IOPS COUNTRY PROFILE: SOUTH AFRICA

DEMOGRAPHICS AND MACROECONOMICS

GDP per capita (USD)	5,299
Population (000s)	55 900
Labour force (000s)	27 000
Unemployment rate	26.7
Population ages 65 and above	5.2
Dependency ration[1]	52

Source: South African Economic Data 2016.

1. Age dependency ration, old (% of working-age population), source: the World Bank, https://data.worldbank.org/indicator/SP.POP.DPND

COUNTRY PENSION DESIGN

STRUCTURE OF THE PENSION SYSTEM

Public pensions

- Means-tested old age pensions: non-contributory, fully financed by the government

Private pensions: occupational

- DC pension plans, mostly established by enterprises in the private formal sector
- DB pension plans, mostly established by the public sector
- Some hybrid schemes also exist

Private pensions: other

- Retirement annuities, mainly offered by insurance companies
- Preservation funds
- Unclaimed benefit funds
- Beneficiary funds

SOUTH AFRICA: THE PENSION SYSTEM'S KEY CHARACTERISTICS

Social Pensions

The social old age grant is a non-contributory and means-tested old age pension which is funded by a pay-as-you-go tax system. An old age grant is a monthly income provided by the South African Social Security Agency to older people. The grant is only paid to people whose financial income is below a certain level. A means test is used to determine the financial level of the applicants. The income and assets of the applicant and their spouse is assessed to determine if they qualify and to what amount they are entitled to.

The pension is payable to South African citizens of 60 years or older. With effect from 1 April 2017, the old age grant amounts to ZAR1 600[1] per month for pensioners over the age of 60 years and ZAR1 620 per month for those over 75 years.

In order to qualify for a grant for older persons, war veterans or the disabled, a beneficiary cannot own assets of more than ZAR990,000 (if single) or R1,980,000 (combined assets if married). These grants are also paid on a sliding scale, which means that the more private income an applicant has, the smaller the government grant.

Special grants are paid to war veterans (up to ZAR1,620) and pensioners who need full-time attendance of another person as the result of a mental or physical condition (ZAR380).

Occupational and Voluntary Pensions

Retirement funds can be established for the benefit of private and public sector employees. Certain funds which were established in terms of separate legislation are not regulated by the Pension Funds Act (PFA) and are therefore not supervised by the Financial Services Board ("the FSB") as regulator. Among these funds is the largest retirement fund established for civil servants (Government Employees Pension Fund).

Self-employed persons and other persons that wish to provide for additional retirement benefits in addition to normal retirement benefits may elect to participate in a tax-efficient retirement annuity fund.

Eligibility

It is voluntary for employers to establish a fund for its employees or to join an umbrella fund as a participating employer for the benefit of its employees, as well as the type and categories of employees eligible, contribution level and benefit structure. It is compulsory for its employees who are eligible to join the fund. For this reason, the system though legally voluntary can be thought of as quasi-mandatory.

[1] Exchange rate (vs USD) 1 USD = 13.7 South African Rand (ZAR)

Contributions

In some instances, employers may determine their respective contribution levels. There are no minimum or maximum contribution limits, unless so provided for in the rules of the fund. Contributions can consist of employer and/or employee contributions depending on the rules of the relevant fund. There are however limits in respect of the maximum allowable tax deductions as set out below.

In other instances, the rates of contributions are an outcome of negotiation between labour representatives and employers (this is the case of so called “bargaining council” and industry funds which effectively act as multi-employer funds). Additional voluntary contributions are allowed, if the rules of the concerned fund permit.

Individuals may make additional voluntary contributions to the fund but the tax deductibility of the contributions is subject to the allowable tax limits determined in terms of the Income Tax Act.

Benefits

Pension schemes can be defined benefit (DB) or defined contribution (DC) in design, or some hybrid of the two. At least two thirds of the benefit that becomes payable in a pension fund or retirement annuity fund must, on retirement, be taken as an annuity, with the lump sum capped at one third. In the case of a provident fund the whole benefit may be commuted as a lump sum on withdrawal and retirement.

Vesting rules

The rules of a fund determine the instances when and extent of the benefits payable in respect of termination of membership of the retirement fund. In most instances the retirement fund will provide for withdrawal, retrenchment, dismissal, death and disability benefits. As membership to an occupational retirement fund is normally conditional on employment with an employer and therefore, on termination of employment before retirement, employees usually receive a refund of their own contributions, employer contributions and, if applicable, a portion of the reserve accounts accumulated with the fund return as a minimum benefit defined in the Pension Funds Act. The relevant provisions in the PFA determine the minimum benefits to be paid to a member on withdrawal from a fund.

Preservation, portability, transferability

There is currently no provision for compulsory preservation of retirement fund benefits upon termination of employment before retirement. However members may, subject to fund rules, transfer their withdrawal benefit to the retirement fund of the new employer, a preservation fund or to a retirement annuity fund. If the current retirement fund rules allow, a member may elect to leave his/her benefit as a paid-up (deferred) benefit until his/her retirement. The National Treasury has prescribed in a regulation that a fund must provide for a default option for a member to preserve his/her benefit in the fund.

Transfer values are determined in the rules of a fund and normally in the case of a defined contribution fund, such value would be the member's individual account. In the case of a defined benefit fund the withdrawal benefit will be actuarially calculated on the effective date of the transfer.

In the case of an industry fund or bargaining council fund where both previous and new employers are participating in the same fund, such member will remain a member of the fund.

In certain instances, transfers of benefits between funds approved in terms of the Income Tax Act are tax neutral transfers.

Taxation

With effect from 1 March 2015, all employer-paid contributions to pension, provident and retirement annuity funds are regarded as a deductible employment expense for the employer and a taxable fringe benefit in the hands of the employee. These taxable employer-paid contributions will however be deemed to have been made by the employee for personal income tax deduction purposes, who shall in turn be eligible for a tax deduction for such contributions to approved funds, in addition to any contributions made by themselves to any of the three fund types.

This system creates an overall tax deduction to the individual taxpayer for all contributions to retirement funds, neutralising the fringe benefits tax up to a prescribed cap. The limits to the tax-deductible contribution are as follows:

- The limitation is now calculated with reference to "taxable income" or "remuneration (whichever is greater).
- The individual's tax deduction, in respect of aggregated employer and personal contributions, shall be limited to 27.5% of taxable income or remuneration (whichever is greater).
- An overall monetary cap of ZAR350 000 per annum limits the available deduction, regardless of the taxpayer's age. This limitation will impact taxpayers with taxable income in excess of ZAR1 272 730 per annum. However, disallowed contributions can be carried forward for deduction in a subsequent year of assessment (subject to the same limits). Contributions which are never deducted shall reduce the taxable proceeds on withdrawal/retirement, as is currently the case.

Benefits and annuities payable from a pension fund are taxable to the extent that contributions have been allowed as a deduction for tax purposes.

PERSONAL VOLUNTARY

Benefits

In the case of retirement annuities, benefits become payable from age 55 onwards. At least two thirds of the benefit that becomes payable in a retirement annuity fund must, on retirement be taken as an annuity, with the lump sum capped at one third. A member does not have an option of a withdrawal benefit prior to reaching retirement age.

Taxation

Contributions to a retirement annuity fund together with contributions to a pension fund are tax deductible to the relevant limits as set out above.

MARKET INFORMATION

Occupational voluntary

The vast majority of employees in the formally employed private sector in South Africa belong to defined contribution (DC) schemes, while public sector funds are still largely defined benefit (DB) arrangements.

The South African environment has also seen considerable growth of multi-employer or “umbrella” funds, which are DC in nature. Umbrella funds, covering multiple employers, are also allowed and have increased in number over time.

Most of the large trade unions have established national defined contribution funds and have negotiated an option for their members to belong to such funds, as opposed to membership of an employer-sponsored fund. In effect therefore, such funds are multi-employer funds, but along industry lines.

As of 31 December 2016, the pensions market had around 5 144 funds, with approximately 16,6 million members and ZAR4,1 trillion assets. Some double counting exists in terms of the number of members, as some individuals are members of more than one fund (for example, may belong to a retirement annuity fund as well as an occupational fund established by their employer). Many funds also offer death and disability benefits.

POTENTIAL REFORM

Reform proposals include the introduction of a contributory social security pillar as well as (where applicable to persons) supplementary mandatory contributions to the private retirement funding arrangements in order to improve the coverage rate and tackle „leakage" problems (early withdrawals leading to substantial sums of money being taken out of the funded pension system). The primary objective of this reform is to ensure a basic level of income during retirement for all South Africans.

Currently, almost 80% of funds have less than 100 members, which tended to raise concerns about the availability of sufficiently trained trustees to govern these funds and the cost-efficiency of such arrangements for the members within these funds.

INVESTMENT MANAGEMENT

Funds have the option to either manage their assets in-house or enter into an administration agreement with an investment manager which has obtained a license and is therefore supervised in terms of the Financial Advisory and Intermediaries Services Act.

The Minister of Finance prescribes prudential investment guidelines in the regulation 28 which determines the maximum percentage limits which a retirement fund may invest in certain asset classes. Amongst others the following asset classes and maximum limits are prescribed:

- a maximum of 90 per cent may be invested in both equities and property;

- a maximum of 75 per cent may be invested in equities;

- a maximum of 25 per cent may be invested in property;

- a maximum of 20 per cent may be invested in deposits with any single bank;

- a maximum of 20 per cent may be invested in securities issued outside South Africa;

- in addition to the abovementioned foreign investment allowance of 20 per cent, an additional five per cent may be invested in investments in Africa;

- a maximum of 15 per cent may be invested in high capitalization listed equity, and 10 per cent in a single other equity; and

- a maximum of 2.5 per cent may be invested in other assets. Certain derivative instruments and investment in unregulated hedge funds are included within this category.

The PFA further prescribes that a fund may invest up to 5% of its total assets in a participating employer of the retirement fund (including a subsidiary or holding company of the employer). The PFA further provides that the registrar may, on application by a fund, consider increasing this limit to 10% if the fund board has certified that it has consulted its members about this investment and that the members support the proposal. Such an investment may only be made if it is in the best interest of the fund and its members.

A retirement fund may, if its registered rules allow, grant housing loans to members or furnish a guarantee in respect of a housing loan granted, or to be granted, to enable the member to:

- redeem a housing loan granted to the member by a person other than the fund, against security of immovable property which belongs to the member or the member's spouse and on which a dwelling has been or will be erected which is occupied by the member or a dependant;

- purchase a dwelling, or purchase land and erect a dwelling on it, for occupation by the member or dependants; and

- make additions to, or repair, a dwelling which belongs to the member or the member's spouse and in which they live.

A housing loan can only be granted if it is secured by a mortgage on the property, by a pledge of the benefits to which the member is entitled or by a combination of the two.

There are currently no prescribed maximum or minimum management fees or administration costs as this is agreed to between the retirement fund and the service provider and contained in the administration agreement between them. In the case of certain insurance policies issued by funds, the costs and commissions will be subject to the provision of the Long-term Insurance Act.

REFERENCE INFORMATION

KEY LEGISLATION

The funded pension system is governed by the Pension Funds Act (PFA) which has been amended a number of times since promulgation in 1956.

KEY REGULATORY AND SUPERVISORY AUTHORITIES

The Financial Services Board (FSB) oversees the regulation of financial markets and non-banking financial institutions, including insurers, fund managers, broking operations and retirement funds.

http://www.fsb.co.za/

Source map: Central Intelligence Agency, The World Factbook, the United States