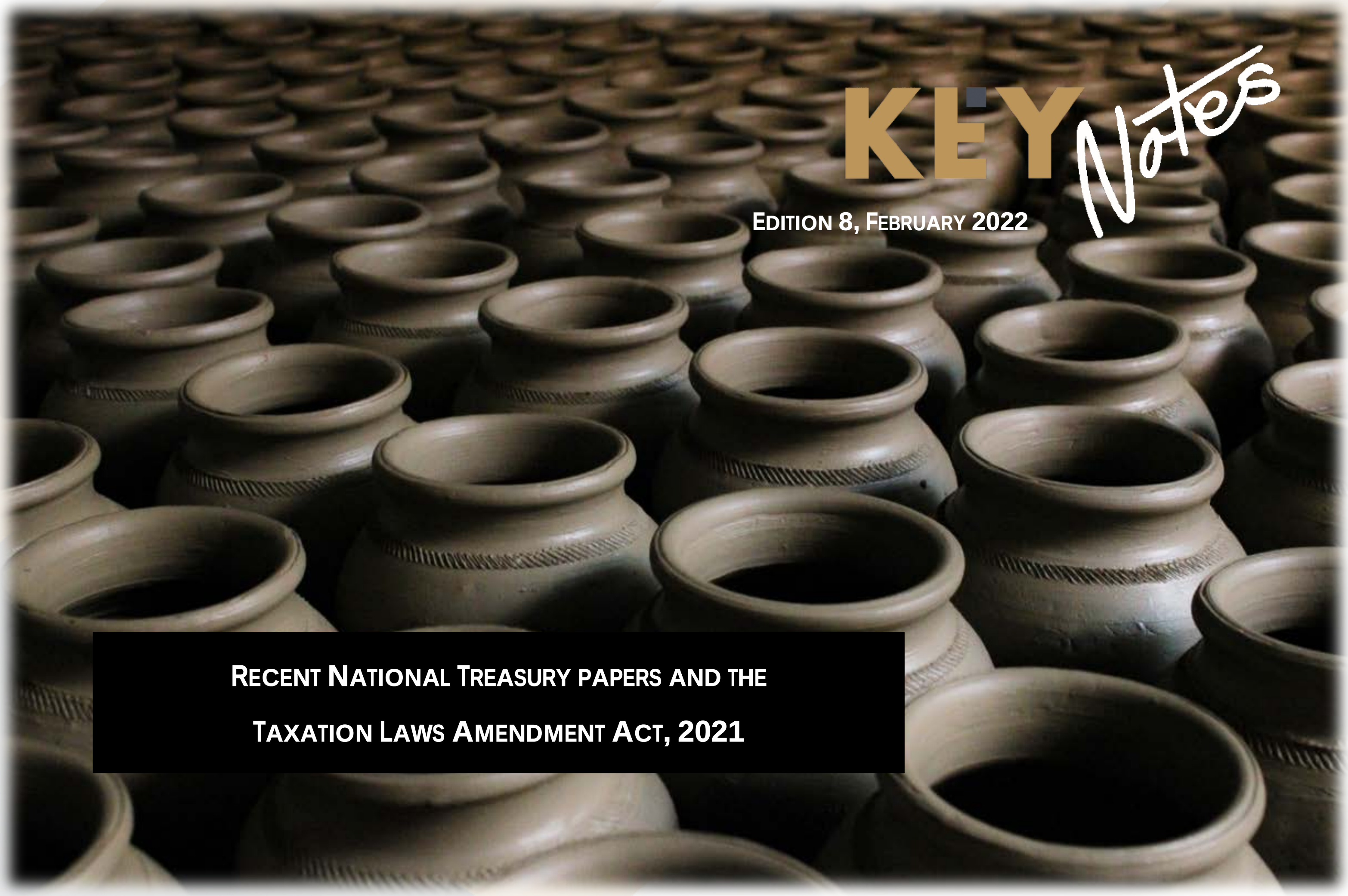

KEYNotes

Edition 8, February 2022

Recent National Treasury papers and the Taxation Laws Amendment Act, 2021

ENCOURAGING SOUTH AFRICANS TO SAVE MORE FOR RETIREMENT

Further to its media release on the issue last year, National Treasury released a position paper on allowing members partial access to benefits (cash withdrawal) whilst in employment with the quid pro quo of requiring partial preservation of future contributions.

The paper proposes that all members will be permitted to access one-third of their retirement funding contributions after the implementation dated (mooted to be 1 March 2023) plus investment return thereon and possibly 10% of their accumulated benefits as at the implementation date, with the latter withdrawal subject to a maximum of R25 000.

The amount accessed will be paid in cash, subject to a minimum amount of R2 000 and members will be permitted to make one, or possibly two withdrawals, in each 12-month period. Funds will be permitted to deduct an administration fee from the member's benefit to cover the administration of the payment. Any amount that is not withdrawn may be taken in cash on retirement.

The balance of two-thirds of the members contributions after the implementation date and investment return thereon must be preserved until retirement, i.e. the member cannot take this amount in cash on subsequent resignation. This amount must be used to purchase an annuity on eventual retirement.

The paper proposes that retirement funding contributions after the implementation date are split between two different pots, essentially an "access pot" (one-third) and a "preservation pot" (two-thirds). There will also be a pot of the member's accrued benefit at the implementation date, possibly split further in respect of any vested provident fund rights (to take cash on retirement) in terms of the legislation that was effective 1 March 2021 and the balance of the benefit (of which a maximum of one-third may be taken in cash and a minimum of two-thirds must be used to purchase an annuity).

The various pots, as proposed in the paper, can be summarised as follows:

	Accrued benefits including investment return	Access pot including investment return	Preservation pot including investment return
Cash withdrawals in service	10% maximum R25 000	Yes (minimum R2 000)	No
Resignation	May be taken in cash	May be taken in cash	Must be preserved
Retirement	Per current position *	May be taken in cash	Must be annuitised

* *On retirement, any portion of the accrued benefits representing vested provident fund rights and one-third of the balance of the benefit (possibly after allowing for any portion withdrawn in cash prior to retirement) may be taken in cash and the balance must be used to purchase an annuity.*

The total amount that must be annuitised on retirement will be subject to the de minimis limit, which is currently set at R247 500 (before any amount commuted for cash) – this means that the "annuity portion" must be R165 000 or more. If the total "annuity portion" of the benefit is less than the limit, the full benefit may be taken in cash.

The paper postulates that the joint measures of allowing access to retirement benefits whilst in employment and requiring preservation of a portion of benefits throughout a member's working career will achieve the joint 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 the majority of employees.

The proposals, in their current form, will have material implications for retirement funds and their administrators as a material number of members could withdraw relatively small cash amounts every year. The administrators and SARS (if a tax directive must be obtained for each payment) may have to commit material additional resources to prevent backlogs.

There are a number of technical issues relating to the proposal, such as the basis of taxation of withdrawn amounts, the treatment of additional voluntary contributions, divorce benefits and other section 37D payments fees and cash withdrawals from defined benefit funds and the GEPF.

The paper also makes reference to and analyses a number of potential options for the auto-enrolment of workers into retirement schemes in the formal sector. There is, however, no concrete proposal or preferred structure at this stage and we expect that progress in this regard will be slow (as has been the case in respect of the National Social Security Fund).

National Treasury requested comment on the proposals by 31 January 2022. We expect the proposals to go ahead in some form, as there appears to be general acceptance of the principles by all parties at NEDLAC. Our understanding is that Labour is looking to implement sooner rather than later in order to provide financial relief to workers through access to their funds.

GOVERNANCE OF UMBRELLA FUNDS

National Treasury has also released a position paper on the governance of umbrella funds, primarily focussing on Type A commercial umbrella funds. Type A funds are multi-employer umbrella funds, usually established on a for-profit basis by a financial institution, where the members of each employer are managed in separate cells with their own benefit structures. Type B funds are multi-employer umbrella funds, usually established by a union, industry association, employer group or bargaining council, with the same benefits for all members in a single pool.

Whilst National Treasury supports the consolidation of small retirement funds into umbrella funds, its major concerns focus on good governance, transparency and costs. For example, the sponsors of commercial umbrella funds may exert undue influence on the trustees of the fund to utilise the services of the sponsor and that there may be hidden charges to the detriment of the members.

The paper covers approaches followed in the United Kingdom (with the establishment of Independent Governance Committees with oversight over the fund) and Chile (where an auction system is used to select the cheapest administrator) without actually making any firm proposals in respect of what they intend to implement in South Africa.

National Treasury requested comment on the issue by 31 January 2022 and will presumably then consider further legislation and conduct standards to improve the governance and transparency of umbrella funds and to reduce (or at least cap) the costs of such funds.

TAXATION LAWS AMENDMENT ACT, 2021

The Taxation Laws Amendment Act, 2021 was Gazetted on 19 January 2022, with the following changes to take effect on 1 March 2022.

Purchase of annuities on retirement: Previously when a member retired from a pension fund, a provident fund, a preservation fund or a retirement annuity fund, the member was permitted to purchase an annuity or combination of annuities inside or outside the fund, but could not purchase a combination which included both in-fund and external annuities. The withdrawal of GN18 in early 2021 and the issuance by SARS of a Binding General Ruling in November 2021 confirmed that such practice would be allowable in future.

The Income Tax Act now explicitly states that such combinations are permissible, but requires that if more than one annuity is purchased by a member on retirement from a fund, each annuity must have a capital value of more than R165 000.

Transfers between preservation funds: Transfers from pension preservation funds and provident preservation funds into other preservation funds are currently permitted, but are a taxable event for members over age 55. This unintended anomaly has been removed and the transfers will be tax-free for all members. Transfers from preservation funds to retirement annuity funds are also now permitted.

Contribution certificates in respect of self-insured risk benefits: Where a fund provides self-insured risk benefits, it has been clarified that these will be considered as a "defined contribution component" and the fund will not need to provide a contribution certificate to the employer in respect of the risk benefits.

Technical issues: Minor technical issues have been corrected in the Income Tax Act, which are not of major relevance or concern.

Deemed tax event on ceasing to be a South African tax resident: The Taxation Laws Amendment Bill, 2021, had a provision requiring retirements benefits to be taxed when a person ceased to be a tax resident, even if the benefit is left in a retirement fund, preservation fund or retirement annuity fund. Following representation by various parties, this provision was not brought through in the Act and may be considered again in future legislation.

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:

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