T-DAY VESTED RIGHTS – REASON FOR CONCERN?

Presented by:

Avishal Seeth | Head: Sanlam Umbrella Solutions

REFORM (IN A NUTSHELL)

- Effective 1 March 2016
  - contributions to **pension funds**, **provident funds** and **retirement** annuity **funds** (RAs) are subject to the **same** rules regarding **deductibility**.

RA = PENSION FUND = PROVIDENT FUND

For TAX purposes

RECAP

- Effective 1 March 2021
  - Contributions and investment returns to provident funds post 1 March 2021 subject to annuitisation
- Members over age of 55 who DO NOT change provident funds after 1 March 2021 retain vested rights even on post 1 March 2021 contributions and investment returns thereon
- Members over age 55 that change provident funds post 1 March 2021 will have contributions and investment returns thereon subject to annuitisation from effective date of transfer

BACK TO **BASICS**

Purpose of contributing to a retirement fund?

- To secure an income in retirement…
  - How do you secure an income in retirement?
  - A) Pension / annuity
  - B) Lump sum… but ----→

RETIREMENT AND DEATH BENEFITS OR SEVERANCE BENEFITS

2022 Tax Year (1 March 2021 – 28 February 2022 – No Change from Last Year

Taxable Income (R)	Rate of Tax (R)
1 – 500 000	0% of Taxable Income
500 001 – 700 000	18% of Taxable Income above 500 000
700 001 – 1 050 000	36 000 + 27% of Taxable Income above 700 000
1 050 001 and above	36 000 + 36% of Taxable Income above 1 050 000

BACK TO **BASICS**

Purpose of contributing to a retirement fund?

INTENTION

- Provide an income in retirement
  (not to place additional burden on struggling social grant system)

- Why would you want to take retirement lump sum in cash?
  Tax penalties are imposed

CONCERNS **RAISED**

- Vested rights of those over 55 at 1 March 2021 in the event that they transfer to a new fund post 1 March 2021
  (i.e. contributions and investment returns thereon subject to annuitisation / non-vested portion)

POINTS FOR **CONSIDERATION**

- Why the concern? We've discussed why annuitisation is a good thing and why taking all of your retirement savings in cash probably doesn't make sense…
- Tax penalties?
- Are we making a decision based on the majority of our members or based on the concerns of just a few…

SOME NUMBERS AND MODELLING

- Sanlam Umbrella Provident Fund
- ≈ 130 000 members at 1 March 2021
- Only look at members over age 55 at 1 March 2021
- Considered the above members and their benefits (assume they moved to a new fund 1 April 2021 – contributions to new fund and investment return thereon subject to annuitisation)
  - Value of the members benefit after 5 years (including investment return)
  - Value of pre 1 April contributions and investment return thereon

SOME NUMBERS AND MODELLING

- 9.7% of all members over age 55 at 1 March 2021
- Of these members, only **2.6%** exceed R247 500 after 5 years of contributions and investment returns thereon
- Average non-vested fund credit for these members: **R870 000**
- Average vested fund credit (pre 1 April contributions and investment return thereon) for these members: **R2 450 000**
- So – on average – these ‘affected members’ can take this R2.4m in cash, subject to TAX of approximately, R635 561
- Is this optimal?

CONSIDERATIONS **FOR ADVISORS**

- From a practical perspective, when a Board of Trustees / Joint Forum makes a decision to move the fund they should consider the fund membership holistically and not focus on a small proportion of the membership that may / may not be affected. Conduct an analysis of members that would be affected considering the below data:

  1. Vested benefits that will be transferred (fund credit as at effective date)
  2. Estimation of future contributions and investment returns until retirement date for the affected members from effective date of transfer (non-vested)
  3. For point 2 above, look at number of members where the calculated non-vested benefit exceeds de-minimis (R247 500) meaning that they will have to annuitise

The above will give the advisor an idea of how many members will actually be affected. If this is a relatively small proportion of membership, should the decision to not move a fund be based on a small proportion of the membership?

CONSIDERATIONS FOR ADVISORS

- The second question is: is annuitisation a bad thing?
  - I think that it is generally accepted that annuitisation is better for members in that they secure some income in retirement. In addition, if you take the benefit in cash then the tax effect is quite detrimental.

The current rhetoric around annuitisation being a bad thing does not make sense to me!

IN CONCLUSION

- At an overall level, a Board of Trustees / Joint Forum / Employer should not base a decision to move or not to move on a small proportion of members that could possibly be affected (why would these members want to take 100% cash when the tax effect is so detrimental?).
- Your basis for making this consideration would be that annuitisation is a ‘bad thing’.
- In addition, these affected members would in most cases have a substantial amount of vested benefits transferred to the new fund that they could take in cash (and in doing so incur significant tax liability).

questions

thank you