

Governance, Legal, Compliance & Sustainability



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ON THE SCALES 4 OF 2024

FSCA Communication 3 of 2024 – rule amendments for Two-pot changes

The FSCA have issued a communication informing funds what should be contained in rule amendments to cater for the Two-pot changes, as well as their expectations on member communication.

The term 'pot' and 'component' are used interchangeably in this publication.

Summary

- Funds rules to allow for:
 - vested, savings and retirement pots

- seed capital allocation from the vested pot to the savings pot
 - split of contributions between the savings and retirement pots
 - transfers and section 37 deductions
 - specific requirements for defined benefit funds
- Member communication should be simple, clear, comprehensive, timely and on-going.

Fund rule amendments

From 1 September 2024 fund rules should include wording that deals with the following.

Vested component

Establish a vested pot in the rules to house existing members' current benefits in retirement funds up to 31 August 2024. No further contributions will be made to this vested pot, but investment return will apply to the balance in the vested pot.

Allow provident fund members who were 55 years or older on 1 March 2021 and who remained members of the same fund until 1 September 2024 to elect whether to participate in the Two-pot system or remain as contributing members according to the pre-1 March 2021 regime.

Allow members to receive the vested pot in cash on termination of employment before retirement.

Contributions

Contribution rules must specifically cater for contributions into funds (including pension funds, provident funds, preservation funds or retirement annuity funds) to be allocated one-third to the savings pot and two-thirds to the retirement pot.

Seed capital

Seed capital of 10% of the value of the member's share in a retirement fund immediately before 1 September 2024, subject to a maximum of R30 000 (thirty thousand rand) must be allocated to the savings pot.

Seed capital will not be applicable to the following types of members:

- Unclaimed benefit fund members
- Pensioners
- Beneficiary fund members
- Members who, on or before 31 August 2024, had exited service and completed and submitted an election form
- Non-contributing members of terminating funds and funds in liquidation.

Savings Component

Establish a savings pot to be credited with the seed capital, plus one- third of contributions and investment returns from 1 September 2024.

The savings pot may be reduced by withdrawals equal to or more than R2000 once in any tax year.

The rules must state that:

- any withdrawals from the savings pot before retirement will be taxed at marginal rates
- any cash withdrawals at retirement will be taxed in accordance with the retirement tax table.

Retirement Component

Establish a retirement pot to be credited with two-thirds of contributions and investment return, accruing from 1 September 2024.

The rules must say that money in the retirement pot cannot be accessed as a cash withdrawal or on resignation from employment.

The amount must be used to provide an annuity subject to the *de minimis* amount and that the annuity will be taxed as and when it is paid to the pensioner.

Defined Benefit Funds

If a part of the savings pot relating to the seed capital is paid to the member before retirement, the pensionable service of the member would need to be reduced to make this payment financially neutral to the fund at the time of payment.

The fund's valuator will need to calculate the capital equivalent of the 10% of pensionable service before 1 September 2024 and one third of pensionable service after 1 September 2024, adjusted for any prior cash payments already made from the savings pot. This will be the value of the savings pot at the intended cash payment date.

Once the member has decided on the amount to be paid, the valuator will be required to calculate the service given up by the member representing the value of the cash payment made and the reduced pensionable service that will be available at retirement in calculating the pension. The definition of pensionable service in the rules will require amendment to allow for this.

An appropriate reduction of the period of service would have to be made for members of defined benefit funds withdrawing from their savings pot before retirement.

If the fund adopts a different methodology, this must be approved by the FSCA in advance and then set out in the fund rules.

Transfers of components

The rules will need to contain requirements relating to transfers, including

- transfer from the savings pot to the retirement pot in the same fund
- a prohibition on transfers into the savings pot, other than the seed capital from the vested pot
- transfers of the savings and retirement pots between two funds but they must be transferred together
- the transfer of vested pots is subject to current rules.

These transfers will be tax neutral and there is no need to make provisions in the rules for tax implications.

Section 37D deductions

These deductions include divorce and maintenance order deductions, housing loans and employer compensation due to the fraud, theft, dishonesty or misconduct of a member.

Fund rules should allow for section 37D deductions to apply proportionately across all three pots.

Member Communication

Funds must communicate the Two-pot changes to members in a manner which is simple, clear and comprehensive and such communication must be timely and on-going as may be required.

The communication should alert members to the impact that any withdrawal from the savings pot will have on the value of the member's benefit. This can be done by way of illustration using examples.

The FSCA may request a copy of the communication issued by the fund or administrator to members.

Benefit statements will need to be adjusted to reflect the different pots and transactions.

Submission of Two-pot amendments

Amendments to allow for the Two-pot changes should not contain other rule changes This will save time when the FSCA consider the Two-pot rule amendments because proposed changes would have been agreed upon in principle.

Extension

If required, funds may apply for to the FSCA for extension to submit their rule amendment.

Comment: Alexforbes has submitted a template Two-pot rule amendment to the FSCA and we are waiting for feedback. Once we have finalised the in principle amendment, we can start drafting rule amendments for funds under Alexforbes' administration.

If you need more information, please contact your Consultant.
