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THE RETIREMENT INDUSTRY NEWSLETTER

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Two-pot retirement system to launch in September

Despite industry players requesting an extension.

Government expects to raise an additional R5 billion in the 2024 tax year from taxpayers who make use of the once-off withdrawals from their retirement savings. In announcing 1 September 2024 as the implementation date of the two-pot retirement system, Finance Minister Enoch Godongwana has heeded calls from the public to hasten the process whereby people can access a portion of their retirement savings.The system was previously due to be implemented on 1 March this year, but this was pushed back following calls from National Treasury and the pension industry.

Industry players preferred – and requested – 1 March 2025 as the implementation date, given the complexity of making the necessary changes to their systems to be able to implement the new system as smoothly as possible.Jenny Klein, principal associate at ENSafrica, says there have been two competing objectives. People have a desperate need to access their retirement savings, in particular, because of the Covid-19 pandemic."On the other hand industry wanted to have sufficient time to implement these extensive changes," she says."It is important to get it done correctly to avoid chaos when millions of members want to withdraw, and the systems are not in place."

How it will work

Contributions to retirement funds will be split, with one third going into a 'savings pot' and two thirds going into a 'retirement pot'. Retirement fund members will be able to withdraw amounts from the savings pot prior to retirement, while the amount in the 'retirement component ' pot remains protected. National Treasury says in the 2024 Budget Review document that savings accumulated up to 1 September will not be affected, except for the initial 'seed capital' amount. This seed capital amount – the lower of 10% of the fund value on 31 August 2024 or R30 000 – will be transferred from the member's accumulated retirement savings to their 'savings' pot.

However, fund members will be able to immediately withdraw from the savings component if they have a financial emergency. Only one withdrawal may take place in a tax year, and the minimum withdrawal amount is R2 000. If, for example, a member's seed capital amount is R30 000, they could withdraw the full R30 000 immediately – but the pot will then be empty and no growth will be able to take place on that component of their retirement savings.The initial seeding will be a once-off event. “If not used, it will still be available in the future,” says Treasury. Thus, a retirement fund member could draw from their savings pot in five years’ time – at which point its value will have grown beyond the initial R30 000 seed capital amount.

Tax implications

Taxpayers are forewarned that pre-retirement withdrawals from the savings pot will be taxed at marginal rates, like all other income.

2024 tax year (1 March 2023 – 29 February 2024)

22 February 2023 – See changes from last year:

Taxable income (R)	Rates of tax (R)
1 – 237 100	18% of taxable income
237 101 – 370 500	42 678 + 26% of taxable income above 237 100
370 501 – 512 800	77 362 + 31% of taxable income above 370 500
512 801 – 673 000	121 475 + 36% of taxable income above 512 800
673 001 – 857 900	179 147 + 39% of taxable income above 673 000
857 901 – 1 817 000	251 258 + 41% of taxable income above 857 900
1 817 001 and above	644 489 + 45% of taxable income above 1 817 000

Source: Sars

Only one withdrawal may take place in a tax year, and the minimum withdrawal amount is R2 000. Amounts left in the savings component on retirement can be withdrawn and will be taxed according to the retirement lump sum table, which includes a tax-free lump sum of R550 000. Nicci van Vuuren, senior associate at Webber Wentzel, previously noted that pension funds still need to communicate all the changes to their members. Individuals need to understand what the changes mean for their retirement.

Treasury also cautioned against unnecessary withdrawals. “The optimal option is still to preserve retirement savings as long as possible, as the amounts grow at compound rates and can attract lower tax rates.” It is referred to as ‘seed capital’ because, once transferred, this amount will continue to grow in line with how the investments underpinning the retirement fund perform. If left untouched, the amount will grow at compound rates and the member will ultimately be better off.

Moneyweb | 21 February 2024

Alexforbes cautions against misinformation on two-port retirement system

Alexforbes has warned against misinformation on the two-pot retirement system.

In a statement, the group said as a prominent stakeholder in South Africa's retirement funding sector, Alexforbes had the responsibility of educating and empowering members to understand the intricacies of the two-pot retirement system, enabling individuals to make informed decisions regarding their savings. "This obligation extends beyond its client base to all South Africans to ensure that members have access to reliable information so that they may balance their retirement funding goals with short-term emergency needs.

"The timing of the two-pot retirement system and access to the savings pot can be emotional. It becomes more challenging when incorrect information spreads, creating wrong expectations among members. Alexforbes supports the implementation of the two-pot retirement system because of the positive impact it will have on the financial future of retirement fund members," it said. According to Alexforbes, it is important to focus on a few of the critical points that members must be aware of regarding the new system:

· The implementation date is 1 September 2024.
· From 1 September 2024, any amounts saved in a retirement fund will be split into a savings component and a retirement component.
· One-third (about 33% of retirement savings) automatically goes into the savings component.
· The initial amount in the savings component will be 10% of the amount saved in the vested component, up to a maximum of R30 000.
· The minimum withdrawal amount is R2 000.

"To ensure members have access to accurate information, it is crucial to verify the factual accuracy of the information they receive. Given the complexity of retirement funding, especially with the introduction of the two-pot retirement system, there is a heightened need for simplified and accurate information. "Having the right information empowers individuals to make informed decisions effectively and responsibly. “Acknowledging the evolving nature of the two-pot retirement system, regular updates are provided to retirement fund members by Alexforbes. To facilitate this, the most up-to-date information related to the two-pot retirement system is available on the Alexforbes My Money Matters platform," it said.

The company said accessing accurate information safeguards the financial well-being of members and enhances confidence in the retirement funding system. "Therefore, Alexforbes encourages all retirement fund members to seek accurate information from reliable sources, and obtain advice from an accredited adviser to understand the implications of their choices. By doing so, disillusionment and frustration among members can be prevented," it said.

Personal Finance | 01 February 2024

1 September 2024 Confirmed implementation date of the Two-pot system

The Draft Revenue Laws Second Amendment Bill (Second Amendment Bill) confirms 1 September 2024 as the implementation of the Two-pot system. This is among other significant changes to the Revenue Laws Amendment Bill (the RLAB) which are set to become effective on the same date. On 21 February 2024, the National Treasury released the Second Amendment Bill to make technical corrections to the RLAB. The Second Amendment Bill follows the proposal by Minister of Finance Enoch Godongwana, that Parliament extend the date of implementation for the two-pot system contained in the RLAB from 1 March 2024 to 1 September 2024 for various reasons supported by industry stakeholders.

Unpacking proposed changes in the Second Amendment Bill Some of the proposed changes in the Second Amendment Bill signify positive adjustments to the existing system. Firstly, the bill acknowledges and incorporates the new implementation date of 1 September 2024, providing clarity and alignment with the extended timeline advocated by stakeholders. Additionally, the bill eliminates the necessity for a tax directive when transferring the seeding amount from the vested to the savings components contemplated in the two-pot system. The proposed amendments to the definitions of the three components exclude maintenance awards. This adjustment ensures consistency with existing tax provisions regarding the tax treatment of maintenance awards under section 7(11) of the Income Tax Act 58 of 1962.

Furthermore, the bill addresses intra-fund transfers and associated tax directives by proposing that the reallocations of amounts between the three components are not treated as transfers for which tax directives are required. Consequently, the requirement to obtain a directive for reallocations between the three components has been withdrawn in the Second Amendment Bill. While these proposed changes are a step in the right direction to give effect to the two-pot system, the lead time provided still falls short of that which industry stakeholders advocate for to overcome the practical challenges associated with the new system, including how it will be implemented for defined benefit funds (DB funds). A major difference between defined contribution funds (DC funds) and DB funds is that in DC funds, it is possible to calculate the value of the contributions that the member has already made, but in DB funds, the final pension fund benefit will be based on the final salary of the member plus the number of years' service. The RLAB has provided for the one-third and two-thirds allocations to the savings and retirement components of DB funds to be determined regarding a member's pensionable service on or after 1 September 2024, or a reasonable method of allocation as approved by the Financial Sector Conduct Authority (FSCA). The implementation of the two-pot system for DB funds must be carefully undertaken to ensure fairness to all members of each DB fund.

Any necessary engagements with the FSCA by DB fund administrators will also require additional lead time from the promulgation date to the implementation date which the Second Amendment Bill does not provide. In a media statement published by the National Treasury, the Second Amendment Bill is aimed at clarifying the language in the RLAB and simplifying the directives system for both administrators and the South African Revenue Service (SARS), allowing for an efficient implementation of the two-pot system. The deadline for public comment on the Second Amendment Bill is 31 March 2024.Webber Wentzel's experienced **tax** and **pension** teams are available to provide legal advice to clients looking to submit comments on the Second Amendment Bill.

FA News | 27 February 2024

Pension-Backed Home Loans: A Strategic Approach to Home Financing Amid Economic Challenges

Before financing a home, Momentum Corporate Business Development Manager of Pension Backed Home Loans, Tebogo Mphafudi, urges South Africans to consider pension-backed home loans as an alternative.

The South African economy is buckling under the strain of loadshedding, interest rate hikes and a steady increase of personal debt to cover day to day living. While waiting for the Finance Minister, Enoch Godongwana to make his budget speech on 21 February 2024, businesses and individuals alike seem to be treading water to hear what the implications on their financial future will be. A property purchase should be the biggest investment most people will ever make but, so many South Africans struggle to get the loan they need to finance their dream home. There is often minimal knowledge that exists around the alternative options to the traditional bank loan.

A pension-backed home loan is a unique financial arrangement that allows you to use your retirement savings as security to access a loan for purposes relating to your home. This approach enables prospective homeowners to use up to 60% of their pension fund as collateral for the loan, providing a source of security for lenders. In addition to securing a loan to buy a house, a pension-backed home loan also allows you to renovate your existing home, buy land to build a home, or even pay off an existing home loan.

Using your future to fund your present

The loan is typically repaid over an agreed-upon period which is usually limited to your retirement age, with the understanding that the pension fund serves as a guarantee. This arrangement offers advantages such as potentially lower interest rates (when compared to other forms of unsecured lending), and increased accessibility to home financing for individuals who might face challenges in obtaining a traditional mortgage. A pension-backed home loan offers compelling advantages, including no requirement to register a bond and pay the applicable registration costs to access the financing as well as no property assessment fees.

The application process is notably swift and efficient, with the potential for preferential interest rates. Monthly repayments are seamlessly deducted from the borrower's salary, enhancing convenience. Furthermore, borrowers may qualify for an additional loan after a few months of timely payments, provided there are sufficient funds in their retirement savings account, and they meet the bank's lending requirements. That is an example of cleverly using your retirement savings to invest in an asset that will likely appreciate over time. A smart investment if you make all the right choices.

T’s and C’s always apply – make sure you are covered

When it comes to home financing in South Africa, the terms and conditions of a pension-backed home loan stand as the bedrock, shaping the dynamics of homeownership and resilience in the face of unforeseen challenges. These contractual nuances are not just legal formalities but are rather intricate guidelines that define the responsibilities and coverage afforded to both the lender and the homeowner. Specifically, when confronted with the aftermath of a natural disaster like what happened in KwaZulu-Natal, the clauses relating to natural disasters, insurance obligations, and loan repayment continuity become critical. It is imperative you fully understand the terms and conditions.

A careful examination of these terms is like fortifying the foundations of a home, providing a structured response mechanism during times of crisis. In essence, they are the guiding principles that ensure a pension-backed home loan not only facilitates homeownership but also serves as a resilient shelter in the face of unexpected adversity. In essence, a pension-backed home loan, when well-understood, doesn't just facilitate homeownership but becomes a fortified shelter in the face of unexpected challenges, ensuring financial security and peace of mind for the future. A future, mind you, that none of us can predict so we might as well be prepared.

FA News | 20 February 2024

Retirement replacement ratio – how much is enough?

This ratio can vary significantly depending on your lifestyle, expenses, and the income you're accustomed to while working. The replacement ratio at retirement refers to the percentage of your pre-retirement income that you will need to maintain your standard of living once you retire. It's a crucial concept in retirement planning, helping individuals understand how much money they should aim to have saved by the time they retire. This ratio can vary significantly depending on your lifestyle, expenses, and the income you're accustomed to while working.

Here are some key points about the replacement ratio:

Typical ratios: Financial planners often suggest a replacement ratio between 70% to 80% of your pre-retirement annual income. However, this can vary based on your circumstances, including your health, debts, and lifestyle choices.

Factors influencing the ratio: Several factors can affect your personal replacement ratio, such as:

Retirement age: The age at which you plan to retire can significantly impact your required savings. Early retirement means you need a higher replacement ratio due to a longer retirement period.

Expenses in retirement: Your lifestyle choices, including travel, hobbies, and living expenses, will influence the amount you need. Some costs may decrease (e.g., commuting expenses), while others may increase (e.g., healthcare).

Income sources: Other income sources in retirement, like social security benefits, pensions, rental income, or part-time work, can lower the replacement ratio needed from savings alone.

Calculating your ratio: To calculate your replacement ratio, you'll first need to estimate your annual retirement expenses. Then, divide this amount by your current annual pre-tax income to get your ratio. Adjustments should be made for expected changes in expenses and income sources in retirement.

Impact on savings goal: Understanding your replacement ratio helps in setting a realistic savings goal for retirement. It guides how much you should aim to accumulate in your retirement accounts, such as retirement annuities, pension funds, provident funds, tax-free savings accounts and other investments (local and offshore).

Adjustments over time: It's important to revisit your replacement ratio periodically, as changes in your lifestyle, economic environment, and personal circumstances can affect your retirement needs. Remember, the replacement ratio is a guideline, not a one-size-fits-all solution. Individual needs vary, and planning for retirement should be personalised to your unique situation. In conclusion, a secure retirement requires careful planning, professional advice, and an active role in managing your retirement funds. Before making any decisions, it's critical to consult with a certified financial planner. The financial landscape is complex and constantly evolving, making it essential to seek advice from those with the requisite knowledge and experience. Be wary of relying on commentary from individuals who may not possess the professional background necessary to provide sound financial advice. “The greatest risk in investing is your own behaviour,” said Warren Buffett.

Moneyweb | **20 February 2024**

Is an annuity worth it for high-income earners?

When running the numbers, the outcome favours the RA as a base investment. Here's why …
Is an annuity really worth it for high-income earners? It is, of course, not tax-free, as is commonly touted. Eventually, you do pay tax, except on the first R550 000. If you have other income streams, you may very well pay 45% of your income from the annuity anyway. You just delay the tax on a fund with inferior growth. So why would you want an annuity when you can get much better growth in a fund with 100% offshore exposure, which Regulation 28 forbids in annuities?

Thank you for your question.
This question always attracts much debate. Tax-sensitive investors tend to be against annuities since the income derived from annuities (compulsory annuities) is fully taxed. Voluntary guaranteed annuities are more tax-friendly since a part of the monthly income paid is deemed to be repayment of capital, thereby reducing the average tax rate substantially. I am not sure if you are referring to pre-retirement retirement annuities (RAs) or post-retirement annuities (living annuities). I assume your question relates more to living annuities even though you refer to Regulation 28 (which does not apply to living annuities). Regulation 28 only applies to pre-retirement products. My comments will thus be more living annuity-centric, with some reference to compulsory life annuities. I will, however, also delve into RAs a bit as well.

At the outset, I want to state that unless you have a provident fund, you have no choice but to purchase an annuity with at least two thirds of the proceeds of your pension fund or retirement annuity. Here, you can choose between a living annuity, where you can annually choose your income as a percentage of the living annuity value on the anniversary date of the annuity, or a life annuity, which provides a guaranteed life-long income. If you have a provident fund, you are entitled to the full amount in cash, subject to retirement tax tables that can ramp up to 36%. You can also choose not to take the cash and opt for an annuity where you will be taxed monthly. As you rightly stated, the first R550,000 of the cash commutation will be tax-free, irrespective of whether the proceeds are from a provident fund, a pension fund or a retirement annuity. It is important to note that the R550,000 is aggregated across all your retirement funds and not per fund. Investors often forget about the amounts they took in cash when they changed jobs and accessed their retirement funds in the past. Past withdrawals, including partial withdrawals, count towards the R550,000.

Invest in annuities or voluntary funds?

In my opinion, it should not be a choice between an annuity or voluntary investments that provide your retirement income. One should have both for various reasons. What percentage you allocate to voluntary versus compulsory depends on your circumstances. Bear in mind that you will have to decide on the split many years before retirement because capital accumulated in retirement funds will have to be placed into some sort of compulsory annuity when you retire unless the fund is a provident fund, as I previously mentioned. My 'thumb suck' recommendation is to split the funding of compulsory funds (retirement funding) and voluntary funds such as cash, unit trusts, shares and exchange-traded funds (ETFs) down the middle to try and achieve a 50/50 split the day you retire.

Why do I suggest this?

One of the most important financial planning strategies and objectives must be to optimise tax. It makes perfect sense to structure one's portfolio and invest in cash until the interest generated becomes taxable. It also makes sense to 'draw income' by selling units (unit trusts or ETFs) or shares to the point where income tax is reduced to single figures, especially where your starting tax is above 30%.Attracting capital gains tax (CGT) is more tax-efficient than pure income tax, like drawing income from fully taxable annuities. Tax is calculated on a 'total taxable income' basis. See the table below as an example (assuming a total investment value of R30 million and CGT base cost of 50% of the investment value. Drawdown at 4% per annum):

Annual income	Income from living annuity	Selling units from voluntary investments	CGT	Total tax	Net income	Marginal tax
1.2 million	1.2 million	Nil	Nil	391,519	808,481	33%
1.2 million	600,000	600,000	44,322	197,477	1,002,523	16%

The above figures are very simplistic, but in theory, this simple example indicates that the income level can be reduced from 4% per annum to around 3% per annum, and that makes a huge difference in the sustainability and longevity of the overall investment. Sure, the figures would look even more impressive if all the investments were voluntary. However, there is a tilting point where it makes absolute sense to have compulsory funds as well as voluntary funds. In most investors' cases, they will have compulsory funds due to historical contributions and their past conditions of employment. ***Full Article***: **Is an annuity worth it for high-income earners? - Moneyweb**

Moneyweb | 21 February 2024

INTERNATIONAL NEWS

Pension fund demand drives resurgence of UK corporate bond market

Schemes increase exposure in wake of 2022 gilts market crisis and as they prepare for buyout deals

Pension funds are piling into UK corporate bonds, encouraging some French and German companies to issue sterling debt for the first time. The UK's £1.4tn "defined benefit" pensions industry has been switching to corporate debt for its higher yields and to prepare the schemes for potential sales to insurers, analysts said. The share of European corporate bond sales denominated in sterling has risen to 8.4 per cent from 6.8 per cent at the beginning of 2023, the busiest start to the year in a decade for investment-grade issuance from non-financial companies. The demand has helped push a number of continental European companies to issue sterling debt for the first time in recent months, including German real estate company Vonovia, German truck manufacturer Traton and French luxury goods group Kering.

A rise in UK interest rates in recent years has meant more DB pension schemes, which offer a guaranteed income for life, have become "fully funded" for their future obligations, because higher rates typically lower the cost of pension promises. This means that offloading liabilities, and the assets backing them, to insurance companies is becoming a viable option for more businesses. Companies looking to do these so-called bulk annuity deals need to make the assets as attractive as possible to potential buyers. A greater focus on having the right assets for a buyout, coupled with regulatory changes, "has created a sweet spot for sterling denominated credit to be in demand", said Paul Whelan, co-head of global fixed income manager research at Aon. Corporate bonds are attractive to insurers, say industry executives, as they can use them as a match for their liabilities under solvency rules. They also provide a higher yield than gilts and can act as a more liquid complement to insurers' hard-to-sell investments such as infrastructure or social housing. "Investment grade sterling credit is arguably the most desirable liquid investment for a pension scheme," said Simeon Willis, chief investment officer at XPS Pensions Group, owing to its "additional return over gilts, sterling interest rate protection and familiarity". Charlie Finch, a partner at consultancy LCP who advises on pension deals, said the improved funding position of DB schemes "has been driving a trend to de-risk their investment strategies, moving into corporate bonds and other low-risk assets as they target insurance buyouts".

A record £50bn in corporate pension deals took place in 2023 involving about 46 schemes, according to WTW, which predicts full buyout deals could reach £60bn this year. "Overall given the stepped change in funding position for many. 2024 has the potential to be the busiest year ever in the de-risking markets," said Jenny Neale, director in the WTW's pensions transactions team, in a recent note. Phil Smith, head of Emea LDI research at BlackRock, the world's largest asset manager, said demand should remain robust, with sterling-denominated corporate bonds tending to make up "the majority" of these funds' credit exposure. New regulations to limit excessive leverage by pension funds in the wake of the autumn 2022 gilts crisis have also spurred demand for corporate bonds.

During the market chaos that followed former prime minister Liz Truss's "mini" budget, many schemes using so-called liability-driven investment — a strategy that uses leverage to manage funds' exposure to swings in interest rates — were forced to dump their gilt holdings to meet cash calls from lenders. Now, many funds prefer to buy corporate debt, which offers protection from interest rate moves without taking on leverage, as well as higher yields than government bonds. Colm Rainey, co-head of European corporate debt capital markets at Citigroup, said he thought a rise in demand from pension schemes "could be quite significant in terms of the direction of travel" for sterling corporate debt issuance.

Financial Times | **19 February 2024**