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## FACULTY OF HUMANITIES

# Investigating the role of trade unions in pension fund investment: *A case of trade unions in South Africa*

A Research Paper Presented by

**Humphrey Fumpa**

**(517735)**

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Partial Fulfillment of the Requirement for Obtaining the Degree of:

Master of Arts in Labour Policies and Globalization

**Supervisor**

Professor Roger Southall

South Africa, February 2011

## Dedication

To my son Mwenya Fumpa

*"It's well past time to challenge the power of today's global capital – before it does any more damage to the lives of working people. Before it succeeds completely in putting a 21st Century face on the Robber Baron values of yesteryear*

*Globalization is the driving force behind this New Age of Robber Barons.*

*It has revolutionized the way business is done – and the way workers' aspirations are dealt with – if dealt with at all.*

*The growing power of global corporations is all around us. We see it in the glut of corporate buyouts in every industry from aluminum to mining, from paper to steel, and many more.*

*But there's a revolution happening right under our noses that's not so easy to see:*

*I'm talking about the growth of finance as the dominant economic force in industrial societies like ours. Today, finance rules the world. Today, finances' share of the nation's Gross Domestic Product is twice as much as manufacturing.*

*And finances' share of corporate profits is nearly five times as great as manufacturing.*
*As a result, today's Robber Barons of Bay Street and Wall Street are reaping billions through reckless financing schemes…*

*While working people keep getting pushed farther and farther down the economic food chain.*
*They've done it by deregulating everything from finance to labour law and creating one Ponzi scheme after another.*

*We're not only being challenged by employers who want to .....rob us of our pensions.*

*Sisters and brothers, seize this moment to rekindle the hope we have for a better future. Our kids and grand kids, our families, our communities and our planet are all counting on us,*

*Sister and brothers, their hopes and dreams are a cause worth fighting for. We must not falter. We must not fail.*

*Seize the moment – now is the time! NOW IS OUR TIME"*

(Leo W. Gerard[i] Keynote Address, "Seize the Moment - This Is Our Time!" June 30, 2008)

# Declaration

The present thesis entitled "**Investigating the role of trade unions in pension fund investment:** ***A case of trade unions in South Africa***" was carried out by me at the University of the Witwatersrand, Johannesburg. Further, I declare that no part of the thesis has been submitted either in part or whole for any degree to the University of the Witwatersrand, Johannesburg or any other university**.**

**----------**

Humphrey Fumpa

February, 2011

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Undertaking a Master of Arts (M.A) degree in Globalization and Labour Policy at the University of the Witwatersrand, Johannesburg, was an exciting and challenging expedition. I would like to acknowledge all those individuals who encouraged me to persevere from all GLU 2010 staff and participants.

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This study would not have materialized had it not been for the financial support of the International Labour Organisation (ILO) and other Global Labour University (GLU) partners. Indeed, the knowledge and experience gained will benefit the noble cause of labour.

My sincerest thanks go to Mr. Darison Chaala, Grayson Koyi, Adrian Shikwe, Joseph Mwansa, Joseph Simbaya and Crispin Somali. I extend my profound gratitude to my wife Bwafya and our son Mwenya for their sacrifice. To Faith and Pulani, 2010 GLU Programme Coordinators, thank you for being there for us and for making our stay bearable. I remain indebted to all those individuals and institutions involved in the study who have not been mentioned here.

Finally, I remain responsible for the views expressed in this paper and deficiencies that may have remained in it.

*Humphrey Fumpa*

**Johannesburg, February, 2011**

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## List of Acronyms and Abbreviations

| | |
|---|---|
| AFL-CIO | American Federation of Labour – Congress of Industrial organizations |
| ANC | African National Congress |
| AZGI | Allianz Global Investors |
| BEE | Black Economic Empowerment |
| CalPERS | California Public Employees' Retirement System |
| CEPPWAWU | Chemical, Energy, Paper, Printing, Wood and Allied Workers Union |
| CLC | Canadian Labour Council |
| COSATU | Congress of South African Trade Unions |
| CRISA | Committee on Responsible Investing by Institutional Investors |
| ESG | Environmental Social and Governance |
| ETI | Economically Targeted Investment |
| FEDUSA | Federation of Unions of South Africa |
| FSB | Financial Service Board |
| GDP | Gloss Domestic Product |
| GEAR | Growth, Employment and Redistribution |
| GEPF | Government Employees Pension Fund |
| GLU | Global Labour University |
| ILO | International Labour Organization |
| LBOs | Leverage Buy-Outs |
| MEPF | Mine Employees Pension Fund |
| MIBFA | Metal Industries Benefit Funds Administrators |
| NEHAWU | National Education, Health Workers Union |
| NFC | Non Financial Corporations |
| NUM | National Union of Mines |
| NUMSA | National Union of Metal Workers of South Africa |
| OECD | Organization for Economic Corporation and Development |
| OPSEU | Ontario Public Service Employees' Union |
| PE | Private Equity |
| PIC | Public Investment Corporation |
| RDP | Reconstruction and Development Programme |
| SHARE | Shareholder Action and Education |
| SRI | Social Responsible Investment |
| TMT | Technology, Media and Telecoms |
| TUAC | Trade Union Advisory Council |
| TUC | Trade Union Congress |

## Abstract

South African pension fund assets are estimated at ZAR 1 924 billion. This is a large pool of funds that is collected from workers. However, the contention is that workers, whose savings make up the assets of pension funds have little influence on how these funds are used. As a result, most of the funds are invested in corporations, which do not reflect the aspirations of the labour movement. The argument is that if these funds were under the control and direction of the working class, enormous contributions would be made towards economic growth, socially useful investments, community development, employment creation and growth in retirement benefits. The purpose of this study was to assess the extent to which trade unions have been able to promote the interest of members and direct pension fund investment in sectors that will have a positive impact on working families and their communities in South Africa. This study adopted a qualitative method, using purposive sampling and a semi-structured outline to conduct face-to-face interviews with union unions and fund managers. Collected data were analyzed using content analysis. Results were categorized into two distinct parts. The first part looked at pension fund investment regulation and management, asset allocation, investment practices and composition of the pension board. The second part described trade unions' role in promoting the interest of pension fund members; the extent of their influence in pension fund investments; their contribution to strengthening pension fund governance and how to enhance their influence and control of pension fund investments. The study suggests that trade unions have a critical role to play in pension fund management through their representation on the pension boards. However, the success can only be achieved if trade unions have a clear policy that spells out labour's agenda on pension issues. Additionally, union trustees should be supported to getting involved in understanding their plans and develop capacities in capital market strategies, investment and economic development.

# Chapter One – Introduction to the study

## 1.1 Introduction

The South African pension industry controls a large pool of funds that are collected from workers' earnings. In 2008, the total assets of the retirement fund industry were estimated at R1 924 billion. This was 0.7 percent decrease from R1 938 billion in 2007. The net assets of privately administered funds decreased by 5.4 percent, from R950 billion in 2007 to R898 billion in 2008, even though the total contributions received by retirement funds increased by 8.6 percent, from R91.1 billion in 2007 to R99 billion in 2008 (Registrar of Pension Funds, Annual Report 2010). These funds provide a major source of investment capital in the South African economy and own substantial stakes in a number of companies (COSATU, 1997).

The pension fund industry is presently dominated by the private sector, making business' agenda more dominant (Pillay, 2003). Most of the funds are invested in corporations, which do not reflect the aspirations of the labour movement. Therefore, workers, whose savings make up the assets of pension funds remain silent regarding the behaviour and practices of the companies that they own shares in. The net effect of this situation is passive ownership (NALEDI Policy Bulletin, August 2002).

According to Naidoo (2003), the South African economy suffers from insufficient investment in productive activities (from 25 percent of GDP in 1981 to 14.7 percent in 2001). He attributes this

low level of investment to the massive outflow of capital. If pension funds were under the control and direction of the working class, enormous contributions would be made towards economic growth, socially useful investments, community development, employment creation and growth in retirement benefits (COSATU, 1999).

Experiences of trade unions in Canada and the United States have shown the important gains resulting from involvement in pension fund investment management. In particular, they have been able to achieve reforms of corporate governance; ensure that companies recognise their social responsibilities; and direct capital to areas of the economy that traditional institutional investment have failed to serve properly (Trade Union Congress, 2003). However, with respect to how the funds are invested in South Africa, it is not clear as to what extent the labour movement has been able to protect these "deferred wages" and influence investments in generating real productive activities and jobs.

This is a case study of three South African trade union, that is National Union of Mines (NUM), National Union of Metal Workers of South Africa (NUMSA) and National Education, Health Workers Union (NEHAWU) to try to investigate the extent to which they have been able to protect the interest of members and the broader social interest of the labour movement such as strengthening corporate governance in the pension industry; and to use enterprises' profits in the social sector for the benefit of workers and communities.

## 1.2 Background to the Study

The background to the study is motivated along the framework of Fung, Hebb and Rogers who argue that the traditional role of trade unions of only bargaining for labour rights is rapidly changing to include issues related to workers' strategy for capital (Fung, Hebb and Rogers, 2001). In light of this, Wheeler (2002) identifies a number of strategies involving the power of workers' capital that are currently being pursued by some trade unions in North America and Western Europe. Firstly, *producer cooperatives* that promote the principle of worker ownership of the means of production. According to Wheeler, "the fundamental logic of cooperatives turns capitalism on its head" (2002: 7), as labour will hire capital and not the other way round. The rationale behind idea of cooperatives is to ensure that there is an equal distribution of workers output among themselves (Wheeler 2002).

Secondly, *worker ownership in shares of their own company.* In many employee-owned companies employee shareholders have opportunities to influence the policies of their employer, especially in the area of corporate governance (Wheeler, 2002). According to Piñera "the world would be a better place if every worker were also an owner of capital" (2001: 1). Since their interests "would be more in line with the interests of those who manage and control those assets, there would be less inequality of wealth, and workers would place a higher value on strong property rights and the rule of law" (Pinera, 2001: 1). Third, *union funds for economic development* – this strategy is about putting unions' funds together for economic development. These funds are part of employees' retirement funds that are mobilized to establish the worker

owned enterprises (Wheeler, 2002: 11). Fourth, *influence through worker pensions funds.* Trade unions have been using the power of workers pension to influence corporate policy by encouraging worker pension funds to engage in social responsible investments (Wheeler, 2002: 10).

These four workers' capital strategies highlight future areas of growth for the revitalization of the labour movement. The focus of this study was on how the trade union movement in South Africa has been able to use pension fund capital in shaping the economy to the benefit of the workers and their communities. According to Croft and Hebb, "this shift in the labour movement to become stronger stewards of its retirement assets has come at a critical time, within the gravitational pull of the progressive new role of the labour movement" (2002: 6) in the globalised world. Bennett and Johnson argue that

> Those who control pension fund assets already wield a tremendous economic power which is rapidly increasing. The allocation of fund assets will greatly influence the direction of economic activity in the years to come; union control of such economic power would greatly enhance the ability of labour unions to achieve their economic and political objectives (1981: 187).

A similar conclusion is reached by an Ontario Public Service Employees' Union (OPSEU) policy paper on pension with respect to union appointed trustees and sponsors for jointly trusted plans:

> Where there is no union control of the pension fund, unions are defenceless in preventing their members' deferred wages from being used against their interests and, ultimately, the interest of the pension fund itself (OPSEU, 2002: 7).

Whatever the specific constraints and motives, it appears that fundamental changes have occurred in the management of pension funds. Consequently, monopolistic control of pension plans by employers has given way to joint trusteeship in most of the funds; investment practices that seemed to serve only the interest of employers and whose returns were well below markets rates have equally been challenged. The argument is that these investments practices did not provide a sustainable fund in the long-run (OPSEU, 2002). Therefore, union representation on pension board of trustees will to some extent protect pensions against the "practices that caused the chronic underfunding of retirement benefits such as contribution holidays, borrowing from the pension fund at low interest" (Verma and Weststar, 2011). Additionally, there is greater role for pension funds in bringing about broader social benefits by sustainably investing in workers and their communities through alternative investment such as the socially responsible investment and economically targeted investment (Verma and Weststar, 2011).

In South Africa, the idea of empowering the working class has been at the centre of the struggle of the trade union movement, given the legacy of apartheid. However, COSATU has become critical of government's black economic empowerment (BEE) strategy and the implementation

of the Growth, Employment and Redistribution (GEAR) strategy. The contention is that GEAR "was an inappropriate growth model for the South African economy", as it "focused not on the interests of the majority, but on the selfish short-term interests of certain sections of business" (Southall, n.d: 1) and that "the pursuit of BEE should be located in a much more extensively transformative programme of worker and popular empowerment" (Southall, n.d: 2).

The control of pension funds, therefore, presents an opportunity for unions to change the current economic configuration in South Africa. With regard to the unions exerting influence over pension funds, however, the legislation requiring at least 50 percent worker representation on the board of trustees has been secured. This provides labour trustees with an opportunity to exert active influence over the companies in which the retirement funds are invested, with the aim of investing in activities that provide workers with "collateral benefits" such as "jobs, affordable housing, local development, the promotion of local businesses, and a range of other economic and social priorities" (Carmichael and Quarter, 2003: 10).

### 1.3 Statement of the Research Problem

The problem being investigated in the present study is how trade unions have been able to promote the interest of pension fund members and the broader social interest of the labour movement such as social investments and the promotion of human and labour rights. Spelled out in the amendments to the Pensions Fund Act in 1996, members of retirement funds have the right to elect representatives onto the boards of their respective funds. With worker elected

representative comprising least 50 percent of the board of trustees, it is argued that they will be able to protect the entitlements of future pensioners and guarantee adequacy of benefits (Gifford, 2004).

If it is indeed the case that trade union participation in pension fund investment do enhance sound investment policies, it is expected that pension fund members would receive good retirement incomes and living in a clean, safe and secure world. The study asks whether indeed the participation of labour trustees on the pension fund boards in South Africa has made the unions' role effective and relevant in the management of pension funds. Accordingly, the research problem is formulated as follows: *investigate the extent to which trade unions have been able to promote the interest of members and direct pension fund investments in sectors that would contribute to the betterment of working families and their communities in South Africa, and thus understand what would constitute sustainable strategies for the trade unions in future.*

## 1.4 Research Objectives

The main purpose of the study is to assess the extent to which trade unions have been able to promote the interest of members through pension fund investment management in South Africa so as to recommend ways of enhancing their influence that will have a positive impact on working families and their communities. More specifically, this study intends to answer the following questions;

i) To what extent have trade unions been able to promote the interest of members and direct pension fund investments in sectors that contribute to the betterment of working families and communities in South Africa?

ii) What contributions have trade unions made in strengthening corporate governance in South Africa?

iii) What strategies would enhance trade union influence and control of pension fund investments in future?

## 1.5 Justification and Significance of the Study

While some partial studies on developed countries have generally recognized that unions have gained greater control of the investment of pension funds; and are on the verge of developing more innovative investment approaches with goals of job creation, community development, corporate governance and long-term view of value (see for instance: Carmichael, 2003 and 2005), very little is known about the extent to which trade unions have been able to promote the interest of members and influence pension fund investment in social sector for the benefit of their families and communities in South Africa. This study, therefore, responds to a felt need. Firstly, it fills the knowledge gap in the existing literature on trade unions and pension fund management in South Africa. Second, it attempts to suggest strategies for appropriate trade

union responses, and thirdly, it provides a basis for further research in this direction as it is consistent with a global revival of interest in the role of trade unions in a global era.

## 1.6 Scope and Limitation of the Study

A comprehensive study into pension fund investment and trade unions is a mammoth task requiring time and resources beyond what is currently available. This study is restricted to analyzing aspects of pension fund investment that have a direct bearing on trade unions. The main limitations was that, even though the study is on trade unions in South Africa, it is focusing on three trade unions, introducing a practical difficulty of generalizing of the findings. Even with this limitation, however, the study offers some very useful insights into the phenomenon of pension fund investment and the role of trade unions that can inform critical debates on the subject as well as advise sustainable strategies for trade unions in the future.

## 1.7 Organization of the Study

This introductory chapter has flagged-off key themes explored in the study and has outlined the research problem and objectives motivating the study. Chapter 2 presents theoretical and empirical literature on pension fund investment and the role of trade unions. The third chapter looks at the methodology used in answering the research question. In chapter 4, the characteristic of the pension industry in South Africa is presented and the change in structure,

management and governance issues over the last decade examined. Chapter 5 presents data on the role of trade unions in pension fund investment management and explores the question of the extent to which trade unions are able to promote and protect the interest of the members and direct pension fund investments in sectors that contribute to the betterment of working families and communities in South Africa. Chapter 6 synthesizes the findings of the study in relation to the research questions and links the results to the conceptual and analytical infrastructure discussed in chapter two. It also proposes sustainable strategies for trade unions in the future. Chapter 7 is a summation of the study.

# Chapter Two – Literature Review

## 2.1 Introduction

This chapter reviews theoretical and empirical literature on pension fund investment management and the role of trade unions. It is organized into five main sections. Section 2 provides an overview of pension funds, paying attention to the growth of assets; and their importance in the financial market. The third section looks at the investment of pension funds. The motivation is to provide an analysis of pension fund investment practices and their impact on the working population (as owners of capital) and society. Section 4 will focus on pension fund governance. This is to give the reader an understanding of the general principles of good governance with the focus on accountability, transparency and socially responsible investment, and understanding why this is critical to the trade unions and other stakeholders in the global era. The fourth section will describe the role of trade unions in pension fund management with a focus on the challenges facing trustee in influencing pension fund investment management. Section 5 will point out key issues from the literature reviewed and their implications for the study.

## 2.2 Overview of pension funds

Simply defined, pension funds are savings of workers that will provide them with an income replacement upon retirement. As a form of institutional investment, these collected funds are

invested to provide for the future pension entitlements to beneficiaries (Davis, 1995; OPSEU[ii] Policy Statement 2002). According to Davis (1995), pension funds provide means for individuals to accumulate saving over their working life so as to finance their consumption needs in retirement. In other words, they are deferred wages that employed workers earn while they are working but are paid upon retirement (OPSEU Policy Statement (2002.): 4). In addition to supplying income upon retirement, pension funds have been a source of capital for corporations, governments for investment or consumption and households at both national and international level.

One important point to note is the rapid growth in pension fund assets over the past decade (Simpson, 2001). For example, the figures from OECD members show that the financial assets of pension funds have grown from US$5.9 trillion in 1994 to US$15.6 trillion by 2004 and further to US$ 18.7 trillion in 2007, before the financial crisis (OECD Observer 2004; OECD 2010). Similarly, the Global Pension Asset Study 2010 shows that global pension fund assets have increased to over US$23 trillion in 2009. These assets amount to 70 percent of the average global GDP (Towers Watson, 2010). Table 1 below illustrates the pension fund assets as a share of GDP in selected countries for the period 2001 – 2009.

**Table 1: Pension Fund Assets as a Share of GDP in selected countries 2001 - 2009**

| Country | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|---|---|---|---|---|---|---|---|---|---|
| Australia | 75.29 | 70.42 | 68.87 | 71.59 | 80.38 | 90.40 | 110.36 | 93.01 | 82.26 |
| Canada | 52.48 | 48.30 | 51.59 | 53.92 | 58.15 | 63.36 | 62.33 | 51.43 | 62.93 |
| Chile | .. | 55.07 | 58.16 | 59.08 | 59.35 | 61.01 | 64.43 | 52.77 | 65.12 |
| Denmark | 27.19 | 26.01 | 28.48 | 30.76 | 33.71 | 32.43 | 32.36 | 47.55 | 43.26 |
| Finland | 49.48 | 49.18 | 53.86 | 61.84 | 68.61 | 71.33 | 71.05 | 60.56 | 76.77 |
| Iceland | 83.97 | 83.90 | 98.26 | 106.60 | 119.58 | 129.73 | 133.97 | 114.05 | 118.30 |
| Ireland | 43.74 | 34.41 | 39.77 | 41.98 | 48.26 | 50.22 | 46.62 | 34.14 | 44.15 |
| Netherlands | 102.62 | 85.50 | 101.19 | 108.12 | 121.73 | 125.74 | 138.05 | 112.72 | 129.86 |
| Switzerland | 102.46 | 95.92 | 102.87 | 107.24 | 117.03 | 119.97 | 119.18 | 101.15 | .. |
| United Kingdom | 72.00 | 58.77 | 64.35 | 67.61 | 78.63 | 83.43 | 78.91 | 64.30 | .. |
| United States | 71.52 | 63.21 | 72.57 | 74.01 | 74.84 | 79.33 | 79.41 | 57.93 | 67.70 |

Source: OECD Stat, 2010

The growth in pension funds as observed above can be attributed to the growth of assets in many advanced markets (US and Japan, together account for more than 70 percent of total assets) (Tower Watson, 2010). Another observable trend over this period is the growing importance of equity investment within the portfolios of pension fund investors (Simpson, 2001). For instance, for over 20 years, the funds allocation to equity stayed close to the 30 percent mark. By 1998 the allocation had moved towards 50 percent of portfolio (Simpson, 2001). With these trends, it is no doubt that pension funds are becoming the leading owners of equity in many markets.

Some commentators contend that workers, whose deferred wages make up the assets of pension funds, and their unions, have little say in the management of pension funds and investment

strategies (OPSEU Policy statement, 2002). Instead, they are controlled by a “pension industry complex”, which is made up of “fund managers, employer intermediaries, consultants and advisors, lawyers and actuaries” (Croft and Hebb, 2002: 14). In other words, “an intricate web of financial and legal standards such as fiduciary responsibility” (OPSEU Policy statement, 2002: 3). Clark (2000) provides an insight into the evolving nature of pension funds and the role they play in today’s financial system. He points out that, the current stage of capitalism is dominated by pension funds who represent broad share ownership, but who are in fact single industry players whose very presence in the market dwarfs and dominates the financial system.

Stafford (1987), asserts that those who control pension fund assets already wield a tremendous economic power, which is still increasing rapidly. He stressed that the allocation of fund assets will greatly influence the direction of economic activity in the years to come. It is clear that to control pension funds is to have power over large sums of money flows (Hayden, 1989: 1032). As suggested by Bennett and Johnson (1981), unions' ability to command such economic power would greatly enhance their ability to achieve their economic and political objectives.

Stafford (1987), explains that how such a large amount of what is called "deferred wages" came to be in the hands of capital and used to further its interest is very important to labour. According to Stafford, these funds have been used in developing new technologies, which have been replacing workers. He points out that the funds are used to finance the movement of capital into regions of lower wage rates, causing the displacement of workers in established industrial regions. This observation in the function of pension funds suggests that labour's wages are being

used against their interests (Stafford 1987). Therefore, how these funds are invested is very important to the labour movement.

## 2.3 Investment of pension funds

As pension funds increase in size, most financial institutions have hired fund managers to manage the investments (Stafford, 1987). As a highly competitive business, a large number of firms are fighting for contracts to manage these portfolios (Crotty, 2004: 12) According to Stafford, this has put great pressure on fund managers, creating conditions under which they are now directing funds into riskier operations in the hope of gaining higher returns and thus retaining their contracts and attracting more clients (Stafford, 1987).

According to Chandrasekhar, increasing financial liberalization following neoliberal era brought significant transformation in the financial market in the 1980s (Chandrasekhar, 2007). This has been necessitated by globalization, that is, "a process that seeks to create a single global market operating according to universal rules driven primarily by the needs of multinational corporations" (Naidoo, 2002: 1), including financial industry. For Naidoo, it is important for labour to discuss the economic dimension of globalization they embark on advocating employee ownership, which include control of pension funds. He argued that economic dimension has the "biggest impact on levels of poverty and on the ability of the poor to influence economic changes" (Naidoo, 2002: 1).

Chandrasekhar (2007) pointed out that there is an increasing desire by pension funds and financial investors to find new avenues for their growing resources. Citing OECD reports of 2001 and 2003, Chandrasekhar demonstrates an increase in pension fund in the US from US$ 786 billion in 1980 to US$ 1.8 trillion in 1985, US$ 2.7 trillion in 1990, US$ 4.8 trillion in 1995, US$ 7.4 trillion in 2000 and US$ 8 trillion in 2004 (Chandrasekhar, 2007: 2). According Chandrasekhar, resources of this magnitude accumulating at this rate forces financial investors to seek new areas if investment that would give them adequate returns to meet their obligations (2007: 2). For instance, as Politi and Guerrera (2006), cited in Chandrasekhar (2007: 2), point out, pension funds' exposure to private equity (PE) has increased over the decade averaging 8 percent of their funds in this asset class.

The other significant development has been related to the relaxation of rules and regulations relating to investments that could be undertaken by institutional investors. For instance, the Competition and Credit Control policy in the UK and the amendment to the Employee Retirement Income Security Act of 1974 in the US relaxed the limitations placed on institutional investors and gave them greater investment flexibility (Chandrasekhar, 2007: 3; Lazonick and O'Sullivan, 2000: 17). As a result, there was an increase in demand for other risky securities like "junk" bonds created by Michael Milken at Drexel, Burnham, Lambert that would deliver quick results (Crotty, 2004: 11; Lazonick and O'Sullivan, 2000: 17). According to Crotty, this became "a viable source of debt finance for virtually any hostile takeover, even of long-established giant firms" (Crotty, 2004: 11).

The proliferation of private equity firms should be of great concern to the labour movement. As Chandrasekhar explains, private equity is acquired either through the private placement of new shares or the sale of pre-existing shares by the controlling interest, and therefore has features that characterize most takeovers (Chandrasekhar, 2007: 1). It is important to note that banks and pension funds account for a significant share of the total capital raised by private equity. For instance, of the total of Euro 161.3 billion raised between 1998 and 2002, banks, pension funds and insurance companies accounted for 58 percent of the commitment in Europe (Chandrasekhar, 2007: 4). Doubtless, similar trends could be observed elsewhere.

The presence and activity of private equity firms have continued to increase. Quoting estimates by Thomson Financial, 2006 was a record year for private equity in both fundraising and investments. 684 PE funds raised a record US$ 432 billion worldwide in 2006, led by Buyout and Real Estate funds with US$ 213 billion and US$ 63 billion respectively. The total value of announced private equity buyout deals hit a record US$ 700 billion in 2006, more than double the record set in 2005 and 20 times bigger than in 1996 (Metrics 2.0, 2007). Clearly, private equity expansion is very strong. According to Preqin, an investor services company, the number of PE firms looking to invest increased to an all-time high of 4,270 in 2009, more than three times as many as there were a decade earlier. Broadening the PE universe to include firms that do not manage or invest out of distinct private equity funds, the total rises to approximately 6,000 (Barn and Company, 2010). In terms of capital that was available for the industry to deploy at year-end 2009, Barn and Company (2010) estimates totaled more than US$ 1 trillion—about three times the amount available at the end of the 200. This is the amount of capital that

was committed but not yet invested. That capital is available for investment across asset classes: US$ 508 billion waiting to be used in buyouts, US$ 159 billion earmarked for venture capital. Real estate assets acquisition would gobble US$ 188 billion. According to Barn and Company, that amount was “prodigious” (p. 20). In other words it was “unmatched”.

As Chandrasekhar (2007) suggested, it is this increased presence and activity of private equity firms that has been a source of contention, especially with the hostile takeovers of the 1980s through leveraged buy-outs (LBOs). The classic example was the $25 billion buyout of RJR Nabisco in 1989. According to Croft and Hebb, what was interesting about this case was that the Oregon Teacher’s Fund helped finance the record buyout. It was considered a disaster and misguided commercial transaction, which resulted in thousands of layoffs (Croft and Hebb, 2002). Central to Croft and Hebb analysis was that worker’s own savings were a principal source of this disruptive restructuring.

These kinds of investment, and the changes in the financial market facilitated by the neoliberal regime, have had adverse effects on economic development and labour. According to Joseph Schumpeter and Alfred Chandler (cited in Crotty, 2004: 2), nonfinancial corporations (NFCs) have been the main source of most of the capital investment, technological change and productivity growth during this period and for most of the twentieth century’s achievements in the United States. For instance, hundreds of thousands of people were employed by only a small number of giant corporations, in the United Stated (Lazonick and O’Sullivan 2000). According Lazonick and O’Sullivan huge revenues generated by these corporations were allocated

according to a corporate governance principle called “retain and invest”. This implied that corporation would retain both the revenues realized and the workers, and reinvest in “physical capital and complementary human resources” (Lazonick and O’Sullivan 2000: 14). As Lazonick and O’Sullivan posit, this retentions provided financial foundation for corporate growth.

However, as Crotty (2004) explains, neoliberalism came with a slowdown in the rate of global aggregate demand growth and increased competition in many product markets; and a shift from long-term growth to impatient short-term financial markets. Crotty goes a step further and asserts that the combined effects of these changes forced management in many firms to switch from the long-term goals and “high-road” labour relations to short-term “survivalist” strategies that involved attacks on labour and on key firm suppliers (Crotty, 2004: 2).

For example, during the 1980s and 1990s the US corporations witnessed strategic shift away from ‘retain and reinvest’ towards downsize and distribute’ (Lazonick and O’Sullivan 2000). As a result, the labour force in most major US corporations since the 1980s had eroded the quantity of jobs that offered stable employment and real pay. The loss of employment also meant weakening the trade unions, who were supposed to be defending the interests of the same employees. The effect was a further deterioration in the conditions of work and living standards.

For those who had lost employment, the chances were that they would not find employment anytime soon. If they managed to find it, the income in most cases was less than what they were getting in their previous job. This brought about insecurity among employees in terms of fear of

losing a job. There was also a growing income inequality as top management received more than workers. This was because their rewards were now linked to the rise in stock prices. Thus, the higher the price, the more management's rewards went up. Lazonick and O'Sullivan (2000) report that job security measured with the proxy of change in job tenure was on the decline and it varied based on gender and the age of workers. The change in job tenure also had had effect on the social security for employees as its precarious nature now affected the pension – accrued and legibility.

Simpson reports that largest pension funds across the globe have rapidly increased their exposure to overseas equity (2001). For example, in 1998, the 200 largest US pension funds held close to US$ 300 billion of assets in their international portfolio. According to Simpson, the California Public Employees' Retirement System (CalPERS), the nation's largest public pension fund in the US with total net assets of $181.1 billion, made a decision to shift overseas allocation from 12 percent to 20 percent of their assets in order to diversify and capture the benefits of high potential growth rate in overseas markets. This shift was facilitated by liberalisation in regulatory rules, for example, in the UK, where pension funds on average now hold 25 percent of their equity assets abroad. The net result of these trends is that financial flows to developing and emerging markets in the past decade have grown dramatically (Simpson, 2001).

## 2.4 Pension Fund Governance

The pension fund growth in assets and equity holdings has been phenomenal. However, as Simpson posits, there are a number of features relating to the structure of pension funds which give them an important role to play in the corporate governance of the companies whose equity they own. She asserts that pension funds invest assets to cover relatively long term liabilities. Therefore, the investment horizon is denominated in decades. Accordingly, pension funds should have an interest in the long term performance of their assets. In equity terms, this means the long term performance of companies (Simpson, 2001).

According to Clark and Hebb (2003), following the collapse of the technology, media and telecoms (TMT) stock bubble in 2000 and the subsequent corporate governance scandals of 2001 and 2002, higher standards of accountability, transparency, and social and environmental behaviour are all receiving more attention from pension fund investors in the post-Enron, post-WorldCom business environment. According to the Trade Union Advisory Committee (TUAC) discussion paper, the Enron scandal, wiped out over 6,000 jobs and attendant health care and retirement savings overnight. As TUAC discussion paper reports, the scandal also took with it Arthur Andersen, one of the world's biggest auditing and business services firms. For Kenneth Lay, Enron's CEO, received a salary in 2000 of US$ 53 million, along with US$ 123 million of exercised stock options and a further US$ 361 million in unexercised stock options (TUAC, 2005).

As if that was not enough, TUAC discussion paper report that, at a time when workers were suffering real cuts in wages, health care benefits and pension provisions, a CEO earned 40 times the average wage of the company's workers in 1980, or now earns around 530 times that in the US (TUAC, 2005). It is these issues that are an irony for trade unions. How do they defend and promote the interest of their members?

TUAC discussion paper attributes the breakdown in corporate governance to "a failure of public policy – the implementation by governments and regulatory authorities of flawed systems of corporate governance and accountability that fail to stop the looting of companies by their elites" (TUAC, 2005: 2)

The collapse in corporate governance can be traced back to the shareholders regaining some control over management through the prism of "maximising share value" in the 1970s and 1980s (TUAC, 2005). The rationale was that management was not acting in the interest of the shareholders. Therefore, there was need to rectify this assumed normally and ensure that managers were accountable to the shareholders. During the 1990s, the emergence of shareholder activism witnessed the growing importance of institutional investors, like pension funds.

According to TUAC discussion paper, the rise of the shareholder value model was facilitated by institutional investors who then became pre-eminent capital market players. Among them were pension funds, which saw their assets rise with a portfolio mix that has shifted towards equities – increasingly foreign, and in ever riskier emerging markets as noted above (TUAC, 2005).

TUAC discussion paper explains that the institutional investors have for a long time delegated their investment policy to asset managers, whose interests lie in short-term profits, not in the long-term interests of their beneficiaries, which are determined by the structure and components of their fees. Accordingly, without proper regulation and market incentives, the needs of the ultimate owners of collective investment schemes, workers and households, have become secondary to the needs of the financial investment industry itself (TUAC, 2005).

As TUAC discussion paper points out, institutional investors' interest lies not in the sustainability of the investments, but in short-term financial returns. Others argue that pension fund managers' tendency toward short-term investment stands in direct contradiction to the long investment period necessary to realize gains from high standards of corporate behaviour (Clark and Hebb, 2003). The only remedy to this problem is the workers' pension fund trustees.

TUAC discussion paper highlights how trade unions in other countries are promoting their members' rights as shareholders to have a voice in corporate decision-making and, more broadly, to bring about good corporate governance regimes in those companies where their pension funds hold equity. The aim of such campaigns is to secure high levels of retirement income, while ensuring that the deferred income is invested in sustainable corporations (TUAC, 2005). Citing the USA, Canada and the UK, the AFL-CIO, the CLC, the TUAC respectively have committed substantial resources to mobilize "workers' capital" behind corporate governance reforms, and are increasingly influencing the pension fund industry, especially through their trustee networks

(TUAC, 2005). This is a big lesson for other trade union internationally, who are fighting for the same cause.

Practical steps in mobilizing workers' capital as proposed by TUAC discussion paper include educating union and other worker trustees of such funds to use their leverage to change the behaviour of pension fund managers. According to TUAC discussion paper, the union leadership can also engage the investment managers of these funds while seeking regulatory changes to empower the trustees and the relevant funds. A number of successes have been registered, notably concerning the remuneration policy of the board of directors, the separation of the CEO and Chair of the board, the promotion of non-executive directors who are "independent" from management, and respect for workers' rights. The AFL-CIO and its affiliates are now the leading US organizations filing proxy resolutions at AGM meetings (TUAC, 2005).

## 2.5 Trade Unions and Pension Fund Management

Pension plans have always been a concern for the labour movement (Freeman, 1983). According to Freeman (1983), the earliest pension plans for blue—collar workers were originated by the labour movement. Cook reports that "the first truly union-sponsored pension plan appears to have been that founded by the Pattern Makers League of North America in 1890", even though "that plan never paid benefits" (2002: 29). According to Munnel (1982:9), the Granite Cutters' International Association of America established the first functional union old - age plan in 1905. However, Lateimer (1932) cited to Cook (2002) points to the International Typographical Union

as the first large union to create a regular pension plan in 1907. The motivation of these efforts by early trade unions was to improve the hardships of workers (Cook, 2002).

In recent years, unions have expanded the scope on pension issues from worker benefits to how pension fund money is being used in the capital market (Freeman, 1983). In his examination of the role of trade unions in pension coverage; expenditures by firms for pensions; the provisions of pension plans and; pension fund investments, one of Freeman's basic findings was that unions greatly increase pension coverage, and alter the determinants of coverage, in ways that go beyond the tradition role of trade unions of bargaining better wages and improved working conditions (Freeman, 1983).

Similarly, Calvert (2005) highlights four reasons why trade unions are seeking joint control of pension fund management as; i) to be able to deal with administrative issues so as to ensure that concerns of plan members and beneficiaries are handle fairly and promptly; ii) to determine the design of pension benefits, including the priority given to options such as early retirement, health benefits and medical coverage; iii) to deal with pension surpluses/deficits and, particularly, the issue of contribution holidays which public employers have been prone to take, unilaterally, during periods of high investment returns, and; iv) to have a say in investment policy (Calvert, 2005: 1).

A strong case can be made that labour unions are concerned about pension funds because the financial leverage provided by the control of fund assets would help labour unions retard, and,

perhaps, reverse a secular decline in membership which appears to be accelerating (Bennett and Johnson, 1981: 182). This pension power, therefore, has been part of the renewal of unions in Canada after the demise of the fordist collective agreements. This theme is discussed in many other western countries as well, and is generally referred to by the term “Working Capital.” The objective is both to change existing investment practices on the part of financial managers and to develop financial innovations for the benefit of workers and the community (Bennett and Johnson, 1981).

Paul Wessel cited in Fogdall (2001) has discussed how unions could use the leverage provided by pension funds in several ways, among them: in "coordinated capital investment boycott campaigns against antiunion industries, in the "exercise of shareholder voting rights, in the use of funds to "finance home mortgages or other loans" for union members, and in the "investment of assets in unionized businesses to create jobs.

The experience of the trade union movement globally, most notably in the US and Canada, has demonstrated that by becoming involved in pension fund management a number of important gains can be made. These include achieving reforms of corporate governance, ensuring companies recognise their social responsibilities, and directing capital to areas of the economy that traditional institutional investment has failed to serve properly (Trades Union Congress**,** 2003: 1). More importantly, getting involved in the management of pension fund will ensure that the interests of plan members and beneficiaries are protected (Carmichael and Quarter, 2003).

Weststar and Verma (2007), suggest three inter-related strategic decisions that unions and their representatives should make regarding their involvement pension fund governance. First, unions must work to obtain a seat on the board, and fill it with either a labour trustee or a professional hired for the purpose. Second, unions build capacity in labour trustee with financial background to enable them to actively participate in investment decisions to protect the pensions of fund beneficiaries. Third, unions must decide if they want their trustees to push for the application alternative investment policies such as Social Responsible Investment (SRI) (Weststar and Verma 2007).

Simply defined, SRI refers to the integration of social, environmental and ethical issues (both positive and negative) into investment decision making (Richardson, 2007). Social responsible investment takes a number of different forms: asset screening, community investing, social venture capital, economically targeted investment and shareholder advocacy (Quarter and others 2001; Munnell and Sundén, 2004 and Yaron, 2005).

Asset screening is a process of applying social screens, either negative or positive, to investments. For instance, a negative screen would result if investments are prohibited in a particular company that has a poor record of labour standards; and a positive screen would involve actively investing in companies with a good environmental record (Gifford, 2004 and Quarter and others 2001).

Community investment refers to capital financing that is aimed at addressing the needs of communities that cannot ordinarily be addressed by traditional investment models. The rational is to better the economic and social development of a historically disadvantaged group or community (Canadian Socially Responsible Investment Review 2006).

Economically targeted investment can be defined "an investment designed to produce a competitive rate of return commensurate with risk as well as create collateral economic benefits for a targeted geographic area, group of people, or sector of the economy" (Bruyn, 1987: 67 cited in OPSEU Policy statement, 2002: 65). Economically targeted investments strategies have proven successful in real estate development and mortgage trusts. The principle behind such investment strategies is the dual outcome of reasonable rate of return for the plan and collateral benefits for the community in the form of jobs, sustainable businesses and affordable housing. Pension funds, therefore, can provide development capital for such needed investment (OPSEU Policy statement, 2002).

Shareholder activism enables investors to engage enterprises in which they invest and play an active role in ensuring that their performance meets the best interest of the beneficiaries. The underlying principle for shareholder activism is to improve long-term corporate performance and to further the interests of beneficiaries. Therefore, to enhance shareholder value, shareholders can participate in the governance of the corporation by voting on shareholder and approve business proposed by corporate management. They also have a major influence on executive compensation and reporting on compliance with international labour and environmental

standards. In cases were investments functions have been delegated to investment managers, the pension trustees have a fiduciary duty to supervise that voting of all proxies are in the best interest of beneficiaries (Yaron and Kodar, 2002).

The Ontario Public Service Employees' Union (OPSEU) pension model provides a perfect example of struggle of workers and their unions for an adequate pension. The union took a proactive position on the investment practices of the public service pension fund. It challenged government's policy of investing exclusively in its own nonmarketable debentures as serving only the employer's interests and inappropriate since the returns were well below market rates and did not provide a sustainable fund in the long run. OPSEU also suggested other investment strategies such as making residential mortgages directly available to members of the plan, and indirectly through the financing of housing projects (OPSEU, 2002).

According to OPSEU, it should be possible to address important social and economic concerns through the investment of the fund. However, investment strategies should reflect the interests of all of those with a stake in the security and economy of the plan. Therefore, there should be a well-established process for considering investments other than those indicated by conventional, technical factors. This process should include equal representation of the employer and the employees (OPSEU, 2002)

Collectively, the trade union movement could have a financial clout to rival that of the banks. To exercise this clout, trade unions and their trustees must develop new areas of expertise in capital market strategies, investment and economic development (OPSEU, 2002).

Indeed, there is a great deal that South African trade unions can learn from these investment practices that can benefit the workers and society in general.

Organized labour's active participation in pension matters continues up to this day. How the workers' money is invested and how it is managed is crucial to delivering an adequate pension benefit to union members. Trade union representation in the administration of pension fund is crucial to ensure that the funds are secure and well managed and the benefits are delivered. Trade unions argue that their representation on pension boards is crucial to ensuring that the funds are secure and well managed to the benefit of workers and their communities. The contention is that, in some cases, pension funds have been mismanaged and performance, as measured by reasonable standards, has been poor (Iglesias and Palacios 2000). Some of the investment practices of pension funds have been misdirected with little public accountability, limited access to information, and unclear management processes.

The Global Union Discussion Paper (2005) noted that countries with funded pension systems, trade unions are promoting their members' rights as shareholders to have a voice in corporate sdecision-making and, more broadly, to bring about good corporate governance regimes in those companies where their pension funds hold equity. This is also applicable to pension issues.

## 2.6 South African labour movement and pension funds

Pillay (2008) asserts that South African working class has been put on defensive by the growing power of capital, "as capitalists penetrate into all components of the economy" (Stafford, 1987:157), through the process of globalization. According to Pillay, even socialism, which was workers' only hope has struggles to reassert itself on the national agenda. One wonders what options are available to the once formidable labour movement to deal with effects of informalization of labour, high unemployment, persistent poverty and growing social inequality (Pillay, 2008: 45). Silver (2003) and Von Holdt and Webster (2008) highlight the different sources of power for trade unions. The focus on the workers' source of power is significant to the trade union as it determine avenues of revitalising trade unions in the global era. The restructuring at the work places has resulted in casualisation and externalisation which has in turn shifted the workers' sources of power. The trade unions need to have an understanding of these alternative sources of power and design strategies of asserting themselves. Control of pension fund investment presents alternative sources of power for trade unions. Weststar and Verma writes that greater activism in pension funds may be a "means to union renewal" at this time of the union decline and debate over their relevance in effectively representing workers interests (2008: 2).

According to Southall (2007), demands among unionised black workers for control over private pension funds became a crucial issue in the 1980s. In 1981 the government was forced by industrial unrest to withdraw legislation which proposed that workers would only be able to

withdraw their pension contributions after they retired. Southall reports that unions in the metal industry won the right to sit on the board of the industry's pension fund in 1983 and in 1987 the Chemical Workers Industrial Union persuaded employers to co-manage the Chemical Industries provident fund with elected union representatives (Southall, 2007).

The labour movement has noted that mutual insurance companies like SA Mutual and Sanlam control and manage enormous sums of provident fund contributions from workers, while they do not grant real ownership rights to the workers (Social Equity and Job Creation; 35). As Pillay (2003) posit, this gave the Mutual Funds an upper hand in setting business agenda. As such it was felt that rules should be changed to allow workers to participate in the management of their funds. The Reconstruction and Development Programme (RDP), a policy framework for the African National Congress (ANC), there was need for the government to change the laws and ensure adequate representation for workers through their trade unions and make the funds more socially responsible (ANC, 1994: 112). Thus, in 1996, the Pension Fund Act was amended granting trade unions 50 percent representation on the board of trustees on pension funds.

Following these victories, the idea grew that union trustees would exert active influence over the companies where retirement funds are invested. The motivation was to enhance company governance, influence investment policy and promote social responsibility. It was hoped that by controlling pension funds, unions would be able to influence investment patterns that would generate real productive activity and jobs; strengthen democratic governance in the way

enterprises are currently managed; and use the profit generated from enterprises in the social sector for the benefit of workers and communities (COSATU, 1997).

However, a study conducted on behalf of COSATU by Fifth Quadrant Actuaries and Consultants in 2003 on performance of trustees on pension fund boards revealed numerous problems. It stated that trustees were often extremely busy people with inadequate time to devote to investment issues; some worker trustees tended to treat their appointment to pension boards as a perk involving time off work, business travel and expense claims; and yet others were intimidated by, or deferred to, management representatives, fund principal officers or asset managers (Southall, 2007). Consequently, the labour movement may fail to effectively utilise these sources of power to their advantage as a result of failure to correctly harness the workers' source of power (Silver, 2003 and Von Holdt and Webster 2008), that is, the pension fund. Therefore, there is need to exploit how pension fund management can be a source of power in the global era.

This research will, therefore, endeavour to review the extent to which trade unions have been able to maintain pension fund benefits and influence investments in social sector for the benefit of workers and communities in South Africa.

# Chapter Three – Methodology

## 3.0 Introduction

The main purpose of this study was to investigate the role of trade unions in pension fund investment management in South Africa with the focus on assessing the extent to which they have been able to promote and protect the interest of their members and direct pension fund investment in areas that would have a positive impact on the working families and their communities. This chapter, therefore, discusses the methodological approach employed in the study. The study used a combination of qualitative and quantitative methods.

## 3.1 Study Setting and Population

The study was carried out in South Africa. Interviews with trade unions and their federation were conducted. Interviews with scheme administrators and service providers were done. Other stakeholders involved in various capacities of pension management were also interviewed. These included Financial Services Board (FSB), as a regulator and other experts in the pension industry.

## 3.3 Selecting Procedure

The study used non-probability sampling techniques. All respondents were purposively selected. Precisely, this was "expert sampling", as the researcher was looking for individuals with particular expertise that would be able to move the interest of the researcher forward (Given et

al, 2008). This was appropriate given the recognition among qualitative researchers that some informants are 'richer' than others and that these people are more likely to provide insight and understanding for the researcher (Marshall, 1996:524). This procedure, therefore, enabled the researcher to obtain systematic information that was able to meet the assumptions of the research design (Watters and Biernacki, 1989). In other words, purposeful sampling afforded the researcher an opportunity to use his judgment in selecting respondents that were considered most informative for the problem being investigated.

Accordingly, three (3) trade unions affiliated to COSATU were selected for this study. These unions provided key information on the experiences and challenges faced in trying to influencing pension fund investment decisions in South Africa. These included the National Union of Mines (NUM), National Union of Metal Workers of South Africa (NUMSA) and National Education, Health Workers Union (NEHAWU). The criterion was to have a union representation from both public and private sector so as to have different perspectives on their experiences with pension fund management. The interviews were conducted at the union offices.

The study envisioned to interview the Congress of South African Trade Unions (COSATU), as a labour federation, on the labour movement's policy with regard to pension fund management. However, at the time of data collection, there was no one in-charge of pension matters at COSATU. The person who was responsible for coordinating national policy on retirement funds was suspended due to alleged corrupt practice regarding his dealings with some service

providers. Unfortunate as the situation may be, it was interesting to the researcher as it bordered on some of the issues that the study was trying to explore.

Effort was made to look at other federation. Therefore, Federation of Democratic Unions of South Africa (FEDUSA) agreed to the interviewed. It has to be mentioned, however, that information from COSATU website was very useful.

Three pension funds, where the unions being considered in this study have seats on board of trustees, were interviewed to provide first hand information on the types of assets, investments and practice of pension fund management. These were Government Employees Pension Fund (GEPF), MIBFA and Mine Employees Pension Fund. Contact with these schemes was established through recommendation from trade unions. Additionally, one investment manager, the 27Four Investment Managers and Todaytrustee were interviewed. All the interviews were conducted at the respective offices of Pension Funds/Administrators.

Due to access problem and time constraint, the views from FSB were sourced from their official documents, many of which are accessible on their website.

**Table 2: Selected Sample**

| Research component | Respondents | Contribution |
|---|---|---|
| Interviews | Investment Manager<br>• 27Four Investment Managers | |
| | Representative from Federation<br>• FEDUSA | Information on labour movement's policy on pension fund management |
| | Three (3) COSATU Affiliates<br>• NEHAWU<br>• NUM<br>• NUMSA | Experiences of trustees and challenges they in influencing pension fund investment decisions |
| | Three (3) Pension Funds/Administrators<br>• GEPF<br>• MEPF<br>• MIBFA | Information on pension fund management practice, size of pension; investment policies |

This relatively small sample size provided thick data with rich narratives (Wang and Lin 2009). In qualitative studies, the sample size is not limited. It is driven by the desire to learn in detail and in depth about the experience of individuals (Tuckett, 2004). As Marshall (1996) posit, an appropriate sample size for a qualitative study should be one that would adequately answer the research question. Marshall further states that the number of required subjects usually becomes obvious as the study progresses, as new categories, themes or explanations stop emerging from the data. This is a point of data saturation where 'no new information of significance is obtained' for ongoing thematic development and theorising (Tuckett, 2004: 8).

## 3.4 Data Collection

Qualitative methods of data collection were used. These enabled the collection of in-depth information on individuals' personal histories, perspectives, and experiences of members of trade unions on pension issues. Both primary and secondary data were collected.

### 3.4.1 Interviews

#### 3.4.1.1 In-depth interviews

The study benefited from individual face-to-face in-depth interviews using semi structured questions. According to Wang and Lin (2009: 279), "in-depth interviewing is a flexible guided method that allows the researcher to lead an open conversation and does not limit participants in terms of sharing so that data collection is even more interactive". In other words, it broadens the scope for open-ended answers and encourages discussion (Woods, 2006). Therefore, in-depth interviews enabled the researcher to collect in-depth information on stakeholders' views and perspectives about the extent of trade unions influence on pension fund investment management.

In order to facilitate detailed and 'objective' analysis, all interviews were tape recorded and detailed notes were taken during interviews (Becker 1998).

### 3.4.2 Document review

A thorough review of important documents that shed light on pensions and trade unions was conducted. This review was both general and specific to the situation of the pension fund investment management in South Africa. The sources for this data collection method included: related books, articles, journals, pieces of legislation, policy documents, published and unpublished papers and documents from the libraries in and outside South Africa and the Internet. The main document reviewed included policy documents, pieces of legislation, annual financial reports and trade union conference resolutions.

The researcher was aware that although review of documents might provide useful information with regard to reconstructing events, and giving information about social relationships, they do not all provide an objective truth (Woods, 2006). The context within which they were construction should be taken into account. As Woods (2006) suggests, the task of the researcher, therefore, was to find out how they were constructed, and tease out areas that are relevant to the study.

## 3.5 Data Analysis

Taking into account the amount of data envisaged, the computer was used to analyse some of the qualitative data. Atlas.ti, computer software for processing and analysing qualitative data was used. Typed transcripts from audiotapes were assigned to Atlas.ti and coded. In addition to pre-

determined, instrument-based codes, all transcripts and the researcher's notes were read thoroughly in order to tease out emerging themes and allow for generation of new codes for data sorting. After generating code-based outputs from Atlas.ti, a further systematic analysis was done, making use of content analytic summary table. These helped present data on codes from different respondents on the same matrix to allow for effective comparison and holistic analysis of the data. Thematic conceptual matrices were also used to analyze data under different themes.

### 3.5.1 Assessment Criteria

The extent to which trade unions have been able to promote the interest of members was assessed in terms of how trade unions have been able to use the social responsible investment approach and the extent to which this framework contributed to social investment and corporate accountability. These include ethical screening and economically targeted investment.

Trade unions' influence in using enterprises' profits in sectors for the benefit of workers and communities were assessed by reviewing the extent to which pension fund are able to invest in areas that would bring about collateral benefits to the community.

The trade unions' contribution to strengthening corporate governance was assessed by focusing on the governance structure of the pension fund, shareholder activism and the selection of trustees.

## 3.6 Ethical Consideration

The study adhered to research ethical required. The research protocol was cleared by the Witwatersrand University Research Ethics Committee (Non – Medical).

Respondents were informed that their participation in the study was entirely voluntary and they could choose not to participate if they did not want to. Further, during the interview they may choose not to answer the questions that they do not want to answer and could withdraw from the interview at any time. In this regard, only consenting participants were interviewed.

To minimize the risk of the study to the respondents and ensure that they were protected, the researcher considered confidentiality and anonymity as major concerns. Therefore, the participants were guaranteed of full protection on the information they provided. No personal identifier has been left on the interview tapes or transcripts. Personal names and other identifying information in the text have been replaced by dummy words (Wang and Lin, 2009). Consent forms and data tapes have been kept in locked files and are only accessed by the researcher. Additionally, computer records have been password-protected to prohibit illicit access.

## 3.7 Limitations and strengths of the study

The study acknowledges the practical problems. Trade unions and pension fund investment management is a broad subject area that require time and resources beyond what is currently available. As such, this had a bearing on the adequate of data to be collected. Consequently, the

analysis was restricted to what was available and not necessarily all that may be needed to undertake a comprehensive research study.

The research instruments employed are also limited in the extent to which can adequately respond to the research question. This has an effect on the credibility and quality of the findings (Miles and Huberman, 1994). As Lincoln and Guba (1985) cited in Wang and Lin (2009) postulate, scientific research should be able to provide results in terms of qualitative research that can be consulted and contrasted in the form that is credible, transferable, dependable and confirmable. To deal with this concern, the researcher used several methods to increase the chances of depth and accuracy. Additionally the researcher benefited from interviewing different respondents on the issue. These are some common forms of triangulation (Woods, 2006).

The study aims to contribute to the debate on the role of trade unions in pension fund investment management. There are 196 registered trade unions in South Africa as at 31 August, 2010[iii]. However, only three trade unions were considered in this case study. Therefore, the scope is limited. In this case, the researcher will take care not to make inappropriate generalizing claims on the findings (Woods, 2006). However, according to Woods (2006), the findings will "contribute to an archive of studies" on a trade unions and pension fund "which then become reinterpreted" and form a basis for future research.

## 3.8 Reasons for using the method

The Study aimed at understanding a particular phenomenon and its manifestations. It is set out to appreciate a particular process. In this case, accessing the extent to which trade unions have been able to promote the interest of their members and also influence pension fund investment decisions. For this reason, it is necessary to collect information from stakeholders in the process to determine their experience on the issue. Therefore, qualitative method is appropriate for its "attention to detail, the ability to embrace both verbal and non-verbal behaviour, to penetrate fronts, discover meanings, and reveal the subtlety and complexity of cases or issues" (Woods, 2006).

# Chapter Four – South Africa Pension Fund Industry

## 4.1 Introduction

This chapter presents an overview of the current pension fund industry in South Africa. The rationale is to identify how the existing framework affects the way trade unions participate in pension fund investment management and promote members' interests. The chapter is organised as follows: Section 2 presents a brief overview of the South African pension industry in relation to the retirement arrangement to render context to the discussion that follows. Section 3 looks at pension fund investment regulation and management. Section 4 examines the types of pension funds and reviews some of the statistical information; how these have changed over the years and explore the implication for trade unions. In section 5, selected pension funds are examined in terms if asset allocation, investment practices and composition trustees. Section 6 concludes the chapter.

## 4.2 South African Pension Industry

The two main components of South African pension system are: occupational (retirement) insurance; and social assistance. The retirement insurance is made up of a number of pension and provident funds and voluntary savings, which provide retirement benefits for the majority of the workforce employed in the formal sector. Social assistance is a non-contributory, means tested public benefit program to ensure that the poorest are targeted (Registrar of Pension Fund, 2003).

It covers social old age pensions, disability grants and child and family grants (Van der Berg, 1999: 12; Allianz Global Investors AG, 2008).

This paper focuses on the occupational pension. The first South Africa's pension fund was introduced in the old Transvaal (South African) Republic in 1882. According to Van der Berg, the system was not backed by legislation or convention, therefore, it could not have been considered as social insurance. Institutionalization of occupational insurance for retirement only took place after the 1920s. However, the enactment of the Pensions Funds Act of 1956 was the high point in regulating the financial responsibilities of pension funds (Van der Berg, 1992, 1999).

### 4.2.1 Pension Fund Governance Regulation

Retirement funds in South Africa consist of pension and provident funds, retirement annuity, umbrella and preservation funds. In terms of the nature and extent of the supervision of such funds, the Pensions Funds Act 24 of 1956 of South Africa, gives responsibility to the Financial Services Board (FSB) over the following:

- Self-administered funds 'that invest their assets with bodies and institutions in the public and private sectors of the economy on their own behalf' (Registrar of Pension Fund, 2003).
- Underwritten funds, which operate exclusively by means of policies of insurance issued by registered insurers in the Republic (Registrar of Pension Fund, 2003).

- Foreign funds, whose head offices, or head offices of the participating employers, are located outside the Republic but administer benefits to their members resident in the Republic and who are South African residents (Registrar of Pension Fund, 2003).

Funds that falls outside the jurisdiction of the Registrar of Pension Fund:

- Official funds, these are "funds that have been established by special laws for employees of the State and certain parastatal institutions" (Registrar of Pension Fund, 2003). The National Treasury supervises these funds.
- Transnet Fund, fund for the employees of Transnet (Registrar of Pension Fund, 2003).
- Telkom Fund, a fund for the employees of Telkom SA Limited and the Telkom Retirement Fund
- The Post Office Pension Fund
- Bargaining Council Funds (BCF), funds that result from a process of collective bargaining. The Department of Labour is responsible for the supervision of these funds (Registrar of Pension Fund, 2003).

One important point to note from the above scenario is the diversity in the legislative landscape, comprising different acts and regulators (Allianz Global Investors AG, 2008). As Van der Merwe (2004: 311) suggested, if standards are applied consistently, one institution should be responsible for the regulation of all pension funds.

### 4.2.2 The structure of pension funds

Retirement funds in South Africa can fall into two broad categories: defined contribution schemes and defined benefit schemes. This categorization is essential in understanding the functioning of the funds, in terms of determining the funding and the levels of benefit (Van der Berg, 2002; Van der Merwe, 2004).

In a defined contribution scheme, the value of the benefit is determined by the value of all the contributions made on behalf of the beneficiary by the employee and the employer, in addition to the accumulated returns from investments made on such funds. The member, therefore, bears the risk of poor investment performance. On the other hand, the value of final benefit or pension in a defined benefit scheme is determined by the number of years of membership of the fund, times a certain percentage of final salary in the last month or year of work (Van der Berg, 2002).

According to Van der Berg (2002), the contributions are to a certain extent obvious in the case of a defined contributions pension. Accordingly, the contributions together with the returns on investment, will determine the final benefit. Van der Merwe reports that defined contributions cannot experience a shortfall because the contributions are certain. This could explain why this setup is most popular among employers (Van der Merwe, 2004). As for a defined benefit pensions fund, the employer takes full responsibility for the funding of the scheme, that is, to "ensure that the value of the assets in the fund are adequate to cover the demands on the funds" (Van der Berg, 2002: 18). According to Van der Merwe, a shortfall in this case, may be corrected

by either “increasing the rate of contributions” or by “requiring a transfer from employers” (Van der Merwe, 2004). In this circumstance, employers bear the investment risk. Arguably, this cost dimension makes the scheme unfavourable among employers.

Van der Merwe goes a step further and distinguishes between a pension fund and a provident fund. In the case of a pension fund, only one third of accumulated amounts may be withdrawn as a lump sum when a person retires (the remaining two-thirds must be taken as a pension), while in a provident fund 100 percent of the accumulated amount may be paid at retirement (Van der Merwe, 2004: 314).

### 4.3 Size, membership and assets of pension funds

Over the past decades, South Africa has witnessed a rise in the number of pension funds. Using the latest statistics from the Financial Services Board, the registered retirement fund were estimated at 10 699 as of 31 March, 2010 (Financial Services Board, 2010). However, as Table 4.1 shows, this figure was less than 11 271 registered private pension funds in 2008. Despite this reduction, the number remains significant.

**Table 3: South Africa Retirement Industry Statistics 2008**

| | Fund | Member | Contribution | Assets |
|---|---|---|---|---|
| | | R million | R billion | R billion |
| Privately administered | | 5,741,605 | 52,551 | 898,933 |
| Underwritten | | 3,180,451 | 18,903 | 229,444 |
| Official | 3 | 1,375,043 | 25,919 | 725,046 |
| Transnet/Telkom/PO | 5 | 167,942 | 1,618 | 71,561 |
| **Total** | **11,271** | **10,496,541** | **98,991** | **1,924,984** |

Source: Financial Services Board South Africa, Annual Report 2006 & 2010

In 2008, the total membership of retirement funds was 10 496 541. Of this figure, 8 557 228 were active members and 1 939 313 pensioners, deferred pensioners and dependants (Financial Services Board, 2010). Caution is required here, as there is a possibility of double counting, for the reason that certain individuals are members of more than one fund. It is estimated that total pension fund contributions amounted to more than R99 billion in 2008. This was an increase of 8.6 percent from R 91.1 billion in 2007 (Financial Services Board, 2010). Table 4.1 also highlights pension funds assets of R1 924 billion in 2008. According to the Financial Services Board, this was a decrease in the retirement fund industry assets of 0.7 percent, from R1 938 billion in 2007. In the case of privately administered funds, the net assets decreased by 5.4 percent, from R950 billion in 2007 to R898 billion in 2008.

## 4.4 Investment Regulation

In order to provide an adequate pension to the members that would prevent them from falling into poverty in their old age, investment of their accumulated assets should be at the center of the retirement fund system. Rusconi (2007) states that the investment strategies chosen by participants can have a significant impact on the value of retirement benefits, but also on the risks to which these accumulating personal assets are exposed. Rusconi (2007) suggests that investment alternatives should not be proliferated as doing so would increase system costs without necessarily providing associated benefit.

Regulation 28 of the Pension Fund Act of 1956 of South Africa sets limits relating to assets in which a registered fund may invest. According to the Regulation, a registered fund may invest only in an asset to the extent that a fair value of the investment of the fund does not exceed a certain threshold. The stipulated investment limits are summarized below (Regulation 28):

- 100 percent of the assets may be held in deposits and balances in current and savings accounts with a bank or a mutual bank, including negotiable deposits, and money market instruments ; however, only 20 percent may be put in one bank
- 75 percent of the assets may be invested in ordinary shares in companies excluding shares in property companies.
- 75 percent of the assets may be invested in shares and convertible debentures listed on the Johannesburg Stock Exchange other than the Development Capital Sector

- 25 percent of the assets may be invested in immovable property and claims secured by mortgage bonds thereon.
- 20 percent Development Boards may be established under the Black Communities Development Act, 1984
    - 20 percent may be invested in Rand Water Board
    - 20 percent may be invested in Eskom
    - 20 percent may be invested in Land and Agricultural Bank of South Africa
- 100 percent of the assets may be invested in bills, bonds and securities issued by the government of or by a local authority outside the Republic' however, only 20 percent per may be put in each authority
- 100 percent of the assets may be invested in bills, bonds and securities issued or guaranteed by and loans to or guaranteed by a local authority authorised by law to levy rates upon immovable property; however, a maximum of 20 percent may be invested in one local authority.

## 4.5 Pension Fund Management

Characteristically, trustees of pension fund consisted of senior management of the sponsoring employer (Kerrigan, n.d.: 1996). However, South African trade unions have for a long time struggled for control of pension fund and the right to direct and decide on funds investments through the employee representation on boards of trustees. This is based on the argument that

pensions are workers' deferred wages. The study indicates that transformation has taken place in the governance of pension fund, initiated by trade unions. As one respondent noted:

> *"*It was the insistence of COSATU to engage with the FSB and then there were amendments to the Pension Act …… to say Pension fund boards need to have a representation of the members of the fund. That is why we ended up with almost equal representation on pension board, where you have half members, though they might not necessarily be unionized" (PAT02[iv]).

Furthermore, the Pension Fund Act of 1956 provides for a Board of Trustees for each pension fund, which is made up of the different stakeholders to protect the interests of members. Research results reveals that almost all the pension funds in South Africa have implemented the legal requirement of a representative Board of Trustees, with at least 50 percent of the trustees elected by plan participants. In this case, it can be stated that the appointment of employee representatives to pension trustee boards is an important aspect of the labour movement's involvement in pension funds (Carmichael and Quarter 2003 cited in Weststar and Verma 2007). This legal framework, therefore, gives trade unions leverage to control or influence investments decisions of their deferred wages.

> "And transformation has taken place where the union and the employers are still 50/50. The pension fund…now clearly the union has got a bigger role to play because they appoint the trustees" (PAT04)

In addition, the FSB issued Circular PF 130 on 11 June 2007, which contains the main principles on good governance of retirement funds with regards to code of conduct, prudent investing and performance appraisals in respect of boards of trustees (Financial Services Board, 2010). This regulation has detailed how the boards of management and asset managers should conduct business in the interest of the members. According to the FSB, the board of trustees holds the fund assets in trust for the beneficiaries. They have a fiduciary relationship to the funds and must, therefore, "act with integrity". Fiduciary duties require the board to "deal with the assets or affairs of the fund in terms of the pension law, the common law, customary law, regulations" and "codes of conduct" applicable to the fund (Financial Services Board, 2007: 1).

The fundamental principle, according to PF 130, is for the board of trustees to "act with the utmost good faith towards the fund and in the best interest of all the members" at all times (Financial Services Board, 2007: 2). The circular requires trustees irrespective of whether they are employer-appointed, members-elected, in the employment of the sponsor or independent board members, to "owe a primary duty of care to the fund and the members and beneficiaries", and "not specifically accountable to or required to disclose any information to that group of persons or entities through whom they were appointed or elected as a board members". According to the PF 130, "the board should be sensitive to managing the diversity of board effectively to ensure that any tension, fears, disagreements, influence, affiliations, special interest, etc. do not hinder decision-making"(Financial Services Board, 2007).

> Union, you know they tried to pull a person out of the board to say they did not follow the mandate of the union. But that's the union to say that once you are in the board you have to act in the best interest of the members, not of the members but of the fund (PAT02).

## 4.6 Review of Pension Governance in Selected Funds

In this section the aim was to look at some selected pension funds and assess the models of the administrative structures that underline their operations and the constitution of their governing bodies. Further, it sought to examine their asset allocations and investment practices.

### 4.6.1 Government Employee Pension Fund (GEPF)

The Government Employees Pension Fund (GEPF) is one of the largest pension funds in Africa. The fund covers over 1.2 million active members, 318 000 pensioners and beneficiaries. Established in May 1996, GEPF is a defined benefit pension fund with assets worth R700 billion. It manages and administers pensions and other benefits for government employees in South Africa.

#### 4.6.1.1 Governance

The GEPF is a jointly-controlled fund with 50/50 union-employer board of trustees. The first board was inaugurated in May 2005. This is a significant progress for the trade unions in gaining

some degree of control over the fund, in view of the fact that, the Minister of Finance had been the sole trustee, initially.

The board consists of sixteen members. Eight of these members represent the government as the employer and eight represent GEPF members and pensioners. Of the eight trustees representing members and pensioners, six are chosen by the labour representatives on the Public Service Co-ordinating Bargaining Council. The other two are a pensioner member and a uniformed services member, both of whom are elected. The pensioner trustee is voted onto the Board by GEPF pensioners in a postal ballot.

The term of office of the Board is four years. This model has a rotating Chairperson and Vice Chairperson of the board. At the time of this research, the Chairperson was an employer representative while the Vice Chairperson was an employee representative.

The board members participate in the following five committees to help with the business of managing the GEPF:

i) Finance and Audit Committee, which advises the Board on financial and audit matters such as the
ii) Appointment of auditors, financial reporting and annual financial statements.
iii) Benefits and Administration Committee, which advices on benefits and pension administration strategies and procedures.

iv) The Governance and Legal Committee reviews and advises on governance, legal and compliance issues, as well risk management, legal dispute resolution and amendments to the Government Employees Pension Law.

v) The Human Resources Committee advises on the GEPF's human resources strategy, policy, procedures and structure. This includes the organisational structure and management.

vi) Investment Committee ensures that the Fund meets its commitments to the United Nations Principles of Responsible Investment, monitors the investment mandate and advises on investment strategy and policy.

The GEPF is an ideal model for trade unions. One aspect of trade unions (NEHAWU) participation in the administration of the fund is through the above committees. Therefore, employee representatives on the board need to have the capacity in order to exercise some degree of control over the management of the fund.

#### 4.6.1.2 Management of GEPF Investments

The Public Investment Corporation (PIC) manages the assets of the GEPF. The PIC is wholly owned by the South African government and is the only asset manager that serves South Africa's public sector. The PIC is registered with the Financial Services Board (FSB) as a financial services provider and is required to follow FSB-approved client investment mandates when investing funds.

When making investments for the GEPF, the PIC invests in four main asset classes, namely:

- Equities;
- Fixed Income;
- Properties; and
- Isibaya Fund.

About 75 percent of the equities owned by the GEPF are managed by the PIC, with the other 25 percent being managed by external fund managers. This is in line with the investment mandate that the GEPF has provided to the PIC.

**Table 4: Government Employees Pension Fund (GEPF) Assets Classes 2009**

| Asset Classes | Percentage |
|---|---|
| Local equity | 56 |
| Unlisted property | 2.1 |
| Listed property | 1.4 |
| Bonds | 36.3 |
| Money market instruments | 3.8 |
| Isibaya Fund | 0.4 |
| **Total** | **100** |

Source: GEPF Annual Report 2009

In the money markets, GEPF only invest in instruments offered by domestic banks. In the case of bonds, GEPF invest in bonds traded through the Bond Exchange of South Africa or issued by

government, parastatals and companies listed on the Johannesburg Stock Exchange (JSE) Limited.

The GEPF has investments in retail, corporate, industrial and specialised properties across South Africa. GEPF also has strategic investments such as the 20 percent share in the Airports Company of South Africa (ACSA).

The Isibaya Fund invests in black economic empowerment and infrastructure development projects that help to create jobs alleviate poverty and transform the economy.

#### 4.6.1.3 Socially Responsible Investment

The GEPF is among the leaders in socially responsible investment in South Africa and has been a signatory to the United Nations Principles of Responsible Investment since 2006. As such, GEPF take environmental, social and governance (ESG) issues into account when making investment decisions. Being a responsible investor means GEPF ensure that all investments not only deliver solid returns but also take environmental, social and governance issues into account. The fund also encourage the companies it invests in to strike a balance between profits and being socially responsible, and to actively manage their environmental impact while maintaining high levels of corporate governance standards.

GEPF is committed to helping to build a better society and to play a part in making this happen. Some of the highlights of their efforts include:

- Developing and implementing a Responsible Investment Policy (RIP) to guide all the GEPF's investment decisions.
- Leading the launch in early 2009 of the Principles of Responsible Investment Network in South Africa. This was in the spirit of promoting the Principles within the local pension fund industry and within the wider investment community.
- Assisting the JSE to review of its Socially Responsible Investment (SRI) index for 2008. The SRI index is used to assess how socially responsible South Africa's top listed companies are by looking at how well they care for the environment, how socially relevant they are and how seriously they take good corporate governance.
- Through the PIC, engaging listed companies whose corporate governance and transformation, for example, have been unsatisfactory

### 4.6.2 Metal Industries Benefit Funds Administrators (MIBFA)

The Metal Industries Benefit Funds Administrators (MIBFA) administers the Engineering Industries Pension Fund and the Metal Industries Provident Fund.

#### 4.6.2.1 Engineering Industries Pension Fund

The Engineering Industries Pension Fund is one of the largest Pension Funds in South Africa with total assets exceeding R37, 7 billion at market value. The Fund provides pension and lump sum benefits on retirement, retrenchment/redundancy and withdrawals to members or to their

beneficiaries on their death. Members automatically belong to the Metal and Engineering Industries Permanent Disability Scheme which provides a salary continuation benefit for members who have been declared permanently disabled by the Medical Advisors of the Scheme.

The fund covers over more than 31 704 contributing members and 37 954 pensioners in receipt of monthly payments. Contribution and Investment income for 2009 amounted to (R 7 858 million).

#### 4.6.2.1.1 Engineering Industries Pension Fund Asset Management

As at 31 March 2009 the total market value of the assets of the Fund amounted to R37 739 million. These assets were held in the following types of investments.

**Table 5: Engineering Industries Pension Fund Assets Classes 2009**

| Asset Classes | Percentage |
|---|---|
| Equities | 30.91 |
| Property | 0.1 |
| International managers | 9.07 |
| External managers | 39.26 |
| Bonds and cash | 20.66 |
| **Total** | **100** |

Source: EIPF Annual Report 2009

The Investments department of MIBFA managed 51.57 percent of the investment portfolio, the balance being managed by external managers.

#### 4.6.2.2 Metal Industries Provident Fund

The Metal Industries Provident Fund was established in May 1991 and provides lump sum benefits to members on retirement, retrenchment, resignation or dismissal or to their beneficiaries on their death. Members also automatically belong to the Metal and Engineering Industries Permanent Disability Scheme, which provides a salary continuation benefit for members who have been declared permanently disabled by the Medical Advisors of the Scheme.

##### 4.6.2.2.1 Metal Industries Provident Fund Asset Management

As at the 31 March 2009 the assets of the Fund amounted to R18 775m. The assets were held in the following types of investments, per market values.

**Table 6: Metal Industries Provident Fund Assets Classes 2009**

| Asset Classes | Percentage |
|---|---|
| Shares in companies | 32.24 |
| Offshore investment | 7.66 |
| Bonds and cash | 21.38 |
| External managers | 38.72 |
| **Total** | **100** |

Source: MIPF Annual Report 2009

#### 4.6.2.2.2 Governance

The management of the Fund is vested in a Board of Trustees, comprising an equal number of employee and employer representatives, with the Chairperson being appointed from either side on a two year rotational basis.

The Employers are represented by the Steel & Engineering Industries Federation of South Africa (SEIFSA), whilst the Employees are represented by the following Trade Unions:-

- National Union of Metal Workers of South Africa (NUMSA)
- Solidarity
- Metal & Electrical Workers' Union of South Africa (MEWUSA)
- United Association of South Africa (UASA)
- South African Equity Workers' Association (SAEWA)

### 4.6.3 Sentinel Mining Industry Retirement Fund

The Sentinel Mining Industry Retirement Fund is a defined contribution pension fund registered in terms of the Pension Funds Act, No 24 of 1956. Sentinel Mining Industry Retirement Fund aims to provide retirement solutions appropriate for all members in the mining and mining related industries.

The Fund offers flexible investment choice and pension income choice to members. Assets are actively managed through a multi-manager approach, and at 30 June 2009 the value of these assets under management amounted to R31 193 million.
Currently the Fund serves the interests of 33 460 members and 22 398 pensioners. One hundred and two employers participate in the Fund.

The Fund provides membership to employers and employees in the mining and mining-related industries in South Africa.

#### 4.6.3.1 Governance

The Board of the Sentinel Mining Industry Retirement Fund comprises 18 trustees, including an independent non-executive trustee (who is also the Chairperson) and 18 alternate trustees, one of whom is an independent non-executive trustee. Seven employer representatives are appointed by the Chamber of Mines of South Africa, six employee representatives are appointed by the United Association of South Africa (UASA), two employee representatives are appointed by the Mines Professional Association and two employee representatives are appointed by the National Union of Mineworkers (NUM).

#### 4.6.3.2 Investment Management

The Board appoints the Investment Committee to monitor and report on investment managers of the Fund. The main responsibilities include review and recommend an overall investment policy

for approval by the Board of Trustees; review in the investment policy regularly. Ensure that the Fund's investment policy is implemented; select and appoint consultants, investment managers and custodians; approve an investment mandate for each investment manager, including an appropriate benchmark for performance measurement purposes; and monitor investment activities.

### 4.6.4 Mine Employees Pension Fund (MEPF)

The Mine Employees Pension Fund is a pure defined contribution pension fund registered in terms of the Pension Funds Act, No 24 of 1956.

The Fund offers flexible investment choice and pension income choice to members. Assets are actively managed through a multi-manager approach and at 30 June 2009 the fair value of these assets under management amounted to R15 629 million.

Currently the Fund serves the interests of 17 462 members and 22 478 pensioners. Fifty-one employers participate in the Fund. The Fund provides membership to employers and employees in the mining and mining-related industries in South Africa

#### 4.6.4.1 Governance

The Board of the Mine Employees Pension Fund comprises 17 trustees, including an independent non-executive trustee (who is also the Chairperson) and 16 alternate trustees, one of whom is an independent non-executive alternate trustee. Seven employer representatives are appointed by the Chamber of Mines of South Africa, three employee representatives are

appointed by the United Association of South Africa (UASA), three employee representatives are appointed by Solidarity, two employee representatives are appointed by the National Union of Mineworkers (NUM) and one employee representative is appointed by the South African Equity Workers Association (SAEWA)

#### 4.6.4.2 Investment Management

Appointed by the Board to monitor and report on investment managers of the Fund. The main responsibilities include: Review and recommend an overall investment policy for approval by the Board of Trustees; review in the investment policy regularly. Ensure that the Fund's investment policy is implemented; select and appoint consultants, investment managers and custodians; approve an investment mandate for each investment manager, including an appropriate benchmark for performance measurement purposes; and monitor investment activities.

# Chapter Five – Trade Unions and Pension Fund Investments in South Africa

## 5.1 Introduction

The study focused on four areas, namely (i) the extent of trade unions in promoting the interest of pension fund members (ii) the extent of trade unions in influencing pension fund investments in sectors that would benefit the workers and their communities (iii) trade unions' contribution to strengthening pension fund governance and (iv) enhancing trade unions' influence and control of pension fund investments.

## 5.2 Extent of trade unions in promoting the interest of pension fund members

Trade unions' promotion of the interest of pension fund members was assessed by evaluating the extent to which union trustees are able to direct pension investments in such a way that they do not damage the fundamental economic and social interests of the fund beneficiaries. In this case, the impact is limited to pension fund members and beneficiaries, not necessarily the community in general. The economic and social interests of workers include: increased jobs and living wages, guaranteed employee benefits (health insurance, retirement plans and educational assistance), wealth building (profit sharing and home-ownership assistance) and skills development programs for employees (Hagerman, 2007).

Overall, respondents held the view that trade unions have had a critical role to play in promoting the interest of pension fund members. They bring diversity to the board of trustees and the necessary checks and balance to the administration of the fund. It should be noted that, prior to the 1980s, black workers did not have benefits such as pension fund and provident fund. According to a trade union respondent, the desire to establish a pension fund dates back to the 1940s, when the then mine workers union called Africa Mine Workers, under the leadership J.B. Marx led a march that was organized to hand a memorandum to the Chambers of Mines. The memo contained some of the demands on decent accommodation and decent jobs. In the context of the quality of jobs, one of the demands was the provident fund. However, that strike did not achieve the intended objectives. In 1982, the launched National Union of Mine Workers (NUM) rekindled the flame. The Union started negotiating with the Chambers of Mines on the same issues. The demands that were put to the Chambers were also improved working conditions, decent accommodation and the provident fund. It was claimed that failure to agree with the Chambers on provident fund was one of the reasons that led to a strike in 1987, demanding the establishment of a provident fund or pension fund for workers. The Union managed to secure the demand of putting together the provident fund, which is called Mine Workers Provident Fund today. This was a significant achievement, even though many mine workers lost their lives in the process (PAT04).

The structure of the retirement fund presents considerable challenge to trade unions in South Africa. As highlighted elsewhere in this report, South Africa has witnessed a shift from defined benefit to defined contribution. With regards to defined benefit fund, the risk is located within

the employer. During the period of economic turmoil that would result in loss of investments, the employer would write-down its asset values. Consequently, workers are guaranteed investment and accumulated benefits. The shortfall between what has been guaranteed must be paid by the employer. For defined contribution, workers are exposed to different risks. They have no protection. Their monies are invested into the equity market. The portion that goes to the most risk investment is bigger. For example, current allocation to equity market by the mine workers provident fund is 60 percent of the investment and very little to the bonds. Large sums of money, therefore, go to the most risky investments, such as equity market.

However, some fund managers expressed the view that defined contribution fund was good as it gave employees the responsibility to make their own choices on how their funds should be invested (PAT01).

The huge challenge for union trustees, however, is how to communicate and educate members about investment choices, risk profiling and decision - making. It was noted that members do not have the necessary level of education and expertise as some of the products could be complicated. As one responded noted:

> "You are asking the guys in the mining or manufacturing sector out of depth to make a decision on ZAR 4.5 billion worthy of pension assets; asking them to choose what is good for their retirement! So handing over the decision-making to the members is ….. a difficult job and often you find that members opt to go for

default options as opposed to exercise their right to make a choice because of the lack of knowledge and understanding" (PAT01).

## 5.3 Extent of trade unions' influence on pension fund investment decisions

Assessing trade unions' influence on the investment of workers' pension fund will focus on the extent to which trustees are able to influence enterprises where pension funds have invested to use their profits in promoting social responsible investment (SRI) through asset screening, community investing, economically targeted investment and shareholder advocacy.

The study observed that there is a general appreciation of social responsible investment among trade unions, pension fund managers and other industrial players. Accordingly, institutional investors in South Africa together under a Committee on Responsible Investing by Institutional Investors (CRISA) to implement the United Nations Principles of Responsible Investing introduced in 2006, of which the GEPF is a founding signatory. The committee has drafted the Code for Responsible Investing by Institutional Investors. These Principles are to persuade investors to integrate environmental, social and governance (ESG) issues into their investment decision making (CRISA Media Release 2 September 2010)[v].

These Codes consists of four principles as cited in the CRISA Media Release of 2 September 2010):

i) Environmental, Social and Governance (ESG) Policy: requires institutional investors to develop a policy detailing the process of assessing the investment target's environmental, social and governance (ESG) fundamentals.

ii) Responsible ownership: requires institutional investors to demonstrate a responsible approach to shareholding by implementing a policy detailing mechanisms of intervention and engagement with companies when concerns have been identified, as well as the means of escalation if concerns raised cannot be resolved. Further, processes of management of conflicts should be detailed.

iii) Promoting the Code through collabouration: encourages institutional investor to consider a collabourative approach, where appropriate, to promote acceptance and implementation of the Principles of this Code and other applicable codes and standards applicable to institutional shareholders.

iv) Disclosure: requires institutional investors to fully disclosure to stakeholders the policies put into place in line with this Code, the implementation of these policies, and the general application of this Code.

### 5.3.1 Investment Screening

There was no direct reference to negative screening among respondents. With positive screening, though not explicit, trade union demands that pension funds include in their portfolios companies that display key principles which underlie the Social Responsible Investments (SRI) such as infrastructure development and social services, Broad base Black Economic Empowerment funding, environmental preservation and community development (COSATU, 1997).

The Government Employees' Pension Fund (GEPF), for example, has directed the Isibaya Fund to play a defining role in supporting the national development agenda. Thus, this fund is placed in unlisted investments with a focus on job creation, job retention, poverty alleviation, BBBEE transformation and regional development. GEPF has also developed an ESG framework to measure the performance of this fund (Public Investment Corporation Annual Report, 2010).

### 5.3.2 Community Investment

With regards to community investment, the observation of the study was that fund managers were integrating social and governance (ESG) issues in investment decision-making. For example, Old Mutual's Community Property Fund has been providing funds for the development of retail shopping centres catering to the needs of underserviced communities throughout the country. At present, the Fund has invested in the development of over 30 shopping centres in rural and townships in eight of the nine provinces of South Africa. These centres are providing

retail services and products to a primary target market of approximately 8 million low- to middle-income groups. Additionally, the fund is benefiting in terms of rental income from national leases of these centres. The following are the retail facilities catering to lower-income households (Old Mutual, n.d.):

- Sontongo Mall – Gauteng
- Megacity – North West Province
- Nkomazi Plaza - Mpumalanga
- Thulamahashe Plaza – Limpopo
- Kanyamazane Mall - Mpumalanga

Housing Impact Fund is another Old Mutual asset allocation with SRI elements. This fund invests in low cost housing and ancillary projects with the objective of alleviating the plight of the previously advantaged by focusing on housing delivery, housing finance and channelling assets into investments which plug the gap in housing.

Apart from development related investments, Old Mutual has a Social Impact Fund. This fund is directed mainly at women's empowerment to address gender inequality and poverty alleviation. According to a respondent:

> "The money is used as fund money to small groups of women who want to go into business who would not get money from the bank under normal

> circumstances because of their credit ratings. We give them access to funding as well as training. We don't just give them money. We give them money and make sure we train them. We also give them access to the market. Because remember as an individual you cannot go and negotiate a deal with Woolworths. But as a Fund of our stature, can talk to Woolworth that we have got people that are canning food and we would like to put them on your store's suppliers list. We have got the muscle to negotiate with Woolworth more than you as an individual. So that's the space that we are also playing here" (PAT03).

GEPF has also reorganized its Isibaya Fund strategy, administered by PIC, to focus on investments with measurable social and developmental impact. Consequently, the Isibaya Fund will explicitly address GEPF's developmental investment strategy focusing on four main investment themes (Public Investment Corporation Limited, 2010 Annual Report):

i) Economic infrastructure, including infrastructure for energy, logistics, water, broadband and commuter transport;
ii) Social infrastructure, focusing on health, education, housing and development finance;
iii) Economic growth investments in sectors that foster growth, job creation and broad-based black economic empowerment particularly in those priority sectors identified by government's Industrial Policy Action Plan (IPAP), including agriculture, agro-processing, alternative energy and environmental projects; and

iv) Dinamane, to focus on microfinance and investment in small, medium and micro enterprises (SMMEs).

Similar trends were observed in other funds. The Sentinel Mining Industry Retirement Fund and Mine Employees Pension Fund are committed to a broad-based BEE policy through a range of operating activities intended to ensure transformation at all levels of society (Sentinel Mining Industry Retirement Fund, 2009 Annual Report; Mine Employees' Pension Fund, 2009 Annual Report). The following are the main vehicles being used in this regard:

- A Socially Responsible Investment (SRI) strategy that allocates a set percentage of total assets to target appropriate SRI projects and investments.
- An incubation programme focusing on emerging black asset and investment managers who have the potential to add value to the Fund's portfolios and who would not be otherwise identified in the Fund's standard institutional investment manager research process.
- Service providers to the Fund, including asset managers, must be committed to the transformational goals of the Codes of Broad-based Black Economic Empowerment.

### 5.3.3 Economically Targeted Investment

In terms of economically targeted investment, there were no specific investments marked as such. However, a critical look at the composition of some asset allocations indicates that the massive investments in infrastructure development, both economic and social provide financial opportunities for institutional investors. In the end, the communities benefit in terms of better infrastructure, community revitalization and job creation. According to one fund manager:

> "…the owners of the money will still get the investment returns and the community will get something tangible. Even the investors will see that there is a hospital here, for example. These are the kinds of things that we try to resolve through this kind of program. We have got high unemployment, so when we start building a shopping mall; we create employment for locals there" (PAT03).

Of course, the first priority for fund managers is investments that could give them a good rate of return, which might probably result in community betterment. As one fund manager asserted:

> We are not saying doing social things is not to the best interest of the fund. We must make sure, as a fund, that we what do is in the best interest of the fund and it might turn out to also have a social benefit (PAT02).

At the same time as there have been these developments in the pension industries, it cannot be argued that they have been due to solely trade unions' role in influencing institutional investors in using their funds in the economic and social sectors for the benefit of workers and communities. Some fund managers did not see any particular role that unions play on the pension fund board apart from representing the interest of the fund.

> For me I would not say that the union trustees have a particular role to play on the board. I think they bring diversity to the board. And they bring the necessary balance and checks. Because once you have got people who come from different backgrounds looking at the same problem, invariably they will come up with …solution to solve it. So you actually increase your capacity to interrogate issues better and manage the fund effectively. I think that is the angle they bring in. (PAT02)

While it is tempting to argue that there have been these massive developments have brought positive benefits to workers and their communities, trade unions contend that the impact has not been satisfactory.

> "Let me be honest with you, as a union we are not satisfied with the current configuration of the SRI because it is not having any maximum impact on the society. Our view is our pension fund, if you look at the distribution and the investment of that money, it is being s invested into affluent societies where the

middle class live. We are saying, we want to see the impact of those monies on the social programmes and development such as development of skills of farmers and development of scarce skill, investment to properties…" (PAT05).

## 5.4 Contributions of trade unions in strengthening pension fund governance

In evaluating the trade union role in influencing pension fund governance, the focus is on the extent to which the unions are able to support shareholder campaigns to influence corporate governance in the pension industry.

Across all respondents, there was an agreement that the pension industry was challenged with malpractices. Corruption and conflicts of interests were cited as compromising the fiduciary responsibilities and consequently affecting the benefit of the members.

"I think service providers know that this is a wealthy industry and trustees know that this is a wealth industry and sometimes it opens up doors for corruptive elements. And you do see this occurring all the time where the service providers who want to get into the fund would offer soft payment to boards of trustees to members of trustees" (PAT01).

Another respondent stated that:

> Our industry is challenged in the sense that by now there is quite a lot of corruption. People don't see the value of what you are ….with if you don't have a budget for bribery. Because we don't have a budget it's a challenge. You can see that people understand what you are selling and they like it but they will not go with it. And you wonder why they are not going with it. Only to find that there is something lacking there. Those are the challenges and sometimes ……the decision making process is too long" (PAT03).

In the case of corporate governance, investment strategies of all the funds visited complied with FSB PF 130. The investment strategies addressed among other things shareholder activism/proxy voting. Accordingly, the study found that PIC has been using the matrix to rate the ESG disclosure practices of the top 40 companies listed on the JSE. Furthermore, PIC attends and vote at the Annual General Meetings of investee companies, and its voting record is published on the Corporation's website for stakeholders' information. For the period 2009/10, the main issues monitored were "board independence, attendance of board meetings, excessive remuneration, retrospective approval of board fees, blank authority to keep shares under direct control and blank authority to issue shares for cash" (PIC 2010 Annual Report). However, the performance on social and environmental remains to be considered.

COSATU and its affiliates have acknowledged PIC's work on corporate governance and proxy voting. Resolutions tabled at the COSATU annual congress indicate that PIC policies and principles were progressive. COSATU, therefore, has resolved to continue strengthening its

relationship with PIC and other funds to enhance proxy voting and Corporate Governance. Accordingly, COSATU has adopted the following PIC principles as well policies and applications to adapt them to its situation (COSATU Resolution of 10 National Congress, 1999):

i) Discipline: proper behavior of senior managers

ii) Transparency: ensuring that outsiders have the power to view and thus assess corporate philosophies and actions.

iii) Independence: the entrenchment of actions and balances of power in corporate structures.

iv) Accountability: the mechanism to expose policies, decisions and actions to investor scrutiny

v) Behavior: the ability to correct actions where necessary

vi) Fairness

vii) Social Responsibility: good co-operative citizenship, non exploitative and responsible actions in relations to environmental and human right issues.

viii) Good stakeholder relations: the ultimate aim of conserving the repository of value represented.

It remains to be seen to what extent trade union have customized these principles and policies to influence corporate governance in the pension industry.

## 5.4 Enhancing trade union influence and control of pension fund investments

Enhancing trade union influence and control of pension fund investments requires a union clear agenda for their representative. This strategy involves the development of labour-centric training programmes and the creation of networks of labour activists and other labour trustees around pension issues. This clear agenda will include among other things recruitment and selection process, training and support for the labour trustees.

### 5.5.1 Trade union policy

The study did not found a documented policy on the pension fund for the unions at the national level. Instead the unions were guided by the resolutions that had been passed at the union congress *(PAT05)*. It was not possible to evaluate the implementation of these resolutions.

However, it was observed that there were many fragmented funds in the industry, especially in the mining sector. Therefore, in order to influence the investments some suggested strategies included consolidating all the funds into one big fund.

> "….because we have got many funds in the mining, which are fragment, we want to consolidate into a one strong big fund at the central level, the likes of PIC. That's the route that we want to take…. consolidation of the all fund into one big fund so that we can be able to influence the investment" (PAT05).

### 5.5.2 Selection of Trustees

The Pension Fund Act provides that trustees must be elected and be appointed into the fund. The appointment after selection is regulated by PF circular 130 of the Financial Services Board. However, with permission from FSB, large funds with many participants opt to appoint trustee due to logistical in organizing elections for trustees.

The study observed that the appointment of trustees in a union is by identifying shop stewards who have the potential to understand the industry itself, that is, financial or pension fund industry. When they are identified, the National Executive Council (NEC) will then endorse the appointment.

### 5.5.3 Training of Trustees

The study found that some of the trustees knew nothing about pension fund investment when appointed to the board of trustees. Therefore, "employer's trustees are the ones running the funds. They dictate the trajectory of the fund, in terms of where to invest and so on" (PAT05)

In line with the PF 130, however, new board members receive training "to enable them to minimize their risk of liability as well as safeguard them against bad decision- making".

The study also found that some unions invest in trustee capacity building. “We do have programmes where trustees are taken for training. These provided by professional institutions. They provides with lessons on how to invest, portfolio management, etc. Trustees are taken through basic education of investment. So far, we have trained more than 300 trustees” (PAT04).

There was appreciation that when many trustees get educated and they understand what the law requires of them and what their fiduciary duty, they avoid being liable. (PAT01).

# Chapter Six – Analysis of the Research Findings

## 6.1 Introduction

This chapter critically analyses research findings. The chapter is organized into seven main sections. The second section analyses the impact of the legal frame on trade unions' participation in pension fund management. The third section analyses the extent of trade unions in promoting the interest of pension fund members in South Africa. The fourth section analyses the impact of the legal framework on the extent of trade unions' in influencing pension fund investments in sectors that would benefit the workers and their communities in South Africa. The fifth section analyses trade unions' contribution to strengthening pension fund governance. The sixth section offers sustainable strategies for enhancing trade unions' influence and control of pension fund investments. The seventh section concludes the chapter.

## 6.2 Analysis of the impact of the legal frame on trade unions

The study confirms that the legal framework limits trade unions' participation in the management of pension fund. According the PF 130, trustees irrespective of whether they are employer-appointed or members-elected owe a primary duty of care to the fund and the members and beneficiaries and not specifically accountable to or required to disclose any information to that group of persons or entities through whom they were appointed or elected as a board members. As one fund manager posits, "the role for the union just goes as far establishing the

board of labour trustees is concerned. However, when it comes to how fund are to be invested, that becomes the role of the trustees. So there is no role of the employer, members or the trade union in the management of the funds. That is the role of the trustees" (PAT08).

This is clearly evident in the PPWAWU NATIONAL PROVIDENT FUND vs Chemical, Energy, Paper, Printing, Wood and Allied Workers Union (CEPPWAWU) case[vi], where the union decided to remove trustees from the board for refusing to follow its mandate. However, the trustees were reinstated by the courts stating that the pension fund trustees are independent.

Apparently, the fund in question was established through negotiation between the union and the employer, which later merged with other trade unions. In March 2002, the trustees decided to terminate the mandate of the fund's existing administrators and to appoint different administrators. This decision was not welcomed by the union. Therefore, at its congress held in August 2002, the union adopted a "Resolution on the accountability of fund trustees established by CEPPWAWU". According to the judgment, the resolution sought to impose obligations on trustees elected or appointed by the union or its members to manage benefit funds established by the union.

Some of the resolutions included the following (PPWAWU NATIONAL PROVIDENT FUND vs CEPPWAWU Judgment):

- That the shop steward Trustees are accountable to union members who elected them.

- That the shop steward trustees must therefore take mandates from union members of the funds on all matters that affect them.
- That the NEC must give guidance on policy matters to the member trustees and the investment company.
- That the Worker trustees are accountable to the union and the members of the funds who elected them.
- That the employee trustees therefore must take mandates from the union before and after they attend board of trustees meetings and the members of the funds on all matters that will affect them before they attend board of trustees meetings.
- That all trustees who fail to adhere to these fundamental democratic principles (which form the basis of CEPPWAWU) must be disciplined in terms of the union's constitution and its policies.
- The NEC should ensure that the two Benefit Funds be amalgamated as soon as possible.
- The NEC should ensure that regular elections are held to renew the mandate of benefit fund trustees.
- The NEC must develop a paper on the role of the funds in the context of the Pension Fund Act and the union's investment policy.

However, on 16 March 2006, trustees unanimously resolved to amend certain aspects of the rules that would weaken the control which the union had over the appointment of members' trustees

The decision by the trustees to amend the rule was objected to by the union. Accordingly, the union charged its seven (7) trustees with three (3) charges (PPWAWU NATIONAL PROVIDENT FUND vs CEPPWAWU Judgment):

1. The union found the trustees guilty of misconduct for failing to inform the NEC of such amendments to the rules of the PNPF.
2. The union found the trustees guilty of misconduct for participating in a meeting where the PNPF Rules were amended, without any mandate from the fund members and/or union constitutional structures.
3. The union found the trustees guilty of misconduct in that, after participating in the meeting where a resolution amending the rules of the PNPF was adopted, they failed to inform the union that the amendments had been affected.

As such trustees contravened the CEPPWAWU 1st National Congress resolution on the accountability of trustees of benefit funds established by the union, and the constitutional provisions of the union.

In his answering affidavit on behalf of the union, Mr W Nolingo, the union's general secretary, states as follows:

> "Rule Amendment 9 has had the effect of removing CEPPWAWU's representation on the board without any consultation having been conducted

> with it prior thereto. This I submit is untenable, given that the large majority of the members of the Fund are CEPPWAWU members. The manner in which this amendment was effected was contrary to the spirit if not the letter of the Rules as they existed prior to the amendment. It was for these reasons that CEPPWAWU objected to the Rule Amendment" (PPWAWU NATIONAL PROVIDENT FUND vs CEPPWAWU Judgment).

The contention of the fund was that the resolution was invalid and that it was unlawful for the union to pursue disciplinary charges founded on the resolution (PPWAWU NATIONAL PROVIDENT FUND vs CEPPWAWU Judgment):

> A fund trustee who complies with all union mandates in the exercise of his or her powers as trustee whether or not he or she believes that the mandated positions are in the best interests of the Fund and its members will be in breach of his or her duties to the Fund and its members.
>
> Persons who have fiduciary duties to fulfil (and these include retirement fund trustees) are not the agents of those who appoint them, do not derive their powers from those persons (instead they derive their powers from the 'trust instrument' such as, in the case of a trustee of a retirement fund, from the Fund's Rules) and cannot lawfully bind themselves to exercise their discretion in a particular way.

Mr Watt Pringle, who appeared on behalf of the fund, submitted that the resolution is contrary to law and/or to public policy and is accordingly invalid and unenforceable. In essence, his argument was that each trustee owes a fiduciary duty to the fund; that the resolution seeks to interfere with the proper exercise of that fiduciary duty in an unlawful manner; and that this renders the resolution illegal, contrary to public policy and unenforceable.

Section 7C (1) makes it clear that – by statute it is the fund's board, and not the union, which is entitled and required to "*direct, control and oversee*" the fund's operations. The assertion in the resolution ("noting" clause 3) that, on occasion, the union's NEC and other constitutional structures "*take decisions*" on benefit funds which the trustees "*are obliged to implement*" is incompatible with this statutory injunction. In my view, the union's misconception in regard to this issue was fundamental and led it to adopt a resolution some of the terms of which are incompatible with the requirements of the PFA and the fiduciary duties of the fund's trustees.

The Judge held that the union was wrong in believing that the members' trustees are "accountable to" it and had no right to require such trustees to be "accountable to" it and its members. The union had no right to impose an obligation on the members' trustees to "take mandates" from the union before and after they attend board meetings nor to oblige them to "take mandates from union members".

The Judge accepted that there is nothing unlawful or improper in the union expressing its views on issues to be decided by the fund's trustees or even in seeking to persuade the fund's trustees

to accept its views. However, it is, in his view, unlawful for the union to seek to compel member trustees to "take mandates" which they are required to implement, failing which they risk disciplinary steps. It is unlawful for the union to threaten disciplinary steps against member trustees for refusing to accept that they are "accountable to" and union and its members, rather than to the fund and its members.

In his view, the resolution in this case is contrary to public policy and unlawful because it seeks to interfere with the rights of pension fund trustees to exercise their fiduciary duties in accordance with their own independent judgment.

This case suggests a tension between the financial industry and the union on the management of pension affairs. It has also put a wedge between trade unions and their trustees. As one respondent stated, "we have some extent control over the trustees. However, we don't have direct control given the fiduciary duty. They have some freedom but at the same time we remind them to observe the policies and guidelines of the union" (PAT04).

OPSEU has dealt with a similar a situation and has gained some level of control over its labour trustees. According to OPSEU, it has been able to get through "the "chill" that has existed between unions and their trustees as a result of the Cowan and Scargill case". OPSEU "acknowledges that trustees - as fiduciaries - are not independent agents, but are accountable to both plan members and the union". Potential trustees are made aware of the union's expectation

trustees will follow union policy on pension issues such as “training, attendance, expense and conflict of interest policies, codes of conduct and all other policies of the union” (OPSEU, 2002).

Furthermore, OPSEU requires a potential trustee to “commit in writing that they are prepared to follow union policies” before that person is accepted to be a union trustee. We read: “While trustees may not be legally the agents of the union all trustees know that they are expected to assert the Union's agenda”. This forms the basis on which the union is able “to support and train trustees for their work on pension boards”. However, OPSEU would not hesitate to remove any union appointed trustee from the board, “in the event that they fail to perform their duties, the Union has a responsibility to remove them” (OPSEU, 2002).

Through its Pension Liaison Committee, OPSEU has continued to recommend “policies and procedures for union-nominated trustees”. These policies would include “ monitoring trustee conduct in line with OPSEU's goals, interviewing prospective trustees, determining education needs and facilitating communication between the union, membership and trustees” (OPSEU, 2002).

### 6.3 Analysis of the extent of trade unions in promoting the interest of pension fund members

According to Weststar and Verma, “those unions that have achieved a seat have largely stalemated at the second stage with only a few achieving some impact on the governance of

pensions in terms of socially responsible investment (SRI), economically targeted investment (ETI) or the leverage of shareholder proxy votes to promote corporate good governance and other outcomes" (2007: 12). This seems to be case of most trade unions in South Africa. While they have able to joint trusteeship of most of the funds, they have failed to break through the "chill" of fiduciary requirements of trustee to advance labour perspective though their union appointed trustees. According to Weststar and Verma, "labour trustees must be able to challenge the traditional models of pension investment and governance" if they are to achieve these ends. Or else, "they risk becoming token members of the board" (2007: 12).

## 6.4 Analysis of extent of trade unions' influence on pension fund investment decisions

*Investment Screening*

The results show that pension funds are directing investments to companies with "positive social goal" or "with more general ethical objectives" (Carmichael, Thompson and Quarter 2003: 6). The SRI Equity Fund of Old Mutual, for example, is based on the SRI principles of the JSE SRI Index and includes listed companies that integrate corporate social responsibility and performance with business activities. The General Equity Fund, is another example, that invests in JSE-listed companies that are "viable and sustainable, and have a clear commitment to job creation, skills development, affirmative action, sound environmental practices and effective corporate governance".

The OPSEU policy paper on pension (2002), reports that screens can be responsive to the concerns of pension plan members if monitored over a long period of time. The OPSEU policy paper, however, warns that financial impact is not necessarily felt by the companies who are screened out (2002: 52), unless it is done collectively by a large number of pension funds. The study confirms that many small funds with uncoordinated programs on, especially, in the mining sector cannot exert pressure to change corporate governance if they operate in isolation.

*Community Investment*

The emphasis of community investing and economically targeted in South Africa has been on reconstruction given the legacy of apartheid. The study noted that most of the initiatives are designed to meet these goals. For example the Financial Sector Charter Council's goal is "to actively promote a transformed, vibrant and globally competitive financial sector that reflects the demographics of South Africa and contributes to the establishment of an equitable society by effectively providing accessible financial services to black people and by directing investment into targeted sectors of the economy" (FSCC, 2008 Annual Report). A critical analysis of the investment allocation with regard to these programs, it is difficult to distinguish between community investing and economically targeted investments. Therefore, most of the community investments are considered as targeted investments.

*Economically Targeted Investment*

Economically targeted investment is a form of social investment that targets a certain amount of assets for specific social goals such as employment opportunities, provide affordable housing, urban revitalization, support of small and medium sized enterprises, renewable energy, and clean technology (Carmichael, Thompson and Quarter 2003; Hebb and Beeferman 2008). Table 7 below shows the amount of funds that were allocated for economically targeted investments in underdeveloped and previously marginalised areas of South Africa. This is according to the stated principles of the Financial Services and Property Charters, whose goal is to actively promote a transformed and vibrant financial sector and contribute to the establishment of an equitable society by effectively providing accessible financial services to black people and by directing investment into targeted sectors of the economy (FSCC Annual Report 2008).

In low-income housing, for example, targeted investments were targeted at R 41.8 billion to be achieved by 2008. However, only R 32 billion of the target was achieved.

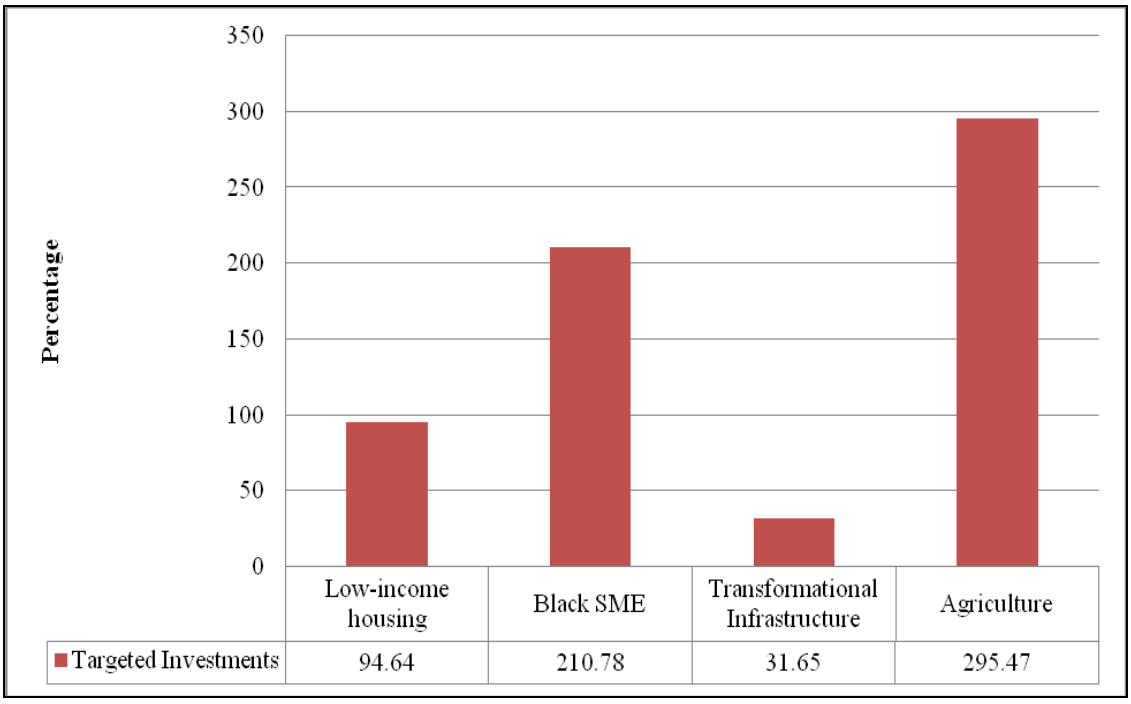
**Table 7: Targeted Investment Performance 2005 - 2008**

| | **2005** | **2006** | **2007** | **2008** |
|---|---|---|---|---|
| Low-Income Housing (R-m) | 13,269 | 25,705 | 26,761 | 31,135 |
| Black SME (R-m) | 6,214 | 9,840 | 8,802 | 11,368 |
| Agriculture (R-m) | 201 | 604 | 3,057 | 4,441 |
| Transformational Infrastructure (R-m) | 4,290 | 9,115 | 12,469 | 17,688 |

Source: The Financial Sector Charter Council, Annual Report 2008

Figure 1 below shows that Black SME's and Agriculture was financed to over 200 percent of the original target. However, there was no information to verify the impact of these investments to the beneficiaries.

**Figure 1: Targeted Investments 2008**




Source: The Financial Sector Charter Council, Annual Report 2008

According to FSCC, however, targeted investments would only be achieved if there is a "partnership between the financial sector and government to effect risk-sharing between government and banks to facilitate the transformation of the low-income housing market, as well as risk mitigation in areas of non-commercial risk" (FSCC Annual Report, 2008). This is

consistent with Carmichael, Thompson and Quarter's assertion that investment in economically targeted investment is supported by regulations that defines collateral benefits of ETIs as well as "guarantee of government funding so that pension funds can be used for urban redevelopment" (Carmichael, Thompson and Quarter 2003).

According to OPSEU policy paper on pension, for pension fund capital to be used more productively, investment vehicles and expertise have to be connected with pension trustees. The policy paper emphasises that social goals may not be realised "without more collaboration between pension funds on social investment strategies with labour sponsored investment funds" (OPSEU, 2002). This could be a possible explanation why the South African trade union movement is not having an impact on the control of pension fund investments.

The Caisse de Dépôt et Placement du Québec offers a good example of economic development by pension funds in Canada (Carmichael, Thompson and Quarter, 2003). As Carmichael, Thompson and Quarter (2003) write, Québec's pension and benefits funds as well as the Québec Pension Plan invest in Caisse. As at 1997, Caisse had net assets of $63.6 billion, making it one of largest investment agency in Canada (Carmichael, Thompson and Quarter, 2003).

Labour-sponsored investment funds (LSIFs), is another economic development initiatives of the trade union movement in Canada and, in North America and Europe (Carmichael, Thompson and Quarter, 2003). According to Carmichael, Thompson and Quarter, pension funds that want to put a small part of their funds to regional venture capital could use LSIFs as an investment

vehicle. LSIFs had assets of almost $4 billion in 1998(Carmichael, Thompson and Quarter, 2003).

Concert Properties, a real estate development company in British Columbia, and its sister investment vehicle, Mortgage Fund One, are both funded by about 26 pension funds shareholders (Carmichael, Thompson and Quarter, 2003). According to Carmichael, Thompson and Quarter, Mortgage Fund One and Concert Properties are good cases of "multisector collabouration across labour and employer groups" (Carmichael, Thompson and Quarter, 2003).

The AFL-CIO Housing Investment Trust has public sector pension funds such as CalPERS, NYCERS and Mass PRIM as investors (Hebb and Beeferman, 2008). There are many other good examples of labour-friendly investment vehicles that have worked in collabouration with pension funds to deliver economically targeted investments.

In view of the above, the study agrees with COSATU's call for the trade union movement in South Africa "to review the potential for using existing union investment companies to create and finance a vibrant co-operative sector" (COSATU, n.d.: ), in "A Growth Path Towards Full Employment document. In particular, further research must be undertaken to explore the extent to which workers' funds held by union investment companies, the pension fund industry and retirement funds, cannot be consolidated to create a progressive developmental investment vehicle (COSATU, n.d.).

## 6.5 Analysis of trade unions contribution to strengthening pension fund governance

There was evidence of shareholder activism in PIC, the investment company for GEPF. PIC periodically produces public voting patterns of its proxy votes that are available on its website. However, others claim that "there are relatively few instances where shareholders in South Africa have actively challenged corporate management, voted out directors, or passed resolutions to facilitate changes in company policy" (NALEDI, Policy Bulletin August 2002). According to Frater, "shareholders' meetings in South Africa are comparatively lonely events, with the main participants and voters being the company directors" **(**NALEDI, Policy Bulletin August 2002).

However, one report on Responsible Investments in South Africa cites Unity Incorporation, an investment group cofounded by unions, as having attempted "to transform the companies in which their pension funds were invested by raising issues of concern to workers, especially working conditions (Giamporcaro, Pretorius and Visser, 2010).

Hebb and Beeferman (2008: 7) highlights recent initiatives undertaken to advance a long-term view of value by the American umbrella labour organizations such as the AFL-CIO and Change to Win (CtW) unions, among others, "to fight over excessive executive compensation, board composition and access to the proxy ballot for nomination of directors' to corporate boards".

## 6.6 Current practices of enhancing trade union control of pension fund investments

*Trade Unions' Policy on Pension Fund Governance*

Weststar and Verma observe that "since their goals in pension governance remain unclear, most unions do not appear to have a formal process to identify and develop their own talent in this area" (2007: 4). Indeed a case can be made that unions in South Africa had no clear policy on pension fund governance looking at the content of their resolutions with regard to pension fund governance. Most of them were responding to a particular issue at that point in time. Thus, this situation defeats unions' efforts to effectively influence investment decisions, which are dominated by the financial industry. One respondent observed that trade unions were falling short in exercising their clout optimally. This is despite unions having huge influence over the sector due to the size of their membership. The respondent felt strongly that unions could consolidate their position and become a real force in the pension industry.

OPSEU for example has developed consistent union policy and objectives with respect to control of pension plans. The policy outlines the union approach to "accountability of trustees, expense allowances, procedures for appointments, removal of trustees, and trustee training" (OPSEU, 2002: 24). The end result is that OPSEU has been able to negotiate pension plans over which it had some control. The union has also been able to deal with its relationship with its trustees in relation to conflicts of interest. Furthermore, the union has been able to carry out social investment initiatives that are in line with the interests of their members and their communities (OPSEU Policy paper on pension, 2002). It can be concluded, therefore, that a clear policy on

pension fund governance would help unions in South Africa to take a proactive position pension fund matters.

*Selection of trustees*

Section 7A (1) of the PFA, requires that at least 50 percent membership of a board of a fund to be elected by the members of the fund. The selection procedures for labour trustees can take many forms. Weststar and Verma report that the union can appoint labour trustees or their representatives "from outside of the union, recommended by the union but officially appointed by the government or the plan itself, elected by plan participants, or selected by the union" (2007: 16).

One of the unions in the study appoints its trustees by identifying shop stewards who have the "potential of understand the pension industry or the financial industry. The identified candidates are then endorsed by the National Executive Council (NEC). This process resonates with Quarter's observation that "most labour trustees have a history of being active in their union – sometimes even on pension and benefits committees - rather than being selected or elected as a raw recruit from the rank and file" (Quarter et al. 2008 cited in Verma and Weststar, 2011).

*Training of trustees*

From the evidence tendered, it is clear that more needs to be done with regard to the training of labour trustees if they are to move forward labour perspectives on the pension fund investment decisions. COSATU acknowledges that "trustees' knowledge on matters of pension fund is very limited and therefore they completely rely on service providers for expert advice" (COSATU, n.d).

The PF 130 provide that "new board members, at the expense of the fund, post appointment and election, receive rigorous and comprehensive training on both the legislation and regulatory framework and governance principles in order to equip them to effectively carry out their functions as board members, and to enable them to minimize their risk of liability as well as safeguard them against bad decision- making".

The PF 130 also requires that "board members be educated on an ongoing basis about new matters relating to funds to ensure that they acquire and maintain an understanding of risk management, investment risks and strategies, benefit structures, legal issues, regulatory and compliance requirements, taxation, actuarial and reform issues".

While specific targeted training is being offered by asset managers, it is the case that training is "bias towards the service providers instead of focusing on members interests" (COSATU, n.d).

In other words, training provided by the financial industry put emphasis on the "high levels of accountability expected of union trustees" (Carmichael, Thompson and Quarter 2003).

In one study interviewee describe courses as "short and introductory" (Weststar and Verma, 2007). According to Weststar and Verman these "these courses typically cater to pension trustees or board members in general and do not address some of the needs specific to labour trustees such as reconciling their role or bringing forth alternative perspectives" (Weststar and Verma 2007).

Carmichael *et al* report that unions and trustees who are keen to broaden their perspective towards investment are not receiving much support from their pension funds (Carmichael and Quarter, 2003). Admittedly, even trade unions' education departments are not in a position to provide training to trustees and union leadership on pension matters (COSATU, n.d), especially alternative investments.

Carmichael (1998) cited in Carmichael, Thompson and Quarter (2003: 2) suggested "that education could be a critical factor in preparing union and other employee representatives to take an active role in pension fund investment". As Rudd and Spalding (1997) contend, if appropriate education was given to trustees, they would be encouraged to place pension funds in economically targeted investments, which have collateral benefits such as job creation for working people (cited in Carmichael, Thompson and Quarter 2003:2).

From the above, it is, therefore, suggested that potential labour trustees or representative should have acquired this kind of education prior to their appointment in order to take an active role in pension fund investment. As Weststar and Verma write, "labour trustees will be more effective members of the pension plan board of trustees if they arrive at the table with a clearly defined role, a well articulated purpose, and sufficient support through training and social networks" (2007: 30).

In line with the above assertion, a member of the Pensions at Work Union Reference Group put forth a suggestion that a pool of plan members be identified, based on interest or ability or both, and be trained in pension issues. The motivation is that new trustees would be selected or elected from this pool whenever a labour trustees' position falls vacant (Weststar and Verma, 2007: 17). This is a cadre of labour trustees who would have developed "their own body of knowledge on capital markets and pension fund investment strategies", based on a union agenda "on the perspectives and interests of working people and their communities" (Carmichael, Thompson and Quarter 2003: 3) independent of the financial industry.

# Chapter Seven – Summary and Conclusions

The study investigated the role of trade unions in pension fund investment management in South Africa with the focus on assessing the extent to which they have been able to promote and protect the interest of pension fund members and direct pension fund investment in areas that would have a positive impact on the working families and their communities.

The implication of this study suggests a conflict. On one hand, it was observed that pension governance and developments in the regulatory framework continue to push the trustees towards the greatest possible degree of independence and away from the influence of any appointing party. This framework does not allow space for union participation in the pension fund management. At the same time pressures from the imperatives of the United Nations backed Principles of Responsible Investing (UNPRI), ILO's international labour standards aimed at ensuring that growth on the economy provides benefits for all and now King III, which sets the tone for corporate governance practices in South Africa.

In the circumstances, the study finds that the hegemonic influence over pension fund investment issues by the financial industry has been significant. It has determined on which side of the balance the weight of the investment policy is placed. As such, there was observed a series of concerted and mutually reinforcing steps towards limiting trade union influence in pension fund management and the reduction of the scope and coverage of fiduciary mandate. However, this study finds that labour representation on the pension boards

of trustees still remains the major determinant of the long-term interests of workers, their families and their communities. Thus, the balance sheet at the moment shows that the development of pension fund investment strategies in South Africa has gone hand in hand with a continuing presence of the trade union trustees on pension boards. In other words, the evidence of labour representation in various subcommittees of pension funds through the presence of union trustees was observed.

This study also revealed that trade union participation in pension fund investment in South Africa has not been without difficulties. Most fundamentally, the study reports that commitment expected of trade unions within the framework of the joint trusteeship of pension fund management has not been fully realized. On the contrary, the failure of financial industry to win the trust and confidence of pension fund members and their community that they could be solely entrusted with the management of pension fund affairs in their long-term interests, would appear to have reinforced stakeholders' high regard for the relevance of the trade union movement. However, the positive respondents' evaluation of the contribution made by trustees was found not to be dependent on whether they were labour or employer trustees, suggesting that the role of the trade union trustees were considered invaluable by the majority of participants. Nevertheless, the evidence of minimal control of pension fund by unions was significant and pointed to the legal limitation and lack of clear policy on pension fund governance. However, this did render trade unions ineffective or irrelevant with regard to their role in promoting the interest of members and directing pension fund in social investments.

A critical look at the challenges facing the labour movement in taking control of pension fund investment in South Africa informed the need for the union to adopt a more transformative educational agenda reinforced by a more workers' friendly investment strategy. Thus, it was suggested that a sustainable trade union strategy must build on: i) providing support to trustees through research and education, ii) getting more involved in projects that provide direct benefits to members of the fund, iii) work in partnership with their pension fund, iv) collabourate with labour investment fund and connect expertise in social investing to trustees and fund managers, and; v) advancing a worker friendly investment strategy.

Based on the evidence of this study, I have no doubt therefore that trade unions in South Africa can leverage the power of the workers' capital to benefit workers and their communities. My conviction is that fiduciary obligation of trustees and investment strategies that takes into account economic, governance and social issues are potentially compatible and potentially beneficial. The success of the unions' participation in pension fund management and influencing investment decision-making, however, will chiefly depend on whether they have clear policies and goals on pension fund governance and are able to initiate a process of engagement. In effect, the trade union movement in South African trade, "one of the most well-organized labour movements in the developing world" (Pillay, 2003) is at the cross roads. Although being challenged by financial industry, their future remains firmly in their own hands.

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# Appendix A: List of Interviews

1. National Treasurer – NUMSA. Interviewed on 8 October 2010 in Johannesburg
2. Managing Director - 27Four Investment Managers. Interviewed on 15 September 2010 in Johannesburg
3. Risk and Compliance Officer - Sentinel Mining Industry Retirement Fund. Interviewed on 15 October 2010 in Johannesburg
4. Principal Officer Engineering Industries Pension Fund and Metal Industries Provident Fund, MIBFA Metal Industries Benefit Funds Administrators MIBFA. Interviewed on 13 September 2010 in Johannesburg
5. Marketing Executive at Old Mutual - Old Mutual Investment Group. Interviewed on 23 August 2010 in Johannesburg.
6. Business Development Executive – Symmetry Multi Managers (Old Mutual). Interviewed on 23 August 2010 in Johannesburg
7. Head: Investment & Actuarial at GEPF. Interviewed on 19 August 2010 in Pretoria.
9. Deputy General Secretary – NUM. interviewed on 17 August 2010 in Johannesburg
10. Editorial Director - Today's Trustee Publishing. Interviewed on 10 August 2010 in Johannesburg
11. National Treasurer – NEHAWU. Interviewed on 2 July 2010 in Johannesburg

**Notes**

[i] Leo W. Gerard is the International President of the United Steelworkers. He has been the driving force behind a network of activists who are creating conceptual, financial and educational tools for capital strategies that will inject the welfare of workers into investment priorities. http://www.usw.org/media_center/speeches_interviews?id=0002 Accessed on 2 November 2010

[ii] Ontario Public Service Employees' Union (OPSEU) – Canadian leader in union control of pension funds

[iii] Registered trade unions in South Africa as at 31 August http://www.workinfo.com/registeredtradeunions.htm Accessed on 6 November, 2010

[iv] PAT01 – PAT10 : refers to interviewees' codes

[v] Committee on Responsible Investing by Institutional Investors in South Africa "Make responsible investing part of your policies, new draft Code tells institutional investors", Media Release 2 September 2010 http://www.iodsa.co.za/products_reports.asp?CatID=362 Accessed on 24 October 2010

[vi] THE PPWAWU NATIONAL PROVIDENT FUND Vs THE CHEMICAL, ENERGY, PAPER, PRINTING, WOOD AND ALIED WORKERS UNION. CASE NO: 06/24039. In The High Court Of South Africa (Witwatersrand Local Division)