MONDAY, 27 SEPTEMBER 2021

irfa dispatch

THE RETIREMENT INDUSTRY NEWSLETTER

TABLE OF CONTENT

LOCAL NEWS

To protect your retirement funds, look offshore

South Africa faces a long, hard road to economic recovery, with the combination of massive unemployment, huge additional debts incurred as a result of Covid-19 and constrained government spending meaning that it will take years just to get back to pre-Covid GDP levels. That's the prognosis of political analyst Daniel Silke, who says that while 2021 was supposed to be an economic recovery year for South Africa after the lows of 2020, the uptick has been muted, with ongoing political disruption adding to the uncertainty. Speaking at Sovereign Trust's annual retirement seminar this month, Silke said the rest of the world was starting to claw its way back to pre-pandemic GDP levels, with a 'K-shaped' recovery starting to emerge and with investors and professionals recovering well.

However, the people and countries that were suffering from job insecurity were still struggling. What this means is that it has never been more important than now to consider future financial sustainability when it comes to retirement planning, said Sovereign Trust (SA) Limited chairman Tim Mertens. "The unprecedented economic downturn has raised questions around investment performance, financial resilience, and supervision of retirement and investment funds. It's critical for South Africans to consider offshore investment options to protect themselves from a volatile economic and political environment," said Mertens.

However, recent significant changes to tax compliance requirements and the ability to encash retirement funds means that any member of a pension fund or retirement plan must plan their emigration carefully, with a view to how they will need to adapt once they attain tax residency in their new home country. Tim Powell, the director of Sable International, said the shift from the previous focus on financial emigration to the current tax emigration regime was having an impact on the ability of individuals to move money out of the country, in particular accessing their retirement funds and inheritances. Previously, expats could withdraw their retirement funds before their retirement age as long as they had financially emigrated.

Since 1 March 2021, they now need to prove they have changed their tax status with SARS to non-resident as well as demonstrate that they have been tax resident in a foreign jurisdiction for at least three consecutive tax years before they can access retirement funds. Tax emigration and the resulting SARS' deemed capital gains tax – the so-called 'exit tax' – could also provide potential liquidity challenges to people suddenly having to pay capital gains taxes on existing worldwide assets.

"Ending your tax residency in South Africa is not just a simple tick-box exercise, and it's critical that those planning to emigrate and move their investments should obtain a professional assessment of their personal circumstances, specifically considering issues like investment allowances, tax clearance applications for foreign investment, and maintaining bank accounts in SA," said Powell. Despite the added tax complexities, however, offshore retirement planning remains the best option to ensure the stability and sustainability of retirement funds, said Richard Neal, MD of Sovereign Trust (SA) Limited.

International retirement plans are not in breach of general anti-avoidance rules (GAAR), as long as they are recognised as bona fide pension schemes, and are administered and run in a proper manner. Offshore retirement funds, like those falling under Guernsey's 40(ee) regulations, provide several advantages over South Africa-based funds. Guernsey 40(ee) schemes are tax exempt for non-residents, and allow contributions in a range of forms. However, the major differences come in with how the investments are made and how benefits are drawn: there are no geographic or other restrictions on investments, and members can take benefits as and how they prefer after the age of 50.

Sovereign's own 40ee plan – branded as the Conservo International Retirement Plan – is an effective estate planning and diversification tool that can be specifically tailored to the needs of South Africans. Unlike traditional pension schemes, there is no centralised 'pot' of funds, with members' retirement funds held solely for their own benefit. "Retirement planning is never a 'one size fits all' situation. It all depends on the specific circumstances and retirement goals of each person. But forward planning pays off, especially at this time," said Neal.

FA News | 20 September 2021

How provident fund annuitisation changes affect approved lump-sum disability benefits

Funds need to consider whether an income structured benefit still meets the intention and expectations in terms of incapacity procedure.

New tax rules on the annuitisation of provident funds and lump-sum payouts made at retirement took effect on March 1, 2021. Fund members should be aware of additional implications for approved lump-sum disability benefits. On retirement, members of these funds who were under age 55 on this date (known as T-day) may still take amounts which accrued prior to March 1 2021, plus the fund return, in cash. Members over age 55 on T-day will have access to all amounts in the fund in cash when retiring from that fund. This is referred to as ‘vested benefits’ as opposed to ‘non-vested benefits’ where annuitisation rules apply to amounts above R247 500.

Approved lump-sum disability benefits paid by a pension fund

The approved (provided by the fund) lump-sum disability benefit in a pension fund was previously included as part of the fund benefit. It was normally treated in its totality as an ill-health early retirement benefit from the fund. The cash amount was limited to a maximum of one-third of the benefit, while the balance was used to buy a pension.

Approved lump-sum disability benefits from provident funds

Those under the age of 55 will have the same limitations on their lump-sum disability benefit and how this is treated in terms of annuitisation as applies to pension funds.

- ***Members over age 55 on March 1, 2021***

  The lump-sum disability benefit will be part of the vested benefits in the provident fund of which the member had membership on T-day. This means that the member can receive this payment in cash, after tax. But if the member transfers to a new fund after T-day, and is then disabled, any lump-sum disability benefit paid out of the new fund will be a non-vested benefit. This means that annuitisation rules will now apply.

- ***Lump-sum disability benefits under 55***

  Only amounts which have accrued before T-day fall into vested benefits. If a member is disabled after T-day, the lump-sum disability benefit payable will not fall into the vested benefits. The payment will be treated as a non-vested benefit. This means that the annuitisation rules, where the total benefit exceeds R247 500, will now apply to the lump-sum disability benefit.

Reform

While the above may be an unintended consequence of the annuitisation rules, we should take a step back and reconsider the real intention of reform. Various stakeholders in the industry introduced and agreed upon reform as it became evident that current regulations were failing the member. Almost 50% of members retire on less than one-third of their final average salary, which renders a large part of people poor and dependent on the state.

This is unsustainable and needs to change. Reform has brought in different forms of laws to increase the savings culture and provide certain incentives – like a tax deduction if a member saves more, up to a certain limit. With the lump-sum disability benefit now subject to annuitisation, funds need to consider this question: Would an income structured benefit still meet the intention and expectations by members, the fund and the employer in terms of their incapacity procedure? The trustees and employer will have to revisit why the approved lump-sum disability benefit was selected in the first place. Was this to ensure that there would be a lump sum to:

- Meet the cost of additional care or adjustments to the home to assist the disabled employee, or
- Provide cash support ultimately to members who are found to be totally and permanently disabled?

If the above intent of providing a lump-sum benefit still stands, the trustees and the employer may need to consider changing the tax status of this benefit from approved to unapproved. This will ensure that the initial intention and expectations are still met. Caution is made that changing to an unapproved benefit would mean that the employee would need to pay fringe benefit tax on the monthly premium. However, the benefit would be paid as a tax-free lump sum separate from the retirement fund for total and permanent disablement.

These discussions must therefore include decision makers on the employer side to:

- Help facilitate the messaging to the employees,
- Manage any payroll impacts, and
- Align with their incapacity procedures.

Any benefit structure implemented must be well considered to best suit the needs of the members. This could enhance the financial well-being of employees and lead to the best retirement outcomes.

Moneyweb | 17 September 2021

South Africa's current retirement conundrum

In the weeks prior to the Medium-Term Budget Policy Statement (MTBPS), South Africans await more clarity from National Treasury on their proposal for limited pre-retirement withdrawals and the logistics required to make this happen. Now is the ideal time to take a closer look at why this proposal arose and which key questions still need to be answered. There are some things in life that are “easier said than done” – and for many, saving adequately for retirement falls into that category.

We know that to retire successfully, we should simply start saving as early on as our first payday, get inflation beating returns and never touch our savings until we reach retirement age – however, this is easy to say, but evidently not so easy to do given that over 90% of South Africans reach retirement with too little accumulated savings to support the same lifestyle they maintained while working.

A NUDGE IN THE "RIGHT" DIRECTION

In most aspects of our lives, the likelihood of success dramatically increases if our immediate environment encourages and enables us to make good choices. This is the very premise of what National Treasury is attempting to achieve with their proposal for limited pre-retirement withdrawals. This proposal encapsulates a system of "two buckets" – the first bucket being preservation until retirement, the second being accessibility of funds in extraordinary circumstances.

The proposal speaks directly to the notion of "libertarian paternalism" where rules have been established to "nudge" people towards making decisions that are in their best interest while still giving them alternatives. For example, the default preservation and portability rules that were enacted in 2017 will make provision for us to automatically preserve our retirement funds if we change jobs, but also give us the option to take the cash immediately. Furthermore, all types of retirement funds must have a default annuity strategy (after retirement an annuity or living annuity must be purchased to convert retirement savings into income) and provide members with retirement benefits counselling.

In theory, these rules create an environment that is in our best interest; however, if the past year has taught us anything, it's that retirement savings seem futile when we cannot put food on the table. This is one of the reasons that have led to the current discussion around allowing us to dip into our retirement savings in "particular unexpected circumstances, extraordinary circumstances or emergencies".

CLEAR NEXT STEPS REQUIRED

For early retirement withdrawal to become a reality, both our laws and our retirement fund rules and systems will need to change. However, the Government Employees Pension Fund (**GEPF**) is not covered by the **Pension Funds Act** and GEPF members are understandably upset that they may be ineligible for such withdrawals. National Treasury is considering allowing withdrawals from retirement annuities and legislation would have to be "harmonised" to enable retirement annuity fund members to access their retirement savings. National Treasury indicated last month that Government is consulting with unions, retirement funds and regulators "to work out how to increase savings, improve preservation and allow limited withdrawals without creating liquidity and investment risks."

Changes are unlikely to come into effect before 2022.

The fact that the financial sector is posing relevant queries to National Treasury regarding the proposal is advantageous to all South Africans as policy makers will be viewing the proposal in respect of the current reality. Some of the queries that should be answered in the near future include:

• How the split between the "**two buckets**" will be determined.

• How much will be accessible to members granted access to their retirement savings.

• Aside from a global pandemic, what will constitute "particular unexpected circumstances, emergencies or extraordinary circumstances" to justify early withdrawals.

• How the mandatory preservation, upon resignation from a job, will work.

South Africans can expect to get clarity on the proposal before or at the upcoming MTBPS in November 2021.

FA News | 14 September 2021

INTERNATIONAL NEWS

UK pensioners underpaid by £1bn after government errors, watchdog finds

More than 130,000 retirees in line for payouts amounting to thousands of pounds

About 130,000 UK pensioners are in line for payouts amounting to thousands of pounds after repeated errors by the government led to more than £1bn of state pensions being underpaid. The scale of the underpayment was revealed by the National Audit Office spending watchdog on Wednesday as it published the findings of an investigation into state pension calculation errors, first brought to ministers' attention in early 2020. The Department for Work and Pensions is now facing calls urgently to compensate those affected after it conceded underpaying 134,000 pensioners a total of £1.053bn, representing an average of £8,900 per pensioner.

However, the bill could rise further, with the watchdog saying the DWP's estimates were "uncertain". "The impact of the underpayment of state pension on those pensioners affected is significant," said Gareth Davies, head of the NAO. "It is vital that the Department for Work and Pensions corrects past underpayments and implements changes to prevent similar problems in future." The errors affected those who first claimed their state pension before April 2016, who do not have a full national insurance record and who should have received certain increases in their basic state pension.

According to the NAO inquiry, the payment problems were due to "repeated human errors over many years, some level of which was almost inevitable, given the complex rules and high degree of manual review necessary when assessing claims". "The department's caseworkers often failed to set (and later action) manual IT system prompts on pensioners' files to review the payments at a later date, such as their spouse reaching state pension age or their 80th birthday," said the NAO. The NAO added that the department's focus on tackling the largest causes of fraud and error meant it "missed" earlier opportunities to identify the underpayments. "Many pensioners — most of whom are likely to be women — have been short-changed by thousands of pounds which they are still yet to receive many years later," said Meg Hillier MP, who chairs the public accounts committee responsible for overseeing government expenditures.

"Correcting these errors comes at great cost to the taxpayer," she added. "DWP must provide urgent redress to those affected and take real action to prevent similar errors in future." The NAO said a "great deal of uncertainty" remained over the estimates provided to it by the DWP and the true number of underpayments would become clear only once the department had reviewed hundreds of thousands of case files by the end of 2023. "We are fully committed to ensuring the historical errors that have been made by successive governments are corrected and, as this report acknowledges, we're dedicating significant resource to doing so," said the DWP.

"Anyone impacted will be contacted by us to ensure they receive all that they are owed. Since we became aware of this issue, we have introduced new quality control processes and improved training to help ensure this does not happen again." The DWP is engulfed in a separate scandal over delays to state pension payments to thousands of new pensioners caused by administrative factors. The department said it was "working hard to clear the current backlog", with some pensioners having had their first payments delayed by months.

Financial Times | **22 September 2021**

OUT OF INTEREST NEWS

Positive signs of earlier economic recovery post-Covid

Challenges abound but SA can be more optimistic about the medium-term outlook than a year or six months ago: BER.

The Bureau for Economic Research (BER) believes the South African economy could recover to pre-Covid-19 levels by the middle of next year. However, National Treasury and PwC are of the view that this will only be achieved in 2023. Hugo Pienaar, chief economist at the bureau, says economic reforms are starting to take form, albeit slowly. Speaking at the annual Tax Indaba hosted by the South African Institute of Taxation (Sait), he said the country can be more optimistic about the medium-term outlook than a year or even six months ago.

Revenue

Tax collections at the end of August amounted to just under R590 billion, 9.7% more than the February budget estimate. The sectors underpinning this growth, according to South African Revenue Service (Sars) Commissioner Edward Kieswetter in his keynote address, include mining and quarrying, manufacturing, agriculture, forestry and fisheries – and, to a lesser extent, electricity, gas and water; and community, social and personal services. He said there is still “low-hanging fruit” in terms of collecting taxes that are due.

Rebuilding Sars is central to improving the integrity of the tax system, he added. “This does not mean that there is not scope for policy initiatives. This can never be taken off the table. There is just too much inequity in the world.” The initiatives include the introduction of taxing the digital economy, global discussions around a minimum corporate tax, and the ongoing issue of wealth taxes. “These are the reactions, and some may [say] they are knee-jerk reactions to the reality of the levels of abuse of the tax system that still exist.”

SA needs to scan the entire horizon

Pienaar cautioned against looking to the mining sector to bail SA out economically. The sector has been doing so, and contributed to the quicker recovery, but it remains cyclical and prices of key commodities have already been coming down in recent weeks. “We need other sectors in the economy to come to the party too,” he said. South Africa needs the productive sectors such as manufacturing, construction and agriculture to do better as these sectors are able to absorb low-skilled workers.

No room to keep making the same mistakes

National Treasury chief director Edgar Sishi, speaking during the same session on the domestic economic rebound post-Covid, said the country doesn't really have a choice other than to fix embedded structural problems. He said Treasury does not want to repeat the mistakes made prior to the 2008 financial crisis. The country had also experienced a commodity price boom then, which resulted in a revenue windfall. "We responded to that by increasing spending in areas that were permanent in nature. In 2020 and 2021 all the spending increases have been on once-off items. We have prevented baseline spending from rising permanently."

Sishi said Treasury's biggest contribution has been to "rein in" spending and to force other government departments into prioritising better on key interventions for the economy. Government is still on track in terms of achieving a primary fiscal surplus in the middle of the decade, but spending risks from state-owned enterprises, particularly Eskom, remain significant. "These risks are percolating all around us and are threatening to become the wolves at the door," he said.

'Dry wood waiting for a spark'

South Africa's unemployment, poverty and inequality levels remain another issue that keeps chief executives of large companies awake at night, according to Lullu Krugel, chief economist at PwC. Combined; these three factors have been described quite aptly as dry wood waiting for a spark to ignite. Sishi expressed Treasury's concern about unemployment. ***Full Report:*** ***https://www.moneyweb.co.za/news/economy/positive-signs-of-earlier-economic-recovery-post-covid/***

Moneyweb | **7 September 2021 | Amanda Visser**

Switchboard: 011 450 1670 / 081 445 8722
Fax: 011 450 1579
Email: reception@irfa.org.za
Website: www.irf.org.za

3 Williams Road
Bedfordview
Johannesburg 2008