



**PFA DRAFT CONDUCT STANDARD OF 2018
PENSION FUNDS ACT, NO. 24 OF 1956**

DRAFT CRITERIA FOR LIVING ANNUITIES IN A DEFAULT ANNUITY STRATEGY

The Financial Sector Conduct Authority hereby, in terms of Regulation 39(3), read with the definition of 'annuity strategy', in the Regulations made in terms of section 36 of the Pension Funds Act, 1956 (Act No. 24 of 1956) and section 98(1) of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017), publish for public comment the draft criteria for living annuities in a default annuity strategy as set out in this Schedule.

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For THE FINANCIAL SECTOR CONDUCT AUTHORITY

DATE:

SCHEDULE

1. Definitions

In this Schedule, “the Act” means the Pension Funds Act, 1956 (Act No. 24 of 1956), and “the Regulations” mean the Regulations made under the Act and any word or expression to which a meaning has been assigned in the Act or the Regulations bears the similar meaning, unless the context indicates otherwise.

2. Purpose

The purpose of this Standard is to-

- (a) set out the drawdown levels that must be complied with as contemplated in Regulation 39(3); and
- (b) determine conditions for a living annuity to be chosen as part of a fund's default annuity strategy.

3. Principles

(1) The default annuity strategy, established by the board, must represent a fund's best proposal for the average member of that fund in order to assist those members who do not feel comfortable making their own decision at retirement.

(2) The best proposal may be different for different categories of members and may therefore suggest different annuities for different categories, depending on the expected needs and circumstances of members.

- (3) With or In a living annuity, a pensioner is individually exposed to the risks of –
- (a) retirement savings being depleted too soon;
 - (b) poor investment returns on capital; and
 - (c) excessive fees and charges

which could result in poor retirement outcomes, such as unsustainable income streams and a reduction in annuity payments over time.

(4) Where a board determines a living annuity as an appropriate default annuity for members, its default annuity strategy framework must ensure that more protection is afforded to these members compared to the case where a member makes a specific choice to participate in a living annuity based on their own circumstances and research. For this reason, more stringent limits relating to drawdown rates are prescribed for living annuities forming part of the default annuity strategy.

(5) The sustainability of income must be regularly measured and clearly communicated to the pensioner both at inception, as well as on a regular basis thereafter.

4. Sustainable income

(1) A fund must measure the sustainability of income by considering the continued payment of a particular income over the lifetime of a person, where the income payments increase in line with inflation.

(2) The outcome in sub-paragraph (1) may be achieved in various ways:

(a) sustainable income may relate to the monetary amount at the outset that is likely (with a 90% probability) to continue to be paid, with annual inflationary increases, for the expected lifetime of the individual, based on the capital available at inception and assuming reasonable real returns earned; or

(b) sustainable income may be measured as the expected number of years until the capital can no longer support a given monetary drawdown, where the monetary amount increases with annual inflationary increases.

(3) The sustainable income level may result in a monthly pension which is lower than the amount required as a living income.

5. Monitoring sustainability

(1) A fund must establish a mechanism to monitor the sustainability of the income from the default living annuity for any pensioner of the fund.

(2) A fund must ensure that:

(a) communication at inception sets out a reasonable commencement income and drawdown rate. This impacts the pensioner's benefit expectations and must provide details on the risks and sustainability of that pension; and

(b) subsequent communication, which must be at least on an annual basis, provides information on the performance of the annuity and an update on the continued sustainability, including warnings where a pensioner is unlikely to achieve the targets or income in the long-term, with the aim of urging the pensioner to consider alternative actions.

(3) The communication must clearly inform the person that there is no guarantee that the plan is sustainable, even if all the recommended actions are followed.

(4) (a) Where the living annuity is paid by a fund, or is a policy in the fund's name, it is the responsibility of the fund to provide communication to its pensioners, at least on an annual basis.

(b) Where the annuity is paid directly to the person by the long-term insurer, the fund must ensure that the long-term insurer issues relevant and

appropriate communication to the pensioner, both at inception and at least on an annual basis thereafter.

6. Drawdown limits for a default annuity strategy in the form of living annuities

The maximum drawdown rates have been determined by age band and gender, since these relate to limits to preserve sustainability, which depends on longevity.

Age	Males	Females
55	4.5%	4.0%
60	5.0%	4.5%
65	5.5%	5.0%
70	5.5%	5.0%
75	6.0%	5.5%
80	7.0%	6.0%
85	8.0%	7.0%

- (1) The maximum permissible drawdown rates are as set out in the Table above.
- (2) The board must determine the appropriate drawdown rates for the member and must apply lower drawdown limits, where applicable. For example, the drawdown rates should be lower in the following circumstances:
 - (a) Where the underlying portfolio chosen for the living annuity is conservative; or
 - (b) Should the annuity be in respect of a couple, rather than an individual.
- (3) While the maximum rates reflected are based on certain assumptions, over time factors change and markets move.
- (4) The Table defining the maximum drawdown rates is not suitable to consider reasonableness of income or its adequacy in meeting living expenses.

7. Short title and commencement

This Standard is called the Conduct Standard on Default Living Annuities and commences on 1 March 2019.