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9 November 2015

Mr Allan Wicomb
Secretary
Standing Committee on Finance

c.c. Ismail Momoniat National Treasury
Chris Axelson National Treasury
David McCarthy National Treasury

TAXATION LAWS AMENDMENT BILL, 2015

The letter (and related documents) dated 5 November 2015 from Y Carrim, MP refers.

Given the very short time frames, we have not had the opportunity to canvas the views of all our colleagues at Towers Watson, but set out below are our thoughts on the various options.

1. Our strong preference is for "Option 1" as described in the media statement, namely the legislation as it stands but with a higher *de minimis* limit. Clearly this option requires the least change to payroll and administration systems and there is no need to restructure retirement funds in the short term.

2. We note that Option 2 does not meet Government's objectives of "horizontal equality" and annuitisation for provident fund members (if agreement on this issue cannot be achieved for 2018).

3. If Option 2 is implemented, it is critical that certainty is provided now as to what, if any changes, will be made in 2017 or 2018.

    - All the stakeholders (including members, trustees, consultants, payrolls and administrators) need certainty so that they can restructure payrolls and funds and amend fund rules as appropriate and if necessary allow members to transfer to different retirement arrangements.

    - Without such certainty, funds will not be able to do anything timeously and will be in a similar position late next year awaiting any proposed changes, and with the same problem of insufficient time to properly implement any changes.

    - Uncertainty results in a material communication dilemma for both funds and employers and ultimately leads to members receiving mixed messages, the result of which is further confusion and mistrust (in employers, Government and the retirement system) by members.
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4. We have several material concerns with Option 2, namely:

    - Allowing member contributions to provident funds on a pre-tax basis in 2016 will be a material financial gain to many members, but the reversal of the position in 2017 when the 10% limit applies will be very problematic, because for many members it will mean a drop in take-home pay in March 2017. Members may look to their employers to make up the shortfall in take-home pay, which is not reasonable, and members may use this as a "platform" to militate against the tax reforms.

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- Further to the previous bullet point, if Option 2 is followed and annuitisation of provident funds cannot be implemented in 2018, it may be more sensible to leave provident funds completely unchanged for 2016 (i.e. the 27.5% would not apply although possibly the R350 000 could apply to employer contributions) and then move into the 10% and R125 000 limits in 2017. This would prevent the problem of an increase followed by a reduction in take home pay for employees.

- Current provident funds with a wide range of membership by salary band will have difficulties in restructuring in a way that suits all members in 2017. Lower income employees may favour remaining in a provident fund, whereas higher income employees may favour converting to a pension fund. It may not be economically feasible (in terms of expenses, governance and death and disability benefit costs) to "split" the membership between a pension fund and a provident fund, and such an increase in the number of retirement funds would in any case be contrary to Government's intention to consolidate the number of retirement funds.

- Further to the previous bullet point, allowing retirement funds to register as both a pension and a provident fund with clearly demarcated membership in each section would resolve this problem and could be considered over the next year if Option 2 is selected.

- The uncertainty as to what will be implemented in 2017 and/or 2018 may lead funds to "do nothing" or to implement changes which will then have to be reversed. Neither scenario is ideal.

- If Option 2 is followed, "vested provident rights" would need to apply to any monies transferred from a provident fund to a pension fund after 1 March 2016.

5. Two further issues which were addressed at the presentation by Mr Momoniat on 30 October 2015, but which we note here for completeness, are as follows:

   - We recommend that the "defined benefit regulations" are issued **as soon as possible**, as employers, funds and valuators need them to calculate the resultant employer contribution rates (and if necessary restructure benefits or allow members appropriate options).

   - The R350 000 cap is now two years old and we recommend it is indexed with inflation for 2014 and 2015. National Treasury noted at the meeting that Rand limits are split into different categories which require either annual or periodic revision. We would suggest that the R350 000 cap falls into the former group.

6. With regard to the wording of the legislation, we would note that:

   - The *de minimis* limit in the legislation is R165 000 which equates to a total retirement benefit of R247 500, whereas the media statement refers to a limit of R250 000. The two figures are very close, but clarity should be provided on which amount is intended.
   - On page 5 line 25 to page 6 line 25, the definition of "pension fund" is amended to allow for protected rights to previous provident funds. However, the references in (b)(iv)(a) (page 5 line 60 to 62) and (b)(iv)(b) (page 6 line 10 to 11) refer to the person being a (current) member of a provident fund. We suggest these references be suitably amended to clarify that they refer to amounts transferred from a provident fund in respect of people who meet the requirements of the references.

     The same comments apply to:

     - Page 6 line 54 to 55 and page 7 line 3 and 4.

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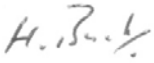
- Page 8 line 13 to 15 and page 8 line 25 and 26.
- Page 9 line 6 to 7 and page 9 line 17 to 18.
- Page 9 line 58 to 59 and page 10 line 8 to 9.

- On page 8, line 21 to 24, the references to “subitem (A)” and subitem (B)” should be to “subitem (i)” and “subitem (ii)” respectively.
- On page 8, line 32 to 35, the references to “subitem (A)” and subitem (B)” should be to “subitem (i)” and “subitem (ii)” respectively.

We note that we do not believe that it is necessary for us to make oral submissions to the Standing Committee on Finance in relation to the above comments.

If you would like us to explain or elaborate on any of the above comments, please let us know.

Yours sincerely



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