIDANCE

Previous *TT* editions have dealt with the FSC scorecard for trustee and consumer financial education.

For practical detail, retirement funds and service providers are referred specifically to the guidance note for criteria and measurement of this aspect. The note GN500 is available on the FSTC website.

IMPACT INVESTMENT

Capitalist manifesto

There's a revolution to be embraced. Sir Ronald Cohen* urges that the marriage of financial goals and social good be hastened.

The existing social contract has expired: we need to draw up a new one. Following the summer G20 summit in Hamburg, it is worth asking again how to address our most pressing global challenges.

Racked by rising inequality and human and environmental crises, capitalism as it exists today isn't delivering on its promises to increase prosperity and social progress for all. The gap between rich and poor grows every day. Meanwhile, the toll on our environment continues to rise – from climate change to deforestation and the pollution of our oceans.

The dominant model of capitalism practised today is more than two centuries old. Our problems have changed and so too must our response.

This moment calls for nothing short of a revolution, for a new approach that asks the question: how can we reach our financial goals while also doing measurable good? Cue the impact revolution.

Capitalism as we practise it is deeply flawed but not hopeless. When it comes to how we invest there is an exciting shift under way, one that takes current thinking about financial risk and return and adds a third dimension, impact, that measures positive outcomes for society and the environment.

Using this new financial model, social impact matters just as much as company earnings. This inspires us to maximise both profit and impact as normal levels of risk, to create the kind of world that everyone wants to live in. Together, we are reinventing modern finance and reshaping modern business.

The private sector is the cause of any number of social and environmental ills but it also fundamental to solving them.

Innovation, risk-taking, achieving scale and the dogged pursuit of measurable results – these are hallmarks of entrepreneurs and the private sector. They are also key to solving complex problems and enacting changes quickly and efficiently.

The tech revolution showed us what happens when private capital meets scrappy and disruptive entrepreneurs. It's time we took a page out of its book. By introducing impact, the risk-return-impact model brings out the best in entrepreneurs and the private sector in addressing our urgent social and environmental problems, which governments and philanthropists are unable to handle by themselves.

Valuing impact does not have to mean sacrificing profit. On the contrary, we can deliver high rates of return because of impact, rather than in spite of it.

The millennial generation is different from its forebears. Millennials want to do more than collect

Cohen . . . world authority

their pay. They genuinely care about doing good. They want to shop, work, launch companies and invest in ways that express their values. And investors, including large asset managers and pension funds, are moving in the same direction. Businesses are taking note. There isn't a boardroom on the planet where the subject of social impact hasn't come up.

If impact investing is our rocket-ship to social change, impact investing is our navigation system. We need to rethink it. For too long we have measured social impact in ways that are imprecise, inconsistent and incomparable.

Many people dismiss impact measurement as impossible. The truth is, we can measure social impact with greater accuracy and vigour than we do financial risk. We just need to be serious about doing it. The absence of measurement leads to a huge failure of our system to deliver social and environmental improvement, at great cost to the world.

Over the past 20 years, we have seen numerous initiatives to establish a standard for impact measurement. One of the most promising, advanced by the Global Steering Group for Impact Investment and the Impact Management Project, is to weight conventional financial accounts for impact. It involves applying coefficients to sales, employment costs, costs of goods sold – all the way down to the profit line – and doing the same for the balance sheet.

Impact-weighted financial accounts will allow for financial measurement and comparison by investors.

SA SUPPORT

Comments from Mabatho Seeiso, a professional trustee:

I heard Sir Ronald Cohen speak at a forum of the Industrial Development Corporation last November. In my opinion, he was the most powerful speaker of the day.

He gave me hope that we can fix the challenges we face in the SA economy, and the continent in general, if we integrate impact investing into our decision-making. On pension funds' boards the argument is too often heard that, as fiduciaries, we cannot expose our members to the risks of impact investing.

It helps to hear from someone like Sir Ronald, who has decades of experience across different continents, attest to impact investing not necessarily meaning lower returns. In fact, it can generate enhanced returns. Let us do the real work to understand impact investments rather than rely on generalisations that are often uninformed.

Innovation is required in our financial-engineering solutions. Many of our pension-fund members have given us a clear message that they want us to engage in impact investing in the interests of themselves and their children. We must invest in the real economy to stimulate growth, to develop an economy based on social justice.

Seeiso . . . highly impressed

I entirely agree that the new model of investment should be based on three pillars: risk, return and impact.

When every company publishes impact-weighted accounts alongside financial ones, impact will have assumed its place in investment and business decision-making.

We are seeing promising changes. Investors and businesses are becoming socially and environmentally conscious; impact entrepreneurs are gaining access to capital they need to bring brilliant, life-improving ideas to scale; governments are seeing the value in harnessing the innovation of the private sector, channelling its talent and capital to find better solutions to society's challenges; philanthropists are beginning to fund the delivery of measured outcomes.

It is time to accelerate these changes, and demand more.

The G20 leaders committed in their declaration to "endeavour to further create enabling conditions for resource mobilisation from public, private and multilateral resources, including innovative financial mechanisms and partnerships, such as impact investment".

Impact investing means evolving capitalist systems to build a better world, one that values social impact just as highly as profits. It means exposing the myth that social good comes at the expense of profit, and the accompanying myth that impact cannot be reliably measured and compared.

Ending the plight of billions of lives and the decline of our planet depends on our urgent, collective action. There is a way. There has never been a greater need or a better time than now.

** Cohen, a venture capitalist and first chairman of independent social-investment bank 'Big Society Capital', is widely published abroad. A prominent philanthropist, he is author of 'On Impact: A Guide for the Impact Revolution' and has advised the UK government.*

SHAREHOLDER ACTIVISM

A fine line

To what extent is collaboration permitted between asset managers, representing such asset owners as pension funds, without contravening the companies and competition regulations? Financial journalist Ann Crotty attempts to find out.

If you set out to design a system that would allow inept corporate executives to function unchecked by the owners of those companies, it would look a lot like the system we have. It wasn't intended to be this way.

On paper, major legislative changes over the past 20 years looked certain to enhance oversight and ensure better governance in the corporate sector. Those changes included the fundamental rewrite of the Companies Act, improved disclosures and a tougher competition regime. They pointed to a much more vigorous investment environment.

Yet practice has fallen short of promise. Powerful institutional shareholders appear to have sat on their hands while generously-paid executives weren't up their jobs at such erstwhile JSE stars as Barloworld and Edcon, Ellerines and JD Group. Even the once-great Woolworths is these days looking less great.

There are recent occasions when institutional shareholders acted to stop the slides, for example at PPC and Group 5. And a chastened Allan Gray moved adroitly to rein in the feral management at Net1 when things got really out of hand.

But by-and-large the institutions tend to prefer private one-on-one engagements to public confrontations. They're also nervous of being seen to assert their cumulative authority because of competition constraints. A block of like-minded shareholders with say 30% of a company, when knocking at the door of its board, would carry more clout acting together than each having small percentages acting individually.

A vigorous approach is all the more necessary given that the lack of liquidity in many companies' shares makes it difficult for institutions to offload large parcels when they're unhappy with the business or its management. They're essentially trapped. Of course, at a price, they could dump the shares and run as Coronation did quite spectacularly from African Bank in 2014.

The 2008 Companies Act of 2008, effective from 2011, appeared set to shake things up. It states as part

of its mission that "the law should protect shareholder rights, advance shareholder activism and provide enhanced protections for minority shareholders". These bolstered rights were supposed to introduce a fundamental shift in power to shareholders.

Unfortunately, exercising these rights requires the consent of the board. Ask activists such as Albie Cilliers or Chris Logan how easy that is. Even powerful institutional investors struggled against recalcitrant boards at PPC and Group 5.

And there certainly wasn't much sign of the enhanced rights' effectiveness when a group of shareholders got together in 2018 to try and appoint directors in a bid to halt the sharp decline at Grand Parade Investments. After a remarkably hostile shareholders' meeting in October, which was unilaterally abandoned by the board, the GPI activists had to await the annual general meeting to secure appointments of their two candidates.

Also last year, a group of powerful institutional shareholders was reduced to pleading with various boards of the Resilient group, urging them to resolve the allegations that had prevailed for several months. In the fourth letter, sent eight months after the initial allegations had already wiped out billions of rand in value, the shareholders said they believed "that the boards need to act more decisively in order to unambiguously address these concerns".

The tone was more 'Sunday school ma'am' than financial hitman. But this was evidently as far as asset-manager signatories (including the PIC, Allan Gray, Prudential, Sanlam, Stanlib, Investec, Old Mutual and Coronation) felt they could go. Even then, one signatory admitted to being extremely nervous about dispatching the letter.

> *The tone was more 'Sunday school ma'am' than financial hitman. But this was evidently as far as asset-manager signatories felt they could go.*

Notwithstanding the new Companies Act, after 16 years the 'Comparex case' still haunts many institutional investors. Back in 2003 the Securities Regulation Panel (forerunner to the Takeover Regulation Panel) had to rule on whether three asset managers – which together owned more than 35% of voting shares in JSE-listed Comparex – had acted in concert to reconstitute the Comparex board.

A shareholding of 35% being considered to represent control, the issue was whether the shareholders' joint action represented a change in Comparex control and so triggered an offer to minorities.

The SRP found that the three firms – Allan Gray, Coronation and Sanlam, joined by RMB group, bringing their total to almost 46% in various portfolios

– had not initiated an "affected transaction". They therefore did not have to make a mandatory offer for the buyout of Comparex minorities.

"We won the legal battle but we lost the war," recalls one. The institutions were unable trade their shares for the two years that the case dragged on. It was a public fight that absorbed substantial resources for minimal return, and for the two years the institutions faced the chilling prospect of making an offer for 100% of Comparex. This was a nightmarish set of circumstances for shareholder activism.

Now move on to March 2012 when, in an attempt to encourage activism, the UN-backed Principles for Responsible Investment body sought guidance from the Takeover Regulation Panel on the circumstances that would trigger a mandatory offer by institutions acting cooperatively.

The response from the TRP was vague. It indicated that there'd be no problems if the investors simply discuss matters of mutual interest or share their views relating to concerns about particular companies. "A concert party is only formed where shareholders agree a common plan under which to work together," said the PRI.

However, its guidance note elaborated that acting in concert doesn't automatically trigger a mandatory offer even if investors hold more than 35% ahead of any agreement. The critical issue is whether any additional shares were bought after agreeing to the action.

TRP deputy executive director Basil Mashabane says he can't recall, subsequent to promulgation of the new Companies Act, when any institutions acting in concert were forced to make a mandatory offer: "The panel would have to consider an allegation. Every case is different."

But it's no longer just the JSE-related regulators watching out. The institutions must also ensure their cross-shareholdings don't run afoul of the competition regulations.

Remarkably, the Competition Commission wasn't dragged into the Group 5 battle launched by Allan Gray which had significant stakes in other construction-sector stocks. The battle saw the Group 5 board being restructured in a move that could have flagged a change in control.

In the US, where the three biggest index funds (BlackRock, Vanguard and State Street) together constitute the largest shareholder in 88% of S&P 500 firms, authorities are concerned that firms are less likely to compete vigorously with each other if they have common owners. This is notable in the US banking and the airline industries.

In SA the trend might be in the opposite direction. Certainly, the number of major players has increased significantly since the 1980s when Old Mutual, Sanlam and Liberty dominated the investment landscape. In addition, the opening up of the economy has seen international investors holding upwards of 30% in several JSE-listed companies.

Despite this, amendments to the Competition Act require the Commission and Tribunal to consider the extent of cross-holdings in any merger. And, as in the battle over Sovereign Food, a board under siege from shareholders cooperating can always scuttle off to the commission with claims there's been a change in control.

Old Mutual Investment Group's governance and engagement manager Rob Lewenson says the PRI is seeking clarity on the scope for collaborative engagement within SA's competition law. Taking the Resilient matter, he's pleased with the outcome of engagement with the group companies and describes a complex cooperative process designed not to contravene regulations or antagonize the targeted boards.

It might need more than PRI guidance notes to persuade institutions to set aside their seemingly instinctive aversion to publicity and to risk relationships sustained behind closed doors. There's also an aversion to disclosing their hands to competitors, which is a precondition for cooperation.

Many SA asset managers are signatories to the PRI, as they are to the Code for Responsible Investing in SA. Both seek to promote shareholder activism. How better than if asset managers and asset owners, such as pension funds, cooperate ("collude" being such an ugly word) in the interests of their clients and beneficiaries without fear of consequence?

Roll on a test case. ■

GRAVY

Naheem Essop, analyst at the FSCA, breathed fire and brimstone at the annual conference of the Pension Lawyers Association. This new body, different from the old, would put a stop to the corruption that he considers prevalent in the retirement-fund industry. But a few observations:

- By not identifying the funds and service providers in the examples he cited, they couldn't defend themselves and the entire industry was tarnished;
- Hammering away on fund costs, nobody dared challenge him over the effect of government performance on investment returns that have a greater impact on member benefits;
- High time that the industry began to question whether the mounting levies paid by retirement funds (a component of their costs) provided value for money from the FSCA, just as it should have (but rarely did) from the FSB;
- It's a little rich to have a go at the private sector when revelations about the state-owned Public Investment Corporation, the largest service provider of all, are pouring from a sewer.

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Neither does it pass unnoticed that, much as the FSCA doesn't like the sponsorship by service providers of retirement-fund events, it itself isn't too averse to the practice.

See the FSCA's three-episode 'Insurance Apprentice' series. The episodes have been sponsored respectively by Emerald Africa, Aon and Marsh Africa.

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And back to the PIC, perhaps asleep at the wheel.

Each day, titles of Independent News & Media SA continue to be produced. Each day, therefore, the group's exposure to the PIC must compound.

Difficult as it is to imagine a SA without *The Star*, *Cape Times*, *Daily News* etc, more difficult is to imagine why the PIC allows publication to continue.

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George Herald, Jan 10

Only a Van could have produced something so multi-purpose.

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CalPers, the largest retirement fund in the world, is disinvesting from tobacco stocks. But it is climbing heavily into shares of companies that produce cannabis.

They're for buying, not for smoking. Or if for smoking, then not for inhaling.

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Onto the board of Sygnia has arrived former deputy finance minister Mcebisi Jonas, as an independent non-executive director, for annual remuneration of R1m. Also on the board is Prof Haroon Bhorat, non-exec chair, for R500k.

Well worth it, considering that Jonas also has experience as former PIC board chair.

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In his SONA address, President Cyril Ramaphosa announced a significant gas find off the Mossel Bay coast.

Funny that, before elections, the National Party government also used to announce a significant gas find off the Mossel Bay coast.

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A golfing buddy of Donald Trump told him of a fantastic dream he'd had. In it there was a huge parade, the biggest ever in Washington DC, with millions of people cheering along the route as Donald passed.

"That's really great!" said Donald. "The best! But tell me, how did I look? Was my hair okay?"

"Couldn't tell," replied the buddy. "The casket was closed." ■