KEY Notes

REVENUE LAWS AMENDMENT BILL, 2022
TAXATION LAWS AMENDMENT BILL, 2022
CONDUCT STANDARD 1 OF 2022

EDITION 10, AUGUST 2022

REVENUE LAWS AMENDMENT BILL, 2022

Following its position paper released last year entitled "Encouraging South Africans to save more for retirement", National Treasury released the draft Revenue Laws Amendment Bill, 2022, on 29 July 2022 for comment. This Bill, which will apply to all the types of retirement funds (namely pension funds, provident funds, preservation funds and retirement annuity funds) introduces what is referred to as the "two pot" system and will allow members partial access to their benefits as a cash payment whilst in employment with the quid pro quo of requiring preservation of part of their benefits to retirement.

It is proposed that, with effect 1 from March 2023 (although National Treasury acknowledge that this date may need to be pushed out), all defined contribution funds will be required to hold three pots which are defined in the Bill in respect of each member, namely:

Vested Pot:	The member's accumulated benefit in the retirement fund as at 1 March 2023 plus investment return thereon
Savings Pot:	At most, one-third of the member's retirement contributions after 1 March 2023 plus investment return thereon
Retirement Pot:	At least, two-thirds of the member's retirement contributions after 1 March 2023 plus investment return thereon

Retirement contributions, for the purposes of the Savings Pot and the Retirement Pot, are defined as:

Member contributions + Employer contributions – Risk benefit premiums – Administration expenses

The legislation effective 1 March 2021 aligning retirement benefits of pension and provident funds remains in place. Under this legislation, provident fund members are required to annuitise at least two-thirds of their benefits on retirement subject to the following protected rights (which are not subject to mandatory annuitisation):

Provident fund members under age 55 on 1 March 2021: Their accumulated benefits at 1 March 2021, plus investment return thereon, may be taken in cash on retirement.

Provident Fund members over age 55 on 1 March 2021: Their accumulated benefits at 1 March 2021 and their future contributions after 1 March 2021 to the same provident fund, plus investment return on both amounts, may be taken in cash on retirement.

If the amount that must be annuitised on retirement is less than R165 000, then the full amount may be taken in cash.

Tracking the various amounts in respect of these "annuitisation" provisions and protected rights will require administrators to split the Vested Pot into two further Pots, namely (our naming convention):

Vested Lump Sum Pot: The accumulated amount as at 1 March 2023 for current and former provident fund members which may be taken in cash on retirement

Vested Annuity Pot: The accumulated amount as at 1 March 2023 for current and former provident fund members which must be treated as a "pension benefit" on retirement, i.e. a maximum of one-third may be taken in cash and the balance must be used to purchase an annuity

Taking protected rights into account, the "two pot" system will actually be administered as four pots. The four pots that must be managed for each member are as follows:

Vested Lump Sum Pot	Vested Annuity Pot	Savings Pot	Retirement Pot
			
Accumulated benefit at 1 March 2023, plus investment return thereon, which may be taken in cash at retirement	*Accumulated benefit at 1 March 2023, plus investment return thereon, of which at least 2/3rds must be used to purchase an annuity at retirement*	*At most, 1/3rd of retirement contributions after 1 March 2023, plus investment return thereon*	*At least, 2/3rds of retirement contributions after 1 March 2023, plus investment return thereon*

When a benefit is paid to a member, each pot needs to be considered separately in terms of the conditions that apply to that pot and the taxation basis if the pot can be paid out. The conditions that can apply are as follows:

Cash	Preserve	Annuitise
		
Cash payment permitted	*Benefit must be preserved (i.e. cannot be paid out)*	*Benefit must be used to purchase an annuity*

CASH PAYMENT WHILST IN EMPLOYMENT

From 1 March 2023 members may, subject to various conditions, request payment of part of, or all of, the balance in their Savings Pot without leaving employment.

Vested Lump Sum Pot	Vested Annuity Pot	Savings Pot	Retirement Pot
			
Cannot be accessed	*Cannot be accessed*	*May be taken in cash* *Minimum R2 000* *Only one payment in a 12-month period* *Taxed as income*	*Cannot be accessed*

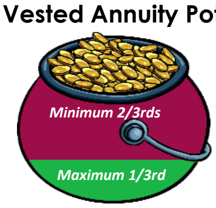
Example:

A member has a Savings Pot of R8 000 on 15 October 2023 and the member requests a payment of R5 000, leaving R3 000 in his/her Savings Pot.
If tax of, say, R1 000 and an administration fee of, say, R300, are deducted from the payment the member will only receive R3 700.
The Savings Pot will continue to grow with investment return and further contributions, but the member cannot receive another payment until 15 October 2024 at the earliest.

Resignation from Employment (including dismissal)

Vested Lump Sum Pot	**Vested Annuity Pot**	**Savings Pot**	**Retirement Pot**
			
May be taken in cash	*May be taken in cash*	*May be taken in cash*	*Must be preserved in current fund or transferred to another fund*
Combined vested benefit taken in cash taxed per withdrawal scale	*Combined vested benefit taken in cash taxed per withdrawal scale*	*Taxed as income*	*No tax on preservation or transfer*

Retirement from Employment (including ill-health/disability retirement)

Vested Lump Sum Pot	**Vested Annuity Pot**	**Savings Pot**	**Retirement Pot**
			
May be taken in cash	*Maximum 1/3rd in cash*	*May be taken in cash*	*Cannot be taken in cash*
	Minimum 2/3rds to purchase an annuity (subject to a de minimis limit of R165 000)		*Must be used to purchase an annuity (subject to a de minimis limit of R165 000)*
Combined cash benefit taxed per retirement lump sum benefit scale	*Combined cash benefit taxed per retirement lump sum benefit scale and combined annuity taxed as income*	*Combined cash benefit taxed per retirement lump sum benefit scale*	*Combined annuity taxed as income*

Death

On death, the member's full benefit is paid in terms of Section 37C and taxed per the lump sum benefit scale.

Transfer to Other Funds

Where any amount is transferred to another fund in terms of Section 14 or on resignation from employment, the amount in each Pot must be transferred to a matching Pot in the new fund.

Other Issues

Other important issues incorporated in the Bill are:

- Members are permitted to transfer their Vested Pot (both the Lump Sum and Annuity portions) and their Savings Pot into their Retirement Pot. They cannot transfer any amount out of their Retirement Pot.

- Divorce orders must be paid pro rata from all the Pots.
- A special provision relates to provident fund members who were over age 55 on 1 March 2021. They appear to be able to either:
    - Continue their contributions to their Vested Lump Sum Pot, in which case they will not have a Savings Pot and will not be able to take a cash payment whilst in employment; or
    - Contribute, as for other members, to a Savings Pot and a Retirement Pot, with permissible cash payments from the Savings Pot whilst in employment, but their Retirement Pot (if greater than the *de minimis* limit of R165 000) will have to be annuitised on retirement.
- The two-pot system will also apply to defined benefit funds, but it is not clear how cash withdrawals will affect future defined benefit payments.

Further clarity is required on a number issues, including the treatment of:

- Surplus allocations to members after 1 March 2023.
- Section 37D deductions other than divorce payments.
- Any restrictions on which Pots that can back housing loans.

COMMENT

Retirement fund administrators will have to amend their administration systems and, in all likelihood, employ additional staff to process cash payments to members. The volume of possible cash payments may, in any event, result in delays, not only for cash payments to members who are in employment but also those members who exit service and become entitled to a benefit payment.

The Bill does not mention or limit administration fees in respect of cash payments whilst in employment, but it is likely that administrators will charge a fee to make such payments. The fee could form a large proportion of the payment, especially if a member requests a small amount (subject to the prescribed minimum of R2 000).

It may be some time before retirement funds can make cash payments as:

- The implementation date of the Bill may be delayed.
- There are likely to be changes required to the Pension Funds Act and these have not yet been drafted and circulated for comment.
- Retirement Funds will need to amend their rules appropriately.
- National Treasury have backtracked on their previous proposal to allow members to take a small portion of their existing benefits in cash. Members will, therefore, need to accumulate sufficient assets in their Savings Pot after the implementation date before they can request a cash withdrawal.

It is expected that the impact of the measures in the Bill allowing access to a portion of retirement benefits whilst in employment and requiring preservation of a portion of benefits throughout a member's working career, will achieve the objectives of:

- Alleviating financial hardship and distress in the case of emergencies, particularly for low-income earners and vulnerable employees, with no savings or access to finance outside of their retirement fund; and
- Enforcing preservation of a portion of member benefits which should, over the long-term, result in better retirement outcomes for all members.

Important note: The Bill is a draft issued for comment and further changes may be made in the Revenue Laws Amendment Act if, and when, it is actually passed by Parliament. Any comments must be submitted to National Treasury by 29 August 2022.

TAXATION LAWS AMENDMENT BILL, 2022

The draft Taxation Laws Amendment Bill, 2022 was also released for comment by National Treasury on 29 July 2022. This Bill will give effect to some of the proposals announced in the 2022 National Budget. The following changes are included in the Bill.

Tax-free transfers from a pension fund to a provident fund: The policy objective of the annuitisation requirements implemented on 1 March 2021 was to harmonise the provisions relating to pension and provident funds and to allow tax-free transfers between such funds. However, due to an error in the Income Tax Act, contributions made to pension funds before 1 March 2021 were taxable on transfer to a provident fund. The Income Tax Act will be amended retrospectively, effective 1 March 2021, to ensure that contributions made to a pension fund prior to 1 March 2021 can also be transferred from a pension fund to a provident fund on a tax-free basis.

Compulsory annuitisation and vested rights on transfer to a public sector fund: The 1 March 2021 vested rights of provident fund members are currently not carried over on transfer to a public sector fund. The definition of pension and provident funds in the Income Tax Act will be amended retrospectively, effective 1 March 2021, to ensure that these vested rights are protected when transferring to a public sector fund. Public sector provident funds will also be subject to the same annuitisation requirements as private sector provident funds.

Partial transfers from a retirement annuity fund: Members with multiple retirement annuity policies with a single retirement annuity fund can currently only transfer all their policies to another retirement annuity fund. The Income Tax Act will be amended effective 1 March 2023 to allow such members to treat their policies separately, subject to the restrictions that the value of each policy transferred must be greater than twice the current *de minimis* amount, i.e. R495 000, and that the total value of the policies remaining in the original fund must also be greater than R495 000 if all the policies are not transferred.

Early retirement of provident fund members for reasons other than ill-health: There is currently an inconsistency in that any amount commuted by such members who elect to retire before age 55 is taxed in accordance with the withdrawal benefit scales, whereas similar commutations for retirees from pension funds are taxed in accordance with the more generous retirement benefit scales. The Income Tax Act will be amended effective 1 March 2023 to harmonise the treatment of cash lump sums on retirement for provident fund and pension fund retirees.

CONDUCT STANDARD 1 OF 2022

The Conduct Standard on "Requirements related to the payment of pension fund contributions", which was first sent out for comment in May 2020, was at last published on 19 August 2022.

The Conduct Standard which will become mandatory for all retirement funds in six-months' time, i.e. from 19 February 2023, specifies:

- The minimum fund and member information that must be provided by the employer to the fund every month. The required information includes each member's contact details and must highlight any changes in the member's salary, contributions and personal information from the previous month.
- Onerous reporting requirements to the Board, affected members and the Authority if the contributions are not paid timeously or if the contributions do not reconcile to the contribution schedule.
- Material contraventions that persist for more than 90 days must be reported to the South African Police Service.
- Late payment interest must be charged on late contributions at a prescribed rate of prime plus 2%.
- Various requirements where the trustee board outsources the recovery of arrear contributions to an attorney.

If you have any questions or would like more information on how the above may affect your retirement fund, please contact your Keystone consultant directly.

Keystone Actuarial Solutions is an actuarial consultancy based in Johannesburg, South Africa. We specialise in providing high quality, genuinely independent advice and services to the Boards of retirement funds and to the sponsors of such funds. Our consulting actuaries share a common vision that independent, focussed consulting advice, provided by an experienced team, will result in better outcomes for retirement fund members and pensioners.

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Please note: