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LATEST NEWS

NATIONAL TREASURY'S DISCUSSION PAPERS – DECEMBER 2021

DISCUSSION PAPER ISSUED BY NATIONAL TREASURY

On 14 December 2021, National Treasury issued a Discussion Paper, for consultation, encouraging South Africans to save more for retirement - which deals mainly with the two-pot system and auto-enrolment.

Comments are due on or before 31 January 2022. The Paper can be found on the National Treasury website: Treasury.gov.za. Legislation will be drafted as part of the 2022 Budget process.

Government notes that it needs to proceed with caution given the macro-economic issues facing the country and because the pension system is a key pillar of the South African economy.

DISCUSSION PAPER: ENCOURAGING SOUTH AFRICANS TO SAVE MORE FOR RETIREMENT

This Paper deals mainly with the two-pot system and auto-enrolment.

National Treasury states that outstanding retirement fund reforms relate to the following three remaining problems:

> "Coverage: Whilst the current retirement system covers many workers, there remains significant categories of workers who are not participating in any retirement scheme;
>
> Preservation: Many members of retirement funds do not preserve their savings, tending to cash out every time they change jobs. Whilst the default regulations do assist with preservation, significant loopholes remain; and
>
> Costs: Whilst the costs applying to retirement funds might be more transparent, most of the cost structure of retirement funds relates to the size and number of funds, which are not economical".

In addition to outlining the two-pot system, the proposals include legislation to enable automatic/mandatory enrolment of South Africans into retirement funds to expand the retirement funds coverage for more vulnerable, contract, temporary workers and those in the gig economy[1].

Consolidation of retirement funds remains an objective with focus on ensuring funds can take advantage of economies of scale, improved governance and disclosure.

A. THE TWO-POT SYSTEM

The basics of how the two-pot system is proposed to work

This system is aimed at allowing limited withdrawals from funds whilst members are still in employment but at the same time ensuring more retirement savings are preserved until retirement.

[1] "Gig economy" means "a labour market characterized by the prevalence of short-term contracts or freelance work as opposed to permanent jobs" – Oxford Languages.

The Paper identifies that there are two main design problems with retirement funds that lead to low savings when members of retirement funds retire:

- insufficient preservation of retirement funds before retirement, that is, when members leave employment they cash out their retirement savings; and
- members of funds can only access their retirement savings (pre-retirement) if they resign from employment.

National Treasury is faced with resolving two conflicting imperatives:

- encouraging South Africans to save more for retirement; and
- allowing South Africans in financial distress to access a portion of their retirement savings in retirement funds without leaving employment.

National Treasury acknowledges that retirement savings should be used for their intended purpose but that there is a need to allow some access to retirement funds for South Africans before retirement. One of the proposals that National Treasury is considering is the two-pot system which restructures retirement funds into two pots.

Pot one – retirement pot	Pot two - access pot
Preserved until retirement, thus not accessible before retirement	Can be accessed at any time for any reason Members do not need to resign from employment to gain access to this pot. Member can gain access whilst still a member and still in employment
A member can gain access on retirement.	A member can gain access (once a year), unless the full amount is not accessed in any year, in which case another withdrawal in the same year is allowed. There may be a minimum amount that must be in this pot before it may be accessed, for example R2 000
Two-thirds of net contributions starting from date 202X (date to be decided) to go into this pot (net of risk premiums and admin charges)	One-third of net contributions starting from date 202X (date to be decided) to go into this pot (net of risk premiums and admin charges) Withdrawing member pays for the cost of the withdrawal Members will have to update their contact details and may be required to undergo retirement benefit counselling/ financial awareness prior to access After accessing, the member should have the option to increase their contribution rate
Investment growth accrues on the contributions in this pot	Investment growth accrues on the contributions in this pot

Vested amounts – that is, amounts already accrued in retirement funds before the implementation date of these changes

The question remains as to how amounts that have already been accrued in retirement funds, on the implementation date of these new changes, will be treated in the two-pot system. In the Paper, National Treasury calls these amounts "vested amounts" (not to be confused with the so-called vested amounts brought in by compulsory annuitisation on 1 March 2021).

There will be some allowance, after the implementation date, for amounts to be withdrawn from vested amounts when members resign from employment in the future. If a person starts a new job after the implementation date, then there will not be any amounts allowed to be paid on resignation after this date unless vested amounts were transferred in from another fund. National Treasury has asked for comments on how vested amounts can be protected.

Preservation funds

The two-pot system will apply to preservation funds. Preservation funds do not have contributions but have amounts transferred in. The vested rights provisions described above are intended to apply equally to amounts transferred into preservation funds before the implementation date.

Amounts transferred into the preservation fund would mirror the structure of the transferor fund. Members transferring into a preservation fund would still have access to amounts in the access pot in the preservation fund that they had access to in the transferor fund.

Members would not be able to access amounts in the retirement pot until retirement.

If any vested rights are transferred into the preservation fund, then a once-off withdrawal right would apply to that amount (even after the implementation date).

If a member of a preservation fund has not yet accessed their once-off withdrawal and the implementation date passes, the member will still have their once-off withdrawal option on the full amount.

Retirement annuity funds and defined benefit funds

The two-pot system will apply to retirement annuity funds (RAFs) and defined benefit funds. The Government Employees Pension Fund (a defined benefit fund) will probably also be included in the two-pot system.

Immediate partial access

National Treasury is considering whether, despite the many real risks involved with this approach, members should upfront be allowed a once-off partial access to their retirement savings, for example a percentage of retirement benefits up to a maximum of R25 000.

It concludes that if immediate access is allowed this should be restricted to "those with greatest need". This would have to be checked, for example by SARS looking at reductions in income by considering IRP5 certificates or provisional tax payments.

Taxation

A large part of the Paper considers the taxation aspects of the proposals and how taxation may need to change to accommodate the changes. The conclusion National Treasury comes to is that *the current tax treatment for contributions to, and withdrawals from retirement funds is unlikely to be appropriate* if the two-pot system is implemented. Treasury spends some time in the Paper discussing alternative taxation mechanisms in relation to the one-third access pot. This will be part of the consultation process.

B. AUTO-ENROLMENT PROPOSALS

Government is concerned about the high number of workers that are not covered by (members of) a retirement fund because they are informal, temporary, contract, non-unionised, employees of small companies, low income, probationary or gig economy workers as well as sole proprietors or independent contractors. In addition, 30% of workers in the formal sector are not in retirement funds. National Treasury is of the view that this is largely due to retirement funds being voluntary to join.

What is auto-enrolment, according to National Treasury?
Making the employer enrol all employees in a workplace pension scheme or another approved scheme, to which the employer must make a minimum contribution; employees have the option of opting out of the scheme

Thus, National Treasury proposes introducing auto-enrolment to cover a broad spectrum of all formal employees. This would improve retirement coverage and provide risk cover for such employees.

It is stated that auto-enrolment tends to work better for formal salaried employees where there is an employee / employer relationship and that this could be the first step to extending coverage in South Africa. The next step would be coverage for the informal or vulnerable sector where it may be more practical to have a voluntary system backed by strong incentives, FinTech and a default fund.

National Treasury states that an alternative to auto-enrolment is mandatory coverage of all employees within the formal sector and then progress this to include informal sector workers.

It is stated in the Paper that Government *will propose legislation to compel all employers to deduct contributions to an occupational fund or another approved fund, for all their employees*. This would not require employers to establish new funds. Employers would enrol their employees into existing funds, which funds would have to bid for the provision of retirement services or products.