

Pravin's big retirement changes on track

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You need to gear up your retirement planning to meet T-Day and P-Day, when government will implement major changes to the R3-trillion retirement savings industry.

T-Day and P-Day are days when retirement fund reforms are scheduled to be implemented in or after 2015, with legislation based on government's latest proposals for retirement reform being put before Parliament this year. The proposals are outlined in a discussion paper titled "2013 Retirement reform proposals for further consultations".

This latest discussion document, released this week with the Budget, consolidates reaction to four discussion documents published last year on various aspects of retirement reform, including the preservation and taxation of retirement savings.

Apart from T-Day and P-Day, a number of other reforms will be implemented to boost the protection of your retirement savings, including the enforcement of better behaviour by your retirement fund trustees and measures aimed at reducing costs. The reforms also propose to bring statutory funds, such as the Government Employees Pension Fund and the Transnet funds, under the ambit of the Pension Funds Act, giving members the rights enjoyed by members of non-statutory pension funds.

T-Day

The recommendations for the still-to-be-set T-Day will affect the taxation of your retirement fund contributions. The recommendations change those made last year by Finance Minister Pravin Gordhan, which were scheduled for implementation on March 1, 2014. The latest recommendations are:

- * Your employer's contributions will be added to your taxable income as a fringe benefit;
- * You will be able to deduct both your and your employer's contributions to a pension fund, provident fund or retirement annuity (RA) fund up to 27.5 percent of the greater of remuneration or taxable income;
- * The premiums you pay on group risk insurance will be included in the amount you may deduct from your taxable income;

- * There will be a rand cap of R350 000 on the total amount you may deduct from your taxable earnings in any tax year;
- * Contributions in excess of the annual cap may be rolled over to future years when you may not reach the cap amount;
- * Any non-deductible contributions will be added to your tax-free lump sum at retirement; and
- * From T-Day, any new contributions made to a provident fund will be subject to the same annuitisation rules as pension funds, namely that at least two-thirds of the savings must be used to purchase a pension at retirement. Any provident fund savings made before T-day, and any investment growth on those savings, will not be subject to the new pension purchase requirement.

P-Day

Government is proposing tighter controls on preserving retirement savings, but it will allow you to access savings before retirement during periods of unemployment.

However, vested rights will be protected to avoid a repeat performance of people resigning their jobs or getting divorced to get their hands of their retirement savings.

Recommendations for the preservation of retirement savings are:

- * From P-Day, all retirement funds will be required to identify a default preservation fund to which members' savings can be transferred if they withdraw from the fund before retirement. The use of an existing retirement fund to preserve savings for retirement is already a no-cost option for members who, if the fund rules allow, can stay on as deferred members with their savings protected and growing until normal retirement age. However, currently, no withdrawals are allowed. This will change with the new withdrawal rules.
- * Currently, you are limited to one withdrawal from a preservation fund before retirement, but the withdrawal may be 100 percent of your savings. The new proposal is to allow for an income stream in periods of unemployment, allowing for one withdrawal a year.
- * Withdrawals will be based on a formula. The proposed annual withdrawal will allow members of preservation funds to withdraw an amount that is the greater of the state old age grant (R1 260 from April 1) or 10 percent of their initial preservation fund deposit, excluding any portion to which vested rights apply. Any unused withdrawal amounts may be carried forward to future years.
- * From P-Day, retirement fund divorce settlements will be subject to the proposed new preservation withdrawal rules allowing for a limited income stream.

Consideration is also being given to relaxing the preservation requirements of RA funds, from which you currently cannot make any withdrawals before the age of 55. (When you do reach 55, two-thirds must be used to purchase a pension).

Treasury is considering allowing RA fund members to transfer their balances to preservation funds, under conditions that will prevent them from seeking out additional tax advantages. The conditions may include preventing individuals who have transferred money out of an RA fund from rejoining that fund, or, alternatively, from receiving a tax deduction in respect of any RA contributions, for a period.

TREASURY INTENT ON OVERHAUL OF LIVING ANNUITIES

Investment-linked living annuities (illas) are due for a major overhaul to ensure that pensioners using them are not left financially destitute before they die because of high costs, poor advice, wrong investment choices and drawdown rates that are too high.

Life assurance companies are set to lose their stranglehold on the provision of illas, with government proposing that the requirement of a life assurance licence to sell illas be dropped.

It is proposed that collective investment scheme management companies such as unit trust and exchange traded fund companies be allowed to sell illas without, as they currently need to do, registering as a life assurance company or renting a life assurance licence.

National Treasury hopes this will increase competition and bring down costs.

It says most respondents to an earlier discussion paper pointed out that an important factor underlying the choice of annuity at retirement was that people with a low level of savings tended to choose illas in the hope that, because they allow for higher initial pension payments than conventional annuities, they could maintain their living standards.

Most respondents were in favour of reforming, rather than replacing illas.

Treasury says:

* Many of the difficulties associated with illas may be direct or indirect consequences of the ways in which intermediaries, including investment platforms, are paid. The Financial Services Board (FSB) is already investigating these costs as part of its Retail Distribution Review on commissions paid for financial products, including illas. This review will include an investigation into the payment of rebates by collective investment schemes to linked-investment service providers, which are currently the main source of illas.

Illas are also part of the scope of the Treating Customers Fairly initiative.

* Consideration is being given to easing rules on using multiple types of pensions to allow retirees to choose different combinations from existing, relatively well-understood pension products.

* Proposed default illas, whether provided within or outside a retirement fund, will be permissible as a default option only if they meet strict conditions, including design criteria and limits on investment choices, drawdown rates and costs. Collective investment scheme managers will also be able to provide retirement funds with default illas, provided they meet the conditions.

Treasury says the progress of these reforms will be monitored through detailed compulsory reporting by product providers on annuity (pension) purchases made by individuals retiring from funds, investment charges and the asset mix of illas, and the purchase prices and terms of conventional annuity policies.

GOVT PONDERES COMPLEXITY OF SECURITY FOR LOW EARNERS

Government must still spell out the details of how it intends extending the retirement system to all employed individuals, particularly those in low-income groups and in irregular employment, who are mainly excluded from the current system and rely entirely on the social old-age grant, which will be increased from R1 200 to R1 260 a month.

The Budget Review says the retirement reform proposals released with the Budget “will lay the foundation for the eventual introduction of a mandatory tier of a comprehensive social security system that provides death, disability and retirement cover to all workers”.

The backbone of the extended system is likely to be the proposed National Social Security Fund (NSSF).

Patrick Craven, spokesperson for trade union federation Cosatu, in reacting to the Budget proposals, says the federation is increasingly frustrated by government’s failure to introduce comprehensive social security that will ensure that nobody falls through the safety net.

Cosatu also rejects the piecemeal reforms of the retirement funding system and wants retirement reform to be part of comprehensive social security reform.

But in its discussion paper, Treasury says the situation is complex. Currently, about half of formally employed workers are members of an employer-sponsored retirement fund. An analysis based on a labour force survey carried out in 2010 by the Centre for Research into Economics and Finance in Southern Africa indicates that 86 percent of workers who don't belong to retirement funds earn less than the tax threshold, indicating that they receive no tax benefit for saving for retirement. Of these, nearly 40 percent work in sectors where employment can be erratic