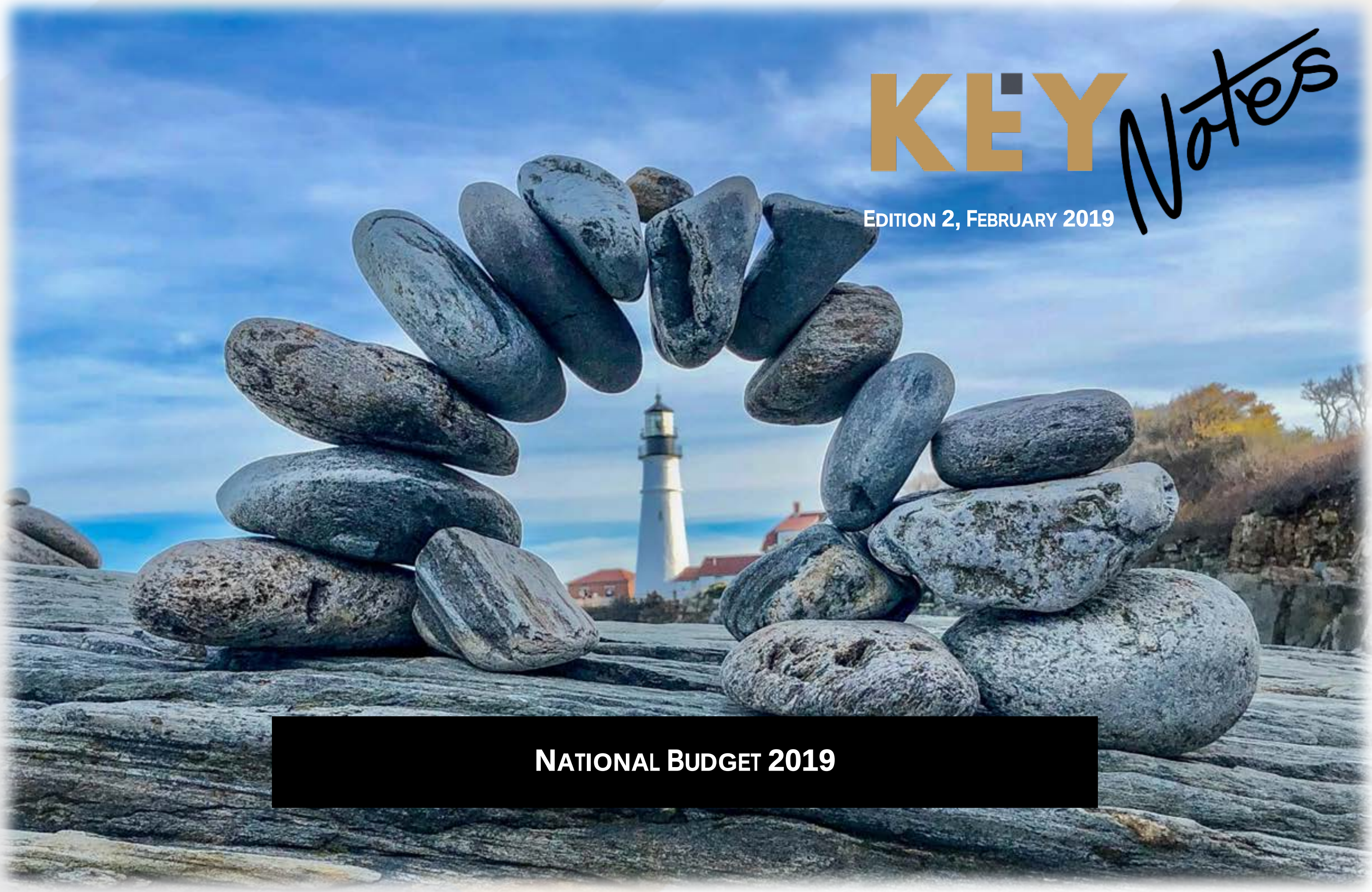

KEY Notes

Edition 2, February 2019

National Budget 2019

Finance Minister Mboweni delivered his first National Budget to Parliament on 20 February 2019. The Budget was built on six fundamental prescripts, namely

- Achieving a higher rate of economic growth;
- Increasing tax collection;
- Reasonable, affordable expenditure;
- Stabilising and reducing debt;
- Reconfiguring state-owned enterprises; and
- Managing the public sector wage bill.

It is clear that there are tough times ahead for many South Africans, while Government grapples with a number of competing imperatives, including reducing debt, creating employment, reigning in Government expenditure and fixing ailing State Owned Enterprises (*"SOE's"*).

> *"…the task ahead is great indeed, and heavy is the responsibility; and yet it is a noble and glorious challenge - a challenge which calls for the courage to dream, the courage to believe, the courage to dare, the courage to do, the courage to envision, the courage to fight, the courage to work, the courage to achieve - to achieve the highest excellencies and the fullest greatness of (people). Dare we ask for more in life?"*
>
> Finance Minister Mboweni, quoting Kwame Nkrumah

Minister Mboweni has sent a strong positive message to the market about Government's intentions regarding the management of SOE's into the future, together with recognition of the fact that the problems that exist will not be fixed quickly, nor without significant pain being experienced by the average South African.

The Budget was light on retirement fund related content, but we have provided some commentary herein on relevant issues as well as those which may be of wider interest.

> *"…in this coming year, we expect revenues of R1.58 trillion and spending of R1.83 trillion. That means we will spend R243 billion more than we earn. Put another way, we are borrowing about R1.2 billion a day, assuming that we don't borrow money on the weekend."*

The following proposals, of wider interest, were tabled:

- Although there is a slight increase in the threshold for personal income tax, the tax brackets have **not been adjusted at all**. This means that the average consumer achieving an inflationary salary increase this year will have lower *real* net take-home pay;
- No adjustment to medical tax credits in the next financial year;
- Additional VAT zero rated products, including white bread flour, cake flour and sanitary pads;
- Fuel taxes to increase by 29 cents per litre for petrol and 30 cents per litre for diesel (split between the fuel levy and RAF levy with effect from 3 April 2019 and a new carbon tax with effect from 5 June 2019); and
- As expected, "sin taxes" and the "health promotion levy" (or sugar tax) will also increase, with increases generally in excess of inflation.

PUBLIC SECTOR WAGE BILL AND WAIVING OF EARLY RETIREMENT PENALTIES

Government has recognised that the public sector wage bill is unsustainable. In order to attempt to address this issue without the need for retrenchments, Minister Mboweni has proposed offering voluntary early retirement packages, limiting overtime and bonus pay, limiting pay progression and reviewing the staffing of diplomatic missions. In a show of solidarity, members of Parliament and provincial legislatures and executives at public entities will not be receiving a salary increase this financial year.

It is proposed that the voluntary early retirement packages include retirement from the Government Employees Pension Fund ("*GEPF*") without the application of the standard early retirement penalty. Waiving of early retirement penalties in a defined benefit fund comes at a cost as pensions which accrue to members are expected to be paid for a longer period and the present value of such pensions is, therefore, higher than would have been the case if a member had retired at their normal retirement age. In terms of the GEP Law, any waiver of early retirement penalties will result in a funding obligation on the State. The expected cost of the intervention (assuming that 30 000 employees take up the offer) is R16 billion over the next 2 years. The Minister has proposed that part of this cost be funded from the contingency reserve and the balance be funded from the assets of the GEPF – the funding from the GEPF will be repaid by the State *"over a longer period"*.

TAXATION OF RETIREMENT BENEFITS

There have 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.

SOCIAL GRANTS

Social grants are expected to reach 17.9 million South Africans in the financial year ending 28 February 2020 at a cost of roughly 3.2% of GDP. Inflationary increases of between 4.2% and 5.0% have been applied to the various grants with effect from for the 2020 financial year – details are provided below:

Nature of grant	Average 2019 / 2020 (monthly)	Average 2018 / 2019 (monthly)	% increase
State old age grant (under age 75)	R1 780	R1 695	5.0%
State old age grant (over age 75)	R1 800	R1 715	5.0%
Child support grant	R425	R405	4.9%
Disability grant	R1 780	R1 695	5.0%
Foster care grant	R1 000	R960	4.2%

OTHER RETIREMENT RELATED PROPOSALS

A number of minor proposals were tabled for the next legislative cycle. These included:

- Once a member of a retirement fund retires and receives an annuity from the fund as a retirement benefit, any contributions to the retirement fund that did not qualify for a deduction when determining the member's taxable income are tax-exempt – this exemption does not currently apply to annuities payable from a provident or provident preservation fund. It is now proposed that this exemption be extended to fund members who receive annuities from these funds (for contributions made after 1 March 2016).
- Upon the death of a member, the surviving spouse may be entitled to receive a monthly spousal pension from the retirement fund. Issues may arise with the calculation of the spouse's tax liability if he or she also receives other income. In order to alleviate any potential cash flow burden for the surviving spouse at the time of assessment, it is proposed that the monthly spousal pension be subject to PAYE at a specified flat rate and that tax rebates should not be taken into account in the calculation of spousal pensions. Any PAYE excessively withheld as a result of this proposal will be refunded upon assessment.
- A proposed study on the tax treatment of amounts received by portfolios of collective investment schemes;
- It is proposed that Government consider the regulation and tax treatment of unlisted Real Estate Investment Trusts ("*REIT*") that are widely held by institutional investors, in line with the announcement in the 2013 budget review.

Conspicuous by their absence were any mention of:

- The harmonisation of annuitisation provisions between pension and provident funds; and
- Prescribed assets (which is a positive signal to the markets that this is not high on the legislative agenda).

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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