The process of ethical decision-making in South African retirement funds

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ABSTRACT
As the principal decision-makers in retirement funds, the trustees have a number of duties placed upon them including a duty of care, a duty of impartiality, a duty to avoid and manage conflicts of interest, a duty to act in accordance with the purpose of the fund and a duty of accountability. Decision-making by trustees and the actuaries that assist them in the context of a complex environment with multiple stakeholders can be informed by considering various ethical theories. This paper reviews the theory of right action, virtue theory and the ethics of care together with the theory of justice and interprets the duties of trustees and actuaries in terms of these theories. A six-step decision-making framework based on the actuarial control cycle is developed to provide an initial attempt to formalise the process of ethical decision-making in South African retirement funds. This framework is applied to case studies involving the review of an investment policy statement, the distribution of death benefits, and annuitisation options. The case studies illustrate that, although the framework does not provide ethical solutions in their own right, it assists trustees and the actuaries who advise them with the process of making an ethical decision.

KEYWORDS
Ethics; ethical framework; retirement fund; trustees; actuaries; fiduciary duties; regulation; theory of right action; utilitarianism; virtue ethics; ethics of care; theory of common good; theory of justice

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As we practice resolving dilemmas we find ethics to be less a goal than a pathway, less a destination than a trip, less an inoculation than a process.

Rushworth Moulton Kidder

1. INTRODUCTION
1.1 The aim of this research paper is to explore how the somewhat abstract and broad concept of ethics can be applied in the day-to-day process of decision-making in South African retirement funds.

1.2 Trustees of retirement funds have certain duties placed upon them in terms of common law and in terms of an array of legislation including trust law (Hanekom, 2013; Downie, 2010). These duties include a duty of care, a duty of impartiality, a duty to avoid and manage conflicts of interest (Hanekom, op. cit.) as well as a duty to act in accordance with the purpose of the fund (Watchman, 2011; du Toit, 2002; Hanekom, op. cit.; Downie, op. cit.). In addition, trustees have a duty of accountability which can be interpreted as being held accountable for all decisions made and being held accountable in terms of these other duties (Downie, op. cit.).

1.3 Trustees may be assisted by actuaries. Members of the Actuarial Society of South Africa (ASSA) are held to a Code of Professional Conduct that emphasises that the services that actuaries render to their clients, including retirement funds, must reflect ethical conduct. This is described as encompassing honesty, integrity, competence and due care and that the actuary's behaviour should uphold the profession's duty to the public. Thus actuaries providing advice to retirement fund trustees should consider not only the duties faced by their clients but those placed on them by the actuarial profession.

1.4 This research paper explores these duties by addressing the following research questions:
— To what extent does the discharge of duties placed on trustees and actuaries of retirement funds lead to ethical issues?
— Can an ethical decision-making framework assist trustees and actuaries with the process of ethical decision-making?

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3 ibid.
1.5 There is a notable absence of actuarial literature specifically focused on actuarial ethics despite Waddock (2005) noting that ethics is an essential part of education for business professionals and Lowther, McMillan & Venter’s (2009) survey suggesting that it is ethical values that are important for actuarial quality. Although Lowther (2004) considered the professional duties involved in the exercise of actuarial discretion when calculating transfer values for retirement funds, this was considered primarily in the context of the application of actuarial techniques in a field where there was existing professional guidance. Lowther & McMillan (2006) state that ethics apply in situations where required codes of conduct and guidance have not been specified. This paper thus represents an initial attempt to formalise the process of ethical decision-making in South African actuarial pensions practice.

1.6 The aim of this paper is not to provide trustees and actuaries with an in-depth analysis of ethical theory, where there is a vast amount of literature and the authors can best be described as interested amateurs. Instead it is to provide a formal and theoretically sound framework that trustees and actuaries can adopt to promote a more ethical process of decision-making which the authors argue is essential in the discharge of trustee and actuarial duties. In order to show the practical application of the framework for ethical decision-making, the authors have selected three case studies based on their personal experience and selected Pension Fund Adjudicator (PFA) cases. Since the specific circumstances have been adapted in some cases, references to specific funds and cases have been omitted as the inclusion of such detail would be misleading. These case studies are used for illustrative purposes. Although the authors aimed to cover a variety of ethical issues that arise when trustees and actuaries discharge their duties, it is important to note that this paper does not focus on whether the final decision reached was ethical but rather on the process of ethical decision-making.

1.7 Establishing whether the discharge of the duties faced by trustees and actuaries lead to ethical issues requires an understanding of what is meant by the term ‘ethics’. This is set out in Section 2. As the emphasis of this paper is on a framework for an ethical decision-making process, the literature review is brief and focuses only on the elements of ethical theory required to appreciate that the discharge of all trustee and actuarial duties leads to ethical issues and to develop a framework for ethical decision-making to be used by trustees and actuaries. In Section 3, the duties of trustees and actuaries are revisited and mapped to the concepts introduced in Section 2. Section 4 sets out an ethical framework for decision-making. Sections 5 to 7 contain case studies illustrating the practical application of the framework provided in Section 4 and Section 8 contains a summary and conclusion.
2. LITERATURE REVIEW

Normative ethics deals with distinguishing right from wrong (Copp, 2006). There are a number of ethical theories that can make this distinction and this section reviews three major theories: the theory of right action, virtue theory and the ethics of care. These theories are then discussed in the context of the theory of justice. The intention of this review is not to provide a comprehensive exposition of these theories but rather to explore those elements of these theories that would assist in the understanding of the ethical nature of trustee and actuarial duties and the development of a framework for ethical decision-making to be used by trustees and actuaries.

2.1 Theory of Right Action

2.1.1 A theory of right action attempts to determine the basic factors that make an action right or wrong (Copp, op. cit.). Of the three ethical theories reviewed, this is the only ethical theory that evaluates the action itself and this may be done via consequentialist and non-consequentialist theories (ibid.).

2.1.2 ‘Consequentialist’ theory is based on the premise that a right action is one that promotes good or one that produces the most value (Copp, op. cit.). In other words, a right action can be judged by its outcome. The most common example of consequentialism is utilitarianism (Brink, 2006). By the standards of utilitarianism, an action is only ethical if the sum of all the utility of one action is greater than the sum of all the utility of another action (Ferrel & Gresham, 1985). This involves consideration of the utility of all stakeholders (ibid.).

2.1.3 ‘Non-consequentialist’ theory or deontology evaluates actions not on outcome but on adherence to duties (Benn, 1998). According to McNaughton & Rawling (2006), the basic features of deontology include the concepts of:

- constraints arising from a moral code;
- duties of special relationships; and
- sufficiency, in that the agent need do no more than fulfil their duties.

The exposition of the moral code underlying these duties is thus central to deontology (Deigh, 1995). The duties that arise under deontology may be governed by legislation or regulation. For this reason, deontology could be seen as a combination of morality, which encompasses the effects that the action has on both individuals and the broader community, as well as legal and regulatory adherence (Jones, 1991).

2.2 Virtue Theory

2.2.1 Annas (2006) describes ‘virtue’ as a “disposition to do the right thing for the right reason in the appropriate way.” In virtue theory, a truly virtuous person would always act ethically in that they would always do the right thing for the right reason. Thus virtue theory requires the cultivation of aspirational virtues (Benn, op. cit.) or character (Hursthouse, 1999). Virtue theory holds deontology as a secondary goal given that those without perfected virtues may need to rely on rules (Copp, op.
cit.). It is noted that virtue theory involves a necessary overlap between personal and professional morality (Fleddermann, 2011).

2.2.2 Thus while theories of right action evaluate the action itself, virtue theory evaluates the character traits behind the action, including adherence to rules.

2.3 Ethics of Care

2.3.1 The ethics of care involves the assessment of the degree to which people's needs are met (Copp, op. cit.). The ethics of care is based on the concept that people are relational and these relationships, both personal and professional, should result in needs being met (Held, 2006).

2.3.2 The theory of common good is a special case of the ethics of care. Audi (1995) defines ‘common good’ as the “common goal of all who promote the justice of that community.” Argondoña (1998) describes the common good as a set of conditions that allow members of society to achieve their personal objectives and thus advance the good of society.

2.3.3 Despite the theory of common good allowing for individuals to pursue personal objectives, the ethics of care stands in contrast to individualism which prioritises the pursuit of individual interests (Held, op. cit.). This is because the theory of the common good involves the promotion of justice (Audi, op.cit.). According to Benn (op. cit.) justice requires that people are treated as “ends” as opposed to “means” which emphasises a relational aspect to justice which is the foundation of the ethics of care.

2.3.4 It could be argued that the ethics of care is similar to consequentialist theories of right action because it considers the cumulative effect of actions in meeting needs. However, the theory of right action emphasises the evaluation of the action itself while the ethics of care would suggest the effect on the relationship would require scrutiny. Although caring is a virtue, the ethics of care is not a kind of virtue ethics because virtue ethics focus on character traits of individuals and the ethics of care focuses on caring relations (Held, op. cit.).

2.4 The Theory of Justice

2.4.1 Although there are distinct differences between the theory of right action, virtue ethics and the ethics of care, there are some similarities between them as noted in ¶2.3.4. It can be argued that these similarities arise due to all normative ethics having the goal of distinguishing between right and wrong (Copp, op. cit.). Held (op. cit.) argues that a complete ethical framework cannot ignore justice. Thus it can be argued that the theory of justice is essential to help distinguish right from wrong, irrespective of the ethical theory applied.

2.4.2 The theory of justice emphasises fairness and equality (Held, op. cit.) as well as individual rights and balancing competing rights (Held, op.cit; Steiner, 2006; Asher, 1998). According to Asher (op. cit.), justice is the art of finding the balance between the needs, actions and values of different individuals. Rawls’ (1971) theory of
justice “rates liberty highest, and then balances equality, prosperity and need by a rule that requires the interests of the worst off to be maximised” (cited in Asher, op. cit.).

2.5 Summary

The theory of right action holds that an individual action can be assessed as right or wrong. The theory of justice can aid in making this distinction. Consequential theories of right action assess the outcome of an action. Deontology examines the rules and process behind the action. Virtue ethics considers primarily the motivation for any action with the process being a secondary consideration. The ethics of care, in contrast, focuses on the relationships between the stakeholders and how their needs are met.

3. THE DUTIES FOR TRUSTEES AND ACTUARIES TO BEHAVE ETHICALLY

This section provides a closer examination of the duties placed on trustees and actuaries and interprets them in terms of the ethical theories set out in Section 2. The authors acknowledge that there are a number of different approaches to analysing the duties of actuaries and trustees and the lists of duties detailed in this section may not be exhaustive.

3.1 The Duties of Trustees

3.1.1 As set out in ¶1.2, trustees have a duty of care, a duty of impartiality, a duty to avoid and manage conflicts of interest (Hanekom, op. cit.) as well as a duty to act in accordance with the purpose of the fund (Watchman, op. cit.; du Toit, op. cit.; Hanekom, op. cit.; Downie, op.cit.). In addition, trustees have a duty of accountability in terms of all decisions made and in terms of these other duties (Downie, op. cit.). The repeated use of the term “duty” indicates that a primarily deontological, or duty-based, framework would apply. The Pension Funds Act now refers specifically to trustees having a duty to comply with all prescribed requirements which results in the Pension Funds Act explicitly stating that trustees have both moral and legal duties which stresses that the duties of trustees are ethical, according to the definition given in ¶2.1.3.

3.1.2 The duty of care involves trustees discharging their duties in the utmost good faith in a prudent manner4 (Hanekom, op. cit.; Downie, op. cit.; du Toit, op. cit.). Case law5 suggests that this means that trustees are required to show greater care in the management of trust assets than they do their own (ibid.) and to be diligent.6 Both Watchman (op. cit.) and Asher (op. cit.) describe this as acting in the best interests

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4 See also PF Circular 69 and the Financial Institutions (Protection of Funds) Act. Act 28 of 2001, Republic of South Africa, as amended
5 Sackville West v Nourse 1925 AD 516
6 Affirm Marketing Pty (LTD) and Others v IF Umbrella Fund and Others, Pension Fund Adjudicator determination, July 2012
of all beneficiaries—which includes members. This is echoed in Section 7C of the Pension Funds Act which states that the board of trustees must “direct, control and oversee the operations of a fund in accordance with the applicable laws and the rules of the fund” and “take all reasonable steps to ensure that the interests of members in terms of the rules of the fund…are protected at all times”. The principle of acting in the best interests of members is also supported by case law. Although Swart (unpublished) suggests that this duty can be understood in terms of virtue ethics, the process of acting in terms of the best interests of others is essentially relational and hence arguably better understood in terms of the ethics of care.

3.1.3 According to the Mouton Committee (1992, as cited in Marx & Hanekom, 2008) the duty of impartiality involves all members receiving “equal and objective treatment” from the trustees. Determinations by the PFA have reinforced that treating different groups of members differently without justification would constitute unethical behaviour which in turn results in a breach of this duty. Impartiality itself is considered to be a virtue and is a critical component of justice (Held, op. cit.).

3.1.4 The duty to avoid conflicts of interest encompasses conflicts between personal interests and official duties (du Toit, op. cit) as well as a requirement to act independently. It also precludes self-enrichment at the cost of the interests of the fund and beneficiaries (du Toit, op. cit.). Avoiding and managing these conflicts of interest is embodied in the virtue of objectivity, referring specifically to the trustee’s ability to consider what is best for the member independently of what is the trustee’s interest.

3.1.5 Watchman (op. cit.) and Downie (op. cit.) indicate that trustees must act in accordance with the purpose of the fund. The purpose of a retirement fund is indicated in the fund rules and is often a generic statement indicating that the purpose of the fund is to provide certain benefits on specified events. The rules may prioritise retirement benefits over other types of benefits. This duty suggests that when interpreting what is just and fair, one should return to the purpose of the fund. Hence this duty informs the understanding of justice in the context of ethical retirement decision-making.

3.1.6 The duty of accountability means that the trustees must be prepared to report on their decisions and reasons for making those decisions (Downie, op. cit., du Toit, op. cit.). Downie (op. cit.) emphasises that the duty of accountability is essential to upholding the duty of impartiality. Section 7D of the Pension Funds Act extends this to include communicating to members their “rights, benefits and duties”. Again,

7 Act 24 of 1956, Republic of South Africa
8 For example Lorentz v TEK Corporation Provident Fund and Others 1998 (1) SA 192 (W) and PPWAWU National Provident Fund v Chemical Energy Paper Printing Wood & Allied Workers Union(2007) 28 ILJ 2701 (W)
9 Epol Provident Fund & Others v Premier Foods Provident Fund and Others, Pension Fund Adjudicator determination, September 2000
10 Pension Funds Act, supra
11 BW Colledge v LTA Limited Pension Fund, Pension Fund Adjudicator determination, September 1999
12 Act 24 of 1956, Republic of South Africa

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accountability is a virtue although this duty is consistent with the ethics of care in that it emphasises the formation of a relationship with reciprocal duties.

3.1.7 Thus, in summary, trustees need to use the purpose of the fund to guide their thinking of what is just. The virtue of justice needs to guide their decision-making. The relationship between the trustee and fund beneficiaries should also be scrutinised in terms of rights, duties and obligations. Ultimately, trustees should develop the virtue of accountability in addition to the virtues of diligence, impartiality, objectivity and prudence. In addition to moral considerations, trustees are also required to comply with all relevant legislation and regulation.

3.2 The Duties of Actuaries

3.2.1 As stated in ¶1.3 actuaries providing advice to retirement fund trustees should consider not only the duties faced by their clients but those placed on them by the actuarial profession. In the case where the actuary’s client is the trustees the actuary has a duty to consider the duties faced by the trustees, outlined in ¶1.2. It is important to differentiate between the role of actuaries as advisors to the trustees and the role of trustees as the decision-makers. However, actuaries are also decision-makers in the context of deciding the advice to provide given professional and ethical requirements.

3.2.2 Lowther, McMillan & Venter (op. cit.) state that the general ethical and professional requirements of actuaries encompass an ability to avoid conflicts of interest and comply with legislation and professional guidance as well as the values of integrity, objectivity, confidentiality, due care, independence, scepticism, accountability, courage, reflection and a commitment to the public interest, social responsibility, ethical business, whistle-blowing and ethical judgement. The current Actuaries’ Code encourages a deontological approach to ethics in terms of compliance with legislation and professional guidance. However, the remaining requirements are a list of virtues suggesting that actuarial actions can be assessed by virtue ethics where there are no rules to follow.

3.2.3 Actuarial recommendations are often based on assumptions about future experience, which may not be borne out in practice. Lowther & Mort (2002) have argued that these assumptions can be tested by considering whether the actuary had acted reasonably with regard to the information available at the time. This emphasises the importance of the virtues of diligence and reflection in actuarial work.

3.2.4 Justice is also a key ethical requirement of actuarial work, and this goes beyond the traditional requirement of impartiality. As discussed in ¶3.1.6, accountability through disclosure is essential to impartiality which in turn is necessary for justice, as outlined in ¶3.1.3. The PFA has supported this logic and has emphasised the importance of justice being seen to be done by various stakeholders (Lowther & Mort, op. cit.). The Academy of Actuaries standard of actuarial practice on general
disclosure requirements, ASOP 41,\textsuperscript{13} places the duty of disclosure firmly in the actuarial domain for actuaries providing recommendations and supporting decision-making. It also notes that a balance needs to be struck between the preservation of confidentiality, a key virtue, and the adequacy of disclosure and accessibility of information to the affected stakeholders, in order for justice to be achieved. ASOP 41 thus emphasises the importance of the virtue of accountability, in terms of disclosure, to achieve justice.

3.2.5 Thus, in summary, actuaries advising trustees need to consider the duties of the trustees, comply with relevant legislation and professional guidance and encompass the virtues given in ¶3.2.2.

4. AN ETHICAL FRAMEWORK FOR DECISION-MAKING

Rest (1986) proposed a four-component model which involves the steps of recognising moral issues, making moral judgements, establishing moral intent and implementing moral action. The definition of ‘moral’ used by Jones (op. cit.) is given in ¶2.1.3 and the authors have chosen to use this framework as a basis for ethical decision-making. The authors have chosen to expand this framework by using the familiar actuarial control cycle to include the legal and regulatory environment, the duties of trustees and actuaries described in ¶3.1 and ¶3.2 respectively and the feedback loop of monitoring the consequences of the solution and taking this into account in future decision-making. This feedback loop was incorporated due to its importance in learning and development (Bellis, 2006).

4.1 Specify the Problem: Recognise the Ethical Issue

Jones (op. cit.) states that in order to begin the ethical decision-making process, one needs to recognise that an ethical issue is present. The definition of an ‘ethical decision’ used by Jones (op. cit.) is given in ¶2.1.3. As demonstrated in Section 3, ethical issues arise whenever trustees and actuaries discharge their duties in relation to retirement funds as decision-makers and advisors respectively. Jones (op. cit.) also suggests including an assessment of the intensity of the ethical issue in terms of factors such as the magnitude of the consequences for affected stakeholders and this would determine the rigour with which the framework would be applied. At this stage, the trustees should begin to consider whether they have the ability to manage these ethical issues and whether additional assistance is required (Jones, op. cit.). This may include actuarial advice, where the actuary will need to consider the duties placed on the trustees.

4.2 Develop the Solution: Gather Information

The virtue of diligence means that trustees must apply their minds to all relevant facts.\textsuperscript{14} Downie (op. cit.) refers to this as “the duty to know”. Young & Annisette (2009)

\textsuperscript{14} Segal and Others v Lifestyle Retirement Annuity Fund, Pension Fund Adjudicator determination, May 1999
state that individuals will not always agree on the material facts of a given situation and suggest that rather than being permanent and easily identifiable, facts are constantly changing and are subject to reinterpretation. This suggests that for decision-making to be effective, information should be gathered and agreed upon. This process would include identifying stakeholders and all alternative courses of action (Frederick, 1999). Actuaries advising the trustees may be required to gather information to support their recommendations.

4.3 Understand the Environment: Consult Legislation, Guidance and Regulation

Given that trustees have a duty to perform certain functions in terms of the Pension Funds Act and that actuaries may have a prescribed role under the same act, an understanding of the legislative environment including case law is essential in a deontological framework. PF130 requires trustees and actuaries to act in accordance with relevant laws and codes of conduct when dealing with the affairs of retirement funds15 which is included in Downie’s (op. cit.) duty to know. However, it is important to recognise that governance measures—values and ethical principles, which are addressed in ¶4.4—are needed because not all circumstances relating to the duties of trustees may be defined within a legal framework. Actuaries will be required to consult and comply with relevant legislation, regulation and professional guidance.

4.4 Develop the Solution: Evaluate Possible Options

4.4.1 Frederick (op. cit.) states that in the process of making an ethical decision one needs to establish all the material alternative actions. This may be impractical where there may be infinitely many solutions available and a shortlist may need to be assessed against a number of tests to see that the trustees are performing their duties. The tests proposed here follow from ¶3.1.7.

4.4.2 The first test is whether the option complies with the law or regulation.

4.4.3 The second test is to consider the purpose of the fund as defined in the fund rules. In certain cases, case law may aid in the interpretation of the rules.

4.4.4 The third test is to consider what would be just. The definition of justice would involve consideration of the needs of various stakeholders, which obviously requires an understanding of who the stakeholders are (Frederick, op. cit.) and who the most vulnerable stakeholders are.

4.4.5 The fourth test considers the obligations placed on the trustee and the actuary in terms of their relationship with various stakeholders. The specifics of the relationship would need to be considered and would be deemed to include the public interest element of professional standards for actuaries.

4.4.6 The fifth test is whether the decision-makers encompass the right virtues. For trustees, this implies diligence, impartiality, objectivity and prudence. For actuaries,

additional requirements include integrity, confidentiality, scepticism, courage, reflection and a commitment to the public interest among others, as discussed in ¶3.2.2.

4.5 Develop the Solution: Make a Decision

Thereafter a decision should be made, actioned and communicated. Ethics does not require accountability even though there is a duty on trustees and actuaries to be accountable. This means being able to justify the decision and communicate it where necessary. As noted in ¶3.2 above, the actuary has a professional requirement to ensure that recommendations and results are communicated in an accessible way and with sufficient detail with regard to, inter alia, assumptions and risk. The ethical implications of the communication itself would need to be considered in light of the third, fourth and fifth tests, as considered in ¶¶4.5.1–4.5.3. The specific questions that the trustees would need to ask may depend on the circumstances.

4.5.1 Test 3: Justice

4.5.1.1 Not all members may have access to the same communication channels. Trustees need to consider whether this will result in certain members having access to the information at different times. This may be unjust if having access to the information for longer confers an advantage to the member.

4.5.1.2 If multiple communication media are used, trustees will need to ensure that all forms of communication convey the same information and give equal emphasis to the same aspects.

4.5.1.3 A further consideration is that when idioms and images are used, they be more meaningful to certain cultural groups than others. If this changes the meaning of the communication for some groups relative to others, this may be unjust.

4.5.1.4 As mentioned in ¶3.2.4, actuaries may assist in balancing the preservation of confidentiality, and the adequacy of disclosure and accessibility of information to the affected stakeholders.

4.5.2 Test 4: Relationships and Care

The trustees will need to ensure that they use language that the beneficiary understands and have allowed the beneficiary the opportunity to query aspects of the communication that they do not understand. This is non-trivial in cases where the beneficiary is not a fund member and there may be no existing relationship between the beneficiary and the fund.

4.5.3 Test 5: Virtues

The virtues, particularly diligence, scepticism and courage tend to encourage full disclosure which includes alternative solutions that were considered and discarded. This may make communication longer and more complicated and may possibly be in conflict with the fourth test, as described in ¶4.5.2. This conflict may need to be specifically acknowledged.
4.6 Monitor the Solution: Future Decision-Making

4.6.1 It is essential that the ethical framework be expanded to include monitoring. Young & Annisette (op. cit.) state that ethical behaviour is a process that requires continuing reflection on decisions and the consequences of these decisions. In other words, the decision needs to be reviewed at a later stage in order to assess if the correct decision was taken and if the decision-making framework could be improved. This is important for decisions with an ongoing effect on a retirement fund where it may not be obvious that not reviewing the decision is itself an ethical decision.

4.6.2 A review of a decision after the fact may indicate that an alternative course of action was appropriate, even though the decision was made using all facts at hand at the time. Jones (op. cit.) also notes the importance of the feedback loop in providing additional information for future decision-making in the organisational context.

4.6.3 Monitoring and evaluating the experience, including the requirement to consider whether the actuarial solution requires modification as a result of analysis of experience, is an important component of the actuarial control cycle (Bellis, op. cit.).

5. CASE STUDY 1: INVESTMENT STRATEGY OF A DEFINED-CONTRIBUTION FUND

The first case study relates to the review of an investment policy statement (IPS) as required by PF130. For illustrative purposes, one can consider a defined-contribution (DC) retirement fund in which there is no member-level investment-channel choice. Therefore, the trustees are required to set a “one-size-fits-all” investment strategy for all members of the fund.

5.1 Specify the Problem: Recognise the Ethical Issue

The IPS describes the investment strategy that the DC fund employs to meet the objective of the fund. The ethical issues that arise here are whether the process used to determine the investment strategy is ethical and whether the IPS allows trustees to discharge their duty of setting an investment strategy to meet the purpose of the fund ethically. A responsibility of the actuary making recommendations with respect to the IPS is to ensure that the trustees are aware of the risks associated with the strategy adopted and how these risks may affect various stakeholders such as the members, pensioners, employer and other market participants.

5.2 Develop the Solution: Gather Information

5.2.1 The trustees need to gather information regarding the nature of the fund’s liabilities. In a DC fund, the accounting liability is simply the members’ accumulated fund credit which is determined by the investment strategy. Since this fund does not have member-level investment choice, the trustees may use a target replacement ratio for the purpose of setting the investment strategy. Replacement ratios from the literature can range between 65% and 89% (Butler & van Zyl, 2012). The trustees
are likely to be relying on projection assumptions recommended by the actuary in assessing these replacement ratios.

5.2.2 The demographics of the membership will influence the implicit liability. Therefore, information on the age, gender and income of members will need to be gathered. At an individual member level, trustees might also want information on current health to assess longevity, current financial obligations, maximum affordable contribution rate and attitude to risk. Gathering this sensitive information may itself raise ethical issues, particularly around confidentiality. Information on the members’ current wealth is a necessity for members who join the fund later in life. Arguably, the member should be engaging with a financial advisor to assist them in managing their current wealth outside the retirement fund. Nevertheless, this information on current wealth would assist trustees in setting an appropriate investment strategy. Most importantly, in order to assess reasonable benefit expectations of members the needs of members will need to be assessed.

5.2.3 Information relating specifically to investments will need to be gathered including categories of investments, expected investment returns, risks associated with different investments and correlations between expected returns on investments.

5.2.4 Information on the fund’s liquidity requirements, cashflow requirements and current financial status will need to be gathered.

5.2.5 Information on the current asset managers, their mandates, benchmarks and performance fees will need to be gathered.

5.2.6 The actuary may assist in gathering this information and using this information to provide a recommended investment strategy.

5.3 Understand the Environment: Consult Legislation, Guidance and Regulation

Section 36(1)bB of the Pension Funds Act states 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. These limits are set out in Regulation 28.

5.4 Develop the Solution: Evaluate Possible Options

5.4.1 The first test is whether the fund complies with the law or regulation. The fund needs to ensure that its current investments do not breach the limits as specified by Regulation 28. However, as stated in ¶2.1.3, an ethical decision is one that is both legal and morally acceptable. Therefore, even though the fund may not be in breach of any regulatory limits, the trustees will need to consider whether the current and future investments of the fund are appropriate to ensure that the members’ interests are protected at all times as discussed in ¶3.1.2. For example, Regulation 28 allows the fund

16 Act 24 of 1956, supra
to invest a maximum of 75% of its assets in equity, but holding 75% in equities may not be ethical if such an allocation does not protect the interests of members at all times.

5.4.2 The second test is to consider the purpose of the fund which is to provide a benefit on retirement. In DC funds, the benefits, particularly on withdrawal or retirement, are a function of the contributions less expenses that are accumulated with investment returns. As mentioned in ¶5.2.1, a target replacement ratio can be set. However, the replacement ratios generally used do not give consideration to the needs of the members. The trustees would need to consider the reasonable benefit expectations of members and set a replacement ratio accordingly. Even in this instance, a single target replacement ratio may not be appropriate for all members (Butler & Van Zyl, op. cit.).

5.4.3 The third test is to consider what would be just. The definition of justice would involve consideration of the needs of various stakeholders. In determining the reasonable benefit expectations of members, the trustees will need to consider the needs of the members. The trustees will also need to consider the stakeholders who require the most protection. The trustees will need to consider the needs of other stakeholders. This requires the identification and agreement of the fund’s stakeholders. In addition, because the fund does not have member-level investment choice, the investment strategy will be set based on the circumstances of the average member. But, the needs and circumstances of individual members may differ. For example, members may have other sources of income or be more or less risk-averse than the average member. Therefore, choosing a “one-size-fits-all” approach is inherently unjust because it may be suitable for some members and unsuitable for other similar members.

5.4.4 The fourth test considers the obligations placed on the trustees and actuary in terms of their relationship with the stakeholders. This may relate to the communication between the trustees and beneficiaries. Usually, members receive information on the value of their accumulated fund, the fund’s investment performance and the average costs per member. The communication is usually from the trustees to the members, however, the actuary may need to alert the trustees to material risks that should form part of this communication. The obligations placed on trustees in terms of their relationship with the members, require trustees to not only resolve members’ complaints but also to engage with members on what their needs are, on whether their needs are being met and to provide clarity on information that they do not understand. This obligation could also be extended to consider whether the communication to members provides them with all the information required to evaluate the adequacy of their retirement provision. The inclusion of benefit illustrations may serve as a key communication to members for this purpose. The method and language of

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17 Amendment of Regulation 28 of the regulations made under Section 36, Government Gazette No. 34070, 4 March 2011
communication also raises ethical issues as discussed in ¶¶4.5.1–4.5.3. In addition, because the member bears the investment risk, they need to be fully informed of the risk they bear in order to be able to consent to bearing this risk. Allowing the member to bear the investment risk without full consent would not pass the fourth test.

5.4.5 The fifth test is whether the decision-makers encompass the right virtues. For trustees, this implies diligence, impartiality, objectivity and prudence. For actuaries, additional requirements are integrity, confidentiality, scepticism, courage, reflection and a commitment to the public interest. Trustees are required to perform due diligence on the information gathered in ¶5.2. But, part of the due diligence process is to address the ethical issues that arise in determining the investment strategy. In addition, the virtue of diligence needs to be balanced with the public interest. The incorporation of sustainability into investment decisions and ethical investments address the issue of the retirement fund acting in the public interest. The amended Regulation 28 deals with the former and PF130 deals with the latter. The conflicting requirements suggested by both will be discussed in ¶¶5.4.6–5.4.7.

5.4.6 The fact that consideration of environmental, social and governance characteristics are required for prudent investing, according to the amended Regulation 28, to the extent that they may affect the sustainability of the long-term performance of the fund, results in trustees having to consider whether their investment decisions are in the public's interest, protect the environment and uphold good governance. Therefore, the virtue of prudence needs to also be balanced with the public interest. As outlined by Reddy & Thomson (unpublished), since environmental, social and economic sustainability are connected, sustainability is affected by the investment choices institutional investors, in particular retirement funds, make and it affects the choices they make. In order for retirement funds to meet the requirement of the amended Regulation 28 to consider the long-term sustainability of the fund the effects of the fund's investment decisions on the environment, society and economy will need to be considered as well as the effect of sustainability concerns, such as resource constraints, on its investment strategy.

5.4.7 In contrast, according to PF130, the primary obligation of trustees is to provide optimum returns for their beneficiaries and only once these returns have been met, should funds consider ethical investments.¹⁹ In this case, it may be considered unethical for the fund to invest in underperforming assets, even if they are considered to be ‘ethical investments’, since optimum returns need to be achieved. PF130 does not provide the time horizon over which the trustees need to achieve these optimum returns. To achieve sustainability of the fund, the fund will need to take a long-term view of returns. In addition, optimum returns may be affected by the effects of unsustainability (Reddy & Thomson, op. cit.). For example, Jones et al. (unpublished) concluded that resource constraints would place a limit on future economic growth rates and hence investment returns will be lower. Therefore, in the pursuit of optimum returns the

¹⁹ Financial Services Board, Circular PF NO. 130: Good Governance of Retirement Fund: Annexe B, supra
fund will need to consider the effects of unsustainability on investment returns. PF130 suggests that an ethical investment can be achieved by investing in companies that meet certain criteria. However, such ethical investments do not consider the effect of that investment decision on society or the environment or whether the members themselves consider such an investment to be ethical. It is these effects that determine whether a decision is moral or not, as described in ¶2.1.3.

5.5 Develop the Solution: Make a Decision

The revised investment strategy that the trustees decide on should enable the trustees to discharge their duties ethically and should also demonstrate that an ethical process was undertaken to arrive at that strategy. PF130 states that in making a decision, trustees may obtain expert opinion and advice but that care must be taken to ensure that the advice obtained is free from conflicts of interest.  

5.6 Monitor the Solution: Future Decision-Making

Not all of the ethical issues that arise in setting the investment strategy will be addressed by the framework but the process of identifying them will assist trustees to question the ethics behind the decisions they make regarding investments and provide information for future decision-making.

5.7 Concluding Remarks

This case study emphasises that the requirement for trustees to act prudently regarding setting an investment strategy is about the process involved and not about the performance of the fund’s investment strategy.

6. CASE STUDY 2: DEATH BENEFIT DISTRIBUTIONS

Complaints regarding the distribution of death benefits represent 10% of matters brought before the PFA.  

6.1 Specify the Problem: Recognise the Ethical Issue

The distribution of death benefits is a trustee duty that is set out in Section 37C of the Pension Funds Act. Thus, because it involves the trustee carrying their duties, it is an inherently ethical issue and ethical duties also apply to actuaries assisting them in this process. It is also an obviously ethical issue in that it involves paying death benefits to those who were dependant on the deceased member and can have a significant impact on vulnerable beneficiaries. Ethical issues also arise in the communication

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20 ibid.
with potential beneficiaries, particularly where relationships are adversarial or where potential beneficiaries are unaware of each other’s existence.

6.2 Develop the Solution: Gather Information

The facts of a certain case were that a male member of a specific retirement fund passed away in July 2011 with a gross death benefit of R867 507–32. The deceased had a spouse, MV, who had a child of her own from a previous relationship, PM. PM lived with the deceased and MV and was a grade 10 learner when the deceased passed away. No information was provided as to the whereabouts of PM’s father. MV was employed but no information was available as to her earnings. The deceased had three children from a previous relationship: KN, K and KC, aged 31, 28 and 26 respectively at the time of the death. There was no completed beneficiary nomination form on file. KN and K were working and withdrew their claims for support. KC was due to complete a degree in mining engineering at the end of 2013. KC was receiving a monthly allowance of R2 500 in July 2011. These facts represented all the information that the trustees had at their disposal when making the death benefit distribution.

6.3 Understand the Environment: Consult Legislation, Regulation and Guidance

6.3.1 The relevant portions of Section 37C of the Pension Funds Act, reads as follows:

1) … 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 sections 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 fund, to one of such dependants or in proportions to some of or all such dependants …

6.3.2 The Promotion of Access to Information Act22 (PAIA) applies and should be considered in light of the Protection of Personal Information Act23 (POPI). Section 63 of PAIA suggests that trustees must refuse a request for access to information if that “would involve the unreasonable disclosure of personal information about … [the] deceased individual”. POPI will allow trustees to collect, record, collate, use and disseminate information if it is required by law or if doing so occurs in the proper performance of legal duties.

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22 Act 2 of 2000, Republic of South Africa, as amended
23 Act 4 of 2013, Republic of South Africa, as amended
6.4 Develop the Solution: Evaluate Possible Options

6.4.1 The first major decision is whether all the benefit should go to one of KC, PM or MV or if it should be shared. There are four options here. Should the benefit be shared, there are infinitely many options.

6.4.2 The first test is whether the option complies with the law or regulation. The facts here are not entirely clear. If MV out-earned the deceased by some margin, it is possible that she was not factually dependant on him. MV has a legal obligation to support PM as does PM’s father. Even though PM was living in the same household as the deceased, there may well be circumstances where PM is not factually dependant on the deceased. KC was clearly factually dependant on the deceased. This means that any solution must include KC as a dependant.

6.4.3 The second test is to consider the purpose of the fund which is to provide a benefit on death. Section 37C informs our understanding that this is primarily to support those who are dependent on the deceased.

6.4.4 The third test is to consider what would be just. Given the emphasis that Section 37C places on supporting dependents, a just distribution would favour those who cannot support themselves or have no other source of support. A quantification of the support lost by various dependents may thus inform a just distribution and the actuary may assist in this regard. The extent of the needs of PM, MV and KC are difficult to ascertain without further factual information.

6.4.5 The fourth test considers the obligations placed on the trustee in terms of their relationship with various stakeholders. A key stakeholder is the state, which would otherwise have to provide for dependents who have no alternative sources of support. In addition, they have a duty to establish the level of need among the various beneficiaries and hence to communicate with the potential beneficiaries. Trustees will need to consider PAIA and POPI requirements in this regard. This means communicating about the various beneficiaries only to parties with a genuine need to know. This is a test of both with whom the trustees communicate and what is communicated. For example, a widow would need to know about her deceased’s husband’s child born to a girlfriend as well as that child’s age as the child will reduce her allocation and any allocation to her children. The widow would not, however, need to know of the identity of the child, their sex or where he or she lives.

6.4.6 The fifth test is whether the decision-makers encompass the right virtues. For trustees, this implies diligence, impartiality, objectivity and prudence. For actuaries, additional requirements are integrity, confidentiality, scepticism, courage, reflection and a commitment to the public interest. In order to test any decision against these virtues, it would be essential to garner more factual information as otherwise the test for diligence is not met. However, the virtue of diligence needs to be balanced with the public interest. Further investigations take time and beneficiaries often require money shortly after the death of a breadwinner. Hence exhaustive, expensive searches may also be unethical.
6.5 Develop the Solution: Make a Decision

Ultimately, the trustees awarded 7% of the benefit to KC, 13% of the benefit to PM and 80% to MV. The trustees were unable to justify this decision and later when the case was taken to the PFA, the PFA found that they had not sourced sufficient factual information to make any decision either before making their initial allocation or before the matter was brought before the PFA. The ultimate allocation of the death benefits is not a matter of public record.

6.6 Monitor the Solution: Future Decision-Making

In this case, the framework leads us to conclude that the most ethical decision would have been to defer making the decision until enough information was at hand. This means that the trustees will need to consider the level of diligence applied in death benefit determinations in future. Given the time limit on death benefits distributions, this may mean that investigations will need to commence earlier and trustees may need to consider the time frames for the processes followed in order to complete all necessary investigations in time.

6.7 Concluding Remarks

This case study emphasises that sometimes halting the decision-making process to gather more information is the most ethical approach.

7. CASE STUDY 3: DEFAULT ANNUITISATION STRATEGIES

Members of retirement funds face the risk of outliving their income (Albrecht & Maurer, 2002). This longevity risk coupled with inadequate advice has prompted National Treasury to propose that trustees of retirement funds should choose a retirement income product that members will be defaulted into on retirement.24 Given the technical issues involved, it is highly likely that actuarial input may be requested by trustees.

7.1 Specify the Problem: Recognise the Ethical Issue

For an individual, the choice of a retirement income product brings with it a number of risks including longevity risk (Albrecht & Maurer, op. cit.) and being unable to support a desired level of spending either through having inadequate funds or through inflation risk (Emms, 2010). Other risks include experiencing a consumption shock that the product is not flexible enough to finance and the risk of counter-party failure. In choosing a default, trustees will be determining the risk taken on by the members and hence must act in a fiduciary capacity. Given the extent to which this influences the rights of members, it is intuitive that the principles of justice must apply in the decision-making process. This underscores the fact that this is an ethical issue.

24 National Treasury, Enabling a better retirement income, Technical Discussion Paper B for public comment, September 2012
7.2 Develop the Solution: Gather Information

7.2.1 The proposals are set out in the National Treasury discussion paper on enabling a better retirement income.25 The current proposal is that retirement lump sums of less than R150 000 will not be subject to annuitisation. For larger retirement benefits, up to one-third may be taken in cash with the remainder annuitised. Retirement benefits of less than R1,5 million must be used to purchase either the default product chosen by the trustees or another qualifying product chosen by the member. The latter is referred to as the ‘opt-out’ option. National Treasury suggested three possible options for annuitisation, namely a conventional life annuity, a retirement income trust (RIT) and a variable annuity. Any retirement benefits in excess of this ceiling may be invested in any product of the member’s choice including products that do not provide longevity protection, such as income drawdown accounts. At the time the discussion paper was written, a retirement lump sum benefit of R1,5 million could buy a monthly income of between R5 000 and R7 500 per month increasing with inflation.

7.2.2 The conventional life annuity option would involve the fund obtaining quotes from a number of different providers for a life annuity with a 5-year guarantee period, with a fixed increase 50% of CPI or 3% and a two-thirds spouse’s reversion for married members. The member would then select a quote or use any other approved annuity vehicle. If the member does not choose then the trustees can select the best annuity for them.

7.2.3 The RIT is a new type of vehicle that National Treasury hopes to introduce as part of the reforms. The product looks like an income-drawdown account in its initial phase with members having to drawdown the account between a minimum and maximum drawdown rate. If a member’s balance drops below a threshold level, referenced against the amount required to buy a certain level of income in the conventional annuity market, then the balance is used to buy a conventional life annuity immediately. Otherwise, the account is used to gradually purchase a series of conventional life annuities for the member.

7.2.4 A variable annuity is a type of with-profit annuity where the mortality and investment profits are shared between the member and the insurer. The income paid to the annuitant is adjusted upwards and possibly downward to reflect these profits arising. These annuities may or may not have a death benefit attached and the key differentiating feature is the extent to which members share in the profits and losses.

7.3 Understand the Environment: Consult Legislation, Regulation and Guidance

There is currently no regulation or legislation in this regard. However, the National Treasury discussion paper sets out the rationale for the default being in place. The key concerns are that assets are depleted too quickly and costs are too high and difficult to compare.

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25 National Treasury, September 2012, supra
7.4 Develop the Solution: Evaluate Possible Options

7.4.1 The first test is whether the option complies with the law or regulation. All three default options pass this test as they were recommended by National Treasury.

7.4.2 The second test is to consider the purpose of the fund which is to provide a benefit on retirement. The discussion paper emphasises the importance of an income benefit in retirement that can provide a benefit throughout retirement. For the conventional annuity option, the spouse’s reversion and guarantee provide for a death-in-retirement benefit that might not be consistent with the aim of providing retirement income benefits. However, death-in-retirement benefits are usually considered fair as they create consistency between members who die just before or just after retirement. The 50% match to inflation means that over time the pension loses purchasing power which reduces the extent to which the retirement benefit will meet the needs of the member. For the RIT, longevity protection is provided by the mechanism that switches the member to a conventional annuity once the fund drops below a certain level. This may avoid the member running out of funds completely, but will lock in large losses which may result in a lower income in retirement than what is required to meet the needs of the member. If a member experiences a market crash early in their retirement, their retirement income may be permanently negatively affected. This can be avoided to a certain degree if the RIT investments are matched to those matching the target annuity. However, this cannot be guaranteed as the member may be able to select their investment strategy. The long-term suitability of this option will also be determined by the choice of the target annuity. For the variable annuity, the suitability of the product to provide a retirement benefit depends on the degree to which members share the profits and losses, the pricing basis and the ongoing management of the product. A level of guarantee to the income level may provide some sort of security but this allows for less competition between providers than the other options.

7.4.3 The third test is to consider what would be just, in other words what would be fair and meet the needs of the individual as well as balancing competing rights and needs of various groups members and other stakeholders. Although there is a death-in-retirement benefit inherent in the conventional life annuity product, it involves a cross-subsidy from those with heavier mortality to those with lighter mortality within the same rating category. Thus, unless, relatively fine rating factors are used to ensure that lives in the same pricing category are relatively homogeneous, there may be cross-subsidies that can be considered inherently unfair. A further issue is the fact that the annuity is purchased at the retirement date when annuities may be relatively expensive or cheap. If the fund’s investment strategy is not matched to the target annuity, this can result in otherwise identical members having very different income levels in retirement. A low match to inflation is more suitable for lives with heavier mortality than those with light mortality who would experience a greater devaluation of their real income over their lifetime. This too may be regarded as unfair. The spouse’s reversion may result in over insurance in households where both spouses work and thus not meet the needs of certain classes of members. The RIT option reduces the level of cross-
subsidy between members as there is initially no risk pooling. In addition, because the purchase of annuity would be phased, members’ exposure to volatility in the annuity market is much reduced. A third benefit is that it allows for greater income flexibility which would allow retirees to adjust to a consumption shock. It does however allow for investment in more risky assets which exposes members to the risk that experience is adverse and a lower income level can be purchased. This option would only be fair if all members understood the potential upside and downside investment risk that they are taking on at inception. The variable annuity allows members to share in profits or losses. However, the extent to which this is fair depends on how rapidly these profits and losses are shared and if there are inter-generational subsidies. In addition, it may be difficult for trustees to justify why a particular level of profit participation is chosen given that different groups of members may have different risk tolerance.

7.4.4 The fourth test considers the relationship between the trustees and beneficiaries. The duty of care means that trustees would need to source the conventional annuity quotes from reputable insurers and present all necessary information to the member in a form that they can understand. This is not limited to the quote information but also the rationale behind the panel. Unless trustees can assist members to interpret this information then it is unlikely that this option can pass this test. For the RIT option, the duty of care would involve selection of an appropriate RIT vehicle and disclosure of all information regarding the RIT and associated risks. It would also mean assessing the ongoing communication provided by the RIT to ensure that the RIT continues to provide adequate disclosure to members. The selection of an appropriate RIT vehicle will lead to further ethical considerations. The variable annuity leaves members exposed to risks inherent in the ongoing management of the variable annuity product. This means that trustees need to be satisfied that the variable annuity will be governed in a responsible manner by a reputable service provider.

7.4.5 The fifth test refers to virtues and is set out in ¶4.4.6. For the conventional life annuity, this means that the panel of insurers needs to be appropriately selected. Given the concerns about whether annuity pricing accurately reflects the heterogeneity in mortality, it may be necessary to have a different panel for impaired lives or lives where the mortality is expected to be heavier. If the member cannot make a decision, the trustees must make one on their behalf in which case the trustees need to demonstrate fair and objective decision-making, possibly by giving clear reasons why one service provider was preferred to another. For the RIT option and variable annuity options, the trustees would need to demonstrate similar diligence.

7.5 Develop the Solution: Make a Decision

7.5.1 The trustees will have to determine the appropriate default option and justify the decisions relating to offering the option selected. As it stands, the framework suggests that none of the three options pass all the tests. If this is to become a regulatory requirement, trustees must select the most ethical of three imperfect solutions.
7.5.2 This decision will need to be communicated fully and clearly to members. The member may have more than one retirement fund at the time of their retirement and will need to consider the implications of decisions made by different trustee boards as well as what their options are should they choose to opt-out as discussed in §7.2.1. The actuary advising the trustees should ensure that risks of different options are adequately disclosed. The actuary should also be mindful of how any benefit illustrations may have affected members’ reasonable benefit obligations and ensure that such illustrations are consistent with the options available at retirement. As noted in §5.4.4 above, it can be argued that the provision of benefit illustrations is a key communication in ensuring that the members are aware of their likely retirement income and can make timeous additional provision if necessary.

7.5.3 Given that none of the three defaults are likely to fully satisfy all ethical tests, the most ethical option for trustees may be to encourage members to exercise their right to choose, irrespective of what option is selected as the default.

7.6 Monitor the Solution: Future Decision-Making

The trustees will need to monitor actual experience of members in the default options and how members would have fared under alternative options in order to review their default decision. The latter is difficult, and potentially expensive to monitor. The experience required for meaningful input into the decision-making process may take a number of years to emerge. The proportion of members opting out would also need to be monitored as this indicates the relative importance of the default. The opt-out options would also need to be monitored.

7.7 Concluding Remarks

This case study emphasises that a decision that is fully compliant with regulation may not in itself be ethical. The framework would suggest that the most ethical option is pursued. In this case, the framework suggests that the most ethical decision by the trustees may be to facilitate choice by the member.

8. SUMMARY AND CONCLUSION

8.1 The aim of this research paper was to explore how the somewhat abstract and broad concept of ethics can be applied in the day-to-day process of decision-making in South African retirement funds. It is important to differentiate between the role of actuaries as advisors to the trustees, and the role of the trustees who are the decision makers. However, actuaries are also decision-makers in the context of deciding the advice to provide given professional and ethical requirements. To address the aim of this research paper the authors considered the extent to which the discharge of duties placed on trustees and actuaries lead to ethical issues and the extent to which an ethical decision-making framework can assist trustees and actuaries in the process of decision-making.
8.2 Establishing whether the discharge of duties faced by trustees and actuaries lead to ethical issues requires an understanding of what is meant by the term ‘ethics’. Various ethical theories were considered. The theory of right action holds that an individual action can be assessed as right or wrong. The theory of justice can aid in making this distinction. Consequentialist theories of right action assess the outcome of an action. Deontology examines the rules and process behind the action. Virtue ethics considers primarily the motivation for any action with the process being a secondary consideration. The ethics of care, in contrast, focuses on the relationships between the stakeholders and how their needs are met. The authors acknowledge that their exploration of ethical theory has been brief and a thorough analysis of ethics for actuarial application is left for future research.

8.3 The legal, regulatory and professional duties of trustees, and the actuaries who advise them, were then mapped to these ethical theories. Trustees need to use the purpose of the fund to guide their thinking of what is just. The virtue of justice needs to guide their decision-making. The relationship between the trustee and fund beneficiaries should also be scrutinised in terms of rights, duties and obligations. Ultimately, trustees should develop the virtue of accountability in addition to the virtues of diligence, impartiality, objectivity and prudence. In addition to moral considerations, trustees are also required to comply with all relevant legislation and regulation. The current Actuaries’ Code encourages a deontological approach to the ethics in terms of compliance with legislation and professional guidance. However, various virtues are listed as professional requirements suggesting that actuarial actions can be assessed by virtue ethics where there are no rules to follow. The specific virtues listed are: integrity, objectivity, confidentiality, due care, independence, scepticism, accountability, courage, reflection and a commitment to the public interest, social responsibility, ethical business, whistle-blowing and ethical judgement. In addition, actuaries advising trustees need to consider the duties of the trustees.

8.4 A six-step ethical framework based on the actuarial control cycle for assessing decisions was developed. The first step is to recognise the discharge of every duty is an ethical issue and to consider specifically how it is an ethical issue. The second step is to gather all information relevant to the decision and confirm stakeholders affected by the decision. The third step is to consult regulation, legislation and guidance. The fourth step is to evaluate all options for the decision against five tests:

— Is it compliant with legislation, regulation and guidance?
— Does it reflect the purpose of the fund?
— Is it just?
— Does it reflect the level of care required in the relationship between the trustees and the stakeholders?
— Does the decision reflect that the decision-makers possess the correct virtues?
In the fifth step, a decision is made and communicated. In the sixth step, the decision is monitored.

8.5 The case studies illustrate that although the framework does not provide ethical solutions in their own right it assists trustees and the actuaries that advise them with the process of making an ethical decision. It is this process of decision-making that reveals the ethical issues that arise. The proposed framework thus demonstrates that the somewhat abstract and broad concept of ethics can be applied by trustees in the day-to-day process of decision-making in South African retirement funds. For actuaries, the framework can assist in making recommendations regarding the decision-making process including diligence in gathering all information, obligations placed on the actuary in terms of their relationship with various stakeholders and promoting public interest and accountability in terms of accessible communication including the effects of risk. Such a framework can be helpful in demonstrating the value of preserving actuarial discretion against a backdrop of increasing regulation and in the context of complex stakeholder relationships.

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