national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Hon. MJ Maswanganyi, MP
Chairperson: Standing Committee on Finance
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Dear Honourable Chairperson

NATIONAL TREASURY SUBMISSION IN RESPONSE TO CALL FOR SUBMISSIONS AND COMMENTS ON THE PENSION FUNDS AMENDMENT BILL, 2020 [B30-2020]

In response to the call for submissions and comments on the Pension Funds Amendment Bill, 2020 [B30-2020] ("the Bill"), the National Treasury sets out below submissions in respect of the Bill. The National Treasury requests an opportunity to make submissions at the public hearings on the Bill which are scheduled to be held on Wednesday 19 May 2021.

The Notice indicates that the Bill would amend section 19 of the Pension Funds Act, 1956 (Act No. 24 of 1956) ("the Act") to enable pension fund members to obtain a loan, secured by a guarantee from a registered pension fund, to alleviate financial pressure during the COVID-19 emergency or any other emergency similar to COVID-19. A registered pension fund would be enabled to offer a guarantee to a pension fund member of a maximum of 75% of their share in the value of the fund.

Before outlining some specific concerns, it must be noted that no economic or financial impact study has been submitted on the draft Bill. Aside from the direct impact for specific funds or their members, the Bill has not taken into consideration the implications on the liquidity of funds, given that member contributions are invested in terms of a long-term investment plan, and that any change in the current investment profile of any retirement fund will have a direct bearing on the growth and sustainability of such fund. There is also no impact study on more macro-objectives like the impact on household savings, nor is there any indication on the impact on current tax incentives and preservation objectives of the broader retirement fund reform programme.

The National Treasury appreciates the objective of the Bill of providing relief to those members of pension funds who are temporarily without income or are in serious financial difficulties as a result of the current COVID-19 emergency. National Treasury is aware of the hardship under COVID on many households, and the need for relief measures, and has made significant announcements in this respect. However, in doing so, it is critical to ensure that we

do not compromise long-term policy objectives. Government has since 2011 developed a comprehensive policy framework to inform retirement reform, and to encourage South African households to save for their retirement. The Minister of Finance also announced recently in the 2021 Budget and 2020 MTBPS that legislation will be introduced later this year or early next year to allow for limited withdrawals from retirement funds under certain circumstances, but to link this with mandatory preservation. Treasury is currently following up on the Minister's announcement, and engaging with relevant NEDLAC stakeholders. The issues are complex, and enacting a piecemeal amendment to section 19 would potentially result in significant undesirable and unintended consequences, resulting in members drastically reducing their retirement savings in the worst scenario.
The current focus of the National Treasury is to provide relief in a manner that is consistent with ensuring the long-term financial security of pension fund members, and that they have appropriate provision for retirement. It is envisaged that the National Treasury will introduce appropriate amendments in Parliament through a Financial Sector Laws General Amendment Bill during the next 12 months.

The comments below will therefore be restricted to a few of our major concerns, and are not comprehensive, as many critical operational details are missing. We also request more detail from the sponsor of the Bill, and to provide a detailed socio-economic impact study, as is required of all legislation that the executive introduces to Parliament. Many of the statements made in the Memorandum on the Objects of the Bill are also not valid in our view, and needs to be supported by hard evidence.

It is indicated in the Memorandum that, "by enabling a member to access a pension-backed loan, that member will be able to leverage their pension fund investment prior to their retirement date, without eroding their provision for eventual retirement. Lending institutions will be enabled to offer loans to pension fund members at competitive interest rates and over extended or deferred payment periods given that the loan is fully guaranteed." The National Treasury would highlight that if a member ends up defaulting on the loan, it would substantially erode their retirement savings. It must also be noted that it is not certain that a competitive interest rate would be granted, and the loan might still unaffordable for the pension fund member. The scope for abuse of such loans has also not been considered.

Government is sympathetic towards the difficulty many South Africans are facing currently, and has continuously been engaging with the regulators and other key stakeholders to work out relief measures for consumers. To date, measures have been implemented to ease the plight of some members. A contribution suspension was enabled through a communique issued by the Financial Sector Conduct Authority ("FSCA") to retirement funds in late March 2020, informing them that employers and/or employees who are experiencing financial distress can consider using existing enabling rules to suspend or reduce retirement funds deductions and contributions, after engagement with the fund. Funds which do not have such rules can urgently apply for their registration with the FSCA, which has already put in place a mechanism to fast-track their processing.

Members who were even on zero salary during this recent period continued to enjoy risk cover in the majority of cases, and preserved their fund credit. They continued to enjoy such risk cover during this period of suspension without reducing or encashing retirement savings. In effect, members have been retained in the retirement savings net which is the aim of retirement funds.

Government has also provided temporary relief to living annuitants by allowing for draw down rates to be reduced to 0.5% (current minimum 2.5%) in order to protect underlying assets. However, for many other living annuitants their living annuity might be their only source of income. For this group of individuals, Government has allowed for a temporary increase to their draw down up to 20% (current maximum 17.5%). Further, the *de minimus* threshold for commutation of small living annuity capital values has been increased to R125 000 (previously R50 000 or R75 000).

Retirement savings being used as security for loans will result in further or new indebtedness of members, and it will also be difficult to supervise or monitor what the money is used for. Pension Fund members might also not understand why they should incur debt when they may view their pension fund interest as being akin to having their “own savings” that they should be able to access and use as they may wish.

The current restriction in section 19 of the Act on granting loans in relation to pension fund interests is based on the policy position that retirement benefits should be preserved for the member’s retirement. The exception of allowing a loan in relation to immovable property is viewed as being consistent with ensuring the long-term security of the member, as the ownership of immovable property also promotes financial security during retirement. Granting loans for other purposes may be inconsistent with that objective. If a guarantee may be granted to obtain a loan which could potentially be used for any purpose, it will not adequately ensure the long-term security of the pension fund member.

The National Treasury does not support that pension fund benefits may used as a guarantee to obtain a loan, and in particular that a guarantee of up to 75% of the pension fund interest could be granted. Incurring substantial indebtedness could certainly have a significant impact upon the pension fund member’s financial security over the long-term, including potentially into their retirement years. If the loan ultimately was defaulted on, and the pension fund was called upon to pay the guaranteed loan, that would substantially impact upon the person’s long-term financial security in retirement.

While a pension fund providing a guarantee would assist a member to obtain a loan, and might enable a loan to be obtained at a more favourable rate than might otherwise be granted, the actual rate of the loan would still be subject to determinations by individual lending institutions, so the rate at which loans would in fact be granted is certainly not definite and cannot be guaranteed. A pension fund member would still be incurring debt, which may potentially be substantial, and be undertaking significant obligations as a result, which the pension fund member still might find challenging to satisfy.

The Bill would potentially enable pension fund members to incur substantial indebtedness that could significantly negatively impact their long-term financial security, without oversight or requirements in relation of the use for of the loan funds, that would sufficiently ensure the long-term financial security of the member. Under section 19 as it currently stands, abuses have been identified, and the potential for negative impacts would be substantially greater under the proposed amendment to section 19 in the Bill.

Retirement savings by South Africans have been extremely low for a lengthy period, and have not shown any signs of improvement. The recent 10X 2020 South African Retirement Realities Survey, for example, found that 49% of people surveyed say they don’t have a retirement plan. The number of South Africans who feel good or pretty good about their retirement plan remains very low at 30%. 69% of people surveyed said they had no retirement plan at all, or just a vague idea. A mere 6% of South Africans surveyed said they were executing a retirement plan that they had properly thought through, which is similar to the National Treasury’s estimates that only 6% of South Africans have sufficient savings for a reasonable retirement. Enabling access of up to 75% of a person’s pension interest would erode the already extremely low levels of retirement savings.

The proposed Bill would only benefit a small minority of pension fund members. The granting of loans proposed in the Bill in relation to pension fund interests would be subject to the affordability requirements of the National Credit Act, 2005 (Act No. 34 of 2005), as the legislation does not explicitly provide otherwise. This would preclude relief being accessed by those pension fund members who do not have sufficient income to meet affordability requirements, or might be blacklisted, which would be inequitable. Significant numbers of pension fund members who are in the greatest financial distress might potentially not be able to access the envisaged relief.

The Bill would create significant burdens for pension funds, and hence on members of such funds. It would be necessary for the Boards of pension funds to make a determination on a case by case basis, which would be very onerous for the Boards. The granting of guarantees by pension funds would result in potentially substantial contingent liabilities for the pension funds. If a guarantee granted to back a loan is called upon, the pension fund would be required to make a quick sale of assets.

The Bill is silent on the tax implications of using a guarantee for up to 75 per cent of the members' fund assets. Any adjustment to the tax regime would require a separate money bill. The current tax regime would require that any payouts from the fund that are made before retirement are taxed according to the withdrawal tax table. Payouts from retirement funds are taxable since the contributions are made before tax is paid, otherwise the income could be received completely tax free. The tax on withdrawals before retirement ranges from 18 per cent on amounts above R25,000 up to 36 per cent on withdrawn amounts above R990,000. If a guarantee is called because the member can no longer service a loan, the retirement fund assets that are withdrawn to honour the guarantee would be subject to this tax. If the guarantee ensures that the post-tax amount of the loan is paid to the loan provider, there may be cases where more than the full amount of the available retirement fund assets is used to service the debt. There would therefore be nothing left in the fund for the member in such a case, and may also create an additional liability that cannot be serviced by the individual's assets.

The National Treasury, therefore, does not support any Bill that provides for the granting of loans backed by a guarantee from a pension fund. The Bill does not sufficiently protect the long-term financial security of pension fund members and the necessity of ensuring that they have adequate financial resources for their retirement -on the contrary, it brings great risk to these objectives. It is critical that any measures to provide access to retirement fund benefits must be balanced with the mandatory preservation of retirement savings.

The National Treasury appreciates the concerns informing the legislation, and the National Treasury and the FSCA will continue to engage with stakeholders regarding various possible measures that could be undertaken to provide any urgent relief to individuals who have been severely financially affected by the COVID emergency. These measures, however, cannot undermine the key objectives for the retirement reform programme adopted by Government since 2011, and it is for this reason that we believe that the Bill cannot be supported by Government.

National Treasury will be happy to make a presentation to the Standing Committee on Finance, where more detail on some of the implications of the Bill can be presented.

Kind regards,

Submitted electronically without written signature

ISMAIL MOMONIAT
DEPUTY DIRECTOR GENERAL: TAX AND FINANCIAL SECTOR POLICY