



2022 PENSION LAWYERS ANNUAL CONFERENCE

The multiple pots required to give effect to the ‘two-pot’ system

Presented by James Coutinho – Liberty Group



Agenda

- National Treasury ('NT') discussion paper
- NT proposals on the 'two-pot' system
- The current VESTED and NON-VESTED BENEFIT system
- The multiple pots of benefits in the 'two pot' system
- Permutations for retirement funds after implementation date
- Examples
- Considerations before implementation



National Treasury discussion paper

- As far back as 2012, National Treasury ('NT') announced various retirement reforms. The aim was to promote a higher level of savings, to consolidate and standardize retirement funds and to ensure the preservation of retirement fund benefits.
- While most of the retirement reforms announced by NT have been implemented, the most notable being the annuitization of provident fund benefits effective 1 March 2021 ('T-Day'), the retirement reforms on preservation have not yet been implemented.
- A NT discussion paper released for public comment on 14 December 2021 ***'Encouraging South Africans to save more for retirement'***



National Treasury discussion paper

- The NT discussion paper makes four broad proposals:
 - The design structure of a **'two-pot' system** for retirement savings i.e. allowing pre-retirement withdrawals from specified benefits while ensuring that the balance of benefits are preserved until retirement and taken only as a compulsory annuity. This proposal has been supported by industry bodies.
 - Immediate partial access to existing benefits (**e.g.10% capped at R25,000**). This proposal has not been generally supported by industry bodies. Those minority members that have supported immediate partial access suggest internal transfers of a portion of existing benefits at implementation date to the Access Pot. These minority suggestions have consequently NOT been considered in this presentation.
 - **Changes to the tax treatment of contributions and benefits.** These suggestions have not been generally supported by industry bodies. Tax changes will therefore not be explored in this presentation.
 - **Auto Enrolment** to retirement funds or, **mandatory coverage** for formal salaried workers. These proposals are still in the early stages of discussion.



National Treasury discussion paper

- Industry comments were provided to National Treasury at the end of January 2022
- NT will hold workshops during 2022 once it has reviewed the submissions
- The implementation date in the discussion paper is mooted as ‘the 2023 year’ i.e. effective 1 March 2023
- No draft legislation has been released as yet.
- Draft amendments to the Income Tax Act may only be released for comment in July/August 2022
- If 1 March 2023 remains the effective date, the deadline for setting up the various pots of benefits for each fund, changes to the fund rules and communications to fund members will be extremely tight.



NT proposals on the two-pot system

The two-pot system aims to address two disparate problems:

- The need for South Africans to save more for their retirement; and
- The needs of South Africans in financial distress, to access some retirement savings without having to resign from employment to do so.



NT proposals on the 'two-pot' system

The NT discussion paper proposes the following for all retirement funds, including Defined Contribution Funds ('DC'), Benefit Funds ('DB'), Retirement Annuity Funds ('RAs'), Preservation Funds and public sector funds:

A member's benefits accumulated before the effective date, plus returns after that date, will be 'vested'. Although still under consideration, it is understood that members will retain all existing access rights to these 'vested' benefits

1/3 of a member's NET contributions (net of administration costs and risk premiums) made after the effective date, plus returns, will be allocated to an '**ACCESSIBLE POT**'.

The benefits in this pot are accessible at any time-but it is suggested that they only be withdrawn once a year (possibly twice), depending on a fund's ability to effect withdrawals and subject to a minimum value, e.g. R2,000

2/3 of a members' NET contributions (net of administration costs and risk premiums) made after the effective date, plus returns, will be allocated to a '**RETIREMENT POT**'.

The benefits in this pot must be preserved until retirement AND at retirement the full benefit value in this pot must be used to purchase a compulsory annuity, subject to a *de minimis* (e.g. R247,500) e.g. Members of occupational funds will not be able to access these benefits, even if they resign from employment.



The current 'VESTED' and 'NON-VESTED' benefits system

- The 'two-pot' system proposes that members of retirement funds who have accumulated benefits before the effective date, plus returns after the effective date, will retain all their existing access rights to those accumulated benefits.
- However, members' benefits will already comprise one or both of the following 'pots' of benefits:

VESTED BENEFITS: These are benefits subject to vested rights which can be commuted for a cash lump sum in full at retirement.

NON-VESTED BENEFITS: These are benefits are subject to annuitization i.e. up to 1/3 can be taken as a cash lump sum and the balance as a compulsory annuity.

If the total value of the NON-VESTED BENEFITS is R247,500 or less, the full value of the NON-VESTED BENEFITS can also be commuted for a cash lump sum.



The current 'VESTED' and 'NON-VESTED' benefits system

A retirement fund member's VESTED and NON-VESTED BENEFITS will depend on that retirement fund member's age on 1 March 2021 and whether that member was a member of a provident fund (or provident preservation fund) on that date:

Provident fund members YOUNGER than age 55 on 1 March 2021:

All the benefits they have accumulated in their provident fund up to 1 March 2021, PLUS amounts credited and fund returns/growth on those benefits after 1 March 2021 will comprise VESTED BENEFITS and can be taken as cash lumps sum at retirement. The NET contributions that these provident fund members make to their provident fund AFTER 1 March 2021, PLUS amounts credited and fund returns/growth on those NET contributions from 1 March 2021 however, will comprise NON-VESTED BENEFITS and will be subject to annuitization (subject to a de minimis of R247,500) .

Provident fund members 55 or OLDER on 1 March 2021

All the benefits these members have accumulated in their provident fund prior to 1 March 2021, PLUS amounts credited and fund returns/growth on those benefits thereafter will comprise VESTED BENEFITS. In addition, any NET contributions made to the provident fund from 1 March 2021 onwards, PLUS amounts credited and fund returns/growth on those contributions will all ALSO comprise VESTED BENEFITS that can be taken as cash lump sum at retirement. This means that all the benefits that these members accumulate in their original provident fund will comprise VESTED BENEFITS until retirement and will be able to take the full value of their retirement benefit as a cash lump sum.



Multiple pots of benefits

- The pots that are suggested in this presentation are seen as distinct and separate pots of benefits with different bundles of withdrawal and retirement access rights. This follows the NT two-pot proposal.
- Some industry bodies have however suggested proportional transfers of benefits (such as the VESTED and NON-VESTED BENEFITS) at the implementation date to the Accessible Pot and the Retirement Pot, so just two pots remain. However, the access rights relating to those transferred benefits will still need to be tracked by administrators in those two pots. Amalgamating the vested benefits and requiring transfers of benefits at implementation date will add another layer of administration and complexity.
- This presentation does NOT consider such transfer suggestions made by these industry bodies but rather aligns to the principles outlined in the NT discussion paper i.e.
 - that the benefits accumulated prior to implementation date plus returns retain their nature; and
 - the NET contributions after the implementation date, plus subsequent returns be split 1/3- 2/3 into the Accessible Pot and Retirement Pot.



Multiple pots of benefits

The 'two-pot' system proposed by NT will accord different access rights to members, depending on the 'pot' the benefits are allocated to.

Member's benefits accumulated up to the effective date may comprise a 'VESTED POT' with VESTED BENEFITS and/or 'NON-VESTED' POT with NON-VESTED BENEFITS.

1/3 of a member's NET contributions after the effective date , plus returns, will be allocated to an 'ACCESSIBLE POT'

2/3 of a members' NET contributions after the effective date, plus returns, will be allocated to a 'RETIREMENT POT'



Multiple pots of benefits

- While the 'two-pot' system only talks about two new pots of benefits with different rights of access (the 'ACCESSIBLE POT' and the 'RETIREMENT POT') we cannot ignore members with VESTED BENEFITS and NON-VESTED BENEFITS accumulated up to the effective date.
- These benefits are already treated as two existing POTS of benefits with specific rights of access at retirement that fund administrators already cater for.
- For purposes of this presentation, they will be referred to as the 'VESTED POT' and the 'NON-VESTED POT'.
- As administrators must already cater for these two 'pots', the addition of the 'ACCESS POT' and 'RETIREMENT POT' will mean that administrators will at the very least have to cater for 4 POTS, each having different rights of access before and at retirement.
- A 5th POT (55+ RETIREMENT POT) should also be considered for existing provident members who were aged 55 or over on 1 March 2021. These members can then make contributions to the new ACCESSIBLE POT and the 55+ RETIREMENT POT. This 5th POT should specifically allow the benefits in that pot to be accessed as a cash lump sum in full at retirement.



Multiple pots of benefits (5)

Member's benefits accumulated up to the effective date:

1. 'VESTED POT'
2. 'NON-VESTED' POT

3. 'ACCESSIBLE POT'

4. 'RETIREMENT POT'

5. '55+ RETIREMENT POT' FOR PROVIDENT FUND MEMBERS AGED 55+ ON 1/03/2021)



Permutations for retirement funds after implementation date

Pension/Provident Funds

	VESTED POT	NON-VESTED POT	ACCESSIBLE POT	RETIREMENT POT	55+ RETIREMENT POT <u>Original member of prov fund 55+ ONLY</u>
Contributions	Ceased	Ceased	1/3 of NET contributions after effective date	2/3 of NET contributions after effective date	2/3 of NET contributions after effective date (<u>if still in original fund</u>)
Investment Returns	Yes	Yes	Yes	Yes	Yes
Pre-retirement access	Yes (full)- <u>resignation</u> , transfer, winding up	Yes (full)- <u>resignation</u> , transfer, winding up	Yes (full)- can access once (or twice) a year, transfer, winding up	No*- must preserve until retirement, transfer, winding up	No*- must preserve until retirement, transfer, winding up
Death in the fund	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum
Retirement access	Up to 3/3 (full) lump sum	1/3 as lump sum and 2/3 as annuity (3/3 lump sum if R247,500 or less)	Up to 3/3 (full) lump sum	<u>Only 3/3 (full) annuity</u> (3/3lump sum if less than de minimis (e.g. R247,500))	Up to 3/3 (full) lump sum
Exceptions/ Additional rights	*Consideration should be given to emigration, cessation of residence, expiry of SA visa				



Permutations for retirement funds after implementation date

Retirement Annuities

	VESTED -POT	NON -VESTED POT	ACCESSIBLE POT	RETIREMENT POT	55+ RETIREMENT POT Original member of prov fund 55+
Contributions	Ceased	Ceased	1/3 of NET contributions after effective date	2/3 of NET contributions after effective date	N/A
Investment Returns	Yes	Yes	Yes	Yes	Yes
Pre-retirement access	Yes (full)- De minimis (R15,000), emigration, cessation of residence, expiry of SA visa, transfer, winding up	Yes (full)- De minimis (R15,000), emigration, cessation of residence, expiry of SA visa, transfer, winding up	Yes (full)- can access once (or twice) a year, transfer, winding up	No* - must preserve until retirement, transfer, winding up	No* - must preserve until retirement, transfer, winding up
Death in the fund	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum
Retirement access	Up to 3/3 (full) lump sum	1/3 as lump sum and 2/3 as annuity (3/3 lump sum if R247,500 or less)	Up to 3/3 (full) lump sum	<u>Only 3/3 (full) annuity</u> or 3/3 lump sum if less than de minimis (e.g. R247,500)	Up to 3/3 (full) lump sum

Exceptions/
Additional rights

*Consideration should be given to de minis (R15,000) ,emigration, cessation of residence, expiry of SA visa



Permutations for retirement funds after implementation date

Pension/Provident Preservation Funds

	VESTED POT	NON-VESTED POT	ACCESSIBLE POT	RETIREMENT POT	RETIREMENT POT Original member of prov fund 55+
Contributions	N/A	N/A	N/A	N/A	N/A
Investment Returns	Yes	Yes	Yes	Yes	Yes
Pre-retirement access	Yes (full)- One full or partial withdrawal, emigration, cessation of residence, expiry of SA visa, transfer, winding up	Yes (full)- One full or partial withdrawal, emigration, cessation of residence, expiry of SA visa, transfer, winding up	Yes (full)- can access once (or twice) a year, transfer, winding up	No*- must preserve until retirement, transfer, winding up	No*- must preserve until retirement, transfer, winding up
Death in the fund	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3(full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum	3/3 (full) annuity or (full) lump sum
Retirement access	Up to 3/3 (full) lump sum	1/3 as lump sum and 2/3 as annuity (3/3 lump sum if R247,500 or less)	Up to 3/3 (full) lump sum	<u>Only</u> 3/3 (full) <u>annuity</u> or 3/3 lump sum if less than de minimis (e.g. R247,500)	Up to 3/3 (full) lump sum
Exceptions/ Additional rights	*Consideration should be given to emigration, cessation of residence, expiry of SA visa				



Example 1 (Pre-retirement withdrawal)

- Ms. Khumalo was a member of a provident fund on 1 March 2021
- She was 35 on 1 March 2021.
- She had accumulated benefits of R1,000,000 by 1 March 2021.
- She continued making contributions to her provident fund after that date.
- The 'two-pot' system is implemented on 1 March 2023



Example 1 (Pre-retirement withdrawal)

- Ms. Khumalo continues making contributions to her provident fund.
- She RESIGNS from employment and withdraws from the fund on 1 March **2036**, at age **50**.
- Assume she makes contributions of R120,000 per annum and returns of 10% per annum. Figures are rounded up
- What can she access as a pre-retirement lump sum withdrawal and what must she preserve to retirement?



Example 1 (Pre-retirement withdrawal)

Ms. Khumalo's Provident Fund at Withdrawal

	VESTED POT	NON-VESTED POT	ACCESSIBLE POT	RETIREMENT POT	RETIREMENT POT Original member of prov fund 55+
Value of pot on 1 March 2021	R1,000,000	R0	N/A	N/A	N/A
Value of pots on 1 March 2023	R1,200,000	R300,000	R0	R0	R0
Value of pots on 1 March 2036	R4,150,000	R1,040,000	R1,120,000	R2,240,000	R0
Pre-retirement access	Yes (full)- R4,150,000	Yes (full)- R1,040,000	Yes (full)- R1,120,000	No- must preserve until retirement	N/A
Total withdrawal lump sum	R6,310,000 (full lump sum)				
Benefit preserved				R2,240,000 (only full compulsory	



Example 2 (Retirement)

- Ms Khumalo was a member of a provident fund on 1 March 2021
- She was 35 on 1 March 2021.
- She had accumulated R1,000,000 on 1 March 2021.
- She did NOT make any pre-retirement withdrawals.
- The two-pot system is implemented on 1 March 2023.



Example 2 (Retirement)

- Ms Khumalo continues making contributions to her provident fund until **2046**, where she RETIRES from the fund at age **60**.
- Assume she makes contributions of R120,000 per annum and returns of 10% per annum. Figures are rounded up.
- How much of her provident fund benefits can she access as a lump sum at retirement and how much must she use to purchase a compulsory purchase annuity?



Example 2 (Retirement)

Ms. Khumalo's Provident Fund at Retirement

	VESTED POT	NON-VESTED POT	ACCESSIBLE POT	RETIREMENT POT	RETIREMENT POT Original member of prov fund 55+
Value of pot on 1 March 2021	R1,000,000	R0	N/A	N/A	N/A
Value of pots on 1 March 2023	R1,200,000	R300,000	R0	R0	N/A
Value of pots on 1 March 2046	R10,750,000	R2,700,000	R3,540,000	R7,080,000	N/A
Pre-retirement access	R0	R0	R0	R0	N/A
Amount to commute to retirement lump sum	R10,750,000	$1/3 * R2,700,000$ =R900,000	R3,540,000		
Total value of retirement lump sum	R15,190,000 (full lump sum)				
Amount to purchase annuity		$2/3 * R2,700,000$ =R1,800,000		R7,080,000	
Total value to purchase a compulsory annuity		R8,880,000 (full compulsory annuity)			



Considerations before implementation

- Fund rules
- Benefits statements
- Business processes/Tax directive applications/Tax certificates
- Administration and Investment systems
- Investment strategies
- Stakeholder communications
 - Members
 - Trustees
 - Financial advisers



Considerations before implementation

- GEPF/public sector fund pre-1998 benefits
- Non-deductible contributions (tax-free amounts)
- Section 37D reductions
 - Housing loans
 - Maintenance orders
 - Divorce orders
- Pre-retirement partial withdrawals
- Retention of vested rights on transfers of pots of benefits to other funds

THANK YOU

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