TUESDAY, 26 FEBRUARY 2019

irfa dispatch

THE RETIREMENT INDUSTRY NEWSLETTER

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LOCAL NEWS

New tax policy proposals announced

In his Budget Speech on 20 February 2019, the Minister of Finance, Tito Mboweni, introduced some new tax policy proposals along with a number of additional tax amendments, which will be introduced this year.

The first of the tax policy proposals, and an item that has been on the government's agenda for a number of years, is **combating Base Erosion and Profit Shifting (BEPS)**. It is important for South Africa to strike a balance between attracting capital and investment, and adequately protecting the corporate tax base. To this end, the government intends to expand the work already under way to combat BEPS and will be reviewing the rules in relation to excessive debt financing against best practice worldwide.

The government will **review its oil and gas tax regimes** as part of its second policy proposal of 2019. The taxation of the oil and gas industry is currently governed by the tenth schedule to the Income Tax Act, 1962, which makes provision for the Minister of Finance to approve a fiscal stability agreement to any qualifying company. The government has not approved any fiscal stability agreements in the past five years.

As the use of electronic cigarettes and tobacco heating products has increased in recent years, the government intends to start **taxing electronic cigarettes and tobacco heating products**. The National Treasury and the Department of Health will consult on the appropriate mechanisms, structure and timing of this tax as its third policy proposal.

There is currently a discrepancy in relation to the fuel sources on which the fuel levy is imposed, which the government proposes to rectify in its fourth policy proposal. The fuel levy is currently imposed on petrol, diesel and biodiesel. However, fossil fuels such as mineral ethanol, illuminating paraffin, aviation kerosene, liquefied petroleum gas, compressed natural gas, as well as biofuels such as bioethanol and biogas, are not subject to the fuel levy. To address this anomaly, government will **review the scope and definition of fuel levy**goods.

The **urban development zone tax incentive** was introduced in 2003 to encourage investment in certain areas in South Africa. Government will review the incentive, which will come to an end in 2020, to determine whether it should be extended, as part of its fifth policy proposal.

As part of its sixth policy proposal, the government will publish a draft **Environmental Fiscal Reform Policy Paper**in 2019, which will broaden the coverage by introducing new taxes that address air pollution, climate change, efficient water use, reducing waste and investigating a tax on "single-use" plastics such as straws, caps, beverage cups and lids, and containers to curb their use and encourage recycling.

South Africa has committed to tackling climate change and has pledged to reduce greenhouse gas emissions. In 2009, the government introduced a tax exemption for income generated from the sale of certified emission-reduction credits. After the introduction of the carbon tax on 1 June 2019, emission-reduction credits could be used to reduce carbon tax liabilities. To avoid a double-benefit scenario, where the same emission reduction leads to both an income tax exemption and reduced carbon tax liabilities, the **tax exemption for certified emissions reductions will be repealed from 1 June 2019**, in the seventh policy proposal.

Currently, vehicles produced locally are taxed at a higher rate than imported vehicles because of the way *ad valorem* excise duty is calculated. To remove this anomaly, in its eighth policy proposal, government will align the tax treatment of ***ad valorem* excise duty on motor vehicles**.

The 2012 Budget proposed a **gambling tax** in the form of a 1% levy to fund rehabilitation and awareness-raising programmes to mitigate the negative effects of excessive gambling. As its last policy proposal, the government intends to publish draft legislation in this regard for public comment during 2019.

FA News | 25 February 2019

How your effective income tax rate has changed

February budget to hit middle income earners harder than high income earners.

When British prime minister Margaret Thatcher came to power in the UK in the late 1970s, inflation had started rearing its ugly head. The minister of finance, Geoffrey Howe, used the opportunity to balance his budget by offering limited relief for fiscal drag. Effectively, the government collected taxes by stealth, something that has become quite common in the tax world – and in South Africa.

When our finance minister Tito Mboweni took to the stage in Parliament for his first budget speech on Wednesday, it was widely expected that personal income tax rates would remain unchanged, but the announcement that tax brackets would not be adjusted for inflation at all came as a surprise. Treasury expects to raise R12.8 billion in tax revenue in this manner. Only marginal adjustments were made to rebates.

But what does this mean for taxpayers? While South Africa's inflation rate is nowhere near that of the UK in the late 1970s (Treasury expects CPI of around 5.2% in 2019), government is raising money in a similar way. It means that even though the tax rate and brackets remain unchanged, an inflationary increase in your salary will increase your effective tax rate.

The impact is probably best explained by way of some examples. The table below follows three individuals below the age of 65 who earned R250 000, R500 000 and R1 million in 2014/15 respectively. We assume their income rose 6% every year. To keep the calculation simple, no tax deductions or credits were allowed. The numbers for 2015/16 are not displayed due to space constraints, but inflationary adjustments to salaries were considered during the year.

The tables below show how the government's budget announcement would affect these fictitious individuals.

Person A: R250k in 2014/15	**2016/17**	**2017/18**	**2018/19**	**2019/20**
Annual income	R280 900.00	R297 754.00	R315 619.24	R334 556.39
Tax calculation	R57 994.00	R62 286.34	R66 881.46	R72 751.98
Primary rebate	(R13 500.00)	(R13 635.00)	(R14 067.00)	(R14 220.00)
Tax per annum	R44 494.00	R48 651.34	R52 814.46	R58 531.98
Effective tax rate	15.84%	16.34%	**16.73%**	**17.5%**
Tax per month	R3 707.83	R4 054.28	R4 401.21	R4 877.67
% increase	–	9.34%	8.56%	10.83%

Person B: R500k in 2014/15	R561 800.00	R595 508.00	R631 238.48	R669 112.79
Tax calculation	R152 559.00	R165 039.12	R177 390.01	R192 160.99
Primary rebate	(R13 500.00)	(R13 635.00)	(R14 067.00)	(R14 220.00)
Tax per annum	R139 059.00	R151 404.12	R163 323.01	R177 940.99
Effective tax rate	24.75%	25.42%	**25.87%**	**26.59%**
Tax per month	R11 588.25	R12 617.01	R13 610.25	R14 828.42
% increase	–	8.88%	7.87%	8.95%

Person C: R1m in 2014/15	R1 123 600.00	R1 191 016.00	R1 262 476.96	R1 338 225.58
Tax calculation	R380 107.00	R406 941.46	R434 656.45	R465 713.39
Primary rebate	(R13 500.00)	(R13 635.00)	(R14 067.00)	(R14 220.00)
Tax per annum	R366 607.00	R393 306.46	R420 589.45	R451 493.39
Effective tax rate	32.63%	33.02%	**33.31%**	**33.74%**
Tax per month	R30 550.58	R32 775.54	R35 049.12	R37 624.45
% increase	–	7.28%	6.94%	7.35%

All three taxpayers will see their effective tax rate rise between 2018/19 and 2019/20. However, the middle and upper-middle income earners (Person A & B) will see it rise more (0.77 and 0.72 percentage points respectively) than the high income earner (Person C), whose effective tax rate will rise 0.43 percentage points.

Moneyweb 22 | February 2019 Ingé | Lamprecht

Pension fund ordered to relook death benefit payment

A pension fund should have exercised better discretion when allocating a more than R1-million death benefit to the deceased's 75-year old mother who already received a State grant, to the total exclusion of his former life partner, the Pension Funds Adjudicator has ruled.
Muvhango Lukhaimane ordered Absa Pension Fund (first respondent) to re-exercise its discretion in terms of section 37C of the Pension Funds Act and consider the request of the complainant, JT Damoense, to be allocated a share of the death benefit.

The complainant was the former life partner of LB Mantjiu who passed away on 4 March 2017. The deceased was a member of the first respondent, administered by Absa Consultants and Actuaries (Pty) Ltd (second respondent). Following the deceased's demise, a death benefit in the amount of R1 065 480.00 became available for distribution to his beneficiaries and dependants. The board resolved to allocate the entire benefit to the deceased's mother, RD Mantjiu, to the exclusion of the complainant.

The complainant submitted she is a nominee in the deceased's beneficiary nomination form and as such, she should have been considered by the fund. The deceased passed away in a car accident together with their minor son. The complainant said that despite the fund's submission that it considered all the relevant factors in deciding to exclude her, it failed to consider the fact that Ms Mantjiu was 75 years of age and received an old age grant from the State which satisfied all her maintenance needs.

She submitted that the board failed to consider Ms Mantjiu's needs, her extent of dependency on the deceased, whether or not only the deceased provided her with financial support and if she received income from other sources. She added that the board failed to consider other sources from whence the deceased's mother could have received some funds and what impact those funds had on her needs. She asked what socio-economic difficulty would have befallen Ms Mantjiu if she was allocated 50% of the death benefit as set out in the beneficiary nomination form.

She further asserted that the board failed to consider her personal circumstances and the fact that the complainant was a nominee entitled to 50% of the death benefit. The second respondent submitted that during its investigation, the board established that deceased's mother, Ms Mantjiu, was a pensioner and was financially dependent on the deceased for maintenance prior to his demise.

She was also nominated to receive 50% of the death benefit in the deceased's beneficiary nomination form. Due to the fact that the deceased had to maintain his mother, she was accordingly identified as his factual dependant. It stated that the deceased was involved in a life partnership with the complainant when he signed the beneficiary nomination form on 5 March 2010. The relationship between the deceased and the complainant was non-existent at the time of his demise.

During their period of break-up, the deceased maintained his son with the complainant. Thus, the extent of financial dependency of the complainant on the deceased was the contributions towards his son's general maintenance and not directly towards the complainant's financial needs. In this regard, it referred to an affidavit signed by the complainant wherein she stated that the deceased provided her with money in respect of their son's maintenance.

The board's investigation revealed that the complainant was gainfully employed and earned R21 000 per month, was 37 years of age and fully able to generate income through her employment. It submitted that even though the complainant was a nominee, the board identified her as not being financially dependent on the deceased. The level of financial dependency to maintain their son did not exist anymore as their son passed away with the deceased.

In her determination, Ms Lukhaimane said in principle a member is legally liable for the maintenance of a spouse and children as they rely on the member for the necessities of life. In the case of factual dependants, where there is no duty of support, a person might still be a dependant if the deceased in some way contributed to the maintenance of that person.

She said having conducted its investigation, the board resolved to allocate the entire death benefit to the deceased's mother, to the exclusion of the complainant. However, she said where there are dependants and nominees, the Act provided for the board to make an equitable distribution. "In the present matter, the amount of the death benefit is R1 065 480.

"Ms Mantjiu was proven to have been financially dependent on the deceased, received an old age pension from the State and was allocated the entire amount of the death benefit. Ms Mantjiu also received a payment in respect of a group life assurance benefit. On the other hand, the complainant who is 37 years of age was excluded and is earning a monthly salary of R21 000."

Ms Lukhaimane said one of the critical sore points was that the deceased completed a beneficiary nomination form assigning 50% of the death benefit to the complainant and another half to his mother. However, the board failed to follow the deceased's wishes. "The board should have considered the complainant on the basis that she was a nominee. The complainant did not have to prove that she was financially dependent on the deceased for her to be considered.

"The mere status of being a nominee compelled the fund to consider her situation together with the totality of other relevant factors." Ms Lukhaimane set aside the decision of the board of the first respondent to allocate the entire amount of the death benefit to Ms Mantjiu, to the exclusion of the complainant, without considering relevant factors. The board of the first respondent was ordered to re-exercise its discretion in terms of section 37C of the Act, considering the issues raised in this determination," said Ms Lukhaimane.

FA News | 22 February 2019

Dodging maintenance? Here's how to get your hands on your ex's pension fund money

One of the key requirements for a court order to be legally binding on a fund is that the fund must be clearly identified by name.

Any parent can approach the maintenance court to ask for an order against the defaulting parent's retirement fund. However, Oupa Segalwe, acting spokesperson for the Public Protector's office, says for a parent to claim maintenance from the other parent's retirement fund, the fund member must ideally have left their employment and their pension or provident fund and must be due to receive a payment from their fund.

This may be if the member resigns, retires, is retrenched or dismissed.

In a recent case where a former Western Cape policeman and father of two was ordered to pay over R344,000 in arrear and future maintenance from his retirement savings to his children, he was with the SAPS for more than 12 years before he was dismissed. Segalwe says if the defaulting parent is still employed, the party seeking maintenance should obtain a garnishee order in terms of which the defaulter's employer will deduct the maintenance from their salary and pay it to the children's guardian. If the parent is self-employed, an order for the attachment of their bank account can be issued. Other options include warrants of execution against their properties to be attached and sold in execution to cover a portion or all the arrears owed, he says.
However, Naleen Jeram, a legal manager at Momentum Corporate and an adjunct professor at the UCT law faculty, says the law allows a private retirement fund to deduct a maintenance claim from a parent's fund benefit while that parent is working and contributing to his or her retirement savings, even though the member is not yet entitled to a benefit from the fund. Jeram says the Pension Funds Act and the Maintenance Act provide, for example, for a mother who does not receive maintenance from the father of

the child or children under an existing maintenance order, to approach the maintenance court for an order against the father's retirement fund to pay the outstanding amount.

He says maintenance orders can be made against pension funds, provident funds, preservation funds or retirement annuity funds. Segalwe adds that the maintenance court usually grants such an attachment order when all other avenues to recover the arrear amounts have been exhausted and have been unsuccessful. In the case of the policeman the maintenance court had granted an attachment order in September 2012 against the father's pension held at the Government Employees Pension Fund (GEPF for maintenance arrears of R40,000. The GEPF failed to pay despite continuous follow-ups from the maintenance court and the mother.

In September 2015, the court issued a new order, attaching the father's pension for arrears of R72,000. Again, the GEPF failed to pay. In November 2016, the mother obtained a further court order for the attachment of outstanding arrears of R104,000 plus R240,000 for future maintenance, totalling R344,000, and yet again the GEPF failed to pay. Having exhausted all her remedies, last year the mother approached the Public Protector for assistance. The Public Protector intervened and raised the matter with GEPF and within five months, the GEPF paid out the monies, Segalwe says.

Jeram says one of the key requirements for a court order to be legally binding on a fund is that the fund must be clearly identified by name in the court order. Most mothers often don't know the name of the fund to which their children's father belongs. They may only know that he has pension monies with an administrator of funds such as Old Mutual or Sanlam or Momentum or only know the name of the employer.

He suggests they approach the fund or the administrator and explain that they are seeking a maintenance order. Jeram says generally fund administrators will be willing to assist where the well-being of children is at stake. What they may not be prepared to provide is the value of the father's fund but this is not relevant because a maintenance claim should be based on the financial needs of the children and what the court has ordered and not on how much he has accumulated in his retirement fund.

In the unlikely event that the fund administrator refuses to provide the fund's name, the mother can obtain a court order ordering the fund to release the information. In the case of private retirement funds, they can turn to the Pension Funds Adjudicator, and in the case of state funds, to the Public Protector.

Full Report: **https://www.businesslive.co.za/bt/money/2019-02-19-dodging-maintenance-heres-how-to-get-your-hands-on-your-exs--pension-fund-money/**

Business Day | 20 February 2019 | Charlene Steenkamp

How to use tax deductions to boost retirement savings

If you don't have cash now, consider contributing a little more each month next year to reduce the tax you pay

February is the last month of the tax year and you may see lots of offers to invest in either a retirement annuity or a tax-free savings account to save on tax. It's only really an option for those who have additional cash in the month of February, which isn't the case for many who have just survived to the end of Janu-worry.

But it is a good time of year to assess whether you could have made more of the tax deductions you enjoy to boost your retirement savings. You are entitled to a tax deduction for any contributions made to your retirement fund or funds of up to 27.5% of your taxable income or remuneration, but limited to R350,000. A deduction enables you to reduce the amount of income on which you pay tax. The R350,000 limit is one that will only affect someone earning over R1.2m a year.

For most people, contributing more than a quarter of their income to retirement savings will be a struggle and so you are probably contributing less than the maximum you can contribute and still enjoy a deduction. Most employer-sponsored funds are set up for contributions between 12% and 15%.

This is why if you are one of those rare people with cash to spare at this time of year, you should top up your retirement savings. If you belong to an employer-sponsored retirement fund or an umbrella fund that your employer contributes to on your behalf, you need to check if the rules of the fund allow you to make an ad-hoc additional contribution in February.

If not, you need to open, or top up, your own retirement annuity.

But, if you don't have cash now, do the calculation and check it again after the budget later this month to see if contributing a little more each month next year won't make a difference to the tax you pay. If you do not already have an automatic increase in contributions set up, ask your employer or your retirement annuity (RA) provider to increase the amount you contribute from March.

Your tax rate and the contribution you make will determine the tax saving.

For example, for this tax year, if you earned between about R200,000 and R300,000 a year, your tax rate is 26% and you can save 26% of whatever you contribute to an RA before the end of February — for example, a R500 contribution before tax year will save you R130.

If you earn between about R300,000 and R420,000 a year, you could have saved 31% of every rand you contributed to your retirement savings — or in the case of a R1,000 top up before the end of February, R310. If you use this saving to further boost your retirement savings, it will enhance your retirement income.

Alternatively, use the tax saving to offset a higher contribution — remember if you save through your employer you get an immediate tax saving on your salary. If you save on your own in an RA, you need to claim the deduction at the end of the tax year and only if your taxes are up-to-date, will you get a refund from the SA Revenue Service.

In both your retirement fund and a tax-free savings account, you can enjoy returns that are free of dividends tax, tax on interest and tax on the capital gains. The difference between the two investments is that contributions to a retirement fund enable you to make a tax deduction whereas contributions to a tax-free savings account are made with your after-tax income.

The reason why investment companies urge you to contribute to their tax-free savings accounts in February is because you can only contribute R33 000 to one of these accounts each year. If that is a limit you are unlikely to get to in a tax year, you don't need to worry about making the most of each year's limit in February – just contribute as much as you can when you can.

Money in tax-free savings accounts can be withdrawn at any time, but remember there is an overall limit on contributions of R500 000 in a lifetime and if you are depositing larger amounts and drawing them out frequently, you could potentially use up that limit. Money saved in your retirement fund should ideally not be accessed until you retire – if you change jobs you can access the cash but you should rather preserve your savings for retirement. If you are saving in an RA, you cannot access your savings until age 55.

When you access your retirement savings, you will pay tax, but at retirement there are generous tax concessions, like the first R500 000 drawn as a lump sum being tax free and your monthly pension will be taxed at a lower rate when you reach 65 and enjoy additional tax rebates. ***Full Report: https://www.businesslive.co.za/bt/money/2019-02-18-how-to-use-tax-deductions-to-boost-retirement-savings/***

Business Day | 19 February 2019 | Laura du Preez

Trending employee benefits -2019

2019 Remuneration Trends

An employee's remuneration package was once carved in stone, consisting of their pay and some standard benefits, like medical aid and pension. However, things are quite different these days, with employers hoping to offer better rewards that entice top talent to join their organisations and stay longer.

Here, we share our views on what workers can expect in 2019.

Designer packages

Flexible benefits will continue to gain popularity with employers this year.
This remuneration model allows employees to decide for themselves how much of their income gets allocated to individual benefits and how much they take home. At any time, provided it falls within limits set by the company, they can rearrange this structure to suit their current lifestyle needs.

So, freeing up cash for a sudden emergency, increasing pension contributions as they near retirement or any other desired change can be made on demand. It's easy to see why employees love it and why it will soon become the norm.

Goodbye, outsourcing

With labour laws being amended around the world to give greater protection to contract workers, companies will find it easier to hire full-time staff to perform previously outsourced work inhouse. This means contract workers may need to settle into permanent positions. However, they will now enjoy the same benefits and protection as other employees whether they remain on contract or not.

Creative EVP

Employee value proposition (EVP) is the complete set of offerings a company gives an employee in return for their qualifications, skills and experience. Expect employers to get creative as they try to design the richest mix of benefits and rewards possible. In addition to the usual benefits, these can include a wellness programme, a say in the organisation's growth strategy, ergonomic working conditions, baby care, and many others. Some companies even offer paid compassionate leave when a pet dies.

However, many benefits will have a tax implication for the employer and the worker. So both parties should carefully consider the impact with the help of their tax advisor.

Lifestyle becomes workstyle

With 24/7 mobile Internet connectivity, the division between work and life will become even more blurred the higher up the corporate ladder one climbs. Executives, managers and even key personnel, like IT staff, are already expected to be available when required. The more work invades their private time, the more they will expect to be compensated for their sacrifice, so employers will have to find attractive rewards to cover this.

A new benefit

The Employee Bursary Scheme is a new kind of benefit. It provides funding for the educational expenses of a worker's immediate family. As with a medical aid, the company contributes a portion that appears on their pay slip as tax free. Although this falls under EVP, it's something we've seen gaining traction and an excellent example of finding ways to help employees retain some of the value they've worked so hard for.

Embracing the trends

The importance of these trends is that they signify the employer's desire to make workers feel more valued, secure and in control. This is especially true of flexible benefits, and we believe that employers who fail to offer this option will quickly see talent drain from their business in the near future. As these and other new trends develop, it's important that employers remain abreast of them or engage the services of a reward specialist who does. Doing so will give them a competitive advantage when attracting and retaining the level of talent required to achieve their business goals

FA News | 25 February 2019

INTERNATIONAL NEWS

State pension rise unlocks billions of euro in savings

Increase will bring the full contributory State pension to €12,911.60 per annum

Thousands of people will have up to €2 billion in pension funds unlocked next month when the Budget 2019 increase in the State pension takes effect. The increase, which kicks in from March 25th alongside other welfare increases set out in the last budget, will bring the full contributory State pension to €12,911.60 per annum.

Crucially it brings the payment above the €12,700 threshold for the first time.

Until now, many people have been forced to lock up to €63,500 of their pension pot with only limited access until they reach the age of 75, unless they have a guaranteed income of €12,700 a year or choose to buy an annuity.

The locked-in funds, called an Approved Minimum Retirement Fund (AMRF), affects those who choose to transfer their pension pot on retirement to a more flexible Approved Retirement Fund (ARF) – keeping it invested and available for transfer to their family should they die. These are an alternative to insurance products called annuities that people can purchase with their pension fund on retirement and which pay a set monthly income for life but die with the annuity-holder.

Annuities have become a very expensive option in recent years, meaning that people's pensions savings often do not provide the income anticipated in retirement. That has led many to opt for the ARF instead.

Threshold

The €12,700 income threshold is designed to ensure people do not fall into poverty in old age. However, many savers have found that their AMRFs are delivering low returns – sometimes even costing them money each year once the effect of fund management charges are taken into account.

Now they will be able to take the money out of the AMRFs and invest it elsewhere with the possibility of greater returns. Tony Gilhawley, an actuary and pensions specialist, says there are no official figures on how many AMRF s are in existence.

Data provided ahead of a paper he presented to the Society of Actuaries with fellow actuary Roma Burke last year pointed to an estimate of 35,000 holders of AMRFs containing total funds of about €2 billion. Mr Gilhawley stresses the figures are sketchy but they are the only ones available at present. They also show that just over half of AMRF holders are 66 or older and so likely to be in receipt of the State pension.

However, to avoid tax, they will need to reduce the size of the pension fund over a number of years. As Mr Gilhawley notes, a person in receipt of the full State pension of just over €12,900 would still be able to draw down €5,000 a year from their AMRF – which confusingly becomes an ARF once the €12,700 annual income limit is passed – without edging over the annual income exemption limit of €18,000.

If they are married and receiving additional benefit for a spouse, the combined State pension of €24,500 leaves them roughly €11,500 below the €36,000 annual exemption limit for couples.

Irish Times |19 February 2019 | Dominic Coyle

We must find the right fix for the UK’s defined benefit pensions

‘Superfunds’ reform could put the system on a sounder footing

Are defined benefit pension schemes really a problem that needs fixing? It may seem an odd question to ask when so many remain mired in funding deficits. The UK’s DB schemes had a collective shortfall of £210bn at the end of January, according to PwC’s Skyval index. But cast your mind back, and that picture isn’t quite so scary. Just three years ago the collective deficit stood at a towering £710bn. Back then people worried that the growing shortfall could presage a series of huge failures, filling the ndustry-funded safety net, the Pension Protection Fund, and tipping more pension funds towards disaster. While the fear has not dissolved entirely, the deficit problem now seems more cyclical than chronic. Should interest rates normalise and shrink pension fund liabilities, it may recede some more.

Which all raises a question about the latest big reform that is proposed for the UK’s 6,000 pension schemes. That is the idea of lumping them into larger units called “superfunds”. It’s a bit like pension insurance buyouts but without forcing companies to stump up the same hefty premiums. The aim is to get benefits of scale, reduce investment risk and give sponsoring companies an incentive to close deficits on the understanding they can cut the link with their fund. To protect members, they need the consent of the scheme’s trustees. True, this may do little to prettify the aggregate deficit. Many companies with the creakiest funds won’t be able to finance the superfund premium. But the reform could still put the system on a sounder footing.

For there are plenty of other ailments menacing the health of schemes. The biggest is the solvency of sponsor employers. Save for those whose liabilities have been “bought out” and passed to an insurer, each scheme relies on the employer’s creditworthiness; something that’s hard to mitigate short of the rare expedient of overfunding. Companies are far from immortal. A 2012 study from the pension consultancy Gazelle looked at FTSE 100 index constituents (among the strongest covenants available) from 1985 and how they had fared in the 27 years to 2012.

A full 7 per cent had failed. A further 26 per cent had experienced financial stress (defined as an event resulting in “a serious impairment in pension funding affordability”). And that’s before you consider the self-inflicted wounds of restructuring. Remember that, before 2007, an employer’s covenant could be hollowed out as conglomerates disposed of subsidiaries to appeal to the stock market’s fashion for more “focused” investments. The future looks no easier, especially when you remember that the ranks of DB employers include few dynamic, growing businesses. They are mostly at the mature end, with a long tail in diminished sectors such as basic manufacturing and high street retailing. These face existential threats to their business, mainly from disruptive competitors. So it’s easy to see how attrition rates could rise.

Nor should one ignore the mindset of company bosses. Most schemes are now long closed and will soon have no members left in the business. According to Ros Altmann, a former pensions minister, that may harden attitudes. “In five to 10 years, there won’t be any connection between this liability and their ongoing business,” she says. “If they cannot afford a scheme buyout, they may just try to engineer insolvency, and hence to push the scheme into the Pension Protection Fund.” So there is a problem to fix, if only to increase the range of options to deal with the bumps that will occur as the DB system slowly runs off over the next three to four decades. At present, the only way companies can break the link is to pay the insurers’ king’s ransom (which few can afford) or — alternatively — to file for bankruptcy and head for the PPF, where employees face an average haircut of 25 per cent on their benefits.

Filling this yawning gap equitably is important. It means balancing today’s investment and jobs with the interests of DB members. The government must resist the urge to protect the insurance industry by regulating superfunds in ways that eliminate the premium saving. Finding the right mechanism isn’t a choice, it’s a must. Indeed the bigger question is whether the pathway to superfunds needs to be wider. Some 42 per cent of schemes are either impaired or at risk of becoming so. As pensions expert John Ralfe points out, few if any of these will have the funds to participate. But helping them aboard may require more than slimmer premiums; it may mean looking at benefit levels too.

Financial Times | 24 February 2019 | Jonathan Ford

OUT OF INTEREST NEWS

Economic growth: SA is almost out of options

Following the same policies can only produce the same outcomes.

One way of defining success is that it is about having options; the more choices you have, the more control you have over your own destiny. Conversely, failure is characterised by being highly restricted in what you can do. It is when your future is largely out of your control.

South Africa’s economy is not quite at total failure stage yet. We would reach that point if we ever had to approach the International Monetary Fund (IMF) for assistance and then have to abide by whatever conditions they attached to a loan – but that is not a likely near-term scenario.

The country is, however, facing something of a last-chance scenario. After the disaster of the Zuma administration and the destruction it caused to South Africa’s governance, its economy and its institutions, the realistic choices from here are limited.

Renewal

In last week's budget speech, finance minister Tito Mboweni had to emphasise the need to renew economic growth. The only way in which tax revenue can be sustainably increased, and national debt brought down, is by growing the economy faster and creating more jobs.

This is not a new message. Every budget speech for at least the last half a decade has made the same point.

Mboweni's comments were therefore neither unexpected nor ground breaking. The question is, what are policymakers actually going to do?

Speaking at a post-budget analysis hosted by Deloitte, Nedbank economist Busisiwe Radebe pointed out that there aren't many levers to pull.

"There are only three ways to stimulate growth in the economy," she argued. "One way is to make money cheap. The second is for government to spend money as it did in 2008 and 2009. And the third is through structural reforms."

Weighing up the options

The way to make money cheap is by dropping interest rates. However, this is not something that can be done in isolation.

"The minute you drop interest rates, you feel the impact of the carry trade," Radebe pointed out. "People will take their money out of the country to where they can get a higher rate of return. That creates a cycle of a weaker rand, and higher inflation. We can't do that because inflation is a tax on the poor."

Government spending is also not a realistic path of action.

"There is no money, so we can't do that," Radebe said. "We would have to borrow money to spend extra in the economy, so that option is not open to us. The credit rating agencies wouldn't like that at all."

The last chance

Which leaves only one viable policy response – to fix and reform the economy.

"It's the only option available to us," Radebe argued. "Instead of taking the little pie we have and slicing it up into even smaller pieces, we have to bake more pies."

Judging by the stance taken by President Cyril Ramaphosa in the state of the nation address and by Mboweni in his budget speech, they both appreciate this. Current economic policy is not working. It is producing levels of economic growth that are simply not high enough.

The reality is that continuing with these same policies can only continue to produce the same outcomes. Government therefore has to reform the economy into one in which it is easier to start a business, is more welcoming of skilled immigrants, and does not place a regulatory burden on companies that outweighs its benefits.

Red carpet

"We need to be more concerned about the jobs we don't have and the businesses we couldn't create due to onerous government rules," said Radebe. "We must make it easier for people to open businesses. If you are a job creator in this country, we must roll out the red carpet for you."

This is the reality that Ramaphosa and Mboweni have appeared to acknowledge. It is, in fact, the reality also acknowledged by the National Development Plan that is still, officially, government policy.

Until now, however, the political will to actually do something about it has been lacking. The hope is that a strong election victory for the ANC will give Ramaphosa, Mboweni and those who share their intentions the space to finally act.

If they can't, or if they don't, South Africa really will be out of options.

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