national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

MEDIA RELEASE

Further details on the 2014 Budget announcements on retirement reform and non-retirement tax free savings products

National Treasury today publishes two papers that provide details on the proposed retirement reforms and tax free savings products as announced by the Minister of Finance in his budget speech last month.

The papers follow on the initial overview document on retirement reform, titled *"Strengthening Retirement Savings: Overview of the 2012 Budget Proposals"* (May 2012). The papers are also consistent with the shift towards a Twin Peaks system of regulating the financial sector, as initiated by the publication of the document titled "*A safer financial sector to serve South Africa better*" (February 2011). In particular, to ensure that customers or members of retirement funds are treated fairly at all times, including after they retire.

The papers released today are:

1) *2014 Budget update on retirement reforms*

This paper provides more details on the retirement reform announcements made by the Minister of Finance in his 2014 Budget Speech. It responds to public comments received in respect of the two papers on retirement reform titled "*2013 Retirement reform proposals for further consultation*" (released on 27 February 2013) and "*Charges in South African retirement funds*" (released on 11 July 2013).

The paper also provides government's response to comments received on findings of the charges paper, and proposes a range of measures to lowering costs, built on a foundation of a mandatory contribution system, optimal preservation, consolidation, and further outlines short, medium and long term reforms in the retirement industry.

This document summarises the process of retirement reform from 2011 until the present, and lays out a future direction for the implementation of reforms over the next few years.

The broad policy goals of the intended reforms are:

- *Implementing auto-enrolment or a mandatory contribution system*: The voluntary nature of our retirement system is a significant factor underlying some micro structural inefficiency in our retirement system. Mandating retirement provision, provided that the process is well managed and regulated, may resolve some of these issues, provided that adequate provision is made for low-income and vulnerable workers.

- *Improving preservation*: The lack of pre-retirement preservation significantly increases workers' financial vulnerability when they retire, and increases costs in the retirement system.

- *Improving fund disclosure*: Without a comprehensive and simple measure of charges in retirement funds, the market for retirement fund provision cannot be expected to function adequately. There is currently no prescribed charge disclosure methodology for retirement funds, and it is imperative that disclosure of charges be improved in the South African retirement industry as a whole.

- *Getting defaults right*: International experience suggests when individuals fail to exercise choice, default options can trigger the 'right' response in a cost-effective way.

- *Consolidating funds*: To reduce the number of funds in order to enhance economies of scale and passing these benefits to members.

- *Simplifying retirement savings products and making them portable between providers*: Too many providers may be competing on the basis of complex product designs rather than on value-for-money for members. A retirement industry based on simpler, more portable products will increase market competition between providers and increase the rewards for market innovations which reduce costs.

- *Ensuring effective intermediation:* An important factor influencing product design in the retirement savings market is the way in which intermediaries sell insurance policies, such as most retirement annuity policies, are remunerated. Intermediaries should be paid in a way which does not create conflicts between their own interests and their duties to their customers.

- *Providing tougher market conduct regulation and more effective supervision*: The government recognises that one of the key lessons from the 2008 Global Financial Crisis is the need for tougher and more intrusive and effective regulation. As is the case with recent global reforms to regulate the banking and insurance sectors more robustly, the savings and retirement sector will need to be regulated more effectively, especially to protect members and improve market conduct practices.

This paper (read with the policy paper titled "*2013 Retirement reform proposals for further consultation*") will form the basis for engaging with key stakeholders (trade unions, trustees, employers, industry) directly and/or through NEDLAC, to finalise the legislative framework for retirement reform. It will also facilitate consultations with ASISA in order to formalise the in-principle agreement to lower costs in the retirement industry.

A formal consultation process will be held once each draft legislation, regulation or further technical paper listed in this document is released for public comment. The set of draft legislative amendments and regulations will give effect to the policy goals over the next year and beyond.

Any new or further comments on this paper can be submitted to Ms. Alvinah Thela, Director: Retirement Funds by email to retirement.reform@treasury.gov.za or per facsimile to (012) 315 5206. The deadline is 30 April 2014.

2) *Non-retirement savings: tax free savings accounts*

This paper provides more details on the non-retirement savings reform announcements made by the Minister of Finance in his 2014 Budget Speech and the Budget Review. The Minister announced in his speech that: *"Legislation to allow for tax-exempt savings accounts will proceed this year, to encourage household saving".*

This paper lays the basis for the legislation that will be published for public comment by July 2014, and for tabling and enactment thereafter in the newly-elected Parliament before the end of the year.

After taking into account comments received on the discussion document titled *"Incentivising non-retirement* savings*"* published in October 2012, government will proceed with the implementation of the tax free saving accounts. This document incorporates revisions to the original proposal based on comments received and from subsequent consultations. It also provides an outline of the administrative requirements and procedures for these accounts.

Most comments supported the establishment of a tax free savings proposal. Many comments were received on the proposal to abolish the interest income exemption. The revised proposal now retains the current interest income exemptions, but it is not intended that the exemptions increase with inflation. This approach should allow a sufficient time for individuals to restructure their financial affairs.

Individuals will be allowed to open one or two accounts, where they may invest in either interest bearing or equity instruments or both types of investments in each account, but total contributions for the tax year may not exceed the annual limit, initially to be R30 000. Unnecessary withdrawals will be discouraged by not permitting replacement of withdrawn amounts. A lifetime limit of R500 000 will also apply.

Institutions that have a banking, or collective investment scheme licence, as well as government, will automatically be eligible to offer products through the tax free savings accounts. Stockbrokers that are registered with the Financial Services Board (FSB) and the Johannesburg Stock Exchange (JSE) will also be eligible to provide investment products through a tax free savings account, provided that products offered comply with the stated principles and characteristics.

Not all market savings or investment products may be appropriate for inclusion in these tax free savings accounts. Most collective investment schemes are the typical type of investment to be included in the tax free savings accounts, along with bank savings accounts, fixed deposits, retail savings bonds, REITs and insurance investment products that meet the stated principles.

In order to ensure that customers are treated fairly, this document seeks to outline a set of principles and characteristics that products should abide by. These include simplicity, transparency and suitability. Direct share purchases will not be allowed although most exchange traded funds (ETFs) will qualify.

Products with contractual periodic contribution obligations (such as insurance contracts) or *excessively* high early termination charges are not considered appropriate. National Treasury and FSB will engage with industry in determining a reasonable early termination charge.

Taxpayers will be responsible for managing their overall yearly contributions to remain within the prevailing limit. Two options to ensure adherence to the annual contribution limits are explored.

Comments on the paper *Non-retirement savings: tax free savings accounts* may be submitted by 30 April 2014, to Mr Chris Axelson, Director: Personal Income Taxes and Savings, Economic Tax Analysis, Private Bag X115, Pretoria, 0001 or by fax to 012 315 5516 or by email to: savings.incentive@treasury.gov.za.

Issued by the National Treasury

14 March 2014