

Death Benefits and Section 37C: The Burden on the Board of Trustees

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When a member of a retirement fund dies before reaching retirement age (and if the rules of the particular fund permits) the lump sum benefit which becomes payable (hereinafter referred to as the “death benefit”) must be paid to the member’s dependants and/or nominees. Section 37C of the Pension Funds Act 24 of 1956 (“the Act”) regulates the payment of death benefits.

This article aims to look at the requirements of this section and the (onerous) duties it places on the board of trustees.

The objective of Section 37C

Section 37C gives the board of trustees discretion, to be exercised fairly and reasonably, insofar as the distribution of death benefits is concerned. The objective of this section is to ensure that those persons who were dependant on the deceased member are not left destitute after his/her death, irrespective of whether or not the deceased was legally required to maintain them.

In essence, section 37C(1) can be summarised as follows:

- death benefits do not form part of the deceased estate of the member (other than in the limited exceptions set out in the section), but will be placed under the control of the relevant fund;
- death benefits are not subject to the law of marriages, which means it does not form part of the joint estate in the case of parties married in community of property;
- the member’s freedom of testation is limited – the trustees are not bound by the deceased’s will or beneficiary nominations; and
- the law of intestate succession does not apply (where the member died without a valid will).

Duty of the Board of Trustees

Section 37C imposes three duties on the board of trustees, namely to:

1. identify and trace “dependants” (as defined in section 1 of the Act) and those persons, if any, who have been nominated by the deceased member;
2. make benefit allocations on a fair and equitable basis; and lastly
3. determine an appropriate mode of payment of the death benefit.

Identifying and tracing “dependants”

There is a duty on the Board to conduct a proper investigation to determine all the “dependants” of the deceased member. What this means is that the trustees cannot merely follow the beneficiary nomination made by the member during his/her lifetime – the Board must establish who the persons are who fall within the ambit of “dependant” as defined in the Act.

The Act defines three categories of “dependants”, namely legal dependants, de facto dependants and future dependants:

1. Legal dependants – include dependants in respect of whom the member owed a legal duty to support, such as a spouse and children (including illegitimate and adopted children). In order to fall within the ambit of this category one would have to prove that the deceased was legally obligated (i.e. in terms of legislation, common law or a legal obligation) to maintain you;
2. De facto (factual) dependants - those persons to whom the deceased owed no legal duty of financial support but who nevertheless depended on him financially. This would include a spouse in respect of whom the marriage or union is not recognised by any law or a financially independent major child. In order to fall within the ambit of this category one would have to prove that the deceased financially maintained you despite not having any legal obligation to do so;
3. Future dependants – those persons whom the deceased did not financially maintain at the point of his death, but whom he would have maintained in future, had he not died. This would typically include elderly parents or a fiancé. In order to fall within the ambit of this category one would have to prove that the deceased would have become liable to maintain you, had he not died.

Do all identified “*dependants*” automatically qualify to receive a portion/all of the death benefit?

No, they don’t - the fact that someone falls within the definition of “*dependant*” only entitles him/her to be considered by the Board when making the benefit allocation decision. It does not mean he/she automatically qualifies to share in the death benefit payable.

What about the nominated beneficiaries?

There is a common misconception that the nominated beneficiary has a right to claim the death benefit by virtue of being nominated by the deceased. This is not correct.

As stated above, the main objective of Section 37C is to ensure that those people who were dependant on the deceased are not left destitute after the member passes away. It is for

this reason that the legislature intended to favour *dependants* over nominated beneficiaries.

Accordingly, Section 37C determines that the trustees are not bound by nomination forms completed during the member's lifetime. The nomination forms will merely serve as a guide to the trustees. Nomination forms can also assist the Board in identifying persons who could potentially qualify as dependants. The overriding factor will however always be the beneficiary's dependence on the deceased when he was alive.

When does the duty to pay arise?

The time frames set out in Section 37C(1) are fundamental in answering the question as to when the death benefit payment becomes due and payable by the fund.

The principle of *mora* is equally applicable to the fund's duty to pay death benefits under Section 37C. To be in *mora* there must be a debt and the debt must be enforceable. A debt becomes due when the *duty to pay* arises.

Where a debtor's liability has to be determined, either because it is in dispute or it is conditional upon the performance of certain conditions (for example the Board having to make a decision), the debtor will not be in *mora* until such time as it is determined that a duty to pay exists. It is also important to remember that *mora* can arise by operation of law where the debtor's need is urgent (time is of the essence) and the creditor's delay is unreasonable. For example, where dependants are in urgent need the requirements of reasonableness may override any time term imposed by the Board.

Section 37C(1) stipulates time frames for five different scenarios for payment of death benefits, being a 12 month period (discussed in more detail below). It is a common misconception that the fund's duty to pay is always contingent on the expiry of this 12 month time period. Put differently, that the Board must in all instances wait for the 12 month period to expire before it can make payment of the death benefit.

This is not correct - the *duty to pay* is not dependent on the expiry of the 12-month period, but rather on whether the Board is satisfied that it has investigated and considered the matter with due diligence and is in a position to make an equitable allocation.

The relevant question will therefore always be whether the Board took all reasonable steps to identify and trace all possible dependants, so as to allow them to distribute the benefit in the most equitable manner to the correctly identified dependants. Section 37C does not prohibit distribution of death benefits within 12 months, nor does it compel distribution at the *expiry* of the 12 month period.

Supporting case law

In the matter of *Dobie NO v National Technikon Retirement Pension Fund [1999] 9 BPLR 29 (PFA)* the Adjudicator considered the principle of mora as well as the time frames of Section 37C in great detail. The complaint related to a dispute of law concerning the payment of interest on a portion of the death benefit paid by the Fund to the deceased estate (Mr Dobie nominated his estate as the beneficiary of the death benefit). The administrator of the fund argued that no interest was due since they were not bound to make any payments until the expiration of the 12 month period. Mr Dobie didn't have any dependants. The respondent therefore contended that Section 37C compels it to hold the benefits for a 12 month period before paying a nominee in order to grant it time to trace dependants.

The Adjudicator had to determine whether the Board of a fund is obliged to take a decision within the 12 month period or whether it's required to wait 12 months before distribution (the idea being that it should wait until the 12 month period had expired in order to see if any unidentified dependants come forward).

The Adjudicator held as follows:

- *"While there may be some wisdom in adopting such a cautious approach, Section 37C(1)(a) does not make such a course of conduct obligatory. A contextual reading of Section 37C as a whole indicates that the phrase "within twelve months of the death of a member" does not qualify the obligation to pay the benefit. It defines the period available for tracing dependants before making payment exclusively to a nominee. Hence, if the board is reasonably satisfied that it has traced all dependants, the stipulated period does not pose any limitation upon the distribution to the dependants. The provision does not prohibit distribution of the benefit within 12 months. Nor does it compel distribution at the expiry of the 12 month period."*

The Adjudicator clearly distinguished between Section 37C(1)(a) (being where the Board has identified dependants and there are no nominated beneficiaries) and Section 37C(1)(b)

(being where there are no dependants, but the deceased has nominated a beneficiary) and confirmed that:

- *“It seems logical, therefore, and the language of the section supports this, to conclude that the debt payable to the nominee becomes due and enforceable at the expiry of the 12 month waiting period.”*

In the recent matter of *Perry v Momentum Retirement Annuity Fund and Another* the Adjudicator made reference to the Dobie-matter, and added that the 12 month period afforded by Section 37C does not mean that the fund can unreasonably delay payment of the death benefit. If the fund, without good reason, fails to take a decision timeously, it will amount to maladministration. The Adjudicator found the six months which the trustees took to make payment of the death benefit to the complainant was an unreasonable and unfair delay. The fund was therefore ordered to make payment of the death benefit together with interest thereon at the rate of 15.5%.

Benefit allocations to the identified dependants

Once the Board has identified all the dependants the next stage of the enquiry would be to examine the needs of each dependant so that it can make an equitable distribution amongst them. In doing so, it has to consider all the relevant facts to the exclusion of irrelevant facts.

In the PFA determination of *Sithole v ICS Provident Fund and Another* [2000] 4 BPLR 430 (PFA), the Adjudicator summarised the factors that the Board should consider when making their decision as to the allocation of the death benefit:

- The age of the parties;
- The relationship with the deceased;
- The extent of dependency;
- The wishes of the deceased placed either in the nomination forms completed during his lifetime and/or his last will; and
- The financial affairs of the dependants including their future earning potential.

These factors were again considered in the recent matter of *Mohlomi v Evergreen Provident Fund and others* [2014] JOL 31440 (PFA) where the Adjudicator had to determine whether or not the trustees had acted equitably in excluding the complainant's children in the distribution of the death benefit, on the basis that they were not biological children of the deceased.

Once the trustees have established the needs of each identified dependant they will distribute the death benefit accordingly. Section 37C(1) stipulates the time frames and preconditions for five different scenarios for payment of death benefits, being:

- The Board has identified dependants and there is no nominated beneficiary (Section 37C(1)(a))
The benefit must be paid to the identified dependants (in such proportions as the Board deems equitable) within 12 months from the date of death. Until such time as the Board makes the decision recognising a dependant as a beneficiary and determining the proportions of the distribution, there is no duty to pay.
- There are no dependants, but there is a nominated beneficiary (Section 37C(1)(b))
If a nominee was appointed who is not a dependant and the trustees confirm there are no dependants, the death benefit will be paid to such nominee on the expiry of the 12 months (provided that where the aggregate amount of the debt in the estate exceed the aggregate amount of the assets, so much of the benefit as is equal to the difference between such aggregate amount of debts and aggregate amount of assets is paid into the estate and the balance of the benefit shall be paid to the nominee).
In short, distribution exclusively to a nominee may take place only after the expiry of the 12 month period has produced no dependants. The duty to pay arises at the expiry of the 12 month period.
- There are both identified dependants and nominated beneficiaries (Section 37C (1)(bA))
Should there be dependant(s), and the deceased also nominated a non-dependant to receive the death benefit – the fund shall within twelve months pay such portion of the death benefit to the dependant or nominee in the proportions as the Board may deem equitable. The debt becomes due and enforceable, as with a distribution under Section 37C(1)(a), once the decision is taken.
- No identified dependant and no nominated beneficiaries (Section 37C(1)(c))
If there is no dependant and also no nominated beneficiary, the death benefit will be paid to the deceased estate. This sub-section doesn't set out a time for performance – it can therefore be argued that the estate is only entitled to payment at the expiry of the 12 months
- There are no dependants and the deceased has nominated a nominee, but only in respect of a portion of the benefit (Section 37C(1)(c))
The Board must distribute the benefit accordingly between the nominee and the estate. Assuming that the nominee is known within the 12 month period (as in Section 37C(1)(b) above), the debt will become due and enforceable on the expiry of the 12 months.

The burden on the Board of Trustees

As stated above, Section 37C imposes various cumbersome duties on the board of trustees: not only is the Board tasked with conducting a proper investigation to determine all the dependants, it also has to make an equitable distribution of death benefits. If the Board fails to properly investigate the matter, or fails to take into account all the relevant factors, or

takes irrelevant factors into account, the Board's decision will be reviewable on the grounds that it exceeded its powers or that the decision constituted an improper exercise of its powers. At the same time any failure by a Board to take a decision timeously will be maladministration, potentially giving rise to a claim for losses suffered.

Section 37C imposes all these duties on the Board without providing any guidelines as to how it is to be achieved. And the reality is any successful claim for maladministration will be borne ultimately by the other members, if not the members of the Board. The Board would (typically) not have any prior knowledge of the parties or their relationship with the deceased member - yet at the same time they are obligated to effect payment in a reasonable manner in accordance with the options provided in the section. This in turn is aggravated by the Act not specifying what would constitute "equitable" nor providing any guidelines as to how the Board must make an *equitable* distribution.

In the matter of *Maake v Old Mutual Superfund Provident Fund and Old Mutual Life Assurance Company (2013)* the Adjudicator stressed the importance of the Board's duty to consider all relevant information and their duty not to fetter their discretion in any way whilst doing so. In this matter the Adjudicator held that by simply accepting an affidavit from a claimant at face value, the Board lost sight of the fact that an affidavit does not necessarily prove the truth of its contents. The Adjudicator confirmed that, although the tribunal understands the practice of using affidavits as part of the death benefits investigation, affidavits submitted by claimants are hardly ever verified except by collecting similar ones deposed to by supposedly independent parties.

Ultimately the incorrect application of Section 37C could lead to the incorrect distribution of a death benefit. An incorrect distribution could lead to numerous issues: the prejudice of certain beneficiaries (where they receive less than they should have received or they are completely excluded from the distribution), the unjust enrichment of a beneficiary (where a beneficiary receives more than he should) and/or a loss by the fund itself (where the fund is unable to recover an incorrect payment already made).

Conclusion

Section 37C as a whole is fraught with great difficulty, and must be carefully followed by the trustees, especially when it comes to determining when the duty to pay arises. In the Dobie matter the Adjudicator pointed out that the time frames stipulated in Section 37C *“have led to considerable debate and confusion in the pension funds industry and require clarification”*. The Adjudicator also noted that, although the intention of the legislature was noble, the problem with this section lies in its application.

A possible solution would be for the legislature to provide more specific guidelines (e.g. regarding the steps to be taken, what would be regarded as equitable, etc.) and then allowing for a final distribution to known dependants and nominees at the expiry of a reasonable period concluding with the necessary indemnities protecting the Board against further claims.

In the meantime, it is advisable for trustees and administrators to keep a close eye on Adjudicator determinations in this regard for guidance on the application of Section 37C.