Living Annuities – National Treasury's 2013 Retirement Reform Proposals

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NT’s proposals re Living Annuities

- Fund trustees required to select default retirement product into which retiring members will be defaulted (if they do not opt out)
- Trustees will be guided by a set of principles in making the default choice
- Living annuities will be allowed as defaults – if they meet “strict” conditions
- Trustees must guide members though the process of converting retirement fund capital into retirement income
- CISs will be allowed to provide living annuities

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Principles for Defaults

- NT want trustees to take more responsibility for the post-retirement phase of pension provision
- What are the regulated principles likely to be?
  - Charges (value for money)
  - Defaults (investment)
  - Investment choice (limited)
  - Drawdown rates (prescribed)
  - Conflicts of interests managed (eg in-house products)
- Advice paid for by **fund** on salaried of fee-for-time basis

Questions

- Will rebates be allowed on funds that are included in default LAs?
- Performance fees?
- Reg 28 compliance?
- Active and passive funds?
- How many investment options?
- Drawdown rates – fixed bands?
- Different defaults for different member segments?

CIS-provided living annuities – potential considerations

#	Question	Implications/Comments
1	On which balance sheet do the assets reside?	**If on Life Office balance sheet:** INCOME TAX ACT - Assets are untaxed (Four Fund Approach) - Pensioner pays income tax on drawdown - Assets are protected from pensioner's creditors (SARS GN18) - Transfer from insurer to insurer has no tax implications LONG TERM INSURANCE REGULATION - Insurer is compelled to transfer product to another provider on annuitant's request (Dir 135 & 135A) - Retirement fund rules provide only long term insurance products may be purchased to provide pension - Capital Adequacy Requirements: Life Co: CAR + SAM Linked life licence: was R10million, now 0.3% of assets ESTATE DUTY ACT - No estate duty liability on death

CIS-provided living annuities – potential considerations

#	Question	Implications
1	On which balance sheet do the assets reside? (cont)	**Once on individual's balance sheet (via eg CIS/NT Retail Bond)** INCOME TAX ACT - Capital Gains Tax & Income Tax apply within the CIS – *plus* Income Tax on drawdown i.e. double taxation - No protection from creditors - Transfer by insurer on to individual's balance sheet will constitute a disposal by insurer and result in CGT implications (change of ownership from insurer to individual) PENSION FUNDS ACT n/a THEREFORE - Will be division of assets on divorce (No obligation to utilise assets to generate pension) LONG TERM INSURANCE REGULATION n/a THEREFORE - Individual may wish to transfer to another provider but the existing CIS LA provider not compelled to transfer product - Retirement Funds' rules will not allow the Fund to purchase the LA from any party other than an insurer, therefore only where Fund rules have been amended will a non-insurer LA be allowed.

CIS-provided living annuities – potential considerations

#	Question	Implications/Comments
		- Longevity of product (could be infinite) – CAR requirements for provider of LA: CIS: 13weeks' costs or R600k (greater of) National Treasury ? ESTATE DUTY ACT - Unsure whether or not estate duty obligation arises.
2	Is it desirable for LA product to be purchased without consistent application of consumer protection measures across all qualifying persons?	Inappropriate underlying assets and excessive drawdown amounts can result in complete erosion of pension capital. Current protection: - FAIS Act - Policy Holder protection Rules (Long-term Insurance Act) - ASISA Standard (ASISA members only) - TCF (FSB regulated entities only)

CIS-provided living annuities – potential considerations

#	Question	Implications/Comments
3	Should s37C Pension Funds Act (or similar) apply to all LAs or only to living annuities provided directly by retirement funds – as is current scenario?	Living annuities provided by insurers allow beneficiary nominations - unfettered by the Pension Funds Act
4	Should Regulation 28 be applicable to underlying assets of all LAs?	If so, monitoring and administration of compliance required when underlying funds are used as "building blocks" to comply vs one or more compliant fund/s
5 i)	Wills Act?	If beneficiary nominations are allowed for all LAs, including those on client's own balance sheet, what are the implications?

CIS-provided living annuities – potential considerations

#	Act	Amendment/s
ii)	Collective Investment Schemes Act	• Need to duplicate market conduct standards as provided in FAIS, Policy Holder Protection Rules (not all mancos are required to have FAIS licenses) • Provide for appropriate CAR where LAs are to be offered – bearing in mind longevity of LAs • Compel transfer between LA providers on investor's request and duplicate Registrar of Insurance Dir 135&135A re living annuity transfer requirements
iii)	Income Tax Act	• Provide exemption from taxation (incl CGT) of assets held in LAs • Provide exemption from CGT where living annuity assets are transferred off insurer's balance sheet on to balance sheet of individual
iv)	Insolvency Act or CIS Act	• Provide for protection of LA assets from creditors and on insolvency

CIS-provided living annuities – potential considerations

#	Act	Amendment/s
v)	Divorce Act or CIS Act; Pension Funds Act	• Provide for division of LA capital on divorce with the proviso that the divided capital must be utilised for the provision of a pension for the ex-spouse
vi)	Pension Funds Act	• Require all Fund rules that currently provide for living annuities to be amended by a given date to cater for LAS, alternatively • Deem all such rules to have been amended to allow transfer to qualifying persons who offer LAs
vii)	FAIS Act (or other appropriate Market Conduct legislation?)	• Consider including a requirement for administers of LAs to apply for a LA administration licence – ensure adequate systems in place and that fit and proper requirements are met
viii)	Estate Duty Act	• Ensure all LAs do not attract estate duty on death of LA-holder

Implications for trustees?

- Unless complete equality is legislated across the LA spectrum, trustees will need to ensure that the fundamental differences between the different types of Las are clearly explained to their retiring fund members if CIS and Treasury Retail Bond living annuities are to be offered (see point 4 slide 1)

Thank you

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