PUBLIC COMMENT: TIMING OF UNIFORM TAXATION AND ANNUITISATION FOR RETIREMENT FUNDS IN THE TAXATION LAWS AMENDMENT BILL, 2015

2 November 2015

BACKGROUND

The South African Reward Association (SARA) is a professional body that promotes, develop and empowers the reward profession in South Africa. This includes setting minimum standards for the industry and awarding professional status to eligible members in various reward categories. We also create knowledge-building, sharing and networking opportunities for our members and those operating in the industry. Our intention is to ensure that Reward specialists and managers, human resources professionals and executives dealing with and responsible for Reward management, have the skills, confidence and passion for the reward discipline to make a significant difference in the way organisations position themselves to achieve their strategic objectives.

SARA plays a key role in the professional development of Reward professionals in South Africa through its internationally recognised training and internship programmes. The South African Qualifications Authority (SAQA) approved SARA's application to be recognised as a professional body in 2013.

The SARA membership listing includes corporate firms, government service and State Owned companies. Most organisations listed on the Johannesburg Stock Exchange are corporate members and we currently have 323 organisations in good financial standing, and 24 individual members.

SARA's head office is based in Johannesburg with branches in KwaZulu Natal and Cape Town to serve our members nationally.

URGENT MEMBER SURVEY

We issued an urgent request for SARA member feedback and commentary on the National Treasury call for public comment on the timing of the uniform taxation and annuitisation for retirement funds in the taxation laws amendment bill of 2015 on Wednesday 28 October 2015. We gave our members three days to respond, providing them with the original National Treasury communication (dated 27 October 2015), and provided the following options for our members to vote on:

- Option 1: Which recommends full implementation 01 March 2016;

- Option 2: Which is explained in the attached (this referred to the National Treasury release, and gives sub-options (a) and (b); and

- Option 3: That the retirement reform should not be implemented, with the motivation being that the Labour and Community constituencies at NEDLAC have strongly demanded that Government release the social security reform paper to enable more informed debate of retirement reform. They have argued that retirement reforms present a "piecemeal" approach in the absence of having sight to the complete proposed design of a social security system.

On the back of our member communication, the South African Payroll Association (SAPA) issued the same communication to their members.

RESULTS

We were surprised by the number of responses received in such a short survey period, which included 100 responses from SARA members and as well as a further 19 from SAPA members. We believe the 119 responses received represent an adequate benchmark for market comparison purposes, and also represent a broad perspective of employer views, specifically of those persons operating on a daily basis with employee remuneration and benefits.

The results have been verified and are as follows:

<u>Option 1 – Implemented as per National Treasury recommendation</u>

- 42% indicated preferred option
- 10% indicated less preferred option
- 48% indicated least preferred option

<u>Option 2 – Phased implementation</u>

- 8% indicated preferred option
- 72% indicated less preferred option
- 20% indicated least preferred option

<u>Option 3 – Not implemented as per NEDLAC concerns</u>

- 54% indicated preferred option
- 9% indicated less preferred option
- 37% indicated least preferred option

Summary

54% of SARA members indicated that option 3 was the preferred option, followed by 40% for option 1, and 6% for option 2.

74% of SAPA members indicated that option 3 was the preferred, followed by 15% for option 1, and 11% for option 2.

COMMENTS FROM MEMBERS

We note below some comments from members, as this raises additional concerns and also confirms some of the statements made in the National Treasury notice.

Preferred Option 1

- The essence of these responses is that the market has waited long enough, with enough delays, and it should simply be implemented.
- Another recurring comment was that Option 2 is strongly opposed and that, as National Treasury has a track record of just implementing, Option 3 is not viewed as a possibility and Option 1 is therefore selected.
- "*Good policy to reduce reliance on government*".
- "*Holding back the reforms will not benefit the members in any manner hence it is time to move forward*".
- "*It is important for this to be implemented - especially for Provident fund members, who are not preserving their benefits up to retirement*".
- *"Option 2 introduces more complexity that will increase risk of being rejected. Option 1 will require significant effort from Funds/Employers to change rules etc. - can the FSB cope? Change management will be important*."
- "*Option 2 is too complicated*".
- "*The implementation of retirement reform wef 1 March 2016, will enable employers who currently run with a pension and provident fund, to collapse the two funds into one, retaining the accrued benefit for provident fund members. This will ensure that economy of scale is achieved, and duplicated costs in terms of running two funds, reduced to the benefit of the members as reduced admin costs will result in a higher contribution towards the retirement benefit. As employer we have already pooled the risk benefits between the two funds in*

anticipation of T-day being implemented on 1 March 2015. A delayed implementation as envisaged in Option 2 will result in more complex administration burden to the funds".

It should be noted that a view that is widely shared, as reflected in the above comment, is that Option 1 will indeed practically result in closing of provident fund options. Whilst we appreciate that some employers may rather close the pension fund, the provident fund will require more changes to align with new legislation, than the pension fund. There can be, in our view, very little argument that employers with a dual pension and provident structure are simply duplicating costs in the new dispensation and the trustee-responsible decision would be that only one fund needs to be operated.

<u>Preferred Option 2</u>

Members that voted for Option 2 provided the following comments, but as you will note from their comments, this appears more a lesser-of-two-evils vote:

- "*We … were only given option 1 and 2. But first prize will be option 3*."

- *"… agree with NEDLAC that Retirement Reform needs to be considered in conjunction with the Social Security Reform paper which has not yet been released. Amongst other things, as it stands the monthly pension created by the requirement to annuitise, could as a result of the means test, preclude pensioners from qualifying for the Government Old Age Grant. AND Most importantly the requirement for annuitisation of Provident Fund benefits is problematic in that annuities are currently not cost effective especially for low income earners. Although the recently released Draft Default Regulations paper partly addresses this matter and National Treasury have mentioned that they have plans to open the market up to other players which will further assist there is still too much uncertainty in this area …*".

- "*1) it is already late in the day for payroll development which was aborted in the very early stages following the press announcement on 16 October 2014 on the delay in the introduction of T-Day. 2) there is little time left for the submission and registration/approval of amended retirement fund rules and 3) the proposal for the actuarial formula to calculate the percentage of employer contributions for taxation purposes in terms of defined benefit funds was left up in the air … If however NT decide to go ahead with T-Day on 1 March 2016 then clearly option 1 is far easier and will require only one retirement fund for defined contribution members as from 1 March 2016. Option 2 will be challenging from a member communication perspective and would also necessitate the continuation of our defined contribution pension fund as well as our provident fund up until annuitisation issues …*".

Preferred Option 3

We encourage National Treasury to strongly consider the views expressed by members under this option, which are very closely aligned, and represent some prominent South African employers:

- "*a) Too little time left for system changes and communication to lower level employees who do not necessarily understand the implications. Ideally, reforms of this nature should be announced at the start of the tax year giving employers and funds sufficient time to implement properly. b) Many employees have loans to build homes against their provident funds and this benefit will have to be removed if provident funds need to be annuitized as the loans can no longer be settled at retirement from the cash proceeds of the provident fund*".

- *"…Government has not demonstrated a clear understanding of the intricacies of the retirement/provident funds in South Africa and if they were to rush into the change I believe that we will be once again set up for failure …*"

- "*Option 3 is more viable, having visibility to the social reform paper will enable all the stakeholders to make an informed decision. This will also ensure that there is alignment on the benefits, promote transparency and eliminate any ambiguity*"

CONCLUSION

As SARA, we appreciate that the overarching intentions of these reforms are good and we support those principles. We especially strongly support reforms which were announced proposing more disclosure of fees and which protects the beneficiaries of employer provided schemes.

Changes of such importance should be done within a holistic framework and we can only comment on such framework, and make contribution thereto, once there is an initial policy document in place.

We strongly encourage that the policy framework should be made available, as previously promised, and that informed contributions are then invited and considered, as we agree in principle with the need to reform.

Without having sight of strategic objectives and how those are proposed to be achieved through the social security system, we are concerned that pushing these proposals through will have unintended consequences.

In closing, thank you for the opportunity to provide public comment on behalf of our members on this important Retirement Reform legislation.

We would welcome an opportunity to discuss any of the above with you further at your convenience.

Yours sincerely,

Jerry Botha

Chairperson: SARA Employee Benefits and Tax

Lindiwe Sebesho

SARA President

Chairperson: SARA Advocacy