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irfa dispatch

THE RETIREMENT INDUSTRY NEWSLETTER

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LOCAL NEWS

Call for government to unlock retirement funds

Eminent pension fund and financial planning experts are calling on the government urgently to amend the laws governing retirement funds to allow members access to some of their retirement savings for emergency cash relief during the Covid-19 crisis. Although the retirement fund industry has always emphasized the importance of preserving retirement savings, the argument is that many employers and employees, whose income has dried up because of the pandemic and lockdown, need money now rather than later to tide them and their businesses over until the crisis has passed.

Personal Finance has received several requests from readers about the possibility of accessing money in their retirement funds. The total assets in South African pension funds stood at more than R4.2 trillion in 2017, according to the most recent annual report of the Registrar of Pension Funds. Releasing 5% of that would provide relief of R210 billion to 17 million fund members nationwide. A downside of accessing funds at this time is that most underlying investments have lost value during the crisis, and any withdrawals would lock in those losses.

In a recent Nielsen Network video podcast hosted by TV journalist Bronwyn Nielsen, five financial and legal experts co-drafted the following Twitter message: “Dear (Finance) Minister Mboweni, (SA Revenue Service) commissioner Kieswetter, acting commissioner of the (Financial Sector Conduct Authority) and all pension and provident fund trustees. Please use your power and allow desperate people tax-free access to some of their retirement savings ASAP.”

The participants were pension fund specialist Rosemary Hunter from law firm Fasken; Professor Alex van der Heever, chair of social security systems administration and management studies at the Wits School of Governance; Xhanti Payi, director of Nascence Advisory; Magnus Heystek, director of Brenthurst Wealth Management; and Andrew Crawford, founder of Seshego Consulting. The group suggested a special relief benefit in the form of a once-off, tax-free lump sum, which could be either a percentage of the fund credit or a fixed rand amount, such as R100 000.

Types of funds

The emergency measures would differ slightly, depending on the type of fund. There are four types of retirement funds:

1. Pension funds. In an article “May a pension fund or provident fund lawfully pay special relief benefits to employed members in Covid-19 related financial distress?” Hunter and her Fasken colleagues Nigel Carmen, Deanne Wood and Johan Coertze argue that there is nothing in the Pension Funds Act that prevents a fund from amending its rules to provide for a special lump-sum deduction from a member’s fund credit. Such an

amount could be tax-free, as it could come off the R500 000 amount you are allowed to take tax-free on retirement. Pension fund trustees would therefore simply need approval from the FSCA to change the fund's rules (as funds may already have had to do to temporarily halt contributions).

2. Provident funds. Hunter et al say that, again, although nothing in the Pension Funds Act prevents provident funds from amending their rules to provide for special relief benefits, there may be adverse tax consequences because of the way the term "provident fund" is defined in the Income Tax Act. Thus, in addition to a fund changing its rules, the Income Tax Act would need to be amended by Parliament.

3. Retirement annuity (RA) funds. You are not allowed to access any savings in an RA before the age of 55, unless you emigrate. At 55, you can take a third of the accumulated savings as a lump sum, unless the fund value is R247 500 or less, in which case you can withdraw the entire amount. Again, the Pension Funds Act does not prevent an RA fund from paying special relief benefits if its rules provide for them, but the Income Tax Act would have to be amended.

4. Preservation funds. As things stand, you are allowed a once-off withdrawal from a preservation fund before 55. You may therefore immediately make a withdrawal if you haven't already done so. However, again, because of possible adverse tax consequences, the Income Tax Act would have to be amended. In the Nielsen Network discussion, another suggestion was that members could take a loan against their retirement savings. This is already permitted in the rules of certain pension funds in the case of buying a property. Hunter told Personal Finance she did not think a loan was appropriate at present.

"We know that the levels of indebtedness in this country are already high, and it is unlikely that many of the fund members who now need early access to some of their retirement savings will soon find themselves in a position not only to resume normal contributions to their funds but also to pay back loans granted to them by their funds," she said. When approached for comment on the proposals, the National Treasury's media division issued the following statement: "Government has been considering the request of early access to retirement savings as a relief measure for members. Various stakeholders, including the regulator, are being consulted in this regard. No policy decision has been made as yet."

IOL | 25 May 2020

Your options when choosing a life annuity

This week I'll delve a little deeper into life annuities: pensions provided by life assurance companies that guarantee you an income for life. These products offer a surprisingly broad range of options for retirees. With kind input from Nicola Symons, business solutions consultant at Sanlam, we'll unpack some of them. Symons says life insurers offer two broad types of life annuity:

1. Conventional annuity: pension payments may be level, increase at a fixed rate each year or increase at a rate linked to inflation (the Consumer Price Index). The underlying investments are predominantly fixed-interest instruments and inflation-linked bonds, Symons says.

2. With-profit annuity: the underlying investments may be spread across a range of assets including equities, property and fixed interest. The annuity payments and annual increases are determined by the performance of these assets, Symons says. "Insurers generally smooth out the returns to try to prevent any sharp changes in income from one year to the next. Some insurers may guarantee that the annuity payment will never decrease." Conventional and with-profit life annuities have a number of options, such as:

- A guaranteed payment term - the minimum term of the annuity payments.
- Your choice of annual payment increase rate.
- Joint life annuities, which include a spouse or other beneficiary as a second annuitant, who will continue to receive payments after the death of the main annuitant. The annuity amount can be reduced after the first annuitant dies.

All of these options will influence your initial income amount, Symons says. "You should also consider any capital you may wish to bequeath to heirs," Symons says. On its own a life annuity does not provide any capital benefit at death. If there is a requirement for capital at death, Symons says, you can consider:

- Using a portion of your retirement savings to buy a living annuity (the other broad type of pension product, discussed last week); or
- Asking your insurer about a capital protection annuity. "With this arrangement, you will receive a regular income for life and your heirs will receive a lump-sum amount when you die. Your income will be lower, since a portion of your purchase amount will need to pay for life cover. However, this can be more cost-effective than buying life cover separately. There will generally be no medical underwriting on the life cover," Symons says.

Regarding the protection of your annuity income, Symons says life insurance companies in South Africa are tightly regulated by the Prudential Authority and the Financial Sector Conduct Authority. "The Financial Soundness Standards (FSS) issued by the Prudential Authority set out prescriptive criteria on the minimum amount of capital an insurance company must hold in addition to the assets it holds to back its policyholder liabilities.

This capital must be of 'sufficient quality and quantity to absorb significant unforeseen losses arising from the risks associated with an insurer's activities. "The FSS also requires that the insurance company must be able to demonstrate that the capital reserve is sufficient to withstand severe market shocks (such as what we have seen in South Africa and across the world as a result of the Covid-19 pandemic). "This requirement, together with the frequent regulatory reporting insurance companies must provide, is designed to enable the regulator

to intervene timeously. This should ensure that action can be taken to protect policyholders long before their benefits would become exposed to the risk of an insurer falling into financial difficulties," Symons says. She says that, according to the Association for Savings and Investment South Africa, at the end of last year the life insurance industry held free reserves of more than double what is required by the FSS.

IOL | 25 May 2020

Hybrid annuities: Something to consider when choosing your pension

The best news often follows the worst. But the best news may take some time to arrive. The worst news in financial markets often comes from unexpected events, such as the international 2008/10 meltdown as a result of the American sub-prime property crash. This has now been followed by the Covid-19 pandemic, which is expected to have a much larger and longer financial impact.

Pensioners are particularly at risk in times of volatile markets, not only in South Africa but around the world. The market crashes have affected both those starting their retirement and those already in it. While markets have recovered more recently, they have not fully recovered and further risks remain. Too often in the financial world we have seen that vested interests of advisers, and those of large financial companies, play a huge role in undermining the financial interests of individuals.

Take the following examples:

- Unit trust money market funds were strongly opposed and retarded by banks. The reason was the banks had a fine business locking peoples' money up for long periods.
- Life assurance companies came out fighting and lost out when people switched from secretive, high cost and poorly priced guaranteed annuities to living annuities.
- The active management versus passive investment approach. For quite a long period, it was a war with one totally opposed to the other. The vested interests that opposed passive management of funds were making a fortune by charging a lot more for active management. What is now being gradually seen is that a mixture of the two, driven mainly by retirement funds, will give the best returns.

It is not a question of which annuity is better – a guaranteed annuity or a living annuity. The answer lies in both. It is something that I have been arguing for many years. In December 2019, a group of British and American academics published a paper on what is called the "sequence of returns" for people living off their accumulated investments. This was research based on the 2008/10 market crash.

The paper, "Developing a Measure of Sequence Risk", was written by Andrew Clare, Simon Glover, James Seaton, Peter N Smith and Stephen Thomas. It is a technical paper, but you can download it off the website. In simple terms, this paper is saying that neither living annuities nor guaranteed annuities should be seen in opposition to each other. In simple terms, this paper is saying that neither living annuities nor guaranteed

annuities should be seen in opposition to each other. The answer lies in what are hybrid (flexible) annuities, which mix and match the annuity types – both linked investments living annuities and traditional guaranteed annuities must be combined. Those pensioners who have already done this should find themselves in a better position following the Covid-19 crash. Asset management companies from the 1990s have sparked much of the innovation of market-linked investments. The driving force was the move from defined benefit retirement funds, where your employer took all the risk, to defined contribution funds, where you take all the investment risk. ***Full report:*** ***https://www.dailymaverick.co.za/article/2020-05-25-hybrid-annuities-something-to-consider-when-choosing-your-pension/***

Daily Maverick | 25 May 2020

SA households rapidly lost R800bn in real net wealth, but rebound seen

Covid-19 and weak economy to blame
South Africans' pension funds and other investments like unit trusts have been hit hard by sharp declines in the value of shares and bonds. This is as a result of the worldwide Covid-19 pandemic; the subsequent lockdown, which incapacitated the global and South African economies; and SA losing its investment grade credit rating, Momentum/Unisa research reveals. South African households' real net wealth decreased by an estimated R828bn from the last four months of 2019 (Q4 2019) to the first four months of this year (Q1 2020), according to the institutions' SA Household Wealth Index, released on Monday.

Johann van Tonder, researcher and economist at Momentum, said this estimated real quarterly decline is 52.5% more than the previous largest estimated quarterly decline of R542.9bn, which was registered during the "great recession" of the third quarter of 2008. "The recent plummet in household real net wealth can be largely attributed to a sharp decline in the real value of households' pension funds and other investments such as unit trusts," said Van Tonder. The real value of pension declined by an estimated R427,6bn over the quarter, while other investments lost R363,9bn."

Van Tonder said households' pension funds and other investments were mainly invested in two asset classes: shares and bonds. "The decline in the prices of shares and bonds were caused by worldwide fear and panic selling of these financial assets stemming from the spreading of the coronavirus." The real value of pension declined by an estimated R427,6bn over the quarter, while other investments lost R363,9bn." The subsequent decisions by governments, including the South African lockdown, in effect incapacitated economies, as very little production was possible.

"Apart from the immediate negative effect on the prices of shares and bonds, the future impact of these decisions will be devastating for economies and households – as company profits will decline, while millions of households are expected to lose their income due to extensive employment losses across the economy, negatively affecting their ability to live properly and save for retirement and other goals." Added to this, he

said the value of shares and bonds were further hit by Moody's decision on March 27 - the same day the lockdown started - to downgrade SA's credit rating to sub investment grade. There is some hope, he signalled. Since the end of the first quarter of this year, Van Tonder said, international shares and bonds have recovered markedly on the belief that the worldwide economic recession would be over soon; that a vaccine will be available before the end of the year; that central banks will "bail" markets out; that governments will provide sufficient support measures to companies and households; and that economies will "open up" soon.

"South African share prices followed suit as many companies listed on the JSE earn the bulk of their profits abroad. This would have had a positive impact on the real value of particularly households' financial assets - specifically retirement funds and other investments." Consequently, about 60% of the decline in the real wealth of households had been recovered by the end of April 2020. He cautioned that should the beliefs of the market not be realised and confidence not restored, the prices of risk assets may retreat again – and this will lessen the real value of households' assets. "This, in turn, will negatively impact the real value of households' net wealth, as well as economic growth and employment creation."

SundayTimes Timeslive | 25 May 2020

INTERNATIONAL NEWS

Coronavirus to drive further exits from sector pension fund to less generous schemes

The financial impact of coronavirus is likely to see more housing associations exit the Social Housing Pension Scheme (SHPS) and move to less generous schemes, pensions figures have said. *Inside Housing* has spoken to a number of pensions experts who predict that coronavirus will accelerate the trend of housing associations reducing numbers of employees on defined benefit (DB) schemes and may tempt others to quit the SHPS as they look to gain more control over their liabilities. Martin Harlow, senior consultant at XPS Pensions Group, told *Inside Housing*:

"I expect there will be further transition from defined benefit to [less generous] defined contribution schemes and coronavirus will only accelerate that." Mr. Harlow also said the pandemic could mean more employers leave SHPS if the **£1.5bn deficit increases**, to avoid having to increase contributions.
"Those who were thinking about leaving will start thinking about it more as a proposition. I don't see there being any slow-up in terms of employers deciding they need to look at this," he said.

A spate of exits occurred in November 2019 when Riverside, Sovereign and Orbit all quit the multi-employer scheme citing the desire for greater control over costs and risks. Rebecca McKay, partner at Trowers & Hamlins, said that the law firm has heard from several clients that want to reduce liabilities

and risks by moving from DB to defined contribution, and transfer out of SHPS. She said that the pandemic has provided a “new kick” for some employers. She said the firm is in the process of facilitating two bulk transfers out of the SHPS this year. Richard Soldan, partner at Lane Clark & Peacock, agreed: “The financial impact of coronavirus is the sort of thing that could increase the general desire to exit SHPS.”

He told *Inside Housing* that if the deficit rises again, “some associations will want more control, meaning it will become more common to exit”. But Mike Richardson, another partner at Lane Clark & Peacock, also suggested that an exit may be too big a project to take on during the pandemic. He said: “An exit out of SHPS is costly and time-consuming and is something that could always be deferred by a year. However, a lot of associations have put it to one side already, so some might think they need to get on and do it.”

Inside Housing | 26 May 2020

UK’s largest pension scheme stockpiles cash

Nest builds up reserves in anticipation of further market uncertainty

Britain’s biggest pension fund has hoarded cash reserves in anticipation of further market uncertainty as companies and countries grapple with the fallout of coronavirus. Nest, the UK state-backed pension scheme with 9m members, making it Britain’s largest, said its allocation to cash in its main investment funds stood at about 5 per cent, compared with 1 to 2 per cent normally. Mark Fawcett, chief investment officer at the £10.5bn pension fund, said that while he did not know “which direction the market will go”, there was a “bunch of risks the market seems to be feeling fairly benign about”.

These risks included the possibility of a second wave of outbreaks and the rapid spread of the virus in emerging markets such as Brazil, as well as a lack of clarity about the pace of recovery and whether people would continue to stay at home even if economies were opened up. “We just don’t believe a V-shaped recovery is very likely,” he said, referring to a fast uptick in growth. “Clearly if a viable vaccine is found that changes things and reduces those downside risks. But it will take a while to vaccinate the world.” He said the pension fund had taken the opportunity to reduce some holdings, such as in high-grade credit, to build cash reserves.

The pension pot has a steady stream of money coming into it from members and has chosen to put some of that aside rather than invest. Mr. Fawcett added that the allocation to cash at 5 per cent was “probably as high as we would ever get”. “If we see some of these risks manifest themselves, we have the ability to increase holdings where we think we need them,” he added. Jan Erik Saugestad, chief executive of Storebrand Asset Management, the Nordic fund house that oversees large chunks of pension assets, shared Mr. Fawcett’s concerns, saying a U-shaped recovery was more likely.

He said that while economic stimulus from governments would work, it would take time. “We are cautious, given the levels and risks we are seeing right now,” he added. According to a survey of fund managers from Bank of America this month, just 10 per cent expected a V-shaped recovery, while 75 per cent anticipated a U- or W-shaped one. The poll found that managers were holding large amounts of cash, with allocations at 5.7 per cent, well above the 10-year average of 4.7 per cent. But others struck a more optimistic note.

Elliot Hentov, head of policy research with the global macro policy research team at State Street Global Advisors, the world’s third-largest asset manager, said he was “slightly more optimistic than the consensus” and in line with how equity markets were pricing a recovery. He added that he expected significant breakthroughs over the summer, whether in treatments, contact tracing or other areas that could help prevent a second lockdown. Nest’s Mr. Fawcett said it was a challenge to run the fund during such market uncertainty. “It is clearly tough, because we have to make sure our members have enough exposure to growth assets that we can build a good pot for them over years, but we don’t want to give them excessive volatility,” he said.

Financial Times | 23 May 2020

OUT OF INTEREST

COVID-19 - SARS outlines process for applying for deferral of tax payments without incurring penalties

The South African Revenue Service (SARS) has published the process that businesses operating in South Africa should follow to request instalment payment arrangements without incurring penalties due to the COVID-19 pandemic. The aim of deferring tax payments without incurring penalties is to alleviate the cash flow burden of tax compliant businesses during the pandemic economic crisis.

This option applies to both small and larger businesses, as well as multinationals operating in South Africa. Taxpayers making use of this relief scheme must be able to prove substantial and material financial hardships as a result of COVID-19. Penalties will only be remitted if taxpayers are able to successfully prove the serious impact of COVID-19 on their business.

Direct Taxes

According to SARS, requests should be sent to dedicated SARS email addresses and should be made on a per entity basis. The email must contain a letter requesting deferral of payments, stating the reasons and specific tax periods applicable. Further information to be included are the business’s latest financial statements and management accounts, a list of debtors and creditors, and cash flow projections for the next three months. Larger businesses with a gross income of more than ZAR100 million, who can’t make a tax

payment because of issues relating to the pandemic, can apply to defer tax payments without incurring penalties by emailing **COVID19IPAaboveR100m@sars.gov.za**.

In April 2020, it was announced that tax compliant Small, Medium and Micro Enterprises (SMMEs) with a turnover of up to ZAR100 million, would be able to defer 35% of their employees' tax payment for the months of April to July without incurring penalties and interest. Further to this, smaller businesses with a gross income below ZAR 100 million are now able to apply for an additional deferral of payments without incurring penalties, by emailing **COVID19IPAbelowR100m@sars.gov.za**.

Taxpayers should be aware that this is simply a deferment process and does not absolve them of their obligations towards SARS. If approved, the tax due will be paid in instalments, the upside being that penalties will not be levied on a successful application. However, no mention is made of interest being deferred and it must be accepted that interest will continue to run on any outstanding debt. Further, there is no mention of which taxes would apply. It can therefore be assumed that it would apply to any taxes due, which will be welcomed by all taxpayers.

Customs

From a customs perspective, in a letter to all stakeholders dated 17 April 2020, SARS communicated its position and decision relating to the extension of the customs deferment payment as guided by the Disaster Management Tax Relief Bill 2020. SARS has acknowledged that it is mindful of the economic hardships that businesses in South Africa and around the globe are facing during this time of the COVID- 19 pandemic and indicated that it will continue to work with all stakeholders and government to ensure a reduction of the impact of the virus on civil societies and business.

SARS also informed companies and traders with payments due in terms of the Customs Act, including customs deferment payments, that they may apply to make payment in instalments. Applications may be submitted to **osc@sars.gov.za** for the attention of Vonani Ntlhabyane. Taxpayers may use the framework of draft rule 105.01 that is currently out for public comment to structure their applications. In summary, the proposed draft rule under the Customs Act provides as follows: an outstanding amount payable in terms of the Customs Act may be paid in instalments if the person liable for payment of the amount has, after obtaining permission in terms of rule 105.03, entered into an instalment payment agreement with the Commissioner.

The instalment payment agreement must be signed by the parties and supporting documents, as may be required by the Commissioner, must be submitted on request. Only persons that are tax compliant and that satisfy certain qualifying criteria may apply for the payment of outstanding amounts in instalments. The term “tax compliant” means that a person has no outstanding taxes, interest, penalties or other amounts due and payable to SARS for which he or she is liable in terms of the Customs Act; or accounts, returns or other documents that must be submitted for tax purposes to SARS in terms of the Act.

If the application is approved, SARS may still require the applicant to provide security in such form and amount as may be determined by the Commissioner. Importantly, the proposed customs deferment payment rules are silent on the accrual of penalties and interest. Given the current state of lockdown in South Africa and the likelihood of it continuing for the foreseeable future, taxpayers should seriously consider these options, but only if they are in a precarious financial situation due to the COVID-19 pandemic.

FA News | 25 May 2020

Rand climbs to 8-week high vs dollar

Optimism around a global recovery from the Covid-19 pandemic boosts riskier assets. The rand raced to its highest in more than eight weeks against the US dollar on Tuesday, as optimism about a global recovery from the Covid-19 pandemic boosted riskier assets, with investors looking past Sino-US trade tensions.

At 14:12 the rand was at 17.41 to the dollar.

The currency was at its strongest since March 27.
"The optimistic recovery narrative is holding within markets, keeping the dollar subdued and seeing the rand remain on a stable footing following last week's rally," Bianca Botes, executive director at Peregrine Treasury Solutions, said in a note. "While there are looming geopolitical risks, it seems as though markets are currently pushing them onto the back burner, and will likely continue to do so until there is a new escalation or increased threat."
Japan's decision to end coronavirus-induced restrictions and a survey showing German business morale rebounded in May lifted hopes of an economic recovery and helped offset a war of words between Beijing and Washington on trade, coronavirus and China's proposals for stricter security laws in Hong Kong. In South Africa, President Cyril Ramaphosa announced on Sunday a further easing of the country's lockdown from June 1, allowing the vast majority of the economy to return to full capacity.

Moneyweb | 26 May 2020

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