Kent Murlis Davis

CRITICAL EVALUATION OF THE POSSIBILITY OF RETIREMENT FUND MEMBERS DIRECTLY CLAIMING DAMAGES FROM THEIR FUND'S SERVICE PROVIDERS FOR LOSS SUFFERED

Submitted in partial fulfilment of the requirements for the degree of Master of Laws by Coursework and Research Report at the University of the Witwatersrand, Johannesburg

13 June 2019

School of Law

LLM BY COURSEWORK AND RESEARCH REPORT

PLAGIARISM DECLARATION

Surname: Davis **First name** Kent **Student No:** 345796

Course Code: LAWS7181A / LAWS7182A Course Name: Research Report (Part-time)

Lecturer / Supervisor: Clement Marumoagae

Assignment Topic: CRITICAL EVALUATION OF THE POSSIBILITY OF RETIREMENT FUND MEMBERS DIRECTLY CLAIMING DAMAGES FROM THEIR FUND'S SERVICE PROVIDERS FOR LOSS SUFFERED

I certify that this submission does not exceed 10 500 words.

Plagiarism is the "failure to acknowledge the ideas or writing of another" or "presentation of the ideas or writing of another as one's own" and should be read to cover intentional and unintentional failure to acknowledge the ideas of others. In this context "others" means any other person including a student, academic, professional, published author or other resource such as the internet. The University of the Witwatersrand, Johannesburg believes that failing to acknowledge the use of ideas of others constitutes an important breach of the values and conventions of the academic enterprise. It has therefore been resolved that all students should be required to sign a declaration that they are aware that they are required to submit their own unaided work and that plagiarism is unacceptable.

I declare the following:

- I am aware that plagiarism (the use of someone else's work without their permission and or without acknowledging the original source) is wrong;
- I am aware that any work that I submit for assessment must be my own unaided work except where I have explicitly indicated otherwise;
- I am aware that I must follow the required conventions in referencing the thoughts and ideas of others;
- I understand that the University of the Witwatersrand may take disciplinary action against me if I do not submit my own unaided work or if I fail to acknowledge the ideas or words of someone else in my writing and that lecturers are obliged to report incidents of plagiarism to the Plagiarism Committee of the School of Law;
- I have been provided with a copy of the Senate Policy on Plagiarism which is also available from LB41 or on http://www.wits.ac.za/depts/wcs/helpdesk/PLAGIARISM%20POLICY.doc

I have read and understood the above plagiarism declaration and confirm that the work submitted is entirely my own except where otherwise acknowledged.

Signature: ________________________________ **Date:** 13 June 2019

Notes (please read very carefully):

- This sheet must be used as a cover page for ALL assignments in the School of Law.
- You are required to present a 2nd copy of your assignment for stamping to Ms Dangor, which copy (once stamped) you will keep as your proof that you have handed in the assignment.
- A percentage of your mark will be deducted for every day (or part thereof) that an assignment is late.

ABSTRACT

This research report proposes that where a service provider of a retirement fund (such as an insurer or asset manager) exercises a high degree of discretion in respect of the investment decisions it makes for, or on behalf of, a retirement fund, if one has regard to the nature of the relationship between such service provider and the members of the retirement fund, a limited fiduciary duty should be imposed on the service provider in favour of the members. It is proposed that the fiduciary duty should be separate from, and in addition to, the fiduciary duties owed by the board of management and should also differ in its content. Further, it is submitted that to the extent a service provider breaches this duty; the members should have a claim against such service provider. Due to the fact that the benefits payable to a member only vest in terms of the rules, any claim for damages would likely occur before a member's right to benefits vests. A member would therefore need to claim for prospective damages and argue that once their benefit vests, they will suffer a loss. Despite the courts not recognising claims for prospective loss, it is submitted that in the case of members, compelling reasons exists to allow a claim for prospective loss provided the claim for prospective loss is established as a matter of reasonable probability.

CONTENTS

CRITICAL EVALUATION OF THE POSSIBILITY OF RETIREMENT FUND MEMBERS DIRECTLY CLAIMING DAMAGES FROM THEIR FUND'S SERVICE PROVIDERS FOR LOSS SUFFERED

KENT DAVIS

I INTRODUCTION

The purpose of this research report (‘report’) is to determine whether retirement fund members ('members') may directly claim damages from their retirement fund's service providers. It is acknowledged that the retirement fund’s board of management ('board') has fiduciary duties that cannot be delegated. However, due to the fact that the board often lacks the requisite skills and expertise to ensure the effective management of the retirement fund and its assets, the board may, and often does, appoint third-party service providers to perform certain functions for, and on behalf of, the retirement fund. In this report, it is argued that under certain circumstances, service providers such as insurance companies and asset managers should owe a limited fiduciary duty to the members and that a breach of that duty should enable members to directly claim damages from such service providers.

In order to establish the above proposal, this report will consider, amongst other things: (i) the general nature of retirement benefits; (ii) the contractual relationships between members, retirement funds and services providers; (iii) the fiduciary duty owed to the retirement fund and its members; and (iv) the quantification of loss, particularly having regard to the nature of retirement benefits.

At the outset, it is important to note that this report will not consider the standard terms and conditions of the agreements entered into between retirement funds and service providers. Apart from certain statutory limitations, the terms and conditions of the agreement between a retirement fund and a service provider (such as limitations of liability and indemnities) are negotiated and agreed between the parties concerned. It is therefore impossible to accurately ascertain what terms and conditions are standard in these agreements.

Further, while it is acknowledged that there are several parties that render services to retirement funds (such as auditors, retirement fund benefit administrators, actuaries, consultants and valuators), the primary focus of this report will be on asset managers and long-term insurers. The rationale for focusing on these two parties is that they both perform a significant role in the management of a retirement fund's assets.

In order to provide context for the necessity of the proposal set out herein, the collapse of Steinhoff International Holdings NV ('Steinhoff') and other selected statistics on the role of service providers will be used in order to demonstrate the impact that service providers have on retirement funds and their members.

II THE ROLE OF SERVICE PROVIDERS WITHIN THE RETIREMENT INDUSTRY

According to the Annual Report of the Financial Sector Conduct Authority ('FSCA')[1] as at 31 March 2018, there were 5 118[2] registered funds in South Africa with a combined asset value in excess of R4 trillion.[3] Of these 5 118 funds, 2 953 were privately administered funds (i.e. assets other than insurance policies), while 2 165 were wholly underwritten funds (i.e. only assets being policies of insurance).[4] Contributions to underwritten funds for 2016 were valued at nearly R43 billion while over R119 billion in contributions were made to privately administered funds.[5] Further, as at 31 December 2016, these funds had a total membership of 16 643 722, 11 069 963 of whom were active members with the remaining 5 573 759 members comprising pensioners, dependants and unclaimed benefit members.[6]

The increasing size of retirement fund assets is not limited to South Africa. In the paper entitled '*Fiduciary Duty in the 21st Century*' ('UN Report') issued by the United Nations Global Compact, UNEP Finance Initiative and Principles for Responsible Investment, the investment practices of retirement funds in several countries including Australia, the United Kingdom ('UK') and the United States of America ('US') were considered. In Australia, the value of total investment of pension funds increased from approximately A$ 700 billion in 2005 to over A$ 2 000 billion in 2015.[7] In the UK, the total investment of pension funds increased from approximately £900 billion in 2005 to £1 700 billion in 2014[8] while the US has seen growth in pension fund investments from about $9 500 billion in 2005 to nearly $15 000 billion in 2014.[9]

---

[1] With effect from 1 April 2018, the FSCA replaced the Financial Services Board.
[2] Financial Services Board and Financial Sector Conduct Authority *2018 Annual Report* (2018) at 43.
[3] Ibid.
[4] Ibid.
[5] Ibid at 46.
[6] Ibid at 45.
[7] United Nations Global Compact, UNEP Finance Initiative, Principles for Responsible Investing '*Fiduciary Duty in the 21st Century*' (September 2015) at 25.
[8] Ibid at 51.
[9] Ibid at 72.

While it may be difficult to fully appreciate the significance of these numbers, they do illustrate the enormous size of the retirement industry both locally and globally and that a need exists for the effective management of the assets of retirement funds. Despite their size, in South Africa the assets of retirement funds are largely managed by a handful of service providers. In its December 2017 Survey of Retirement Fund Investment Managers,[10] based on its survey of 58 asset managers and 369 retirement funds,[11] Alexander Forbes reported that as at 30 June 2017, the value of assets under management of the top 20 asset managers in South Africa totalled nearly R5 trillion.[12] Service providers such as asset managers therefore play a significant role in managing the assets of the country's retirement funds. The investment decisions of these service providers have a significant impact on the value of the retirement funds' assets and ultimately — the value of the benefit that the member will receive on retirement. In order to protect retirement funds and their members, and given the large sums of money and assets under the control of these service providers, it is essential that these service providers are adequately regulated.

The impact that service providers have on retirement funds and their members was illustrated in the collapse of Steinhoff. On 5 December 2017, the share price of Steinhoff dramatically collapsed in what has become known as one of the largest cases of corporate fraud in South African business history.[13] Olano Makhubela, the deputy executive officer of the Financial Services Board ('FSB')[14] (now the FSCA) stated that 948 of the 1080 funds surveyed[15] had exposure to Steinhoff amounting to R25 billion on 1 December 2017.[16] Approximately a week after the scandal broke, this exposure had significantly shrunk by R7 billion which equates to a loss in value of R18 billion or rather 1% of the total assets of the sampled funds.[17]

The role of service providers in this scandal did not go unnoticed. Magda Wierzycka, chief executive officer of Sygnia Investment Management, was quick to implicate asset managers in the scandal. In an open letter published on 7 December 2017, Wierzycka posed the

[10] Alexander Forbes *Manager Watch Annual Survey: Survey of Retirement Fund Investment Managers* (December 2017).
[11] Ibid at 7.
[12] Ibid at 10.
[13] CNBC Africa 'Inside the Steinhoff sage, one of the biggest cases of corporate fraud in South African business history' (28 June 2018), available at *https://www.cnbcafrica.com/insights/steinhoff/2018/06/28/steinhoff-rise-fall/*, accessed 12 October 2018.
[14] At the time when this statement was made, the FSB was still in existence.
[15] excluding the Government Employees Pension Fund and the funds of state-owned enterprises.
[16] Linda Ensor 'Pension funds lost billions over Steinhoff' *Timeslive* 31 January 2018, accessed 2 February 2018.
[17] Ibid.

question — how did so many active asset managers in South Africa miss this?[18] She pointed out that the annual financial statements of Steinhoff were obfuscated and that its financial items did not make sense.[19] Wierzycka alleged that asset managers acted negligently in relation to the manner in which they invested in Steinhoff.[20]

The Steinhoff debacle presents interesting questions about the liability of service providers in relation to the loss that members experienced. As will be explained below, members do not have any contractual relationship with service providers despite such parties having control over a substantial amount of assets which underpin the value of the retirement benefits the members hope to receive upon retirement.

It should be noted that this report will not consider whether the members or the retirement fund may claim against the company that the retirement fund invested in or such companies' directors. An example of such a suit is the recent class action lawsuit brought against, amongst others, Steinhoff and its former directors.[21] Rather, the report is focused on the liability of service providers for their investment decisions.

Naturally, it might be argued that since service providers are appointed by the retirement fund, the retirement fund itself should seek recourse against the service provider for the loss suffered and not the members. Such a claim would be justified (as seen in the case of Steinhoff) on the basis that it is the retirement fund's assets (and not the members' assets) which reduce in value as a result of a service provider's negligence. This view is further strengthened by the fact that retirement funds are more sophisticated than their members and have, or have access to, the requisite skills to formulate and institute proceedings against the service providers. Furthermore, retirement funds have a contractual relationship with service providers and accordingly there is a clear legal nexus between the retirement fund and its service providers.

However, as much as these contractual relationships may serve as a basis to institute a claim, these agreements may contain indemnities or limitations of liability clauses in favour of the service provider against claims from the retirement fund and other third-parties. It remains a debate for further research whether it is in line with board's fiduciary duty to enter

[18] Magda Wierzycha 'Magda Wierzycha asks hard questions about Steinhoff and asset managers' *Fin24* 7 December 2017, accessed 3 January 2018.
[19] Ibid.
[20] Ibid.
[21] Gareth van Zyl 'Steinhoff along with Jooste, Wiese sued in mega R185bn class action lawsuit' *BizNews*, available at *https://www.biznews.com/sa-investing/2018/08/10/steinhoff-jooste-wiese-class-action-lawsuit*, accessed 5 January 2019.

into agreements that contain terms which are unfair or unreasonable towards the fund. However, such clauses may, in practice, limit any claim that a retirement fund may have against a service provider with the result that the fund cannot successfully claim against the service provider.

Nonetheless, in the case of a member, as will be elaborated further in this report, no such contractual impediment exists due to the absence of any contractual relationship between the member and the service provider. It may therefore be in the interests of the members to pursue claims directly against service providers when their retirement fund is contractually prohibited or limited from doing so.

III TYPES OF RETIREMENT FUNDS

The Pension Funds Act[22] ('PF Act') recognises two categories of retirement funds, namely defined contribution funds ('DC Funds') and defined benefit funds ('DB Funds').[23] The manner in which a member's benefit is calculated, and who bears the investment risk, will depend on the category of retirement fund that the member is a member of.

In respect of DB Funds, the amount of the employee's pension is fixed in advance and does not depend on the retirement fund's investment performance.[24] A DB Fund is created by the employer or its sponsor and the employees are promised a periodic benefit when they retire.[25] The retirement benefit is guaranteed or predetermined by a formula based on the employee's period of service, their salary history and age.[26] The employer is the ultimate guarantor of the benefit and it would be obliged to increase its contributions in order to provide for the benefit, if necessary.[27] In *ICS Pension Fund v Sithole*, Rabie J described the investment risk of a DB Fund as follows:

> 'If the investments made by such a fund perform well, the members do not benefit proportionately. However, if the investments perform poorly, members have the advantage that their pension benefits remain guaranteed by the employer. The employer carries the risk of the investments and the members' pension benefits are secure.'[28]

[22] Pension Funds Act 24 of 1956.
[23] Simphiwe Mduli 'The Role of the Board of a South African Defined Contribution Fund that Offers Investment Choice' (2011) 23 *SA Merc LJ* 247–68 at 258.
[24] Ibid at 249.
[25] Clement Marumoagae 'Liability to Pay Retirement Benefits when Contributions were not paid to the Retirement Fund' (2017) 20 *PER / PELJ* 1-39 at 7.
[26] Ibid.
[27] Rajeev Kesarparshad 'Can the 'pension promise' be broken' (August 2010) *De Rebus* at 1.
[28] *ICS Pension Fund v Sithole* 2009 ZAGPHC 6 (13 January 2009) para 3.

The investment risk in a DB Fund is in stark contrast to the risk of a DC Fund. In a DC Fund, the contributions of the employer and/or the member are specified in the rules and are credited to the individual members' accounts.[29] The contributions are invested and are typically assigned to a notional individual 'pot'.[30] Unlike a DB Fund, the benefits are not underwritten by the employer and the members obtain the advantage if the fund performs well and conversely, if the fund performs poorly, the members' pension benefits are reduced accordingly.[31] Therefore, a member's ultimate retirement benefit depends upon the retirement fund's rate of investment return,[32] the levels of contribution and the fees charged.[33]

DC Funds also allow for 'member investment choice'. Under member investment choice, members are allowed to decide in which asset portfolios/classes their contributions are invested.[34] In *Christopher Banham v Lifestyle Retirement Preserver Pension Plan and Liberty Group Limited,* the Pension Funds Adjudicator ('PFA') remarked that:

> 'I am satisfied that the complainant *chose the portfolios* to invest his funds and consequently *he carried the investment risk*. This means, because his investment is dependent on market volatility, he will suffer the effect of poor investment returns but at the same he will also enjoy the benefit from positive investment returns. As stated the complainant’s funds were invested in portfolios that he chose. The mere fact that Portfolio achieved negative investment growth is not sufficient to amount to maladministration on the part of the insurer. *In addition he has also not provided any evidence in support of his allegation of maladministration*.'[35] (own emphasis)

As seen above, in *Banham*, the member chose the portfolios in which his contributions were invested — this is an example of member investment choice. While the member may elect the portfolios in which the contributions are invested, the board will decide the investment portfolios which will be made available to the members.[36]

---

[29] Kesarparshad op cit note 27 at 1.
[30] England and Wales Law Commission *Consultation Paper No. 125 Fiduciary Duties of Investment Intermediaries* (2014) para 2.22.
[31] *ICS Pension Fund* supra note 28 para 4.
[32] Ibid.
[33] England and Wales Law Commission op cit note 30 para 2.12.
[34] Jeram, N 'Investment Switches in Retirement Funds-the Legal Consequences' (2008) 29 *ILJ* at 2428.
[35] PFA/WE/5029/05/VIA para 5.7.
[36] Ibid.

IV LEGAL RELATIONSHIPS AND ROLE PLAYERS

(a) Members and retirement funds

There are several relationships in the context of retirement funds, each with its own legal constructs and consequences. The relationship between members and the retirement fund is established in terms of the rules of such fund, the PF Act and the common law. Further, a contractual relationship exists between the retirement fund and service providers.

The relationship between the retirement fund and its members is primarily governed by the rules of the retirement fund. The rules operate as the constitution of the retirement fund and the rules contained therein determine the rights and obligations of various stakeholders.[37] In terms of section 13 of the PF Act, the rules of a registered retirement fund shall, subject to the provision of the PF Act, be binding on the members, shareholders and officers and on any person who claims under the rules or whose claim is derived from a person so claiming.[38] The PFA has described the function of the rules as follows:

> 'The rights, duties and the benefit entitlement of the members of a pension fund will always be confined to that which is prescribed in its registered rules. Put differently, the rules determine the right of a member's benefit entitlement regardless of the action or attitude of a functionary such as the participating employer, the board of trustees or the administrator.'[39]

The rules of a retirement fund are supreme and a retirement fund may only do what is contained in the rules.[40] However, as stated by Nkosi, the rules of the retirement fund must be subject to the PF Act and no rule may be in conflict with the provisions of the PF Act.[41]

A notable exception from the above list of persons who are bound by the rules is third-parties such as service providers in relation to their delegated services by the board.[42] Service provides are not bound by the rules, nor do the rules create any legal relationship between the members and service providers or between the retirement fund and service providers.

[37] Rosemary Hunter et al *The Pension Funds Act: A Commentary on the Act, regulations, selected notices, directives and circulars* (2010) at 83-4.
[38] Kobus Hanekom et al *Manual on retirement funds and other employee benefits* (2016) at 141.
[39] *Van der Burgh v Eskom Pension and Provident Fund* PFA/GA/7389/06/VIA para 5.2.1.
[40] Thulani Nkosi 'The Rules of an Occupational Retirement Fund and the Problem of Defaulting Employers: A Reconsideration of Orion Money Purchase Pension Fund (SA) v Pension Funds Adjudicator' (2016) 19 *PER / PELJ* 1-24 at 4.
[41] Ibid at 5.
[42] An exception to this principle is fund administrators who are, in part, regulated in terms of section 13B of the PF Act.

In addition to the duties imposed on the board by the rules of the fund, members of the board owe a fiduciary duty to the retirement fund, and its members and other beneficiaries.[43] The principle that members of the board owe a fiduciary duty to the retirement fund, its members and other beneficiaries is not universally accepted.[44] However, the issue of fiduciary duty will be dealt with in more detail below in Part V.

(b) Asset managers

In simple terms, the role of an asset manager is to decide what to buy or sell, or actually buy and sell, on behalf of a client (such as a retirement fund) in terms of a mandate.[45] In the case of retirement funds, asset managers need to ensure that there is a mixture of assets in order to achieve the long-term income goals of the retirement fund.[46] Asset managers will typically utilise a combination of 'safe' assets, riskier 'high-yield' assets and other investment tools such as derivatives in order to reduce risk and optimise the investment returns of the retirement fund.[47] Where an asset manager acts for a retirement fund, due to the fact that the board must monitor compliance of its service providers and advisors with Regulation 28 of the Regulations promulgated in terms of the PF Act[48] ('Regulations'),[49] the asset manager also needs to ensure that it manages the retirement fund's assets in accordance with Regulation 28. Regulation 28 places a restriction on a retirement fund's ability to invest beyond certain prescribed limits in, amongst other things, certain assets, issuers and offshore assets.[50]

The services performed by an asset manager are 'financial services' as contemplated in the Financial Advisory and Intermediary Services Act[51] ('FAIS Act'). More specifically, the conduct of an asset manager falls within the definition of an 'intermediary service'. An 'intermediary service'[52] is broadly defined to include the buying and selling of financial

---

[43] Muthundinne Sigwadi 'The Personal Liability of Pension Fund Trustees for Breach of Fiduciary Duties' (2008) 20 *SA Merc LJ* 331-46 at 333; *TEK Corporation Provident Fund and Others v Lorentz* 1999 (4) SA 884 (SCA) para 15; *PPWAWU National Provident Fund v Chemical Energy Paper Printing Wood and Allied Workers Union* (2007) 28 ILJ 2701 (W); *Johannesburg Municipality Pension Fund v NCB Employee Benefits (Pty) Ltd* unreported case no 74/01.
[44] MC Marumoagae 'Do Board of Trustees of South African Retirement Funds Owe Fiduciary Duties to both the Funds and Fund Members? The Debate Continues' (2012) 15 *PELJ* 554-69 at 566.
[45] Hanekom op cite note 38 at 724.
[46] Katie Morley 'Pension funds', available at *http://thegatewayonline.com/other-finance/private-equity/pension-funds*, accessed on 3 January 2019.
[47] Ibid.
[48] Regulations in terms of section 36 of the Pension Fund Act 24 of 1956 published under Government Notice R98 in *Government Gazette* 162 of 26 January 1962 (as amended).
[49] Regulation 28(2)*(c)*(ii) of the PF Act.
[50] Hanekom op cite note 38 at 177-85.
[51] Financial Advisory and Intermediary Services Act 37 of 2002.
[52] Section 1 of the FAIS Act.

products[53] which products would include securities such as listed and unlisted shares, debentures and derivatives instruments. In order to lawfully render an 'intermediary service', an asset manager must be licensed under the FAIS Act as an authorised financial services provider ('FSP') or act as a representative of a FSP.[54] In *Tristar Investments v The Chemical Industries National Provident Fund,*[55] Nugent JA described a FSP who renders an 'intermediary service' as '[q]uintessentially, that person is the asset manager, who is mandated to act on behalf of the fund.'[56]

The relationship between the retirement fund and the asset manager would typically be set out in a mandate. This mandate is based on the principles relating to the law of contract [57] and would specify the retirement fund's strategy in terms of asset allocation and acceptable risk.[58] The mandate may also grant the asset manager discretion to pick investments as it deems appropriate in order to meet the strategic requirements of the retirement fund.[59] It is important to note that the asset manager is appointed by the retirement fund in respect of the assets of the retirement fund. The asset manager has no contractual relationship with the members and it does not, nor is obliged to, conclude any mandate with the members.

(c) Insurance companies

A retirement fund may elect not to utilise an asset manager to manage its investments, but may rather decide to enter into a policy of insurance with a long-term insurer registered in terms of the Long-term Insurance Act[60] ('LTI Act'). Retirement funds are entitled to utilise long-term insurance policies as opposed to holding their own assets in order to fund their liability to members to provide benefits. Such retirement funds are known as 'underwritten funds' and their only 'asset' is its claim under a long-term insurance contract.[61]

Retirement funds will generally enter into insurance policies known as 'fund policies'. The parties to a fund policy are the retirement fund and the insurer while the member will be the

---

[53] Section 1 of the FAIS Act.
[54] Section 7(1) of the FAIS Act.
[55] *Tristar Investments v The Chemical Industries National Provident Fund* (455/12) [2013] ZASCA 59 (16 May 2013).
[56] Ibid para 13.
[57] MFB Reinecke et al 'Insurance: Part 2' *The Law of South Africa* vol 12 (2) (2012) para 200.
[58] England and Wales Law Commission op cit note 30 para 3.22.
[59] Ibid.
[60] Long-term Insurance Act 52 of 1998.
[61] *Mungal v Old Mutual Life Assurance Co SA Ltd; Freeman v Old Mutual Life Assurance Co SA Ltd* [2010] 2 All SA 139 (SCA) para 4.

'life assured'.[62] Fund policies can be linked directly or indirectly to a particular portfolio of investment assets.[63] In the case of a linked fund policy, the policy benefits which accrue to the retirement fund (as policyholder) are determined with reference to the value of a portfolio at that time.[64] As such, the value of policy benefits which the retirement fund receives from the insurer can fluctuate if such value is directly linked to a portfolio. In order to counter this fluctuation, insurers offer 'smooth bonus' policies which are indirectly linked to an investment portfolio. The insurer manages these policies so that the fluctuations of the portfolio are 'smoothed' out when the value is attributed to the value of the policy. This 'smoothing' creates a degree of predictability and allows the policy benefits to be positive, even if the portfolio is depressed.[65] Further, fund policies may contain a 'guarantee' which guarantees that the value of the policy benefits will not be less than an agreed amount.[66]

The policy benefits that accrue under the policy of insurance are paid by the insurer to the retirement fund.[67] Whereafter, the retirement fund can utilise the funds it received from the insurer to pay the members the benefits to which they are entitled to in terms of the rules. In practice, the insurer may often directly pay the member the value of their retirement benefit. This practice should not be misconstrued as the insurer having any contractual duty to perform towards the members. Rather, the insurer, by performing to the members, extinguishes its obligations towards the retirement fund. Similar to the arrangements between an asset managers and a retirement fund, the contractual nexus of the fund policy therefore exists between the retirement fund as policyholder and the insurer.

While there is no contractual relationship between the insurer and members, in the recently published Prudential Standard GOI 2 entitled *Governance of Insurers* ('GOI 2') promulgated under the Insurance Act[68] ('Insurance Act'), GOI 2 appears to place duties on an insurer in respect of parties with whom the insurer does *not* have a contractual relationship. GOI 2 requires that in exercising the responsibility for effective governance of the insurer, it must act with 'independence of mind in pursuing the best interest of the insurer, policyholder and other stakeholders'.[69] The term 'stakeholder' is not defined in the Prudential Standards or

[62] Ibid.
[63] Ibid para 16.
[64] Ibid.
[65] Ibid.
[66] Ibid para 30.
[67] Ibid.
[68] Insurance Act 18 of 2017.
[69] Section 8.1 (b) of Prudential Standard GOI 2 *Governance of Insurers*.

the Insurance Act. The Online Oxford Dictionary defines a 'stakeholder' to include '[a] person with an interest or concern in something, especially a business'.[70] Applying this ordinary grammatical meaning, the term 'stakeholder' is broad enough to denote a shareholder or, relevant for current purposes, the members of a retirement fund. If this interpretation is adopted, it is proposed that the insurer has a general legal duty to act in the best interests of stakeholders, which would include the members despite having only issued an insurance policy to the retirement fund.

(d) Other duties applicable to asset managers and insurers

In addition to their statutory duties in terms of the FAIS Act and the Insurance Act, and their obligations under the mandate or insurance policy, as the case may be; asset managers and insurers also have additional duties in terms of the Financial Institutions (Protection of Funds Act)[71] ('Protection of Funds Act'). The objects of the Protection of Funds Act are, amongst other things, to provide for the laws relating to investment, safe custody and administration of funds and trust property by financial institutions.

Asset managers, insurers and retirement funds qualify as a 'financial institution' for the purposes of the Protection of Funds Act. The Protection of Funds Act requires that persons who invest, hold, keep in safe custody, control, administer or alienable any funds of the financial institution, or any other trust property, must, with regard to such funds, observe the utmost good faith and exercise proper care and diligence.[72] As such, when an asset manager invests or controls the assets of the retirement fund (as a financial institution), it is obliged to exercise utmost good faith and exercise proper care and diligence. Unlike an asset manager, an insurer does not invest or control the assets of the retirement fund as, in law, the assets are those of the insurer and the retirement fund merely has a contractual right against the insurer with reference to such assets. However, the persons who invest the assets of the insurer (as a financial institution) would need to observe the same duties to the insurer. Given that these are statutory obligations, an asset manager or insurer cannot contractually exclude the duties imposed on them by the Protection of Funds Act.

---

[70] Oxford Online Dictionary, available at *https://en.oxforddictionaries.com/definition/stakeholder*, accessed 16 October 2018.
[71] Financial Institutions (Protection of Funds Act) 28 of 2001.
[72] Section 2(a) of the Protection of Funds Act.

The FAIS Act and Protection of Funds Act are set to be repealed by the Conduct of Financial Institutions Bill[73] ('COFI').[74] The objects of COFI include to 'protect financial customers, promote the fair treatment and protection of financial customers by financial institutions'.[75] It is proposed that retirement funds should be required to be licensed under both the PF Act and COFI while service providers (including retirement fund benefit administrators) will in future be licensed and authorised under COFI only.[76] A 'financial customer' is defined in COFI with reference to the same definition in the Financial Sector Regulation Act[77] ('FSR Act'). The FSR Act defines a 'financial customer' as —

> '"financial customer" means a person to, or for, whom a financial product, a financial instrument, a financial service or a service provided by a market infrastructure is offered or provided, in whatever capacity, and includes:-
>
> (a) a successor in title of the person; and
>
> (b) *the beneficiary of the product, instrument or service*;'[78] (own emphasis)

As seen above, the definition of a 'financial customer' includes the 'beneficiary' which, in the case of retirement funds, would include the member.

Chapter 3 of COFI proposes that financial institutions (such as insurers and asset managers) must, amongst other things: (i) pay due regard to the interests of its financial customer; (ii) pay due regard to the information needs to its financial customers; and (iii) conduct its business with due skill, care and diligence.[79] Accordingly, once COFI comes into effect, financial institutions will owe statutory duties towards the underlying beneficiaries of a financial service or a financial product which will include the members.

[73] Conduct of Financial Institutions Bill [B - 2018].
[74] National Treasury *Explanatory Policy Paper accompanying the Conduct of Financial Institutions Bill-Paper accompanying the first draft of the COFI Bill* (December 2018) at 20.
[75] COFI at 2.
[76] National Treasury op cit note 74 at 26.
[77] Financial Sector Regulation Act 9 of 2017.
[78] Section 1(1) of the FSR Act.
[79] National Treasury op cit note 74 at 44.

V FIDUCIARY DUTY

(a) General

In *Hofer v Kevitt,*[80] Conradie J remarked that the concept of a fiduciary duty is one with 'no clearly defined meaning'.[81] However, the purpose of a fiduciary duty is to protect the vulnerable when others have discretionary powers to act on their behalf.[82] In its assessment of fiduciary duties, the English and Wales Law Commission ('Commission') in its Consultation Paper entitled '*Consultation Paper No. 215: Fiduciary duties of investment intermediaries*' ('Consultation Paper') stated that fiduciary duties may arise in two circumstances. First, a fiduciary duty may arise on status based circumstances where the relationship falls under a previously recognised category.[83]

Secondly, where the facts and circumstances of a relationship are of a particular nature, it may give rise to a fiduciary duty.[84] In determining whether a fiduciary relationship exists and the nature and extent of the duties of that relationship, one must consider the facts of the particular relationship.[85] A fiduciary duty typically exists whenever a person acquires power of any type, on the condition that the recipient utilises that power in the best interests of another.[86] In *Phillips v Fieldstone*, Heher JA stated that:

> 'There is no magic in the term "fiduciary duty". The existence of such a duty and its nature and extent are questions of fact to be adduced from a thorough consideration of the substance of the relationship and any relevant circumstances which affect the operation of that relationship ... . It is the nature of the relationship, not the specific category of actor involved that gives rise to the fiduciary duty. The categories, like those of negligence, should not be considered closed.'[87]

Accordingly, even if a relationship has not previously been recognised as giving rise to a fiduciary duty, if the facts and circumstances are of a particular nature, they may give rise to a fiduciary duty.

[80] *Hofer v Kevitt* 1996 2 SA 402 (C).
[81] Ibid para 407B.
[82] England and Wales Law Commission op cit note 30 para 4.12.
[83] Ibid at 65.
[84] Ibid.
[85] *Bellairs v Hodnett* 1978 1 SA 1109 at 1130E-F.
[86] JC Shepherd *The Law of Fiduciaries* (1981) at 35.
[87] *Philips v Fieldstone* 2004 (3) SA (SCA) para 27.

(b) The PF Act and fiduciary duty

The PF Act is an example of the first scenario contemplated in the Consultation Paper of when a fiduciary duty exists. The PF Act expressly deals with a fiduciary duty in the context of retirement funds and places such duty on the board. Section 7C(2)*(f)* of the PF Act provides that:

> 'In pursuing its object the board shall have a *fiduciary duty to members and beneficiaries* in respect of accrued benefits and any amount accrued to provide a benefit, as well a fiduciary duty to the fund, to ensure that the fund is financially sound and is responsibly managed and governed in accordance with the rules of this Act.' (own emphasis)

In Information Circular PF No.2 of 2016,[88] the Registrar of Pension Funds, in commenting on a variety of sections of the PF Act, which included section 7C(2)(*f*), remarked that it is clear that the board has an obligation to act with due care, diligence and good faith, to ensure that members' rights are protected at all times.[89]

As alluded to above, the principle that the board owes a fiduciary duty to the fund, its members and other beneficiaries is not universally accepted. Marumoagae argues that the board should only owe fiduciary duty to the retirement fund and that it should merely owe a duty of good faith towards the members.[90] However, in light of several judgments which have unequivocally stated that such fiduciary duty does exist[91] and the express wording of section 7C(2)(*f*) of the PF Act, it is clear that the board does not merely owe a fiduciary duty towards the fund but rather to the fund, its members and beneficiaries.[92]

For the sake of clarity, even if the proposal set out herein is accepted, this report does not suggest that the fiduciary duty of the board (no matter how its scope is understood) is somehow replaced, altered or delegated by the existence of a fiduciary duty owed by the service providers to the members. This was confirmed in *Twerefoo v Liberty Life Association of SA Ltd and Others*[93] where the PFA commented that the members of the board cannot

[88] Information Circular PF No. 2 of 2016 available at *https://www.fsb.co.za/Departments/retirementFund/Circulars/Information%20Circular%202%20of%202016.pdf*.
[89] Ibid at 2.
[90] See Clement Marumoagae 'The need for effective management of pension funds schemes in South Africa in order to protect member's benefits' (2016) 79 *THRHR* 614-31 at 621and Marumoagae op cit note 44 at 566.
[91] See note 43.
[92] Tukishi Manamela 'South Africa's occupational retirement system: A comparative social security perspective' (LLD Thesis, UNISA 2015) at 300.
[93] *Twerefoo v Liberty Life Association of SA Ltd and Others* [2000] 12 BPLR 1437 (PFA) at 1448-9.

abdicate all responsibility for the investment performance once they have delegated this duty. However, given that the duties of the board are not the primary focus of this report, it is unnecessary to consider the duties of the board in any further detail.

(c) Duties of a fiduciary

While the PF Act may expressly set out the aspects of the fiduciary duty owed by the board, the general duties of a fiduciary also exist in common law. As a general principle, a person who stands in a fiduciary relationship may not exceed his or her powers; exercise his or her powers for improper or collateral purposes; fetter his or her discretion; or place himself in a position in which his or her personal interest conflicts or may possibly conflict with his or her duties.[94] A fiduciary must also act in the dependent's interest, and not his or her interest.[95] In trust law, the concept of acting in the 'interests' or 'best interests' of a trust has been held by English courts to be equivalent to the principle that power should be exercised to promote the purpose of a trust.[96] However, it is important to note that the aforementioned duties are not exhaustive as the duties of a fiduciary will change depending on the facts and circumstances of each case.[97] Accordingly, it is possible that in addition to the duties mentioned herein that a fiduciary may owe other duties, however, it is not necessary that a fiduciary owe each of these duties.

According to du Toit, a South African fiduciary is under a single fiduciary duty which comprises a number of specific component duties.[98] The relevance of the component duty of this 'general fiduciary duty' will be dependent on the particular circumstances of a specific scenario having regard to the relationship between the various parties as well as any relevant circumstances which have an effect on the operation of such relationship.[99] This principle is confirmed by Lord Browne Wilkinson in *Henderson v Merret Syndicates Ltd* who held that —

[94] Sigwadi op cit note 23 at 333.
[95] Benjamin J. Richardson 'Do the Fiduciary Duties of Pension Funds Hinder Socially Responsible Investment?' (2007) 22 *Banking and Finance Law Review* 146-201 at 150.
[96] *Merchant Navy Ratings Pension Fund Trustees Limited v Stena Line Limited and others* ([2015] EWHC 448 (Ch)). See also Keith Bryant SC '*Abridged Joint Opinion: The Legal Duties of Pension Fund Trustees in Relation to Client Change*' (25 November 2016) para 17, available at *https://www.documents.clientearth.org/library/download-info/qc-opinion-the-legal-duties-of-pension-fund-trustees-in-relation-to-climate-change/*), accessed 12 October 2017.
[97] Ibid.
[98] Francois du Toit 'The fiduciary office of a trustee and the protection of contingent trust beneficiaries' (2007) 3 *Stell LR* 469-82 at 473.
[99] Ibid.

> 'The phrase 'fiduciary duties' is a dangerous one, giving rise to a mistaken assumption that all fiduciaries owe the same duties in all circumstances. That is not the case.' [100]

While the duties of a fiduciary will differ depending on the circumstances, such duties will also change over the passage of time. A fiduciary duty is not static and is subject to evolution over time[101] as a result of changing social norms, technology and markets.[102] Therefore, the mere fact that a fiduciary duty has not been previously recognised in the same circumstances should not automatically shield one from the claim that a fiduciary duty exists. The existence and scope of such a duty depends not on the prior recognition of such a duty but is rather dependent on a factual enquiry having regard to the circumstances of the relationship. Similarly, the scope of such a duty will depend on the circumstances under consideration.

(d) United Kingdom Approach

The argument that service providers should owe a fiduciary duty in the absence of any existing contractual or statutory relationship with members finds support in the UK from Professor Kay in his report entitled '*The Kay Review of UK Equity Markets and Long-term Decision Making: Final Report*'[103] ('Kay Report'). Kay was requested by the Secretary of State for Business, Innovation and Skills to compile a report on how well the UK equity markets were achieving their core purpose of enhancing the performance of UK companies and to enable savers to benefit from the activity of these businesses through returns to direct and indirect ownership of shares in UK companies.[104] Principle 5 of the Kay Report emphasised the role of a fiduciary duty in the investment chain. Principle 5 states that:

> '*All participants in the equity investment chain should observe fiduciary standards in their relationships with their clients and customers*. Fiduciary standards require that the client’s interests are put first, that conflict of interest should be avoided, and that the direct and indirect costs of services provided should be reasonable and disclosed. These standards should not require, nor even permit, the agent to depart from generally prevailing standards of decent behaviour. Contractual terms should not claim to override these standards.' (own emphasis)

---

[100] *Henderson v Merret Syndicates Ltd* [1995] 2 AC 145 at 206.
[101] James Hawley, Keith Johnson and Ed Waitzer 'Reclaiming Fiduciary Duty Balance' (2011) 4 *Rotman International Journal of Pension Management* 4-16 at 7.
[102] Freshfields Bruckhaus Deringer, *A Legal Framework for the Integration of Environmental, Social and Governance Issues into Institutional Investment* (October 2005) at 9.
[103] J Kay *The Kay Review of UK Equity Markets and Long-Term Decision Making: Final Report* (2012).
[104] Ibid at 9.

The above proposed Principle 5 must be understood in the context of changes to the structure of investments. The Kay Report highlights the fact that there has been increased growth in intermediation in the context of investment.[105] Kay suggests that while an increase in the number of intermediaries in the so-called 'investment chain' has benefits such as greater professionalism and efficiency, it has also led to an increase in costs and the potential for misaligned incentives.[106] For example, members have a long-term interest in investing which may not be properly served by all participants in the increased investment chain.[107]

In response to the Kay Report, the UK Government commented that the phrase 'fiduciary' may be used to refer to a strict legal relationship and to which the strictest duties of loyalty and prudence are applicable; alternatively '[o]thers however use the word fiduciary to describe a more general duty of care'.[108]

The UK Government's response to the Kay Report provides some useful guidance to understand the content of a service provider's duties. Although it elected to avoid using the word 'fiduciary' and the following principles were suggested to apply to the equities market (in general) and not specifically to the retirement industry, the UK Government proposed the following principles to apply to all participants in the investment chain (i.e. service providers).[109] First, they should act in good faith; in the long-term best interests of their clients and beneficiaries (i.e. members); and in line with generally prevailing standards of decent behaviour.[110] Secondly, these duties should not be contractually overridden.[111]

Although the UK has not formerly adopted the principle that service providers owe a fiduciary duty towards members, there is government-backed research and proposals that support the argument that all participants in the 'investment chain' (such as asset managers and insurers) should adhere to standards that are applicable to both clients and beneficiaries.

(e) Service providers as fiduciaries

At the outset, and as explained above, it is worth noting that neither an asset manager nor an insurer owe a contractual or statutory duty towards a member except for a limited duty of an

[105] Ibid at 10.
[106] Ibid.
[107] Sir George Cox, *Overcoming short-termism within British business: The key to sustained economic growth* (2013) at 20-1.
[108] Department for Business, Innovation and Skills, *Ensuring equity markets support long-term growth: The Government Response to the Kay Review* (2012) para 2.8.
[109] Ibid.
[110] Ibid.
[111] Ibid.

insurer to act in the best interests of stakeholders in the case of governance. Prior to considering whether a service provider should owe a fiduciary duty towards members, the reasons informing a courts' potential reluctance to extend a fiduciary duty to service providers will be considered.

In its Consultation Paper, the Commission proposed three reasons for courts' reluctance to extend fiduciary duties in financial markets. Although the Consultation Paper originates from England and Wales, it is submitted that the arguments and findings set out therein should be applicable, or at least analogous, in South Africa given the absence of similar research in South Africa. Further, with the recent adoption of the 'Twin Peaks' model of financial regulation, South African financial regulation has moved towards greater conformity with the international experience, particularly the experience of the UK.[112]

First, the Consultation Report states that judges are reluctant to assign a fiduciary duty in a commercial relationship.[113] The Consultation Paper refers to authority and case law from Australia, New Zealand and the US[114] which all support the principle that in the case of arm's length commercial transactions, courts should not impose a higher degree of obligation than what was agreed between the parties.[115]

Secondly, courts tend to interpret the obligations owed by parties in line with the rules set out by regulatory authorities.[116] It is argued that regulatory authorities are the parties responsible for determining standards in financial markets and it is not the role of courts to interfere with those standards.[117]

Lastly, in order to understand a party's duty, courts use the contract between the parties as a starting point and interpret a party's duty in line with the contractual terms.[118]

The above three reasons serve as a rebuttable to the argument proposed herein that service providers ought to owe a fiduciary duty to members. While these reasons may be convincing when argued in the general context of financial markets, they do not necessarily hold true

[112] Andrew Godwin, Timothy Howse and Ian Ramsay 'Twin Peaks: South Africa's Financial Sector Regulatory Framework' (2017) 134 *SALJ* at 672.
[113] England and Wales Law Commission op cit note 30 at 171.
[114] See Kennedy J 'Equity in a Commercial Context' in P Finn *Equity and Commercial Relationships* 1 ed (1987) at 15; *DHL International (NZ) Ltd v Richmond Ltd* [1993] 3 NZLR; and *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41.
[115] England and Wales Law Commission op cit note 30 at 171-72.
[116] Ibid at 172.
[117] Ibid.
[118] Ibid at 174.

when compared against the arrangements between a member and a service provider in the South African retirement funds sector.

In response to the first reason set out above against the extension of a fiduciary duty in the case of arm's length commercial transactions, South African law already recognises duties in the Protection of Funds Act that exist in addition to contractual arrangements. These duties include the duty to act in utmost good faith and to exercise due care and diligence. These duties are similar to the duties imposed on a fiduciary in common law. Therefore, the claim that the existence of a commercial contractual relationship should exclude a fiduciary duty does not necessarily hold true in a South African context as South African law is receptive to the extension of duties similar to those of a fiduciary in addition to those duties contained in the agreement between parties.

In response to the second reason, while the services rendered by service providers to the retirement fund are commercial in nature, there is no commercial relationship between the members and the service providers. The members do not contract with the service providers and therefore have no ability to negotiate the terms upon which the service provider must perform their duties. In this regard, the members are vulnerable to the investment decisions of the service providers as they cannot exercise any control over such decisions.

Lastly, while the absence of regulatory standards describing the duties owed by a service provider to a member may indicate that no fiduciary relationship should exist; such absence is not definitive in and of itself. In determining whether a fiduciary duty exists, one must consider each relationship on its own facts. Furthermore, as illustrated in GOI 2 and COFI, there appears to be growing regulatory recognition in South Africa that a financial institution's duties are not limited to the person with whom it contracts and may be extended to stakeholders and beneficiaries.

It is submitted further that the relationship between a service provider and members, depending on the circumstances, support the existence of a fiduciary duty for the following reasons. While the retirement fund may provide a mandate within which service providers must operate, both assets managers and insurers are afforded a high degree of discretion in relation to investment decisions. Given this discretion, the actions of these service providers will have a material impact on the benefit that the member ultimately receives from the retirement fund. As was illustrated in Part II above, service providers have a significant amount of retirement funds' assets under management. To the extent that the service provider achieves good investment returns, such benefits will be passed onto the retirement fund either in the form of income or capital growth (in the case of an asset manager) or increased policy benefits (in the case of an insurer). The retirement fund will therefore be able to provide an increased benefit to members upon retirement (particular in the case of a DC Fund). However, the converse is also true. Where a service provider is unable to generate above market investment returns or the value of the retirement fund's assets reduce, this will have a negative indirect impact on the value of the members' retirement benefits. This reality was recognised by Sir George Cox in the Cox Review, an independent review commissioned by the British Labour Party wherein he stated that '[t]he ultimate shareholder, the individual saver or pension holder, is a long way removed from the company on whose growth his or her prosperity ultimately depends.'[119]

If one has regard to the circumstances surrounding the relationship between members and a service provider, compelling reasons exist to regard a service provider as a fiduciary who owes a fiduciary duty to the members. While the arrangements between retirement funds and service providers may be arranged to reduce the discretion granted to service providers or afford the retirement fund and its members some protection from investment risk (for example, smooth bonus policies or fund policies with guarantees), members are ultimately dependent on these decisions despite being removed from the decision making process. Secondly, albeit only in the case of insurers, there is regulatory recognition that financial institutions owe duties to stakeholders such as members despite the absence of contractual duties. However, COFI does recognise that, in future, financial institutions will owe duties towards beneficiaries. Furthermore, over time, the number of persons involved in the 'investment chain' has evolved such that there is recognition in foreign jurisdictions that each person in the investment chain should owe a fiduciary duty. Accordingly, it is submitted that a service provider should, particularly where they exercise a high degree of discretion, owe a fiduciary duty towards the members.

This conclusion may cause many in the investment community to recoil at the thought that they owe a fiduciary duty towards their clients' clients. This sense of dread may arise from the term 'fiduciary' and the way in which it has been interpreted and understood. However, as explained above, not all fiduciaries owe the same duty. One must therefore determine the content of a service provider's duty in order to assess whether it should be understood in a strict or more general sense.

---

[119] Cox op cit note 107 at 20.

It is submitted that the primary fiduciary relationship in the context of retirement funds must exist with the board. This view is shared by National Treasury who stated that once COFI comes into effect, boards will remain responsible and accountable for ensuring compliance with applicable legislation in line with their broader fiduciary duties.[120] Given its contractual relationship with the retirement fund and the fact that it is not a service provider's duty to provide members with benefits, the content of a service provider's fiduciary duty must differ from that of a member of the board.

It is submitted that the UK Government's response to the Kay Report could be used to inform the content of a fiduciary duty owed by a service provider. It is proposed that service providers should act in good faith; in the long-term best interests of their clients and beneficiaries (i.e. members); and in line with generally prevailing standards of descant behaviour.

Lastly, a service provider may encounter significant difficulties if it owes a fiduciary duty to each individual member. For example, depending on the age and risk-appetite of individual members, they will each have different investment requirements. If a service provider is required to act in the long-term interests of each individual member, it will inevitably breach its fiduciary duty to act in an individual member's long-term interests when it adopts a particular investment strategy which is contrary to those interests. It is therefore submitted that any duty that is owed by a service provider should be owed to the members as a class of persons, and not on an individual basis.

VI ABILITY TO RECOVER DAMAGES FOR BREACH OF FIDUCIARY DUTY

A claim for damages for breach of a fiduciary duty may arise because of a breach of contract or in delict.[121] Given the absence of a contractual relationship between the members and the service providers, any claim for damages brought by the members against the service provides would need to be based in delict.

It is settled law that the essential elements for delictual liability are harm sustained by the plaintiff, conduct on the part of the defendant which is wrongful, a causal connection between the conduct and the plaintiff's harm and fault or blameworthiness on the part of the defendant.[122] However, the mere fact that a member may suffer a loss or harm due to

---

[120] National Treasury op cit note 74 at 26.
[121] *Daewoo Heavy Industries (SA) (Pty) Ltd v Banks* [2004] 2 All SA 530 (C); *Da Silva v CH Chemicals (Pty) Ltd* [2009] 1 All SA 216 (SCA).
[122] JR Midglev 'Delict' *The Law of South Africa* vol 15(3) (2016) para 3.

negative investment performance is insufficient to found a claim in delict.[123] In *Stephenson v KD Homes Pension Fund*,[124] the PFA held that:

> 'As far as the performance of the underlying portfolio in which the complainant's benefit is invested, *something more is required than the bare fact that it has not performed well, or even that the complainant has sustained loss in investment value*. The nature of defined contribution schemes is that the member assumes the risk of investment return, and is therefore subject to prevailing market conditions.... In any event, the complainant has not suggested that the board of trustees [management] was negligent in terms of investment decisions taken, or that there was a failure to adopt specified investment strategies. Without those allegations, it is not possible to establish any entitlement to the relief sought.'[125] (own emphasis)

In *Stephenson*, the complaint related to the decrease in the value of the complainant's retirement benefit which complaint was levelled at the retirement fund, and not at its service providers. It is submitted that the same principle should apply in the case of service providers; namely — mere loss is insufficient and there must be fault or blameworthiness on the part of the service provider in order for a delictual claim to succeed.

As was argued above, where a service provider exercises a high degree of discretion with respect of investment decisions, it should owe a limited fiduciary duty to the members. In particular and as proposed, the content of that duty requires that service providers must act in good faith; in the long-term best interests of members and in line with generally prevailing standards of descant behaviour. Whether or not a service provider has failed to satisfy these requirements will depend on the facts of each claim. However, for current purposes, it will be assumed that a service provider did breach their fiduciary duty by breaching one or more of the aforementioned requirements.

In the event that a service provider breaches its fiduciary duty which results in a reduction of the notional individual 'pot', it is debatable whether the member actually suffers a loss. In the case of DC Funds, the member bears the investment risks. Further, the member has no right to the benefit unless provided for in the rules as a member's right to claim a benefit only accrues when the event giving rise to such benefit has occurred and the benefit is due and payable.[126] As such, a member has no right to a benefit and the board may change the rules of

---

[123] Jeram op cit note 34 at 2428.
[124] *Stephenson v KD Homes Pension Fund (*PFA/KZN/5475/06/NS).
[125] Ibid para 5.7.
[126] Kesarparshad op cit note 27 at 2.

the fund, provided the requirements of section 12 of the PF Act are satisfied.[127] A member will therefore only have a right to a benefit when such right accrues in terms of the rules. Until such time, a member has no right to a benefit.

Given the fact that in terms of most rules, the right to a benefit only accrues upon retirement, death or when the member exits the retirement fund, if the notional benefit standing to the credit of the member is reduced (even significantly), due to the legal position that the member does not have a right to such amount until provided for in the rules, or stated otherwise, the right to such benefit has not accrued, the member never actually suffers a loss. The effect of this construction is that it would severely limit members' ability to institute a delictual claim against a service provider because even if they could establish that the service provider breached its fiduciary duty, they cannot recover damages for such breach as they do not suffer a loss.

However, it may be possible for a member to claim for prospective losses. However, this would be contrary to the general rule that damages cannot be claimed solely for prospective loss, because a plaintiff's cause of action is only established once damage has indeed been sustained.[128] However, Boberg supports the view that, where prospective loss can only be established as a matter of reasonable probability, a claim for damages in respect of such loss should lie.[129] Boberg's contention was acknowledged by the Supreme Court of Appeal in *Jowell v Bramwell-Jones,*[130] but Scott JA opined that —

> 'the inevitable uncertainty associated with such an approach is likely to prove impractical and result in hardship to the plaintiff particularly insofar as the running of prescription is concerned'.[131]

The court in *Jowell* accordingly left the question of the appropriateness of an action only for prospective loss open.

It is submitted that given the nature of retirement benefits, members should be entitled to claim for prospective loss provided the loss can be established, as Boberg suggests, as a 'matter of reasonable probability'. To disallow a member to claim damages against a service provider for a breach of its fiduciary duty would be contrary to the maxim 'ubi jus ibi remedium' or rather, for every right the law provides a remedy, either by way of an interdict

---

[127] Ibid at 2.
[128] du Toit op cit note 98 at 480.
[129] Ibid.
[130] *Jowell v Bramwell-Jones* 2000 (3) SA 274 (SCA) para 22.
[131] Ibid para 22.

to protect it or by way of an action to enforce it or to recover damages for its invasion.[132] Furthermore, to disallow a claim of damages purely because the loss has not materialised would be severely prejudicial to the members. As seen in the case of Steinhoff, even though the active members may not have actually suffered a loss, there is certainly a reasonable possibility that, assuming the relevant service providers breached their fiduciary duty, such members will suffer a prospective loss as a result of the conduct of their retirement fund's service providers when they become entitled to their retirement benefit.

Much of the above debate on damages would not be applicable to DB Funds. As stated in Part III, in the case of DB Funds, the employer (as guarantor) bears the investment risk. As such, even if a DB Fund suffers a significant loss due to a service provider's wrongful conduct, the members will never suffer a loss (prospective or otherwise). Accordingly, the above discussion on damages and retirement funds would only be applicable in the case of DC Funds as the members of such funds bear the investment risk and therefore would have an interest in pursuing damages against their retirement fund's service providers.

VII CONCLUSION

Service providers perform an important and significant role in the retirement fund sector. While the retirement fund board of management retains its fiduciary duty towards the retirement fund, members and beneficiaries; service providers hold a substantial amount of retirement funds' assets under management and their investment decisions do have a bearing on the benefit that a member will ultimately receive. However, as the law currently stands, apart from a general duty on insurers to act in the bests interests of stakeholders in the case of governance, neither insurers nor asset managers owe any contractual or statutory duty to the members. However, due to the important role that service provider's play and changing social norms, there is growing recognition, both locally and abroad, that such service providers must owe duties towards beneficiaries such as members. The UK has recognised that each person in the investment chain should comply with certain standards while COFI has proposed that financial institutions owe certain duties to beneficiaries of financial products and financial services.

Although COFI should be welcomed as it recognises the fact that financial institutions must owe duties to beneficiaries, it is submitted that the current absence of any statutory recognition of such duties should not prohibit a member's ability to recover damages from a

[132] See *Amod v Parsotham* 1929 NPD 167.

service provider. Where a service provider is afforded with a high degree of discretion, having regard to the nature of the relationship between such service provider and the members, a fiduciary duty should be imposed on the service provider in favour of the members. This fiduciary duty is separate from, and in addition to, the fiduciary duties owed by the board and differs in its content. Further, it is argued that to the extent a service provider breaches this duty; the members have a claim against such service provider. While it is unlikely that members of a DB Fund will ever seek damages from a service provider as their benefits are guaranteed by the employer, members of DC Funds, given that they bear the investment risk, would have an interest in pursuing action against the service provider. Lastly, given that the benefits only vest with the members in terms of the rules, any claim for damages would likely occur before a member's right to benefits vests. A member would therefore need to claim for prospective damages and argue that once their benefits vest, they will suffer a loss. Despite the courts not recognising claims for prospective loss, it is submitted that in the case of retirement fund members, compelling reasons exists to allow a claim for prospective loss provided the claim for prospective loss is established as a matter of reasonable probability.

BIBLIOGRAPHY

(a) Books

Hanekom K et al *Manual on retirement funds and other employee benefits* (2016)

Hunter R, Esterhuizen J, Jithoo T, and Khumalo S *The Pension Funds Act: A Commentary on the Act, regulations, selected notices, directives and circulars* (2010)

Kennedy J 'Equity in a Commercial Context' in P Finn *Equity and Commercial Relationships* 1 ed (1987)

Midglev JR 'Delict' *The Law of South Africa* vol 15 (3) (2016)

Reinecke MFB et al 'Insurance: Part 2' *The Law of South Africa* vol 12 (2) (2012)

Shepherd JC *The Law of Fiduciaries* (1981)

(b) Cases

Amod v Parsotham 1929 NPD 167

Bellairs v Hodnett 1978 1 SA 1109

Christopher Banham v Lifestyle Retirement Preserver Pension Plan and Liberty Group Limited PFA/WE/5029/05/VIA

Da Silva v CH Chemicals (Pty) Ltd [2009] 1 All SA 216 (SCA)

Daewoo Heavy Industries (SA) (Pty) Ltd v Banks [2004] 2 All SA 530 (C)

DHL International (NZ) Ltd v Richmond Ltd [1993] 3 NZLR

Henderson v Merret Syndicates Ltd [1995] 2 AC 145

Hofer v Kevitt 1996 2 SA 402 (C)

Hospital Products Ltd v United States Surgical Corporation (1984) 156 CLR 41

ICS Pension Fund v Sithole 2009 ZAGPHC 6 (13 January 2009)

Johannesburg Municipality Pension Fund v NCB Employee Benefits (Pty) Ltd unreported case no 74/01

Jowell v Bramwell-Jones 2000 (3) SA 274 (SCA)

Merchant Navy Ratings Pension Fund Trustees Limited v Stena Line Limited and others ([2015] EWHC 448 (Ch))

Mungal v Old Mutual Life Assurance Co SA Ltd; Freeman v Old Mutual Life Assurance Co SA Ltd [2010] 2 All SA 139 (SCA)

Philips v Fieldstone 2004 (3) SA (SCA)

PPWAWU National Provident Fund v Chemical Energy Paper Printing Wood and Allied Workers Union (2007) 28 ILJ 2701 (W)

*Stephenson v KD Homes Pension Fund (*PFA/KZN/5475/06/NS)

TEK Corporation Provident Fund and Others v Lorentz 1999 (4) SA 884 (SCA)

Tristar Investments v The Chemical Industries National Provident Fund (455/12) [2013] ZASCA 59 (16 May 2013)

Twerefoo v Liberty Life Association of SA Ltd and Others [2000] 12 BPLR 1437 (PFA)

Van der Burgh v Eskom Pension and Provident Fund PFA/GA/7389/06/VIA

(c) Internal sources

CNBC Africa 'Inside the Steinhoff sage, one of the biggest cases of corporate fraud in South African business history' (28 June 2018), available at *https://www.cnbcafrica.com/insights/steinhoff/2018/06/28/steinhoff-rise-fall/*, accessed 12 October 2018

Ensor L 'Pension funds lost billions over Steinhoff' *Timeslive* 31 January 2018.

Morley K 'Pension funds', available at *http://thegatewayonline.com/other-finance/private-equity/pension-funds*, accessed on 2 February 2018

Oxford Online Dictionary, available at *https://en.oxforddictionaries.com/definition/stakeholder*, accessed 16 October 2018

van Zyl G 'Steinhoff along with Jooste, Wiese sued in mega R185bn class action lawsuit' *BizNews*, available at *https://www.biznews.com/sa-investing/2018/08/10/steinhoff-jooste-wiese-class-action-lawsuit*, accessed 5 January 2019

Wierzycha M 'Magda Wierzycha asks hard questions about Steinhoff and asset managers' *Fin24* 7 December 2017, accessed on 3 January 2018

(d) Journal articles

du Toit F 'The fiduciary office of a trustee and the protection of contingent trust beneficiaries' (2007) 3 *Stell LR* 469-82

Godwin A, Howse T, and Ramsay I 'Twin Peaks: South Africa's Financial Sector Regulatory Framework' (2017) 134 *SALJ* 665-702

Hawley J, Johnson K, and Waitzer E 'Reclaiming Fiduciary Duty Balance' (2011) 4(2) *Rotman International Journal of Pension Management* 4-16

Jeram N 'Investment Switches in Retirement Funds-the Legal Consequences' (2008) 29 *ILJ* 2427-39

Kesarparshad K 'Can the 'pension promise' be broken' (August 2010) *De Rebus*

Marumoagae MC 'Do Board of Trustees of South African Retirement Funds Owe Fiduciary Duties to both the Funds and Fund Members? The Debate Continues' (2012) 15 *PELJ* 554-69

Marumoagae MC 'Liability to Pay Retirement Benefits when Contributions were not paid to the Retirement Fund' (2017) 20 *PER / PELJ* 2-39

Marumoagae MC 'The need for effective management of pension funds schemes in South Africa in order to protect member's benefits' (2016) 79 *THRHR* 614-31

Mduli SM 'The Role of the Board of a South African Defined Contribution Fund that Offers Investment Choice' (2011) 23 *SA Merc LJ* 247-68

Nkosi TG 'The Rules of an Occupational Retirement Fund and the Problem of Defaulting Employers: A Reconsideration of Orion Money Purchase Pension Fund (SA) v Pension Funds Adjudicator' (2016) 19 *PER / PELJ* 1-24

Richardson BJ 'Do the Fiduciary Duties of Pension Funds Hinder Socially Responsible Investment?' (2007) 22 *Banking and Finance Law Review* 146-201

Sigwadi M 'The Personal Liability of Pension Fund Trustees for Breach of Fiduciary Duties' (2008) 20 *SA Merc LJ* 331-46

(e) Legislation and sub-ordinate legislation

Conduct of Financial Institutions Bill [B - 2018]

Financial Advisory and Intermediary Services Act 37 of 2002

Financial Institutions (Protection of Funds Act) 28 of 2001

Financial Sector Regulation Act 9 of 2017

Information Circular PF No. 2 of 2016 available at *https://www.fsb.co.za/Departments/retirementFund/Circulars/Information%20Circular%202%20of%202016.pdf*

Insurance Act 18 of 2017

Long-term Insurance Act 52 of 1998

Pension Funds Act 24 of 1956

Prudential Standard GOI 2 *Governance of Insurers*

Regulations in terms of section 36 of the Pension Fund Act 24 of 1956 published under Government Notice R98 in *Government Gazette* 162 of 26 January 1962 (as amended)

(f) Law Commission Reports

England and Wales Law Commission *Consultation Paper No. 125 Fiduciary Duties of Investment Intermediaries* (2014)

(g) Other

Alexander Forbes *Manager Watch Annual Survey: Survey of Retirement Fund Investment Managers* (December 2017)

Bryant K SC '*Abridged Joint Opinion: The Legal Duties of Pension Fund Trustees in Relation to Client Change*' (25 November 2016) para 17, available at *https://www.documents.clientearth.org/library/download-info/qc-opinion-the-legal-duties-of-pension-fund-trustees-in-relation-to-climate-change/*), accessed 12 October 2017

Cox G *Overcoming short-termism within British business: The key to sustained economic growth* (2013)

Department for Business, Innovation and Skills *Ensuring equity markets support long-term growth: The Government Response to the Kay Review* (2012)

Financial Services Board and Financial Sector Conduct Authority *2018 Annual Report* (2018)

Freshfields Bruckhaus Deringer *A Legal Framework for the Integration of Environmental, Social and Governance Issues into Institutional Investment* (October 2005)

Kay J *The Kay Review of UK Equity Markets and Long-Term Decision Making: Final Report* (2012)

Manamela T ‘South Africa’s occupational retirement system: A comparative social security perspective’ (LLD Thesis, UNISA 2015)

National Treasury *Explanatory Policy Paper accompanying the Conduct of Financial Institutions Bill - Paper accompanying the first draft of the COFI Bill* (December 2018)

United Nations Global Compact, UNEP Finance Initiative, Principles for Responsible Investing 'Fiduciary *Duty in the 21st Century*' (September 2015)