LEGAL MATTERS

glacier
by Sanlam

JANUARY 2019
VOLUME 74

The retirement fund industry vs. the return of the *Prescribed Assets* requirement

Compiled by: Lize de la Harpe, Legal Advisor: Glacier by Sanlam

This publication is intended for use by intermediaries.

Introduction

The ANC's 2019 Election Manifesto as recently launched has left many retirement fund members gravely concerned about the impact of their intention to "*investigate the introduction of prescribed assets on financial institutions' funds..*".

In this article we will dig a bit deeper into the concept of "*prescribed assets"*, recap the current legal stance as set out in legislation applicable to pension funds and then lastly look at the process to be followed in order to enforce such a change.

Prescribed assets: an (unwelcome) blast from the past?

Unfortunately, the concept of *prescribed assets* (which refers to assets which must be held by a retirement fund by law) is not new to South Africa. The concept was introduced by the National Party (during the apartheid era) as a means to force pension funds to invest in its schemes and state-owned companies.

The Pension Funds Act No. 24 ("the Act"), as promulgated in 1956, formally introduced the concept and forced retirement funds to invest a significant percentage of assets in state-owned enterprises (including Sasol, Iscor and various Homeland Development Corporations) and government bonds.

Glacier Financial Solutions (Pty) Ltd, I A member of the Sanlam Group | Private Bag X5 I Tyger Valley 7536 I Email: client.services@glacier.co.za
Tel +27 21 917 9002 I Fax +27 21 947 9210 I Web www.glacier.co.za | Reg No 1999/025360/07 I Licensed Financial Services Provider

This document is intended for use by intermediaries. The information contained in this document has been recorded and arrived at by Glacier Financial Solutions (Pty) Ltd in good faith and from sources believed to be reliable, but no representation or warranty, expressed or implied, is made as to its accuracy, completeness or correctness. The information is provided for information purposes only and to assist the financial intermediary to submit an investment proposal to the client and should not be construed as the rendering of investment advice to clients.

By 1977 the level of prescription reached its highest level - retirement funds had to include at least 77.5% of its assets in a combination of state-owned companies (SOCs) and government bonds.

In 1989 – as apartheid was coming to an end - the prescribed assets requirements were scrapped.

Pension Funds Act and Regulation 28 – today

Section 36(1)(bB) of the Pension Funds Act 1956 provides that the Minister of Finance may make regulations limiting the amount and the extent to which a pension fund may invest in particular assets or in particular kinds or categories of assets, prescribing the basis on which the limit shall be determined and defining the kinds or categories of assets to which the limit applies.

Currently, these limitations are set out in Regulation 28. The main purpose is to protect the members' retirement provision from the effects of poorly diversified investment portfolios. The preamble to Regulation 28 clearly states that "*a fund has a fiduciary duty to act in the best interest of its members whose benefits depend on the responsible management of fund assets... This duty supports the adoption of a responsible investment approach to deploying capital into markets that will earn adequate risk adjusted returns suitable for the fund's specific member profile, liquidity needs and liabilities*."

Amending Regulation 28

The re-introduction of the concept of prescribed assets will require Regulation 28 to be amended (or replaced).

As mentioned above, section 36(1)(bB) of the Act enables the Minister of Finance to make regulations limiting the amount and the extent to which a pension fund may invest in particular assets/categories of assets. Section 36(1)(bB) must however be read in the context of Section 40C of the Act which sets out the process to be followed when issuing regulations:

> **40C Scrutiny of Regulations**
>
> Before regulations in terms of this Act are promulgated, the Minister must publish the draft regulations in the *Government Gazette* for public comment and submit the regulations to Parliament, while it is in session, for parliamentary scrutiny at least one month before their promulgation.
>
> [S. 40C inserted by s. 29 of Act 11 of 2007.]

The process for implementing (and amending) laws

Parliament has the power to pass new laws, amend existing laws and repeal old laws in the "national sphere" of government. The same power is exercised by provincial legislatures in the "provincial sphere" and by municipal councils in the "local sphere". This function is guided by the Constitution of South Africa, which governs and applies to all law and conduct within South Africa.

Both Houses of Parliament, the National Assembly (NA) and the National Council of Provinces (NCOP), play a role in the process of making laws. The draft legislation (a "**Bill**") can only be introduced in Parliament by a Minister, a Deputy Minister, a parliamentary committee, or an individual Member of Parliament (MP) and must be formally submitted to Parliament before Parliament can consider making it a law. Most Bills are prepared by government departments under the direction of their minister.

Diagram of how a law is made in South Africa:

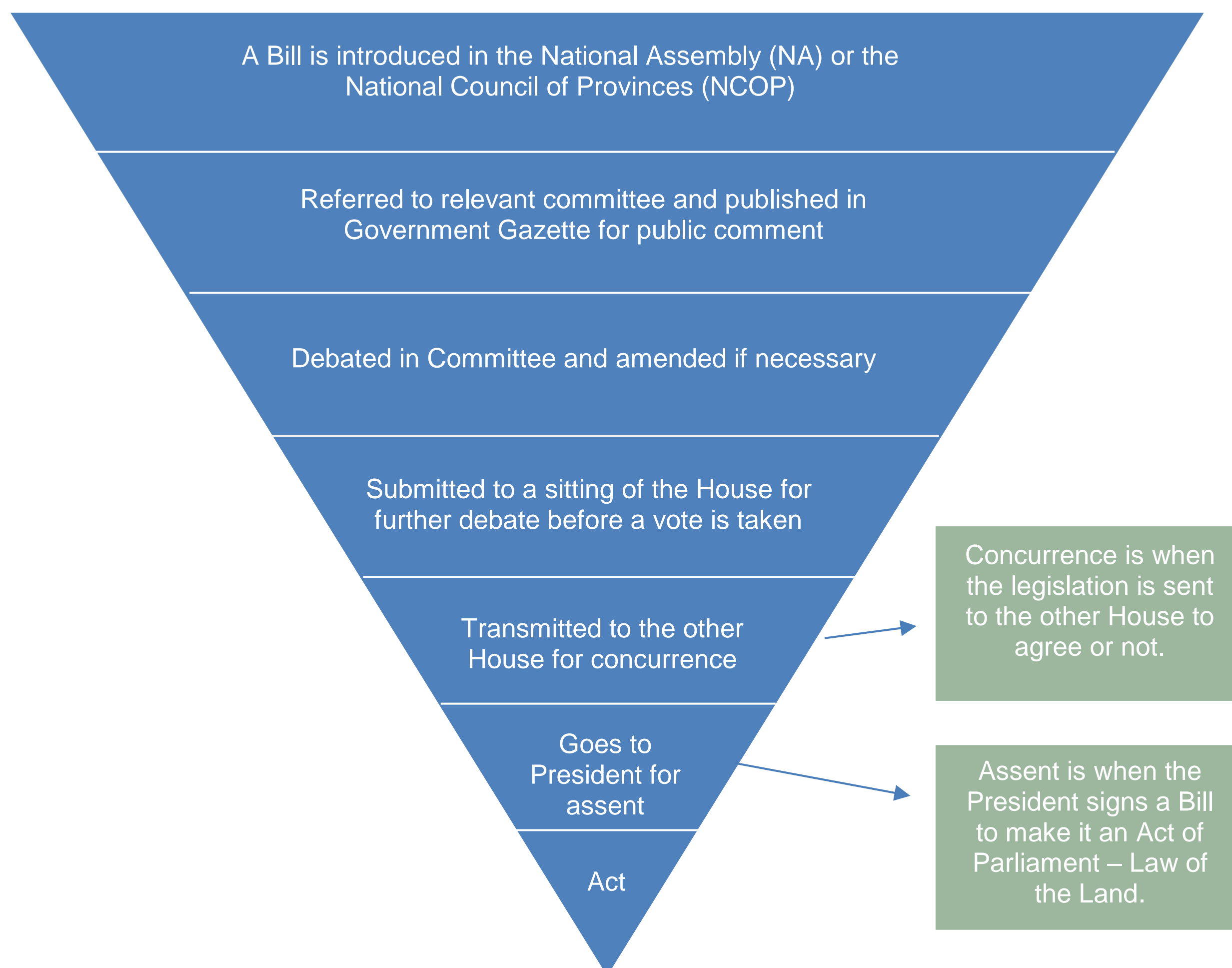

Diagram derived from https://www.parliament.gov.za/how-law-made

The preparation of a Bill involves a number of steps, for example the investigation and evaluation of the legislative proposals (which can either be proposed amendments to existing legislation or proposed new legislation) and consultation with interested parties.

The process may start with a discussion document called a Green Paper which is drafted in the Ministry or department dealing with a particular issue. In essence, it's a discussion document which gives an idea of the general thinking that informs a particular policy. It is then published for comment, suggestions or ideas. This document forms the basis for a *draft* Bill or, if the government feels it's necessary, for a White Paper which is a broad statement of government policy. Comment may again be invited from interested parties.

Once all relevant inputs have been taken into account, the minister and departmental officials draft the legislative proposals. These are usually in the form of a Draft Bill and an explanatory memorandum. The minister will submit these documents to Cabinet in order to obtain approval for the introduction of the Bill in Parliament.

Before a Bill can become a law, it must be considered by both Houses of Parliament (National Assembly and National Council of Provinces). Accordingly, once Cabinet has approved the draft Bill, the relevant Minister must submit a copy of the draft Bill to the Speaker of the National Assembly and the Chairperson of the National Council of Provinces. Prior to this, however, the State Law Advisers must be approached to certify the draft Bill. The role of the State Law Advisers in this regard is to ensure that a draft Bill is in line with the existing law and the provisions of the Constitution. If they are satisfied that the Bill is technically correct and its provisions are legally sound they approve

the Bill (called the certification of a Bill). The relevant Bill is then ready to be formally submitted to Parliament - in Parliamentary language the introduction is called “tabling”.

All Bills may be introduced only after **prior notice** of the tabling has been given in the Government Gazette. This notice must be accompanied by an explanatory summary of the Bill. If the Bill itself (instead of a summary) is published, the notice must contain an invitation to interested persons to submit written representations to the secretary of Parliament.

The Constitution distinguishes between four categories of Bills:

- Section 75 Bills are ordinary Bills not affecting the provinces;
- Section 76 Bills are ordinary Bills affecting the provinces;
- Section 77 Bills are money Bills that deal with appropriations, taxes, levies and duties; and
- Section 74 Bills that amend the Constitution.

The Constitution also prescribes the parliamentary process through which each of these categories of Bills must go before they can be passed by Parliament and become law.

A Bill is only referred to the President *after* it has passed through the National Assembly and NCOP. The Constitution requires that the President must assent to and sign a Bill. However, if the President has reservations about the constitutionality of a Bill, he or she may refer it back to the National Assembly for reconsideration. If the Bill affects the provinces, the NCOP must participate in the reconsideration of the relevant Bill.

A Bill that has been assented to and signed by the President becomes an Act of Parliament and must be published shortly thereafter in the Gazette. An Act takes effect (becomes binding on everyone) when it is published in the Gazette or on a date determined in terms of the Act. Sometimes an Act may require certain actions to be taken by the Department before it can be implemented, for instance subordinate legislation (regulations, determinations, rules, etc.) may have to be prepared and promulgated to further regulate aspects in terms of an Act. In such instances an Act contains a provision that the Act comes into operation on a date determined by the President by proclamation in the Gazette.

Once the necessary actions have been finalised, the President is approached and requested to put the Act into operation on a certain date. After the President has assented to the implementation of the Act, a proclamation is published in the Gazette and the Act comes into operation on a date determined in the proclamation.

*summary of the legislative process as set out on www.justice.gov.za

Post script

The “threat” of reintroducing prescribed assets has been casually thrown into speeches and media releases every so often over the last ten years – it would thus be premature to frantically start preparing for the worst. For the time being, Regulation 28 (and the protection it offers to members) as it stands. will remain in force.

And as one can see from the above, changing legislation is not a quick process – and it most certainly does not happen in isolation. Whether or not this will become a constitutional issue also still remains to be seen.