KEY Notes

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NATIONAL BUDGET 2021

Finance Minister Mboweni delivered the National Budget to Parliament on 24 February 2021 with a focus on cutting government spending rather than increasing revenue collection. This is a welcome move in fiscal consolidation for an economy that is already overburdened and overindebted.

> "Hope is being able to see that there is light despite all of the darkness."
>
> Finance Minister Mboweni, quoting Archbishop Desmond Tutu

Minister Mboweni is making a habit out of delivering national budgets that surprise on the positive side. Whilst most commentators expected tax increases (including a potential wealth tax) in order for Government to attempt to plug the ever-increasing budget deficit (with large collection shortfalls, exacerbated by the impact of Covid-19), the Minister announced the following:

- Personal income tax relief through adjustments to the personal tax brackets and rebates by approximately 5% across the board – these adjustments are in excess of current inflation;
- Increasing the medical aid tax credits;
- A reduction in the corporate tax rate from 28% to 27% for companies for years of assessment commencing 1 April 2022; and
- An intention to reduce the issuance of bonds to finance spending.

There were of course the usual increases in the fuel levy and "sin tax" increases in alcohol and tobacco excise duties.

The intention behind these measures is to support economic growth, which has been declining steadily.

The key focus of the budget was on the reduction of structurally high spending. This will be achieved by reeling in the spending on the public sector wage bill, with the negotiations soon to get underway on the next three-year wage deal – that against the backdrop of the looming court case against government terms of the previous agreement.

We will be watching this space along with all South Africans, affected public servants and international ratings agencies to see whether government has the political will to follow through with these proposals.

The budget was again "light" on pensions-related issues – we have highlighted a few of these below.

RETIREMENT FUND REFORM

There had been no firm progress on the harmonisation of retirement funds for a number of years. This changed over the last year, with agreement being reached by all NEDLAC constituencies on the issue of Provident Fund annuitisation at retirement. The changes required to the Income Tax Act to implement the above were signed into law on 20 January 2021 and will come into effect from 1 March 2021. These changes align the tax treatment of contributions and the benefit structure of Pension and Provident Funds, subject to certain grandfathering provisions.

The requirement to increase the coverage of workers currently excluded from the social security system will see renewed focus in the current year. Specifically, Minister Mboweni referred to the accelerated introduction of auto-enrolment and the establishment of a fund to cater for such workers. This is a continued move towards the long awaited National Social Security Fund.

In addition to the above, there continues to be engagement between NEDLAC and National Treasury around providing access to retirement benefits in the face of crises faced by fund members (whilst these members remain in employment). As we understand it, any concessions in this regard may be tied to enforced preservation on withdrawal. There are a number of very complex issues and risks to navigate in this space and it is, therefore, unlikely that meaningful progress will be made in the short-term.

AMENDMENTS TO REGULATION 28

There was no mention of "prescribed assets" (which may be viewed as a positive signal to the markets that this is not high on the legislative agenda). It would appear that, with the proposed changes to the Regulation 28 (described below), government is encouraging retirement funds to opt for investment into much-needed infrastructure projects, rather than compelling them to do so.

National Treasury has published draft amendments to Regulation 28 of the Pension Funds Act for public comment. The intention is that the proposed amendments will make it easier for retirement funds to increase investment in infrastructure. Specifically, we understand that infrastructure investments already permitted through various asset classes will be de-linked from hedge funds, private equity funds and "other assets". De-linking this asset category will make private equity a separate asset class with a higher investment limit.

CLARIFYING DEDUCTIONS IN RESPECT OF CONTRIBUTIONS TO RETIREMENT FUNDS

From 1 March 2016, all employer contributions to a retirement fund on behalf of employees were considered taxable fringe benefits for the employees (for which there was an offsetting tax-deductible amount, subject to legislated limits). If the contribution contains a defined benefit component, the fringe benefit is to be calculated based on a contribution certificate issued by the fund (rather than using the actual contribution paid).

Whilst most funds are defined contribution in nature and these provisions will not apply to them, there are some defined contribution funds that self-insure their death benefits (and possibly lump sum disability benefits). Such self-insured risk benefits resulted in an anomaly which caused the whole defined contribution component to be considered defined benefit in nature.

It is expected that we will see changes to the Income Tax Act that will result in self-insured risk benefits being classified as defined contribution components. This implies that defined contribution funds that self-insure their benefits will be classified as defined contribution fund (and not defined benefit funds).

Other Future Potential Amendments

Other legislative and tax changes that will be considered in the short- to medium-term include:

- Clarifying the tax treatment of retirement benefits for individuals who cease to be a South African tax resident (to ensure that South Africa, and not the individual's new tax residency, receives the appropriate tax on benefits).
- Clarifying the tax treatment of the transfer of an over 55-year-old member who has opted to retire into another retirement fund. Our understanding is this was intended to be a non-taxable transfer, but may require amendments to the Income Tax Act to ensure that intention is realised.
- Increasing the de minimis amount for withdrawals from a "paid-up" retirement annuity benefit from R7 000 to R15 000.
- Increasing the flexibility of members on retirement around the selection of various annuities. It is our understanding that the intention is to allow a retiring member to select a combination of an in-fund annuity and an annuity purchased from an external insurer or annuity provider (which is currently prohibited under GN18) – this would certainly be a welcome change. The wording of the budget review is, however, not entirely clear in this regard and we will have to wait for draft legislation or further details for clarity.

Social Grants

The number of South Africans in receipt of a social grant is expected to increase to 19 million by the 2022 / 2023 financial year. Increases (primarily below current inflation) of between 1.6% and 3.4% have been applied to the various grants for the 2021 / 2022 financial year – details are provided below:

Nature of grant	Average 2021 / 2022 (monthly)	Average 2020 / 2021 (monthly)	% increase
State old age grant (under age 75)	R1 890	R1 860	1.6%
State old age grant (over age 75)	R1 910	R1 880	1.6%
Child support grant	R460	R445	3.4%
Disability grant	R1 890	R1 860	1.6%
Foster care grant	R1 050	R1 040	1.0%

Taxation of Retirement Benefits

There have, again, been **no changes** to the tax rates applicable to lump sum payments from retirement funds on withdrawal, death, retirement or retrenchment. These rates remain as follows:

Death, Retirement or Retrenchment

Value of lump sum	Rate of tax
R0 to R500 000	0%
R500 001 to R700 000	18% of the amount above R500 000
R700 001 to R1 050 000	R36 000 plus 27% of the amount above R700 000
R1 050 001 and above	R130 500 plus 36% of the amount above R1 050 000

Withdrawal (Resignation or Dismissal)

Value of lump sum	Rate of tax
R0 to R25 000	0%
R25 001 to R660 000	18% of the amount above R25 000
R660 001 to R990 000	R114 300 plus 27% of the amount above R660 000
R990 001 and above	R203 400 plus 36% of the amount above R990 000

Tax on a specific retirement or withdrawal lump sum benefit is equal to:

- the tax determined by the application of the tax table to the aggregate ***retirement lump sum benefit*** or ***withdrawal lump sum benefit*** and all *previous lump sum benefits* *(Note)*; less
- the tax determined by the application of the tax table to the aggregate of all *previous lump sum benefits*.

Note: Previous lump sum benefits include:

- all retirement fund lump sum retirement benefits accruing from October 2007;
- all retirement fund lump sum withdrawal benefits accruing from March 2009; and
- all other severance benefits accruing from March 2011.

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.

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