Unpacking Beneficiary Funds

Presented by:

Mpho Kgomongoe
Tashia Jithoo

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Background

Background & Current State of Play

Beneficiary Funds (BF) were introduced in 2009 following the Fidentia scandal which exposed governance failures and the need for greater regulatory rigour

Significant growth since, with industry currently holding about R27.5bn in AUM for about 165 000 members

Can now also receive an expanded range of benefits including S37C monies, approved group life benefits, other benefits payable on employee's death and maintenance payments

Current maturity of the BF industry enables RFs to be selective and consider a wider range of factors when engaging a BF – Eg:

- Innovative payment methods that enhance accessibility
- Tech that empowers G/CG and members with updated info – eg re status of benefits or capital requests
- More sophisticated and innovative tracing methods
- Initiatives that assist members obtain IDs

These strengthen and expand BF service delivery

Primary Purpose of a Beneficiary Fund

Vehicle where s37C benefits can be:

managed and appropriately invested with limited risk and proper regulatory oversight …

… to ultimately enable use for education, medical, daily living or well-being

Impact of socio-economic developments on BFs

- Factors like increased mobility, emigration and more younger people leaving rural areas and family homes increases the numbers of older parents needing physical and financial support
- Rise in use of BFs for discretionary monies – eg for incapacitated or elderly parents of deceased benes

This changing economic landscape requires BFs to assess how they function, reach and engage with members – all while also managing risk

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Lifecycle

Typical Lifecycle of a BF

- s37C
- Payment into BF
- Assessment and engagement with G/CG
- Decision on type/method of payment
- Annual assessment
- Termination

Factors for retirement funds to consider

Factors for retirement fund to consider when selecting a beneficiary fund

- Registered under section 5 of PFA
- Separate legal entity to the retirement fund
- Purpose: death benefit to be housed, managed and appropriately invested – safeguard beneficiaries' financial wellbeing

Factors

- Service level standards
- Costs/Fees
- Reach – foot soldiers
- Fidelity cover
- Administration service and system to make the payments
- Flexibility to accommodate the different types of payments
- Legal and governance compliance – cyber security, POPIA

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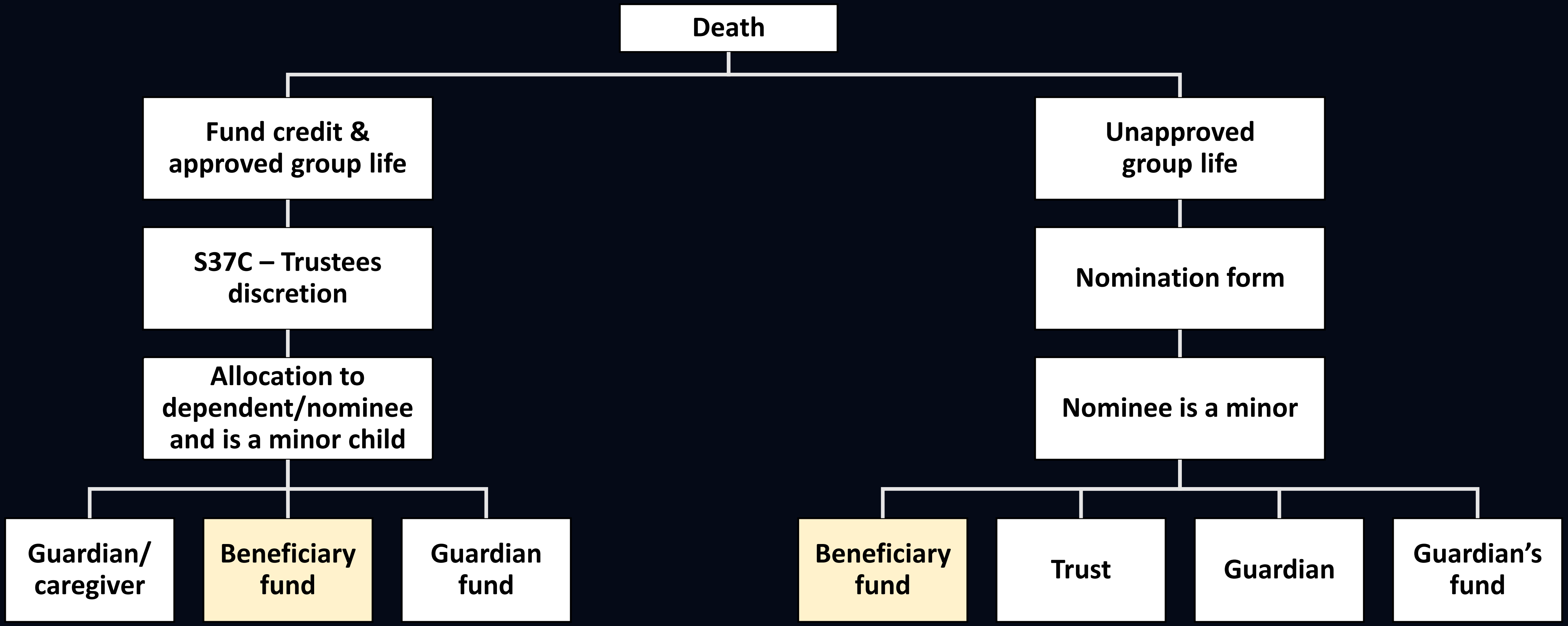
Decision to place benefit into a beneficiary fund

Decision to place benefit into a beneficiary fund



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Handover to beneficiary fund trustees

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Handover to beneficiary fund trustees

- When does this happen?
- Do the BF trustees acknowledge receipt of the responsibility?
- Do the BF trustees decide to calculate the monthly benefit by merely diving the benefit into equal payments?
- Fund as defined in the PFA and registered ito section 5
- Separate legal entity to the retirement fund

- Section 37C(2)(iii) PFA – Absolves the retirement fund trustee's beneficiary fund trustees
- Section 7A, 7C & 7D applies to beneficiary fund trustees
- Beneficiaries are the members of the BF
- Primary goal of BF is to safeguard a child's financial wellbeing until they turn 18
- Aim is to stretch the funds as far as possible – "drawdown phase"

6 Guardianship/Caregiver assessment and engagement

Guardianship/Caregiver assessment and engagement (1/2)

Section 18(3) of the Children's Act – Guardianship

- Administering & safeguarding a child's property and property interests
- Assisting or representing the child in administrative contractual and other legal matters
- Giving and refusing consent that is legally required in respect of the child

Best interest of the child is paramount.

Section 1(1) of the Children's Act – Care-giver

Williams and others v Hortors Group Pension Fund:

- ✓ Nature of care – parent/legal guardian/caregiver;
- ✓ Education level of the guardian;
- ✓ Employment status and stability of employment;
- ✓ Financial position (credit record/asserts and liabilities/income and expenditure);
- ✓ Health of the guardian;
- ✓ Signs of substance abuse and mental health issues.

Guardianship/Caregiver assessment and engagement (2/2)

Factors that should deter fund from paying to guardian

- Relationship with minor
- Lack of support structure by guardian
- Insufficient funds for own obligations
- Lack of financial literacy
  - General financial matters
  - Minor's financial affairs
  - Poorly managed or outstanding debts
- Criminal convictions
- Mental or physical illness

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Challenges

Examples of common legal challenges (1/2)

Disputes around payment methods – eg RF decision to use BF vs direct payment to G/CG

- Not a direct BF decision, but can impact administration of benefit, eg risk that payment to BF is set aside or RF is required to include additional dependant

Inadequate guardian investigations

- Eg legal challenges to a BF only being willing to pay to service providers and not directly to G/CG where inadequate evidence to justify that BF's approach

Fettering discretion or Set-up processes that aren't always thorough or well thought out – egs

- blanket approach re when and whether to place monies in BF
- Eg using a standard model and refusing capital payment requests in order to ensure the money 'lasts until age 18' regardless of specific circumstances

Examples of common legal challenges (2/2)

Benefit reallocation issues

- Eg Can BF pay to bene that RF didn't know about?
- BF cannot vary the RF's s37C allocation
- New bene needs to challenge the s37C decision first

Unclaimed benefits in BF when no G/CG or bene can be traced

- BF received payment for bene from RF but cannot trace the bene. Remains the BF responsibility to trace bene or if that fails to pay to an unclaimed benefits fund.

General challenges to BF refusal to pay in line with G/CG request – egs

- BF pays but not the full amount that was requested
- BF pays but only to service provider and not to G/CG directly

Managing operational issues can help avoid triggering legal disputes

Maximise the set-up phase

- Helps to get buy-in and compliance with processes if:
    - BF has understanding of full family circumstances
    - There is an understanding and engagement with G/CG around the 'how & why' of BF processes
    - The reasons for verification processes are clearly explained
- A lack of understanding re the reasons for operational processes can trigger disputes if G/CG just perceive them as unnecessary roadblocks

Balancing short-term and long-term needs

- Value of clear operational policies and approaches as risk mitigation tools
    - Helps to enhance predictability and consistency
    - Better able to defend decisions and therefore can help reduce legal challenges
    - Enhances consistent and defensible exercise of legal discretion

Examples of ways short-term & long-term needs are managed

Income policy

- Structured approach to how, when and how much minimum monthly income is paid – eg pegged to monthly social grant amount but can increase based on benefit size
- Manages legal risk by reducing inconsistency and arbitrariness in decision-making. Easier for BFs to defend decision

Capital distribution policy

- Caters to most common types of ad hoc payment requests in the BF
- Guides decisions around ad hoc payment requests in manner that is defensible
- Manages risk by balancing the need for consistency, with proper consideration of circumstances – so not fettering discretion. Trustee applications for cases outside the norm

Moving from just Proof of Existence to also 'Verifying Circumstances'

- Failure to track changed circumstances could create legal risk and potential liability
- Egs benefit paid to G/CG but member no longer living there or passed away. Or potential second household/connected member raises legal challenge that they should have received the benefit had proper due diligence been exercised

To manage legal risk and ensure thorough engagement, seeing more BFs move from simple Certificate of Existence to broader in-person verification processes, eg a call or field agent visits

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Termination

- Start pre-termination process early – age 15/16. Also allows members to consider further study options based on available funds
- Being proactive about termination requirements helps avoid BF running into roadblocks that can trigger operational challenges and legal disputes. Eg:
  - If members don't have IDs, they can't set up bank accounts to receive money. Build awareness about this early
  - Note – fund can't allow undue payment delays if alternative methods exist – eg e-wallets. Set up capability for these alternatives early to avoid legal disputes

Some food for thought

Are we moving to a broader view on when benefits can and should be paid to BFs?

Traditional view: BFs used if indications are that G/CG could not or would not, properly manage money for minor.

? But should these payment decisions only be based on 'ability to manage the money'?

? Do RF's have any fiduciary duty to properly inform all G/CGs about the BF payment option so they can make informed decisions about its use or not?

G/CG may want the convenience of investment experts, regulatory oversight and safety nets, tax advantages and the assurance that if they pass the minor's benefit will still be ringfenced, administered and used for their sole benefit. No risk of the benefit going into the estate and being used for purposes that don't benefit intended beneficiaries etc.

Some 17 years on from the registration of the first BF, we now have better regulation, more innovation, and the ability to offer G/CG greater agency to make informed choices about their payment options.

Questions?

THANK YOU