

DISPOSAL OF DEATH BENEFITS PAYABLE FROM RETIREMENT FUNDS

Introduction

The disposal of death benefits is one of the main responsibilities of the Trustees of a retirement fund.

The purpose of this document is to assist Trustees, (and the persons delegated by them to investigate the circumstances of the deceased's nominees and beneficiaries) in the process that should be followed in making a proper determination as to whom a benefit should be paid, in what portions the benefit should be paid and how the benefit should be paid. Circumstances vary widely and a Trustee who adheres strictly to these guidelines cannot be assured of having fulfilled all his/her or her obligations. Trustees should always adopt a robust, common sense and fair-minded approach to their task, and err on the side of caution.

Overview of the procedure

The disposal of benefits from a pension or provident on the death of a member is governed by Section 37C of the Pension Funds Act, 1956 (Act 24 of 1956), as amended. The Act refers to "any benefit payable by such a fund upon the death of a member". This is commonly interpreted to pertain only to the lump sum benefits, and exclude monthly pension benefits payable to spouses and children.

Lump sum benefits generally arise from two sources:

- The Accumulated Fund Credit ,
- The (insured) Risk Benefit - commonly a multiple of annual rate of pay, provided by the Fund.

Trustees of a pension and provident fund have the responsibility to allocate and distribute death benefits to dependants and nominees of such funds after the death of a member.

Within a twelve-month period after the death of a member, the Trustees must establish:

- who was a legal dependant of the deceased;
- who was financially dependant on the deceased;
- who was nominated as a beneficiary;
- whether the deceased member completed a valid will;
- whether any estate left by the deceased was solvent;

Having identified all the dependants and nominees (or as many as they can within reasonable time and expense limits) the Trustees must:

- 1 decide in what proportions the money will be allocated to each person that they consider to be dependant;
- 2 determine the amount payable to nominees; and

3 decide whether such money should be paid in cash, periodic or paid into a trust.

If no dependants can be traced within twelve months of the death of the member and the estate is insolvent, the benefit must first be applied towards making the estate solvent before any benefit is paid to any nominees. Only that portion which exceeds the net liabilities of the estate is payable to the nominees.

In the case of minor children, the money MUST be:

- (i) paid to a guardian;
- (ii) or paid into a duly registered trust; or
- (iii) paid into the Guardians Fund
- (iv) retained in the Fund and paid out in installments until the minor attains majority.

Retaining the benefit in the fund and paying it out in installments is permitted in terms of an amendment to the Act, which became effective in April 1996. The amendment permits the payment of death benefit in installments in respect of both major and minor dependants and nominees. In the case of major dependants and nominees, the fund is required to enter into an agreement with such person. In the case of minor dependants and nominees, the installments may be paid until the minor attains 21 years of age. At that point the balance of the benefit must be paid out to the erstwhile minor. Alternatively, an agreement may be entered into in terms of which the benefit is retained in the fund.

For both major and minor dependants and nominees the fund will be liable to pay interest at a reasonable rate having regard to the investment return earned by the fund. In considering this option, Trustees need to take account of the additional administrative activities and costs which the fund will have to bear to comply with their decision.

Once the final decision has been taken, the Trustees must record the content of this decision. The penultimate step is to advise the recipients of the decision and indicate any options available to the recipient in respect of that benefit.

THE PENSION FUNDS ACT

The law relating to the disposal of death benefits arising from retirement funds is contained in the definition of "dependant" (Section 1) and in Section 37C of the Pension Funds Act, 1956 (Act 24 of 1956). These provisions read as follows:

DEFINITION OF 'DEPENDANT' IN SECTION 1 'dependant, in relation to a member, means

- (a) a person in respect of whom the member is legally liable for maintenance;
- (b) a person in respect of whom the member is not legally liable for maintenance, if such person –

- (i) was, in the opinion of the board, upon the death of the member in fact dependent on the member for maintenance;
 - (ii) is the spouse of the member, including a party to a customary union according to Black law and custom or to a union recognized as a marriage under the tenets of any Asiatic religion;
 - (ii) is a child of the member, including a posthumous child, an adopted child and an illegitimate child.
- (c) a person in respect of whom the member would have become legally liable for maintenance, had the member not died;

SECTION 37C

- (1) Notwithstanding anything to the contrary contained in any law or in the rules of a registered fund, any benefit payable by such a fund upon the death of a member, shall, subject to a pledge in accordance with section 19 (5)(b)(i) and subject to the provisions of section 37A(3) and 37D, not form part of the assets in the estate of such a member, but shall be dealt with in the following manner:
- (a) If the fund within twelve months of the death of the member becomes aware of or traces a dependant or dependants of the member, the benefit shall be paid to such dependant or, as may be deemed equitable by the board, to one of such dependants or in proportions to some of or all such dependants;
 - (b) If the fund does not become aware of or cannot trace any dependant of the member within twelve months of the death of the member, and the member has designated in writing to the fund a nominee who is not a dependant of the member, to receive the benefit or such portion of the benefit as is specified by the member in writing to the fund, the benefit or such portion of the benefit shall be paid to such nominee: Provided that where the aggregate amount of the debts in the estate of the member exceeds the aggregate amount of the assets in his estate, so much of the benefit as is equal to the difference between such aggregate amount of debts and such aggregate amount of assets shall be paid to the estate and the balance of such benefit or the balance of such portion of the benefit as specified by the member in writing to the fund shall be paid to the nominee.
 - (bA) If a member has a dependant and the member has also designated in writing to the fund a nominee to receive the benefit or such portion of the benefit as is specified by the member in writing to the fund, the fund shall within twelve months of the death of such member pay the benefit or such portion thereof to such dependant or nominee in such proportions as the board may deem equitable: Provided that this paragraph shall only apply to the designation of a nominee made on or after 30 June 1989: Provided further that , in respect of a designation made on or after the said date, this paragraph shall not prohibit a fund from paying the benefit, either to a dependant or nominee contemplated in this

paragraph or, if there is more than one such dependant or nominee, in proportions to any or all of these dependants and nominees.

- (b) If the fund does not become aware of or cannot trace any dependant of the member within twelve months of the death of the member and if the member has not designated a nominee or if the member has designated a nominee to receive a portion of the benefit in writing to the fund, the benefit or the remaining portion of the benefit after payment to the designated nominee, shall be paid into the estate of the member or, if no inventory in respect of the member has been received by the Master of the Supreme Court in terms of section 9 of the Estates Act, 1965 (Act 66 of 1965), into the Guardian's Fund.
- (2) For the purpose of this section, a payment by a registered fund to a dependant shall be deemed to include a payment made by the fund to a trustee contemplated in the Trust Property Control Act, 1988 (Act 57 of 1988), for the benefit of a dependant or nominee contemplated in this section shall be deemed to be a payment to such dependant or nominee.
- (3) Any benefit dealt with in terms of this section, payable to a minor dependant or minor nominee, may be paid in more than one payment in such amounts as the board may from time to time consider appropriate and in the best interests of such dependant or nominee: Provided that interest at a reasonable rate, having regard to the investment return earned by the fund, shall be added to the outstanding balance at such times as the board may determine: Provided further that any balance owing to such a dependant or nominee at the date on which he or she attains majority or dies, whichever occurs first, shall be paid in full.
- (4)(a) Any benefit dealt with in terms of this section, payable to a major dependant or major nominee, may be paid in more than one payment if the dependant or nominee has consented thereto in writing: Provided that -
- (i) the amount of the payment, intervals of payment, interest to be added and other terms and conditions are disclosed in a written agreement; and
 - (ii) the agreement may be cancelled by either party on written notice not exceeding 90 days.
- (4)(b) If the agreement contemplated in paragraph (a) is cancelled the balance of the benefit shall be paid to the dependant or nominee in full.

DEPENDANTS, NOMINATED BENEFICIARIES AND TRUSTS.

DEPENDANTS

In terms of the definition of dependant in section 1 of the Pension Funds Act there are three categories of dependants:

1. Legal Dependants (paragraph (a) of the definition)

Defined as a person in respect of whom the member is legally liable for maintenance. By maintenance is meant the provision of the necessities of life (food, housing, education, and welfare) to the dependant by the member.

The following persons qualify as legal dependants:

- a member's spouse under civil marriage;

- a member's legitimate and/or illegitimate children. This includes the minor or major children; adopted children of the member fall into this category (step and foster children are not legal dependants);
- a member's indigent parents; and
- a member's indigent grandparents where the children of the grandparents are unable to support them.

2. Factual Dependants: (paragraph (b) of the definition)

Defined as a person in respect of whom the member is not legally liable for maintenance if such person:

- (i) was in the opinion of the board of the fund, upon the death of the member, in fact dependent on the member for maintenance;
- (ii) is the spouse of the member including a party to a customary union according to Black law and custom or to a union recognized as a marriage under the tenets of any Asiatic religion.

The following persons qualify as factual dependants:

- a member's customary law spouse according to Black Law or custom or a union recognized as a marriage under the tenets of any Asiatic religion. These marriages were not recognized under civil laws, but spouses of such unions are factual dependants. As far as Black customary unions are concerned, proof of such unions can be attested by affidavit by the Chief or Headman at the place where the parties married or presently reside, or from their relatives. Customary marriages have to be registered in Kwa-Zulu/Natal but in other provinces of the Republic it is not compulsory. The register could thus serve as proof of a customary marriage. As far as unions under the tenets of any Asiatic religion are concerned the religious officer officiating at the marriage ceremony will issue a marriage certificate. This would constitute proof of the union.
- a person with whom the member lived as man and wife. Note that this category refers to parties who have not contracted either a civil law or a customary marriage or a marriage under the tenets of any Asiatic religion.
- an indigent relative of the member, i.e. a brother, sister, uncle, aunt and the children or, grandchildren of such relatives; and
- any other person who, to the satisfaction of the trustees, can prove factual dependency on the member, i.e. ***can prove reliance upon the member at date of death, for the necessities of life.***

3. Prospective Legal Dependants (paragraph (c) of the definition)

A person in respects of whom the member would have become legally liable for maintenance had the member not died, i.e. an unborn child of the member.

NOMINATED BENEFICIARIES

Section 37C makes provision for persons to be nominated as beneficiaries. Paragraphs (b) and (bA) require the nominations to be in writing to the fund.

Definition

A nominated beneficiary is a person chosen by the member to share in the benefit arising on his death. There is no specific definition in the Act, merely a reference to nominees. This, it is accepted, is restricted to natural persons (as opposed to juristic persons such as companies and close corporations).

Where a nominee was nominated prior to 30 June 1989, such nominee is not entitled to any share of the death benefit where the member had a dependant or dependants. Even if only one dependant is traced, such dependant is entitled to the whole benefit.

Nominations after 30 June 1989 (due to an amendment of Section 37C (1) (bA) of the Pension Funds Act) must be considered with dependants in the apportionment of a death benefit. Thus the date of nomination is important for Trustees in the meeting of their obligations.

Process of Nomination of Beneficiaries

The Act does not prescribe how nominations are to be made; the only requirement is that it must be in writing to the fund.

- (a) It is usual for pension/provident funds to require their members to complete a beneficiary nomination form from time to time. Such a form, duly completed, will constitute a nomination to the fund as required by the Pension Funds Act. If such a practice has not been instituted, it would be prudent for the Trustees to distribute nomination forms with the annual benefit statement to members.
- (b) A member may validly nominate beneficiaries to share in the death benefit by naming them in his will and specifying that such persons are to receive the benefit payable under the particular fund. A copy of the will must be furnished to the fund to constitute a valid nomination.
- (c) A letter to the fund nominating beneficiaries will also constitute a valid nomination.

Where there is more than one nominee, the fund should require that the share of each nominee be specified.

TRUSTS

Subsection (2) of section 37C makes provision for the payment of a benefit to a trust. Such trust must be duly registered in terms of the Trust Property Control Act, 1988 (Act No 57 of 1988) and must be for the benefit of the dependant or nominee to whom the Trustees have allocated the payment.

To give effect to a payment in terms of this provision, fund Trustees should ensure that the trust meets certain requirements.

- (1) The trustees of the trust may not have a discretion regarding:
 - to whom the benefit will be payable

- the amount of the benefit

The trust must merely act as a conduit for the payment once the board of the fund has exercised its discretion as to whom and how much shall be paid.

- (2) The benefit must vest in the beneficiary. It is not permissible for the trust deed to provide for example, that on the death of the beneficiary the benefit will remain in the trust.

It is prudent for fund Trustees to ensure that no provisions exist whereby the trust deed may be amended at a later date which could frustrate these requirements.

When paying a benefit into a trust, it is good practice for an Act of Settlement to be entered into. Such a document prescribes any conditions in terms of which the benefit is paid into the trust.

Before the benefit can be paid into a trust, it is necessary for the Trustees to authorize an individual to act on behalf of the Fund. Proof of such authorization should be retained in the Fund Register.

There is an opinion subscribed to by the FSB that any initial charges incurred in establishing a trust which are deducted from a member's death benefit will constitute a contravention of sections SPA and 37D of the Pension Funds Act. The FSB acknowledges that this may give rise to practical problems but it is nevertheless a consideration and Trustees should take note of the point.

APPLICATION OF DISCRETION

Trustees have a duty in terms of Section 37C of the Pension Funds Act to determine the dependants of the member. Once the Trustees have identified persons to be dependants, they must apportion the benefit among these dependants and any nominated beneficiaries.

Identification of Dependants

Trustees must identify with certainty the dependants of the member. As indicated above, Trustees will have to identify whether a person is a dependant - a legal, factual or prospective legal dependant. The Act states that Trustees must trace or become aware of the dependants. The Trustees thus have a duty to make reasonable and diligent inquiries in their efforts to obtain information and trace dependants. Although it is solely the decision of the Trustees as to when they consider that all reasonable steps have been taken to identify all the deceased member's dependants, this decision may be challenged. It is therefore prudent to have sufficient records to defend any dispute as to the decision.

Factors to be considered by trustees in determining who qualifies as a dependant

- **For legal dependants:**
Proof of relationship between the dependant and member should be obtained. In the case of a spouse, the marriage certificate will serve as proof; in the case of children, their birth certificates will meet this requirement. In the case of indigent parents and grandparents, affidavits deposing to the relationship between such persons and the member should be obtained.
- **For factual dependants:**
Proof of factual dependency will usually require extensive inquiries. A useful test in

determining the extent of factual dependency is to ask: "What effect would the removal of the member's support have had on the person?" Once the extent of dependency has been determined, the Trustees can then apply their minds to the apportionment of the benefit to the dependants.

Nominees

In terms of section 37C of the Pension Funds Act the Trustees have to consider the apportionment between dependants and nominees on an equitable basis (this refers only to those nominees nominated by the member after 30 June 1989). Those nominated earlier and not re-nominated have no claim should there be any dependants.

Apportionment should take place within a reasonable period. The Trustees must act once twelve months have elapsed since the member's death.

GUIDING PRINCIPLES

In the exercise of their powers concerning any aspect of the management of a fund, Trustees must be guided by certain principles. Thus, when disposing of death benefits, the Trustees must measure the exercise of their discretion against the following standards.

To Act in Good Faith

This is an overriding principle. It means that Trustees must be diligent and honest in the carrying out of all their duties. They must observe a higher level of care than they would exercise in their own affairs.

To Avoid Conflicts of Interest

Trustees (especially Trustees who are Fund members) must not take advantage of their position as Trustees to enrich or gain advantage for themselves at the expense of the Fund. To gain such an advantage could result in criminal liability.

To Know and Understand

Trustees act in a fiduciary (position of trust) capacity. To enable Trustees to fully comply with this principle, they must, among other things, know and understand the legislation impacting on their position. The most important Act with which Trustees need to be familiar is the Pension Funds Act, 1956. However, there are other Acts, such as the Financial Institutions (Investment of Funds) Act, 1984 (Act 39 of 1984) which impact on the function of Trustee.

Trustees must also acquaint themselves fully with the Rules of the Fund.

The more fully acquainted Trustees are with the legislation, the easier it is for them to appreciate the nature and application of their function as Trustees.

To Exercise Discretion Judiciously

The discretionary powers, which Trustees have to exercise in terms of fund rules, are very important. Trustees must never act capriciously or in an arbitrary or unfair manner. Good faith, fairness, and reasonableness must guide the exercise of their discretion. Trustees cannot delegate their discretionary powers. The Trustees will remain accountable for all decisions.

These principles have been codified in the Pension Funds Act. Section 7C(2) specifically provides that the board of a fund shall, inter alia, act with due care, diligence and good faith, avoid conflicts of interest and act impartially in respect of all members and beneficiaries. The Financial Institutions (Investment of Funds) Act also establishes ethical standards for Trustees and prescribes penalties for failure to meet these standards.