



Subject: Defined Benefit Retirement Fund Funding Guideline

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Scope: Retirement Funds, Members, Employers, Valuators

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Introduction

The objectives of this Guideline are to:

- i. provide information on how Defined Benefit Retirement Funds should be funded to maintain financial soundness; and
- ii. to give guidance on how to treat fund deficits as well as surpluses, in various situations.

This Guideline is issued pursuant to section 33 of the Financial Services Regulatory Authority (FSRA) Act, 2010, which empowers the Authority to issue guidelines for providing guidance in furtherance of its regulatory objectives in terms of the FSRA Act read together with the Retirement Funds Act, 2005 (the Act).

Definitions

Authority – means the Financial Services Regulatory Authority established under section 3 of the FSRA Act, 2010.

FSRA Act – means the Financial Services Regulatory Authority Act, 2010.

The Act – means the Retirement Funds Act, 2005.

Any word or expression used in this Guideline which is defined in the Act or the FSRA Act shall, unless the context otherwise requires, have the same meaning as in those Acts.

Application

The Guideline applies to the management board, members, employers, valuers and any person to whom the trustees have delegated their functions to the extent relevant to the nature of their involvement.

A. Determination of financial soundness

1. The valuation of a fund shall be conducted:
 - i. every three years or more frequently in accordance with section 23 of the Act. For a fund to be financially sound, its funding level shall be equal to or exceed 100%; and
 - ii. before the distribution of a surplus, conversion, amalgamation or winding-up of a fund. An exception to this requirement shall be made for a surplus distribution applied for within one year after a regular valuation has been done.
2. Every valuation shall be conducted in line with the standards set by the Actuarial Society of South Africa in accordance with Directive 7 of the Retirement Funds Directives, 2008.

B. Fund in a deficit position

1. Where the fund is deemed not to be financially sound through a return or valuation, the Authority shall request the management board to submit a scheme of restoration in accordance with section 25 of the Act.
2. The Authority shall require a scheme of restoration when the fund's funding ratio is 94% and lower.
3. The scheme of restoration must satisfy the following criteria for it to be deemed as acceptable to the Authority in line with subsection 25(3) of the Act:
 - i. the scheme shall be certified by the valuator prior to submission to the Authority; and
 - ii. the scheme shall specify a timeframe for restoration that meets the following conditions:
 - where there are active or deferred members, the period shall not exceed the average remaining years to normal retirement age of such members, unless approved by the Authority; or
 - where all members are retired, the period shall not be more than 5 years, unless approved by the Authority; and
 - iii. the Authority shall require the employer to indicate approval of the scheme of restoration, otherwise the scheme shall be considered unacceptable.
4. The management board shall monitor compliance and take all reasonable steps to ensure that contributions are made in accordance with the scheme of restoration.
5. If the scheme is not being complied with, the Authority shall take intervention measures in order to ensure compliance with the scheme of restoration which may include seeking an order of the court for the winding-up of the fund in terms of section 41 of the Act where appropriate.
6. If the court orders an involuntary winding-up upon an application by the Authority, the provisions of section 41 of the Act and the Companies Act shall apply.

7. Where the Authority receives an application for conversion, an amalgamation, a transfer, or a voluntary winding-up of a fund, the Authority shall require that all unpaid contributions and deficit be paid prior to approval of the application.

C. Fund in a surplus position

1. Where the valuator has certified that the fund is financially sound and is in a surplus position, the surplus shall remain indefinitely in the fund.
2. Subject to the Authority's approval, the management board may use the surplus for:
 - i. contribution holiday;
 - ii. reserving all or a portion of it for future contingencies, or
 - iii. distribution to current and former members.
3. In accordance with the Income Tax Order, a surplus shall not be refunded to an employer.
4. The Authority will approve the use of the surplus for contribution holiday, provided:
 - i. the rules of the fund do not prohibit contribution holiday;
 - ii. the contribution holiday is approved by the management board;
 - iii. the contribution holiday is supported by a recent (within the past 18 months) opinion from the valuator;
 - iv. the contribution holiday is approved by the Income Tax Commissioner; and
 - v. members are notified of the contribution holiday, but without the power to approve or disapprove.
5. The Authority shall not approve a contribution holiday if it would result in a funding ratio of 110% or lower.
6. The Authority will approve the use of the surplus for reserves and future contingencies, provided:
 - i. the rules of the fund do not prohibit the establishment of a reserve;
 - ii. the management board adopts rules regarding the purpose and use of the reserve, which must be approved by the Authority;
 - iii. transfer of funds into or out of the reserve is approved by the management board; and
 - iv. transfer of funds into or out of the reserve is supported by a recent (within the past 18 months) opinion from the valuator.
7. The Authority will approve the use of the surplus for distribution to current and former members provided:
 - i. the rules of the fund do not prohibit the distribution of surplus;
 - ii. the proposed distribution is approved by the management board;
 - iii. the distribution is supported by a recent (within the past 18 months) opinion from the valuator, which deals with the following:
 - financial soundness of the fund in line with the proposed distribution;
 - fairness of the proposed basis for allocating surplus among current and former members; and
 - appropriateness of the proposed mechanisms of distribution;

- iv. the distribution is approved by the Income Tax Commissioner; and
 - v. members are notified of the distribution of surplus, but without power to approve or disapprove.
8. The following factors shall be considered by the Authority when deciding whether to approve or disapprove a proposed distribution of surplus:
- i. If the fund will continue to operate and to provide defined benefits, the Authority shall not approve a distribution of surplus if it would result in a funding ratio of 110% or lower.
 - ii. If the fund is being converted to defined contribution or is winding up and will no longer provide any defined benefits, the Authority shall approve the distribution of the entire surplus, net of the conversion or winding up costs.
 - iii. If the fund is being amalgamated with another retirement fund or obligations are being transferred to another retirement fund, the Authority shall not approve the amalgamation or transfer unless the proposed allocation of surplus and its possible distribution treats both the members subject to the amalgamation or transfer and those who remain in the retirement fund fairly.
 - iv. The proposed basis for the allocation of surplus and the mechanisms of distribution shall be reasonable and appropriate.
9. The surplus may be distributed to current and former members using various mechanisms, which may include:
- i. lump-sum cash payment;
 - ii. transfer to a fully vested individual account within a retirement fund;
 - iii. transfer to a preservation fund;
 - iv. transfer to a beneficiary fund;
 - v. provide higher future benefits from the retirement fund, if it will continue to provide defined benefits; and
 - vi. purchase an annuity.