

How to do an apportionment of surplus – practical steps and guidance

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Preparing a surplus project plan

- Identify:
 - what is required for each action item
 - how long will it take to complete
 - what needs to be completed before the task can commence
 - what needs to wait until this task is completed
- Set target dates for completion of each action item
- Check that dependant deadlines match

Step 1: Pensioner liability and pension increase policy

- Establish a Pension Increase Policy – Section 14B(3)
 - Applicable to both pensioners and deferred pensioners
 - Must aim to award a percentage of inflation
 - Affordability?
 - Must state frequency of review (at least annually)
 - Triennial comparison to minimum pension increase
 - Communicate policy to pensioners

Minimum Pension Increase – Section 14B(4)

- Starts with pension increase to be granted on the effective date of the first actuarial valuation following 7 December 2001
- Minimum pension is the lesser of:
 - Increase implied by calculation of notional pensioner account

- Increase to give full CPI increase from retirement to current
- Subject to overall minimum of pension increase policy

Notional pensioner account

- Information required for full review:
 - Actuarial reserve at date of retirement per pensioner
 - Fair value adjustment at date of retirement
 - Amount commuted
 - Pensions paid

Notional pensioner account Cont.

- Reasonable expenses
- Cost of special increases
- Gross investment return earned on Fund assets
- Reasonable expenses to deduct from investment return

Notional pensioner account

- May use an “approximate method”
- For example, increase implied per pensioner based on net investment return earned per annum after allowance for post-retirement interest rate

Step 2: Improper uses

- Investigation of improper uses – Section 15B(6)
- Events giving rise to improper uses
 - Benefit improvements for executives
 - Employer obligation to subsidise medical costs after retirement
 - Recognition of service for selected members/members transferred in
 - Employer contribution holiday after 7 December 2001

Improper uses

- Review:
 - Minute books
 - Actuarial valuation and other actuarial reports

- Company personnel records in respect of exiting executives
- Communication to members and pensioners

Improper uses

- List potential improper uses
- Review each against the wording contained in the Act
- If unclear consider obtaining a legal opinion
- Document the investigation and findings
- Approach the employer to discuss funding of improper uses
 - Maximum period of 9 years?

Step 3: Contingency Reserve Accounts

- Contingency Reserve Accounts set up “to provide for explicit contingencies”
- Deducted from value of assets together with value placed on liabilities
 - Deduction reduces surplus
 - The Registrar may reject any Contingency Reserve Account that does not reflect the financial position of the fund

Contingency Reserve Accounts

- List explicit contingencies
- Method and basis on which reserve calculated must be clear in respect of each contingency
- Reasonable cut-off for period over which contingencies will be reserved for?

Step 4 Surplus at Surplus Apportionment Date

- Calculation requires the following to be available, all as at Surplus Apportionment Date:
 - Annual Financial Statements
 - Actuarial Valuation results (actuarial value of assets and liabilities)
 - Contingency Reserve Accounts
 - Value of Improper Uses
 - Will require a minimum of 6 - 12 months to compile the above

Surplus at Surplus Apportionment Date

- Actuarial value of assets
- Actuarial value of active member liabilities including allowance for minimum benefits
- Actuarial value of pension liability including calculations of notional pensioner account
- Contingency Reserve Accounts
- Value of Improper Uses

Step 5 Former Member Issues

- Appointment of the former member representative – Section 15B(3)
- Former member representative only required if the fund has a surplus
- Should:
 - Have knowledge of pension funds and financial matters
 - Have specific knowledge of fund circumstances
 - Should be able to communicate with former members
 - Should be seen as unbiased

Former Member Issues

- The trustees must agree on the appointment
- The individual should be approached, and if they accept, a contract should be drawn up covering duties, payment, etc.

Former Member Issues

- Advertisement aimed at former members – Section 15B(4)(a)(iii)
 - Advertisement should be placed nationally and locally
 - Should clearly specify information required and submission of this information

Former Member Issues Cont

- Must wait 6 to 9 months before excluding former members because of lack of data
- Should aim to place advertisement as soon as possible (if the fund has a surplus)

Former Member Issues

- Collation of former member information – Section 15B(4)
 - Obtain records from the administrator
 - Personnel records
 - Receiving fund records for transfers
 - Trade union/staff representative organisation records
 - Response to advertisement by former members

Step 6 Minimum Benefit Calculations

- Minimum benefits for pensioners
 - Calculated as a part of minimum pension/notional account calculations before determining surplus
- Minimum benefits for former members
 - Collation of former member data required before top-up calculations can be completed

Step 6 Minimum Benefit Top-Ups

- Minimum Benefits for Former Members – Section 14B(2)
 - Calculation required per former member
 - Compare the minimum benefit calculated at date of exit with the actual benefit paid
 - Any positive difference must be accumulated with nett actual fund returns from the date of exit to the Surplus Apportionment Date.
 - If surplus exceeds value of minimum benefit top-ups they may be reduced proportionately

Step 7 Apportionment of Residual Surplus

- Residual Surplus - Section 15B(5)(d)
- Calculated after all actuarial surplus and minimum top-up calculations for former members have been completed

- Residual surplus must be equitably split between:
 - Existing members/pensioners, former members and the employer
 - Secondary top-up process?

Apportionment of Residual Surplus

- Must take into account financial history of the fund:
 - Annual Financial Statements
 - Actuarial valuation reports
 - Minute books
 - Investigate origin and use of actuarial surpluses in the past

Step 8: Communication of Surplus Scheme

- Communication – Section 15B(9)(d) and (e)
- Communication must:
 - Be clear and understandable
 - Give details of the allocation of actuarial surplus
 - Be explicit about how and where complaints can be lodged
 - Allow 12 weeks after despatch of communication for stakeholders to lodge written complaints

Communication of Surplus Scheme

- Each complaint must be dealt with appropriately:
 - Written response
 - Review of scheme based on objection
- All complaints and responses must be documented

Step 9: Review of Surplus Apportionment Scheme

- The trustees must review the objections to decide if the surplus apportionment scheme needs to be amended
- All objections and the trustees' responses must be included with the submission of the final surplus apportionment scheme

Step 10: Submission of Surplus Scheme

- Format and attachments for submission – Section 15B(9)
 - Specified format for submission
 - Copy of every actuarial or other statement taken into account
 - Former member report
 - Valuator's certificate and other particulars/reports
 - Independent actuary's report (if required)
 - Details of objections raised by stakeholders and actions taken to address objections

Step 11: Implement Surplus Apportionment Scheme

- Registrar will issue a certificate in terms of Section 15B(9)(i)
- Certificate will indicate that all the requirements of the subsection have been fulfilled
- The trustees can then proceed with:
 - Payment of top-up benefits to former members
 - Distribution of residual surplus

Step 12: Amend Rules of Fund

- Various amendments can be completed at different stages of the process
- Need to allow time for agreement on changes, drafting, signature, submission to the authorities and receipt of approval/registration

Step 12: Amend Rules of Fund

- Amendments required:
 - Surplus apportionment scheme
 - Contingency Reserve Accounts
 - Member and Employer Surplus Accounts
 - Minimum benefits for active members
 - Treatment of surpluses arising after Surplus Apportionment Date

Conclusion

- Very lengthy process
- Many steps dependant on other steps
- Need to plan to have everything required per step to be completed before commencement of that step
- Need to allow adequate time for the actions required under each step
- Need to allow time for the trustees to review and approve each step