

FSCA GUIDANCE NOTICE 1 OF 2023 (RF)

PENSION FUNDS ACT, 1956 (ACT NO. 24 OF 1956)

FINANCIAL SECTOR REGULATION ACT, 2017 (ACT NO. 9 OF 2017)

**GUIDANCE NOTICE ON THE APPLICATION OF SECTION 14(7) OF THE
PENSION FUNDS ACT, 1956**

1. PURPOSE OF THE GUIDANCE NOTICE

The purpose of this guidance notice, which is published by the Financial Sector Conduct Authority (“Authority”) in terms of section 141 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (“the FSR Act”), is to provide guidance on the application of, and expected compliance with, section 14(7)(b) of the Pension Funds Act, 1956 (Act No. 24 of 1956) (“PFA”). The guidance set out in this guidance notice reflects the manner in which the Authority construes section 14(7) of the PFA for regulatory purposes.

2. BACKGROUND AND APPLICABLE LEGISLATION

2.1 Section 14(7) of the PFA has the following aims:

- To ensure that that retirement annuity funds do not prevent members and non-member spouses to transfer their interests from one retirement annuity fund to another should they so request (s.14(7)(a));
- to curb incentive-driven advice to effect such transfers (s.14(7)(b)(i); and
- to enable and regulate fees and commissions for financial services after such transfers (s.14(7)(b)(ii)).

2.2 Section 14(7) of the PFA provides as follows:

- “(a) *Notwithstanding anything to the contrary in the rules of a fund, a retirement annuity fund shall not prohibit the transfer of business that relates to a member’s interest or non-member spouse’s interest, at the request of such a member or non-member spouse from one retirement annuity fund to another.*

- (b) *No fees or commissions of any nature are payable by any party or by any agent, mandatory or representative of such party -*
- (i) *in return for the facilitation, intermediation or recommendation of the transfer; or*
 - (ii) *for financial services rendered by a financial services provider or representative after the transfer in respect of the transferred interest of the transferring member or non-member spouse which exceeds the fees or maximum commission that would have been permissible for such services in terms of the Long-term Insurance Act, 1998 or any regulations made thereunder had the transfer not been done other than fees-*
 - (aa) *payable to the registrar;*
 - (bb) *negotiated and agreed to in writing by the transferring member or non-member spouse annually, which fees are-*
 - (A) *payable by the transferring member or non-member spouse personally; or*
 - (B) *authorised by the transferring member or non-member spouse to be paid by the fund or administrator.”*

3. GUIDANCE ON THE APPLICATION OF SECTION 14(7)(b) OF THE PFA

- 3.1 Section 14(7) deals with the transfer of assets relating to a member's interest or non-member spouse's interest (interests) from one retirement annuity fund to another, with section 14(7)(b) focusing on fees and commissions payable for services rendered before, during and after such transfer.
- 3.2 In terms of section 14(7)(b)(i) of the PFA, no fees or commissions are payable for the facilitation, intermediation, or recommendation of the transfer. This prohibition is directed at services rendered in relation to the transfer itself and makes no distinction between underwritten¹ retirement annuity funds and non-underwritten² retirement annuity funds. The prohibition, therefore, applies to the facilitation, recommendation and intermediation in respect of all transfers between retirement annuity funds, regardless of whether or not either the transferor or transferee funds are underwritten.
- 3.3 Section 14(7)(b)(ii) deals with the payment of fees and commissions for financial services rendered by a financial services provider or representative **after** the transfer of interests.

¹ The term “underwritten fund” for purposes of this guidance notice means that the members' benefits of the retirement annuity fund is secured by one or more policies issued to the fund by a long-term insurer, in terms of which policy the long-term insurer accepts liability / takes on the risk for a fee. The fund's liability to pay is therefore underwritten by an insurer.

² The term “non-underwritten fund” for purposes of this guidance notice means that the fund's liability to pay its members' benefits is not underwritten by a long-term insurer.

- 3.4 The PFA does not define the terms "financial services" or "financial services provider". The use of these terms is however understood to take on the meaning of the definitions in the Financial Advisory and Intermediary Services Act, 2002 (Act No. 37 of 2002) ("FAIS Act"). This understanding is informed by the deliberations and voting by Parliament's Finance Standing committee, held on 5 June 2007³ during Parliament's consideration of the then proposed Pension Funds Amendment Bill [B11-2007] which inserted sections 14(5) – (8) into the PFA. During the deliberations the National Treasury advised that "the FAIS Act provides a sound framework to deal with the issue.". It is, therefore, understood that the references were intended by the policymaker to cross reference the definitions in the FAIS Act.⁴
- 3.5 Accordingly, the reference to "financial services rendered by a financial services provider" in section 14(7)(b)(ii) of the PFA is understood to refer to "advice" and/or "intermediary services" as contemplated in the FAIS Act, where these services are rendered **after** the transfer.
- 3.6 Section 14(7)(b)(ii) sets out a prohibition on the payment of fees or commissions that exceed the fees or maximum commission that would have been permissible in terms of the Long-term Insurance Act, 1998 (Act No. 52 of 1998) or the regulations made thereunder ("the LTIA Regulations") if the transfer had not been done.
- 3.7 The prohibition on the payment of fees or commission is, therefore, linked to the maximum commission provided for in the LTIA Regulations, in that it prohibits the payment of any fees which exceeds the maximum commission that would have been permissible had the transfer not been done. However, sections 14(7)(b)(ii)(aa) and (bb) contain exceptions to this prohibition. Accordingly, no fees or commissions may be paid in excess of maximum commission payable for furnishing advice and/or rendering of intermediary services provided after the transfer, unless the fee is negotiated with, and agreed to in writing, by the transferring member or non-member spouse, on an annual basis.
- 3.8 Any fees which are negotiated with, and agreed to in writing by, the transferring member or non-member spouse must either be payable by the transferring member or non-member spouse personally (per section 14(7)(b)(ii)(bb)(A)) or, the transferring member or non-member spouse must authorise the fund or administrator to pay such negotiated fee (per section 14(7)(b)(ii)(bb)(B)). Provided these requirements are met, there is no prescribed maximum cap on the amount of such negotiated and agreed fees.
- 3.9 Accordingly, it follows that regardless of whether or not the maximum commission provided for in the LTIA Regulations had been paid before the transfer was effected, negotiated and agreed fees contemplated in section 14(7)(b)(ii)(bb) are permissible, provided the requirements of that section are met.

³ Meeting summary available at <https://pmg.org.za/committee-meeting/8163/> (accessed 14 March 2022)

⁴ Considering that the amendments which inserted Sections 14(5) to 14(8) into the PFA came into effect in 2007, which was long before the enactment of the FSR Act in 2019, it could likewise be argued that the reference to the terms "financial services" and "financial services provider" cannot be interpreted to refer to the meaning of these terms in that Act. This strengthens the argument that the terms are meant to cross reference these terms in the FAIS Act.

- 3.10 The restrictions and requirements imposed by section 14(7)(b)(ii) are only in respect of the transferred amount. Fees or commissions for services rendered in relation to new on-going or additional lump sum contributions after the transfer, or in relation to any value attributable to investment growth after the transfer, are not subject to section 14(7)(b) of the PFA. This guidance on the application should be considered together with applicable provisions in the General Code of Conduct for authorised Financial Services Providers and Representatives, 2003 ("FAIS General Code"), which are explained in detail in paragraph 5 below.
- 3.11 Section 14(7)(b)(ii) only applies where the LTIA Regulations would have applied to the transferor fund - in other words, where the transferor fund is an underwritten fund. Section 14(7)(b)(ii) does not distinguish between an underwritten fund and a non-underwritten fund. The distinction is drawn from the PFA read with the LTIA Regulations, in that the limitation on commission in the LTIA Regulations would apply to fees and commissions related to an underwritten fund, whilst the limitations on commission would not apply where the transferor is a non-underwritten fund. Accordingly, the restrictions and requirements of section 14(7)(b)(ii) apply to transfers from an underwritten fund to another underwritten fund, and to transfers from an underwritten fund to a non-underwritten fund. Section 14(7)(b)(ii) does not apply to transfers from a non-underwritten fund to another non-underwritten fund, nor to transfers from a non-underwritten fund to an underwritten fund. However, see paragraph 5 below.
- 3.12 Where a member or a non-member spouse authorises the payment of on-going fees by the fund or administrator as contemplated in section 14(7)(b)(ii)(bb)(B), it is not sufficient for the financial services provider or its representative to rely on such authorisation indefinitely until the member or non-member spouse informs the fund or administrator otherwise. Section 14(7)(b)(ii)(bb) is clear in that any such fees must be negotiated and agreed to in writing *annually* by the transferring member or non-member spouse. It therefore follows that any authorisation by the transferring member or non-member spouse for the fees to be paid by the fund or administrator must also be confirmed on an annual basis.⁵
- 3.13 Where a fund or administrator obtains the authorisation contemplated in Section 14(7)(b)(ii)(bb)(B), the fee must be confirmed in writing annually thereafter subsequent to the annual negotiation and agreement referred to in section 14(7)(b)(ii)(bb).

4. APPLICATION OF THE LTIA REGULATIONS

- 4.1 Parts 3A and 3B of the LTIA Regulations regulate the payment of commission for rendering services as intermediary in relation to long-term insurance policies. As such, these parts of the LTIA Regulations apply to services as intermediary rendered in respect of long-term insurance policies issued to underwritten retirement annuity funds. These policies are referred to as "fund member policies" in the LTIA Regulations.

⁵ As noted in paragraph 5.2 below, affected financial institutions are reminded that section 3A(1)(a)(iv) of the FAIS General Code applies to the fee authorisation in addition to the requirements of section 14(7)(b)(ii)(bb)(B).

- 4.2 The practical overall effect of the relevant provisions in Part 3A and Part 3B of the LTIA regulations, **read in isolation**, is that:
- Any remuneration payable for rendering services as intermediary, including any fees agreed to by the customer concerned (such as those contemplated in section 14(7)(b)(ii)(bb) of the PFA), would be subject to the maximum commission caps and other limitations of the LTIA Regulations if the transferee fund is an underwritten retirement annuity fund; and
 - no remuneration is payable for rendering services as intermediary in relation to a fund member policy that is transferred from one retirement annuity fund to another. Accordingly, the fees contemplated in section 14(7)(b)(ii)(bb) of the PFA would not be permissible where the transferee fund is an underwritten retirement annuity fund.
- 4.3 Section 14(7)(b)(ii) of the PFA effectively allows for the negotiation of a fee between the financial service provider and the transferring member or non-member spouse annually, above and beyond the permissible commission allowed for in the LTIA Regulations. As such, the provisions summarised in paragraph 4.2 above are inconsistent with the provisions of section 14(7)(b)(ii) of the PFA insofar as it relates to transfers from one underwritten retirement annuity fund to another.⁶
- 4.4 In considering this inconsistency it must be noted that section 14(7) is primary legislation whilst the LTIA Regulations are subordinate/delegated legislation. It is trite in the law of interpretation that subordinate legislation must be consistent with primary law, where a conflict exist the primary law must succeed. Section 14(7) must therefore prevail as this primary legislation is "superior" to subordinate/delegated legislation in their classification.
- 4.5 As such, the Authority confirms that, notwithstanding the above inconsistencies between the PFA and LTIA Regulations, the Authority will apply section 14(7)(b)(ii) of the PFA in accordance with the interpretation set out in paragraph 3 above.

5. APPLICATION OF THE FAIS GENERAL CODE OF CONDUCT

- 5.1 Financial institutions are reminded that section 14(7)(b) of the PFA should be read together with the FAIS General Code which also applies to the rendering of the financial services concerned.
- 5.2 In particular, without limiting the generality of paragraph 5.1, the following provisions of the FAIS General Code should be borne in mind when applying section 14(7)(b)(ii) of the PFA:
- Section 3A(1)(a)(iv); and
 - section 3A(1)(d).
- 5.3 These provisions of the FAIS General Code also apply to fees paid in the scenarios described in paragraphs 3.10, 3.11, and 3.12 above, notwithstanding that such fees are not also subject to section 14(7)(b)(ii)(bb) of the PFA.

⁶ As explained in paragraph 3.11 above, section 14(7)(b)(ii) of the PFA only applies where the transferor fund is an underwritten retirement annuity fund.

6. CONCLUSION

- 6.1 When applying section 14(7)(b)(ii) of the PFA it must be kept in mind that sections 3A(1)(a)(iv) and 3A(1)(d) of the FAIS General Code apply together with the sections of the PFA.
- 6.2 In respect of the payment of fees and commissions for financial services rendered by a financial services provider or representative after the transfer of interests, any fees and commissions over the allowed maximum allowed for in terms of the LTIA Regulations would require that the requirements of section 14(7)(b)(ii)(bb) are met.
- 6.3 The PFA prevails over the LTIA Regulations in respect of the existing inconsistency that exists in relation to remuneration payable in the context of transfers from one underwritten retirement annuity fund to another.

7. ENQUIRIES

- 7.1 For further information regarding this Guidance Notice and the contents hereof please contact the FSCA by emailing Johann.Vanderlith@fsc.co.za



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