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irfa dispatch

THE RETIREMENT INDUSTRY NEWSLETTER

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RA or TFSA? How to maximise your retirement savings

If you still want to take advantage of this year's tax exemptions, the clock is ticking. What is the best way to maximise your savings? Theoretically, the most efficient option is investing in a retirement annuity (RA) before investing any excess amounts in a tax-free savings plan (TFSA). However, there are other factors that may outweigh the purely theoretical aspects:

• **Withdrawal considerations.** You can withdraw from a TFSA at any time, and there is no tax on withdrawals. RAs are only accessible at retirement (under normal circumstances), and you need to buy an annuity with at least a part (currently two-thirds) of the accumulated value.

• **Asset allocation considerations.** There are no restrictions on asset allocation in the TFSA, whereas restrictions apply to RAs in terms of Regulation 28 of the Pension Funds Act.

• **Estate planning considerations.** While an RA will not form part of your estate, a TFSA will.

It is generally considered good practice to use the TFSA to supplement retirement savings, even if you have not reached your maximum allowable contribution to an RA.

Only use the cash flow flexibility of a TFSA as a last resort

The flexibility of the TFSA is a great benefit. These investments can be used for emergencies, house deposits, school fees etc. However, it is important to remember the following:

• You can't invest more at a later stage to 'make up' for the withdrawal. The contribution limits of R33 000 a year and R500 000 over your lifetime remain.

• TFSAs are not designed to be used for regular withdrawals over the short term. Rather, their value is maximised when you benefit from tax-free compounding in growth assets over the long term.

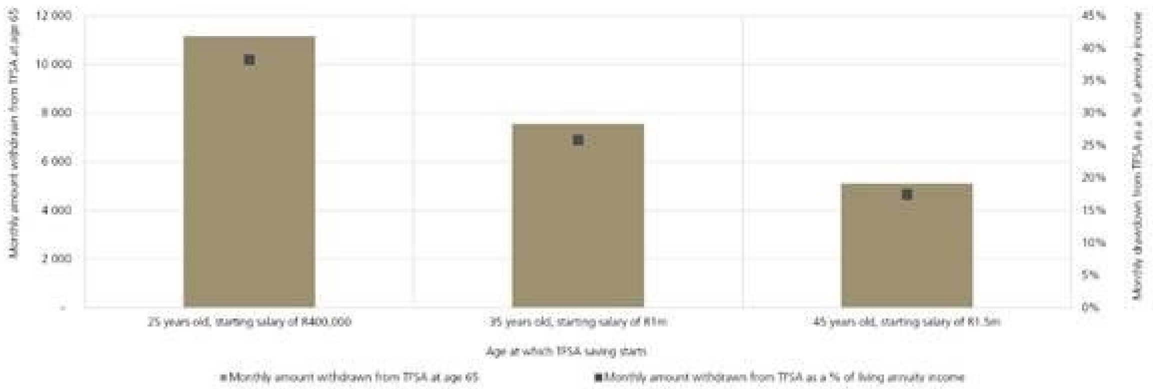
How to use tax-free investing to complement RA savings

A TFSA can make a valuable and flexible addition to your retirement income. The simplified example below considers an investor who saves in a TFSA, while already having contributed 15% of their salary to an RA from the age of 25 years. The investor retires at age 65, converts the untaxed lump sum portion of their RA to a living annuity and selects a drawdown rate of 6%.

Note that the amount accumulated in the RA will depend on each investor's age when starting the investment as well as their income. We assume the investors contribute the maximum R33 000 to the TFSA until their R500 000 lifetime limit is reached.

At retirement, the investor could decide to use their TFSA savings as an additional source of tax-free retirement income. The additional monthly income they can add to their RA income from their TFSA is shown below.

Additional income generated at retirement by drawing on TFSA savings (in today's money)



Assumptions: Lifespan after retirement of 30 years, maximum amount allowed saved in the TFSA. No withdrawals from the TFSA before age 65.

Use TFSAs as part of your overall savings plan

You'll need to consider your financial needs and goals carefully to make an informed choice about the best savings option for you. Remember that to truly maximise the benefits of a TFSA, you need to start investing regularly, and as early as possible – even if the amounts are small to begin with. The sooner you start, the more time your money has to compound and grow tax free. When used as a long-term savings tool, TFSAs can make a meaningful difference to your retirement outcome. A qualified financial adviser can help you understand your options better.

Investing in a TFSA on behalf of minors

A TFSA can be opened by anyone who has a tax number, including a minor. This can be useful for parents who want to start saving for their children. However, be aware that if you exhaust their R500 000 lifetime contribution allowance they will not be able to make their own contributions later in life. On the plus side, they will benefit significantly from the longer period of tax-free compounding!

FA News | 11 January 2019

Retirement Annuities - Plan your current investments today to ensure your desired lifestyle tomorrow

According to Lourens Coetzee of Marriott Asset Management, maintaining your lifestyle in later years should be the core objective of your investment plan. However, to achieve this objective, you are often required to adjust your lifestyle today so that you are not forced to do so in the future.

Employees generally contribute to compulsory pension or provident funds through their employers. More often than not employees know only their market value and have no idea how much income their savings will give them when they retire. According to Coetzee, it is critical to know what income will be generated from your accumulated savings when you are no longer working. “Further to this, income must be converted into a present day equivalent, as the purchasing power of income is affected by inflation over time.

By considering the future level of income in today’s terms, you can gauge whether it will be sufficient to sustain your desired lifestyle,” he said. “Should this not be the case, you will need to make additional voluntary contributions into either a retirement annuity or discretionary product such as a unit trust.”

Coetzee says that one of the most tax efficient means of saving outside of an employer pension fund is through a retirement annuity. Not only is the income earned exempt from all forms of tax, but the contributions made are tax deductible, subject to certain limits. “While the income earned from these savings is fully taxable when being drawn in latter years, the benefits of tax-free capital accumulation from the re-investment of income, coupled with a likely lower marginal tax rate on retirement, makes this a highly tax efficient savings vehicle,” he said.

Contributions to a retirement annuity are flexible, and it is therefore possible to contribute monthly or to invest an annual lump sum before the tax year end in February. Consequently, it is well suited to self-employed individuals or commission earners who do not belong to a company pension or provident fund or have a variable monthly income.

“It is vital to understand that when you are investing in retirement annuities and pension funds, you are investing for income,” said Coetzee. “The income you earn from these investments will fund your lifestyle in the future. This income, therefore, should be reliable and predictable, which will help you to plan with more certainty.”

But how does an investor ensure their investments produce this dependable income? According to Coetzee, there are local and international companies that will continue to produce both reliable and growing income regardless of global slowdowns, exchange rate volatility and varying interest rates. “By including these companies in your retirement annuity, you can determine how much income you will earn from those investments in the future. Informed decisions can then be made as to whether you are saving enough,” he said.

Coetzee also stresses that chasing the best performing unit trust and superior returns do not necessarily help you to achieve your objectives as this brings more volatility and less reliable to your outcome. “This could not only leave you with an income gap in the future, but also cause much financial anxiety along the way,” he said.

To assist investors in this planning process, Marriott have developed a unique online investment planning tool. When transferring an investment into, or making a new investment in the Marriott Retirement Annuity, this tool will be able to demonstrate not only the income currently generated by that investment, but will also reflect a reasonable expectation of the monthly income generated and the capital value at the investor's chosen future retirement date.

"This is based on the principle that Marriott only invests in reliable income streams," said Coetzee. "By knowing this information and being able to rely on it with more certainty, you will be able to adjust your lifestyle today so that your future lifestyle is not left to the whims of the stock markets or the hope of phenomenal future returns."

FA News | 10 January 2019

Have you saved enough for retirement?

Even mid-career, retirement may seem like a distant prospect, and not a high priority amid the busyness of day-to-day living. But retirement can be expensive, and the best way to be ready for it is to start early. So how do you know if you're on track?

In order to retire with an income of around 75% of your final salary, you need to have saved roughly 15 times your annual salary (before tax) at the time you retire. To be on target for this amount, after working for about 10 years (or, around age 35) you should have saved roughly 2.5 times your annual salary (before tax); after working 20 years, (age 45) you should have saved about 5.5 times your annual salary; and by age 60, you should have saved around 12 times your annual salary.

With longevity increasing both worldwide and here in South Africa, the possibility of running out of income needs to be avoided. There are also other factors to consider when calculating whether you've saved enough: what kind of lifestyle do you want to maintain? Where do you plan to retire? The cost of living can vary greatly between different areas, and if your retirement plans include travel and other luxuries, then you need to have more saved than if all you want is a simple life. Will you have anyone depending on you for support? Do you plan to continue working? If you can put off accessing your retirement funds, you can further build your savings, while allowing the amount already saved to keep growing.

As you reach your later years, health becomes a more pressing concern. Treating illness and accidents can put pressure on your savings, so when planning for retirement it is a good idea to provide for such eventualities. (One possibility is to opt for cover that protects you in the event of illness or disability). Similarly, inflation and economic uncertainty can put your savings under strain.

In short: retirement can be expensive, and it is important to begin saving for it as early as possible. Not only does this give you time to accumulate more savings, but given more time, compound interest can generate a good return on your investment.

And, once you've started saving, keep it up. In the event that you change jobs, are retrenched or fired, don't be tempted to eat into your accumulated nest egg. If you can no longer continue your membership in your employer's retirement fund, consider moving your savings into a provident fund, which will safeguard your savings with tax benefits. For example, using Assupol's preservation fund, your savings can stay invested with uninterrupted growth, and will not be taxed until retirement.

So, start as early as possible and avoid drawing on your retirement savings before you retire. Consistency will go a long way to insuring that you have enough to retire on when the time comes and knowing that you are prepared brings great peace of mind.

FA News | 10 January 2019

What happens to your retirement fund benefit when you emigrate?

Expected changes to the income tax laws in March 2019 will allow members who emigrate before they reach retirement date more flexibility to withdraw their retirement funds when they leave the country.

There are a number of ways people leave South Africa to live in another country.

Citizens of South Africa and permanent residents qualify to officially emigrate. Certain emigration allowances are allowed to be taken out of the country. On emigration, one ceases to be a “country resident” of South Africa.

If a citizen or permanent resident merely leaves South Africa to live in another country but does not officially emigrate pending approval by the South African Reserve Bank, that person is still considered a “country resident” and does not qualify for the emigration allowances. That person will continue to qualify for the investment allowances afforded to “country residents”.

Temporary residents who have temporary visas to live in South Africa do not qualify to emigrate because they were never citizens or permanent residents. However, they are usually allowed to take their funds out when they leave South Africa.

A member who emigrates is entitled to have a pension paid to him or her in the country of emigration. However, a fund member, before electing to draw a pension, might prefer to take the pension benefit in cash. If a person was a member of an employer pension or provident fund before normal retirement age and decides to emigrate, the member may withdraw his or her benefit. There is no restriction.

A member of a retirement annuity fund (RAF) is not usually allowed to withdraw from an RAF before age 55 and on retirement is only permitted one third of the benefit in cash. The rest must be used to buy a pension. An exception applies if a member officially emigrates or the member relocates on the expiry of a temporary resident visa. In this case, the member may withdraw the full capital amount.

Currently, a member of a pension preservation fund is allowed one right of withdrawal before retirement. However, with effect from 1 March 2019, the emigration benefit which applies to RAF members will be extended to members of pension preservation funds. (Provident preservation fund members are allowed to withdraw the full amount in cash).

If a citizen or permanent resident relocates without emigrating, a withdrawal benefit of the full lump is not permitted and the member may only retire from age 55.

Advice from the Exchange Control department of your bank as well as a financial adviser should be obtained before a decision to withdraw is made. There are tax implications and the tax payable might differ depending on the timing of the withdrawal and where you are tax resident at the time of withdrawal.

It is important to note that this does not apply to pensioners who are already drawing a pension or annuity income. Pensioners may have their retirement income paid to them in the country of residence but may not access the underlying capital.

Personal | **Finance** | **9 January 2019**

Your company gets liquidated: What happens to your retirement fund?

The fortunes of a company and its staff are inextricably linked. But there is one area where even if the company is liquidated, an employee is not affected – the management of the individual employees' retirement fund.

While a company is responsible for collecting each staff member's contributions made to the company provident or pension fund, once the contributions have been forwarded to the administrator managing the retirement fund, they become assets of the employee. In the unfortunate event of the company being liquidated, creditors of the company have no claim on the retirement funds collected on behalf of employees. Retirement funds belong to the employees and will be safely looked after by the fund administrator. We know of companies that experience cash-flow problems, and the deciding factor is how they choose to deal with it. The key is honest communication from the outset.

There are cases where liquidation is unavoidable, employee retirement funds cannot be attached to cover any debt owed by the insolvent company, as they are not the company's assets, but the assets of the relevant employee. They remain their property until the employee decides how they wish to apply the savings.

There are certain steps to follow in the case of an imminent liquidation, which can soften the blow for the employees and ensure they gain the benefit of their retirement funds.
As the company enters the liquidation process, an effective date of the liquidation will be decided upon by liquidators. The company will cease making retirement contributions to its employees' retirement funds after this date and contributions will remain under the management of the fund administrator.

The date of termination of employment often differs from the effective date of the liquidation of the fund.

Claims are processed as deemed resignations and the fund cannot be terminated without the members being informed of the process the company will be following. In terms of retrenchment packages, these will have to be looked at in terms of the Labour Relations Act and the company should acquire the assistance of a Labour Relations expert to determine if employees have recourse against the company.

In the case of business rescue, the terms and conditions will need to continue on the fund but the fund can be liquidated with the agreement of the members. The contracts are usually suspended on insolvency from a sequestration order.

Risk cover benefits will depend on the date of termination of the fund as well as the risk policy documents. Once the risk benefits have been terminated due to non-payment of premiums, employees are unable to claim any of the benefits.

Whether employees are able to convert risk benefits to personal benefits, will depend on whether the scheme has that conversion option, as well as if the conversion is done within the time frame allowed by the risk cover provider. Employees must be informed of the termination of the risk benefits to ensure there is no open liability should a claim arise after the date of termination.

The process followed for the liquidation of a fund and company liquidation are different. In terms of a company liquidation, once all employee contributions have been forwarded to the fund, the assurer can start processing claims on the funds.

As soon as their employment is terminated, employees have the option to either receive cash (net of tax), preserve their funds tax-free in a preservation fund, or transfer tax-free to their new employer's Retirement Fund. However, there will be a time delay as payments can only be made once the ‘liquidation’ of the Fund has been finalised.

The employer is obliged to make good on the investment of all retirement fund contributions deducted from an employee’s salary. Employers should not be able to access their employees’ retirement funds unless the fund is a self-administered fund under management control, or where the management have not paid over contributions to the fund administrators.

Firms are obliged to continue making these payments, on pain of litigation from the insurance company, which has a claim on those payments on behalf of the employees.
Companies facing liquidation should communicate openly with their staff from the onset. They should explain when the effective date of termination will be, and that contributions will continue to be paid until that date.

This also makes staff aware of the date after which their disability and severe illness benefits will no longer be valid. They can then try to ensure they are in new employment by that date or make provision in their personal capacity.

What the newly retrenched individual chooses to do with their retirement funds, will depend on their situation. When in a financial tight spot, it’s natural to want to dip into our funds, but it’s advisable to try to preserve most of them. Preserving their funds allows the employee to enjoy the benefits of compounding interest over the remaining years of their career.

The liquidation period is one of some stress and anxiety, but employee benefits consultants consulting to the fund can explain options to staff, liaise with the insurance company, and give members their benefit statements. A consultant will also be able to explain the implications of risk benefits such as life cover, disability cover and income protection cover.

In the event of a company’s liquidation, employee rights to their retirement funds remain protected. However, it is crucial that all employees remain involved and aware of their retirement fund position. This means getting regular valuation statements, engaging with employee benefits consultants, asking questions and taking advice.

Personal | Finance | 8 January 2019

INTERNATIONAL NEWS

Superannuation overhaul presented to government could add $500,000 to some accounts

Australians entering the workforce would be up to $533,000 better off in retirement under plans handed to the Morrison government that would weed-out scores of under-performing superannuation funds and force regulators to focus on the interests of consumers.

In its final report into the superannuation system, the Productivity Commission argues people in their mid-50s stood to gain up to $79,000 in retirement from changes that would put both the industry and retail sectors under increased scrutiny and competition.

Admitting some funds are likely to exit from superannuation altogether, the commission has proposed a system that would drive perennial under-performers out of the market with millions of Australians potentially moved into stronger funds.

The commission has strengthened a series of proposals from its original draft report into the superannuation sector, which has $2.7 trillion in assets under management.

One of the biggest moves by the commission is a plan to force all APRA-regulated funds to carry out an annual outcome test across their portfolios.

If investment options fell short of their stated benchmark by more than half a percentage point a year over a rolling eight year period then the fund would have 12 months to sharply lift performance.

If that failed, the product would have to be withdrawn from the market and the super fund member moved to a better performing option. The new system would start from the end of next year for MySuper products.

Up to 2017, 17 MySuper funds covering 1.6 million members and holding $57 billion in assets averaged at least a quarter percentage point their own benchmark returns over the previous 13 years.

The commission estimates getting out of the bottom 25 per cent of funds delivers an average gain of $188,000 to someone entering retirement.

The Productivity Commission has retained its earlier proposal to overhaul how new workers are given a default super fund.

About 450,000 people with $1 billion in super contributions enter the workforce for the first time every year.

These people would be offered a top 10 "best-in-show" list of the nation's best performing funds. This fund, unless the person decided to move their retirement income to another fund, would stick with the worker through life.

The list would be chosen by an expert panel, a proposal that prompted concern that it may be loaded with representatives from a particular part of the superannuation sector or with certain political views.

The commission has proposed the panel be chosen by a group at arm's length from the government of the day, with the commission suggesting the Reserve Bank governor, the head of the Parliamentary Budget Office and the chairman of the Australian Competition and Consumer Commission plus a representative of consumer interests.

The Productivity Commission has also stuck with its proposal to make insurance through superannuation opt-in for people under the age of 25. Insurance would also end on accounts where no contributions have been made for at least 13 months, with the commission finding insurance was effectively eating away the balances of these "accounts. ***Full Report:*** ***https://www.smh.com.au/business/the-economy/superannuation-overhaul-presented-to-government-could-add-500-000-to-some-accounts-20190109-p50qe7.html***

The Sunday Morning Herald (Australia) | Shane Wright 10 | January 2019

South Korea corporate pension funds post sub-par return

South Korea's corporate pension funds posted a sub-par return of 1.88% through the first nine months of 2018 even though assets rose 2.2%, according to the Financial Supervisory Service (FSS).
Total assets of the funds, which are defined-contribution schemes, topped 172.1 trillion won (US$153.5 billion) as at September 30, 2018, from 168.4 trillion won at the end of 2017, the regulator says in a statement on January 7.

Although contributions are "steadily increasing", the annualised return between January and September 2018 was less than the 2.39% average over the past five years, it says. According to the FSS, the below average return was due to the fact that the majority of funds are low-return principal guaranteed type products, and that the overwhelming majority – 91.4% – of members did not provide instructions to rebalance their fund options and allocations.

The South Korean government introduced the corporate pension scheme in 2005 in order to mitigate mounting financial pressure on the public retirement system from an ageing population, a problem which many other countries also face. The United Nations has predicted that the share of seniors in South Korea's population will almost double to 24% by 2030 from 13% in 2016.

The Korean government is worried that contributions and returns of pension funds will be insufficient to cover withdrawals as the population grows older. It has forecast the National Pension Service (NPS), the country's largest public pension plan, to dry up by 2060. NPS, the world's third largest pension fund with 637 trillion won of assets under management, recorded an average annualised loss of 0.57% between January and October 2018.

Latest figures from Statistics Korea show that there were 5.83 million members in retirement pension plans as of June 2017. Of this, 42.1% were members of corporate pension funds. The statistics department says about 66.3% of pensioners overall withdrew their contributions prior to retirement for various reasons, including to purchase homes.

Asia Asset Management | 10 January 2019

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