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THE POLITICS OF SOCIAL SECURITY AND RETIREMENT REFORMS AND RETIREMENT SAVINGS CULTURE IN SOUTH AFRICA

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Abstract

Purpose: The South African government is determined in alleviating poverty while encouraging job creation and protecting the disposable incomes of poor households. This article looks at the challenges that are facing the South African Social Security system and argues that the provision of income security is amongst the most practical expressions of a nation's cohesion and values.

Research Design, Data and Methodology: There are seven proposals in the Social Security and Retirement Reform and these proposals are based on the following two principal objectives of the government, that is, to ensure a basic standard of living and to prevent destitution in old age or in circumstances of unemployment or incapacity partly or wholly through redistributive measures, and to encourage savings to provide for the replacement of income on retirement, disablement or death through long-term insurance arrangements.

Results: This article evaluates these seven proposals, state old age pension ,wage subsidy, mandatory participation in a national social security system for all, mandatory participation in private occupational or individual retirement funds, Voluntary additional contributions to occupational or individual retirement funds, reform of the governance and regulation of the retirement funding industry and reform of the tax system.

Conclusion: This article concludes that the population size of South Africa has increased significantly to 51, 8 million in 2011 and therefore the time is right for bold new steps in improving income security of the poor and strengthening the fabric of social solidarity that binds all South Africans together.

Keywords: Social security, Retirement reforms, governance, savings and South Africa.

JEL classifications : D63, P36.

1. INTRODUCTION

The South African social insurance system was formalized as early as the 1950 through the enactment of the South African Pension Funds Act 24 of 1956. The Act came into operation during the apartheid government and offers little relief to the majority of retirees and this automatically calls for a plethora of reforms in that regard.

According to Strydom EML, le roux PAK, Landman AA, Christianson MA, Dupper OC, Myburgh P, Barker FS, Garbers CJ, Basson AC, Dekker A and Esselaar V (2006:19-20) the social security system in South Africa has a long and complex history which was inherited by the government in 1994 when it first came into power. This represents a transition from apartheid system of governance to the democratic government which promotes non-racialism and sexism, equality, respect for human dignity and social justice. The social security system prior the coming into operation of the Constitution, Act 108 of 1996 was characterised by racial discrimination which existed in respect of membership and entitlement to benefits in pension, provident and medical aid funds as well as in respect of old age and child grants.

During this period there were also a large number of unemployment persons and this was aggravated by a number of factors. The retrenchment of employees and the lack of the creation of new jobs led these persons living in absolute poverty despite having been employed because they do not have enough savings to ensure they will be able to survive the uncertain future. National Treasury (NT), *Retirement Fund Reform discussion paper* (2004:4) provides that many employees also reach retirement age without a funded pension benefit and hence rely on a government social assistance grants programme. There was therefore a need to have arrangements for income security in old age, unemployment insurance, and protection of families in the event of death, disability or illness of breadwinners. Social security programmes are temporary measures to address basic necessities of life, but in South Africa, there are permanent measures since the majority of people rely on it for survival on a daily basis.

According to Nevondwe (2009) the provision of income security is amongst the most practical expressions of a nation's cohesion and values. It relies on confidence in the long-term continuity of institutions. It rests on trust in the law and sound financial and economic management. It embodies the core principles of solidarity and risk-sharing.

In light of the above challenges, numerous reports and proposals have been made to government by different stake holders in order to restructure the South African social security system. The Department of Social Development issued the Committee of Inquiry into a Comprehensive System of Social Security for South Africa Report, 2002 for public comment ranging from different stakeholders. This report contained adequate reviews of the shortcomings that related to social protection arrangements, and outlined recommendations for broadening social insurance and implementing a "comprehensive and integrated medium-to-long-term framework for income support." The Committee Report also discussed options for extending access to health insurance, and improved alignment between the public and private health care delivery systems.

In 2004, the NT issued a Discussion Paper on Retirement Reform which sparked extensive debate. The objectives of the 2004 Discussion paper are to:

- Encourage individuals to provide adequately for their own retirement and the needs of their dependants.
- Encourage employers and employees to provide for retirement funding as part of the remuneration contract.
- Ensure that retirement funding arrangements are cost-efficient, prudently managed, transparent and fair.
- Promote the retention of purchasing power of pensions through protection against the effects of inflation, within the resource constraints of the fund.
- Improve standards of fund governance, including trustee knowledge and conduct, protection of members' interest, accountability, and disclosure of material information to members and contributors.
- Provide, through social assistance, an assured basic income entitlement to elderly persons without means.

The objectives stated above should be welcomed because they aim to increase the savings rate of the population. It is through compulsory contribution that the low savings rate may be decreased. However, this discussion paper had narrowly focused on the governance and regulation of retirement funds. It also had its focus on reforming the private pensions sector and the protection of member benefits. The 2004 discussion paper did not re-visit the role of the government and private sector in as far as providing financial security in the event of unemployment, disability and death of a bread winner.

According to Nevondwe (2010:288) the South African government is determined in alleviating poverty while encouraging job creation and protecting the disposable incomes of poor households. The process of social security reform announced by then President of the Republic of South Africa, Thabo Mbeki in his State of the Nation Address on 9 February 2007 is a confirmation of the democratic government ' s commitment to its vision of a caring and poverty-free society. The President indicated that the then Minister of Finance, Trevor Manuel would provide further details on a contributory earnings-related social security arrangement, informed by the principle of social solidarity. The NT issued the Second Discussion Paper on Social Security and Retirement Reform on 23 March 2007 for public comment. The 2007 Second Discussion Paper was a ground breaking as it proposed National Social Security Fund, governance of retirement funds, mandatory and voluntary participation to retirement funds, wage subsidy and taxation of retirement funds reform.

A primary reform objective is to provide basic income protection for all South Africans through a combination of social assistance and contributory savings and insurance arrangements. The aim is to close the gap between, on the one hand, poverty relief measures and social grants programmes, and on the other the tax incentivised long-term insurance and savings environment, which provides inadequately in certain respects for low-wage.

According to Hunter (2007:1) the significance of the 2007 paper is vital since if implemented it will be the biggest reform of economic policy since 1994.

2. THE SOUTH AFRICAN SOCIAL SECURITY SYSTEM: ISSUES AND CHALLENGES

Despite the fact that, the South African social security system is intact, well established and comparable with other developed and developing countries, the retirement system has some unsatisfactory features in that the system suffers from a serious fracture which has divided the first and the second economy along racial lines making the system inevitably beneficial to one group and detriment to the other especially the historically disadvantaged black majority.

The major problem with the existing system is the modes of funding, the gap between social old age grant for the poor and the tax incentivized private pension sector that is favourable to high income earning individuals as opposed to low income individuals in that, the current means test applied by government is not consistent and as a result present a double edged sword to the poor for the little that they save preclude them from accessing the government grant and diminishes as their income rises while the tax incentive for the rich rises in value as lifetime income increases.

It therefore discourages the poor from saving during their working age in that, the little that they save will not be enough to replace income on retirement and on the other hand make them fail the means test thus disqualifying them to receive the old age grant, by implication, they will be too rich to qualify for the government grant, yet too poor for self-sustainability.

Secondly, the fiscus cannot accommodate a high number of poor retirees due to the social security funding model which is not contributory in nature and thus not sustainable. This model is responsible partly for the irresponsible financial behaviour of young people in the formal sector who defer financial security decisions with the intention to rely on the old age grant on retirement.

The flexibility principle currently practiced by social insurance funds which allow members to withdraw their savings before actual retirement encourages poor preservation of pension savings. Compulsory preservation principle needs to be introduced to encourage a culture of savings.

The problems and challenges faced by retirees is that they are not aware of their pension law rights and how their benefits are being invested in retirement funds. This study will assist them to understand their rights and how the social security and retirement laws will be reformed to address their challenges.

3. RESEARCH METHODOLOGY

The research methodology used in this study is qualitative as opposed to quantitative. This research is library based and reliance is on library and online materials such as textbooks, reports, legislations, regulations, case laws and articles. Consequently, a combination of legal comparative and legal historical methods, based on jurisprudential analysis was employed. A legal comparative method was applied to find solutions, especially an investigation on the way forward for the social security and retirement reforms. The study established the development of legal rules, the interaction between law and social justice, and proposed solutions or amendments to the existing law based on practical or empirical and historical facts. Concepts were analysed and arguments based on discourse analysis were developed.

4. THE ROLE OF THE NATIONAL TREASURY UNDER RETIREMENT REFORMS

The NT is an organ of state that is responsible for managing South Africa's national government finances. The NT derives its mandate from two legislations: the Constitution and the Public Finance Management Act 1 of 1999. This entity has a mandate, in terms of section 216 of the Constitution, 1996, to ensure transparency, accountability and sound financial controls in the management of public finances. The NT applies to the following:

- departments,
- public entities listed in schedule 2 or 3 of the Public Finance Management Act
- Constitutional institutions; and
- parliament and provincial legislatures

The Minister of Finance is empowered to delegate a power or assign a duty to any official in NT. This delegation must, in terms of section 40A of the Pension Funds Act, 24 of 1956, be in writing. The Minister of Finance may regularly review, if necessary, amend or withdraw the delegation. The NT is therefore empowered by the Minister of Finance to release proposals on retirement reforms for public comments.

Retirement reforms come into existence as a result of pension funds and the role they play in the South African economy. Government encourages pension funds to provide members with cost-effective risk benefits; it views the main role of pension funds as making possible life cycle savings to support consumption in retirement.

South African law allows individuals leaving pension and provident funds on job changes to access their entire retirement balances in cash, although tax is payable on the withdrawal of a lump sum benefit pre-retirement. In addition, non-member spouses may receive cash payments in the case of divorce orders.

Many institutional features of South African pension funds are designed to encourage individuals to save for retirement since majority of South Africans are not saving enough for retirement, they wait until they are nearer to retire. Pension fund membership is usually a condition of employment; the fund sets minimum contributions; contributions are deducted from gross salaries; and a board of trustees rather than individual fund members often make retirement fund investment decisions. According to the NT's, *Preservation, portability and governance for retirement funds* (2012:11) a glaring omission in law is that preserving retirement assets on change of job is not mandatory.

Nevondwe (2009) observes that retirement Reform is a good sign and it proves that the government acknowledges the need to build better lives, alleviate poverty and implement a comprehensive social security system for the benefit of all South Africans. These critical steps by the government are necessary in building the nation.

5. LESSONS TO SOUTH AFRICA: THE CHILE AND SWEDEN EXPERIENCES

According to Mitchell (2005) the reform is "one of the most difficult reforms in any economy".Chile, a country often used as a model for the South African social security system – is already in its fourth cycle of reform. The Chilean Pension Reform was introduced at the beginning of the 1980s as the successor to the old state run system, which went bankrupt. Like Chile, many countries, including the United States, are facing the insolvency of their social security system. This is influenced by the fact that their populations are aging; and their systems must pay a high level of benefits compared with a low level of revenues. Chile's experience is relevant for every country that is trying to make its system solvent again.

According to Nevondwe (2010:290) the Chilean reform includes the concept of individual capital accounts. This feature appeals to many people who believe that governments are often unable to maintain sufficient assets to finance a retirement system. Individual accounts can be better protected against political risks. Its retirement reform incorporates a 'security network' in the form of minimum pensions and old-age benefits guaranteed by the government. And the model of European efficiency, Sweden, is busy with its sixth iteration. In Sweden, the generous Defined Benefit state scheme has been replaced by National Defined Contribution scheme and there is a mandatory funded individual account and also the choice of 700 investment funds.

We opine that South Africa should not aim to imitate international countries in its reform. Economies of each country differ tremendously and as a result each country should adopt reform features that are suitable to its own economy and standards. Masilela (2009) observes that the real challenge for South Africa is to learn from these countries and adapt their best features in the construction of a solution for the very unique South African social, political and business landscape.

The reform is like a journey and a long one, but it needs the government and the private sector to assist each other to have a reform which will rectify the injustices of the past and create an environment wherein they will be consistent in the industry or the standard uniform.

6. SOCIAL SECURITY AND RETIREMENT REFORMS PROPOSALS

There are seven proposals in the Social Security and Retirement Reform discussion paper and these proposals are based on the following two principal objectives of the government:

- to ensure a basic standard of living and to prevent destitution in old age or in circumstances of unemployment or incapacity partly or wholly through redistributive measures, and
- to encourage savings to provide for the replacement of income on retirement, disablement or death through long-term insurance arrangements.

6.1 State old age pension

It is proposed that social assistance grants continue to be provided to the elderly, the disabled, children and care-givers. It is also proposed that either the threshold for the deduction of independent income from the grant be increased or the means test be scraped. We opine that the scrapping out of the means test is vital because it does not work effectively and it encourages dishonesty. Nevondwe (2010:291) argues that the means test penalises the low-income earners for saving. It appears that South Africans will continue to receive SOAP when they retire, but it is not clear if they will also all get disability benefits or childcare grants if they have the means to survive without them. The SOAP amounts to R1260, 00 as at April 2013, this amount changes annually.

6.2 Wage subsidy

Wage subsidies may be seen as prominent features of the employment and social protection policies in many countries. The government proposes to introduce an explicit wage subsidy and continuing minimum benefits through social assistance, rather than indirect cross-subsidisation. The wage subsidy could take the form of a reimbursement to the employer in the form of a rebate or credit in the PAYE system.
It would only be paid in respect of employees earning below a specified level of wages, such as R43 000 and will be greater in value, the less that the employee earns. The details of the proposal are scant and government recognises that there are numerous design issues that will have to be carefully considered and addressed. For example, it considers that it may be that it would be more cost-effective to subsidise workers in particular sectors, or only first-time entrants to the labour department.

The wage subsidy is intended to encourage employment creation and also to support a “living wage” in labour intensive sectors and low-wage occupations. According to Nevondwe (2010:291) the wage subsidy is more likely to protect the living standards of working people than is regulation of labour relations. It is also more likely to promote, rather than inhibit, economic activity.

6.3 Mandatory participation in a national social security system for all.

According to Nevondwe & Ndaba (2012:23) this is the most controversial policy proposal and one that threatens the business of many providers of retirement funding products and services to the low-income, formally employed market.

The proposal is that all employed in the formal sector will all be obliged to contribute to a national social security fund. Compulsory contributions by domestic workers and the self-employed would be phased in over time. It remains to be seen whether voluntary contributions by people employed in the informal sector will be feasible.

Investigations will also have to be done to determine whether it would be feasible to implement the proposals in the 2004 Discussion Paper that contributors be allowed to withdraw amounts from the scheme to deal with life crises with due consideration for the need to encourage preservation. It is proposed in the 2007 Second Discussion Paper that compulsory preservation would apply to compulsory contributions.

According to Nevondwe & Ndaba (2012:24) the rate of contribution would be between 13 per cent and 18 per cent of after-tax wages (or between 11.5 per cent and 15 per cent of before-tax wages) up to a threshold of, say, R60 000 a year. If the percentage is 15 then, if you earn R70 000, you will be obliged to contribute 15 per cent of R60 000, that is R9000 a year or R750 a month. The cost of the contribution payable by a low-income worker should be covered by his or her wage subsidy.

Further according to Nevondwe & Ndaba (2012:24) the fact that the rate of compulsory contribution will depend on each contributor's rate of earnings means that the system will recognise the economic link between earned income and the affordability of benefits and will add both real and perceived value to the employment and remuneration contract.

If one earns less than the minimum taxable income (now R45 000 a year), his / her contributions to the social security fund would be paid by the state through the wage subsidy. This should mean that these new obligations do not increase the cost of the employment of low-income workers. This is one of the 'redistributive' elements of the overall proposal but entails an explicit subsidy rather than the cross-subsidy by some contributors of the cost of providing benefits to others.

South African Revenue Service (SARS) will need to undergo administrative reforms to enable it to maintain individual contributor records and ensure efficient and reliable benefits administration although the latter could be conducted by the Social Security Agency. Nevondwe & Ndaba (2012:24) opines that the cost of this reform may, however, be offset by the savings and efficiencies that will result from the consolidation of the social security arrangements that are now in place to finance unemployment insurance, maternity benefits, compensation for illnesses contracted at work and injuries sustained at the workplace or on the road.

And the reason for this proposal? The fact is that none of the South Africans save enough. South Africans underestimate the financial risks that they face and we put off making savings and investment decisions. Nevondwe & Ndaba (2012: 25) observes that most of South Africans prefer default arrangements over those that require them to make a decision. The people who are most vulnerable will tend to be excluded if participation is subject to choice or selection. They are also the most vulnerable to the relatively high costs of private sector retirement funding arrangements, and therefore will benefit from the economies of scale that will be achieved.

For some reason, perhaps related to South Africans' national inferiority complex, South Africans seem to feel a little better if what is being proposed has been successfully tried out in other countries, especially western countries. In the light of this, many South Africans will take comfort from the fact that almost all members of the OECD, which comprises developed and middle-income countries, have some form of mandatory, earning-related provision, although there is variation in the measures used. Many people have expressed doubt about whether government is capable of running such a large scheme. They forget that SARS manages to collect tax 'contributions' from approximately eight million tax-paying individuals and the Social Security Agency pays out nearly 12 million social security grants each month. According to Nevondwe & Ndaba (2012:25), it is common cause that there are instances of fraud in relation to social grants, but corruption is not an element of the product or delivery design as it has arguably been in the case of some private sector retirement funding products. Nonetheless, government intends to research and consult over the possibility of 'outsourcing' some of the management of the scheme, even considering the 'contracting out' options adopted by some overseas jurisdictions.

6.4 Mandatory participation in private occupational or individual retirement funds

According to Nevondwe (2010:293) many employees do recognises the importance of retirement provision and state an intention to join a retirement plan or to increase their savings, however evidence shows that only a fraction do so in practice. They remain at the mercy of social assistance grants although there was an opportunity to make savings and prepare for an uncertain future.

It is proposed that people employed in the formal sector be obliged to make additional contributions to occupational retirement funds or individual retirement funds out of their earnings above the earnings ceiling, up to a monetary cap. Nevondwe & Ndaba (2012:25) opine that this should allow individuals to save to provide for an adequate income replacement after retirement. It is suggested that the individual's post-retirement saving should be reasonable in relation to their pre-retirement income.

It may come as a relief to providers in the private sector that government recognises the benefits of the capacity, innovation and competition evident in the private sector. It is also proposed that funds be allowed to make transfers to the new national social security fund for the credit of individual members and then continue to collect contributions as "top up" occupational or individual retirement funds. Unless this is made compulsory or at the election of individual members, Nevondwe & Ndaba (2012:25) opine that it cannot be foreseen that funds will want to make these transfers because it will reduce their economies of scale.

6.5 Voluntary additional contributions to occupational or individual retirement funds

It is proposed that additional voluntary contributions to private occupational or individual retirement funds be encouraged by means of tax incentives. Those tax incentives will not apply to contributions over a specified monetary cap.

6.6 Reform of the governance and regulation of the retirement funding industry

Good governance and trust are the foundations of any sound retirement system. Members contribute in the present to save for the future. They have a right to expect that their funds will be managed prudently, in their best interests and in accordance with the law. Several recent high profile lapses highlight a broader problem with fund governance that, if unchecked, will damage the trust underpinning the system.

In 2007, the Financial Services Board issued PF Circular 130 on good governance of retirement funds. The circular recommends that trustees put in place a documented code of conduct, an investment statement, a communication strategy for members and a performance appraisal system for trustees. The circular also places an obligation on board members to receive training. The Financial Services Board has launched an online education programme, known as the Trustee Toolkit, to develop and educate retirement fund trustees. Currently, both PF Circular 130 and the use of the trustee toolkit are voluntary. Nevondwe & Ndaba (2012:26) welcomes the active support of both industry and union leaders to improve governance.

The industry recognises that practices like surplus stripping (where employers obtain surplus assets from a fund illegally) and bulking (where administrators pool the assets of many funds to obtain higher deposit rates, but keep the interest for themselves) undermine the entire industry.

Improving fund governance also requires dealing with conflicts of interest. The current system of 50:50 representations requires both employers and workers to take joint responsibility for managing such funds. Under this system, trustees do not represent the constituency that appointed them; rather, whether appointed by employers or unions, trustees must act independently and without fear or favour in exercising their fiduciary duties to promote the interests of all members of the fund.
To ensure this is achieved, it could become a statutory requirement that trustees have relevant qualifications and expertise in the management of pension funds, with training completed within a set period after appointment.

According to Hunter (2009:7-11) the Second Discussion Paper on Social Security and Retirement Reforms stipulates that "a frank assessment of the current South African retirement savings landscape suggests that while many people in formal sector jobs contribute to retirement funds, the vast majority start too late in their careers to save enough for retirement, or cash in their retirement savings when they change jobs. Rates of contribution appear reasonable on average, but are increasingly being eroded by rising administration costs and risk premiums. The high proportion of DC retirement funds in the private sector means that the risk of governance failures, expense inflation and inadequate benefit protection fall on the individual member, who is often the least equipped to manage or withstand the loss."

To address these problems, the reform suggests a number of reforms such as –

- facilitating effective competition through increased transparency and disclosure, properly aligned incentive structures for intermediaries, removing regulatory barriers to the entry of a wider range of product providers and allowing transfers between funds and products without excessive penalty;

- achieving economies of scale by introducing accreditation standards that which should encourage, if not compel, the consolidation of smaller occupational retirement funds into "umbrella" or multi-employer funds;

- allowing a range of social security benefits to be provided by private retirement funds including short-term disability benefits, funeral benefits and post-retirement medical aid funding;
- protecting retirement savings from erosion by risk premium costs by setting minimum allocations of contributions to retirement savings, compulsory preservation and portability, regulated minimum early withdrawal benefits and restricted deductions;

- requiring the preservation of retirement savings on changes of employment through transfers to the employee's new fund, an individual retirement fund or the national social security fund while possibly allowing withdrawals on loss of employment, possibly after the exhaustion of the unemployment insurance benefit;

- to the extent possible, ensuring continuing income during disablement and/or retirement and for the dependants of members after the death of those members, by requiring that a portion of the benefits be paid in the form of an annuity (although transitional provisions will be required to protect provident funds while they adapt) or that only so much as is not required to fund a multiple of the state old age pension be allowed to be withdrawn;
- improving the cost-effectiveness of annuity products by facilitating the wider provision of pensions by funds themselves, rather than by insurers, or by using an annuity provided by the national social security fund;

- protecting pensions from the ravages of inflation;
- achieving a better balance between the social service function provided by trustees in distributing death benefits and the need to ensure simplicity and speed in that distribution exercise;
- improving the security of dependants served by dependants' umbrella trusts through better oversight and possibly the establishment of dedicated "caretaker funds" regulated by the Financial Services Board;
- protecting unclaimed benefits through the establishment of a national Unclaimed Benefits Fund;
- regulating all retirement funds, including bargaining council funds and funds established in terms of specific statutes, in terms of a single Retirement Funds Act, extending the jurisdiction of the pension funds adjudicator to funds over which she does not now have jurisdiction and reforming the institution of the adjudicator's office. Currently the Adjudicator has jurisdiction only in funds which are registered with the Registrar of Pension Funds in terms of the Pension Funds Act 24 of 1956. The Adjudicator lacks jurisdiction on the Government Employees Pension Fund which has more than one million members, the Transnet Pension Fund and South Africa Post Office Retirement Fund. This creates a concern since members of the above fund do not have recourse since they have to deal with the fund directly if they are not satisfied with the benefits they have received.

6.7 Reform of the tax system

To simplify the retirement system, government proposes a uniform retirement contribution model, under which all contributions to retirement funds – including annuities, pension and provident funds and all benefits from these funds will be subject to the same tax treatment. Employer contributions to all types of funds will be included in an employee's remuneration as a fringe benefit, but individuals will be permitted a deduction of up to 22.5% of their income if they are under 45 years of age and 27.5% if they are 45 years of age and above. According to Nevondwe and Ndaba (2012:29-30) this will apply to both employer and employee contributions.

To cater for the self-employed and partially self-employed, and to ease administration, the income base upon which this deduction is calculated will be changed to the greater of remuneration and taxable income.

To improve equity in the tax system, and to enable lower-income individuals and those with variable incomes to contribute more, it is proposed that the maximum permitted deduction will be greater than R20 000 and less than R250 000 (R300 000 for those of 45 and above), regardless of income. The higher limits for older workers make allowance for those who did not save earlier in their lives.

According to the NT's discussion paper on *strengthening savings* (2012:14) a special arrangement will be made for defined benefit funds that still exist, including the Government Employees Pension Fund, to prevent excess contributions regarding current fund surpluses or deficits, or complications caused by ageing schemes, to have negative tax consequences for current members.

These changes are unlikely to affect the tax liabilities of the vast majority of taxpayers. By increasing pension contributions, such liabilities could even be reduced.

According to Hunter (2009:11-12) a number of inequities and complexities that need to be addressed in our tax system have been identified. At the same time the tax system needs to maintain sufficient incentives in place to encourage voluntary additional provision for retirement, particularly as

- the requirements and the costs of regulatory compliance by retirement funds is higher than the requirements and costs of such compliance by other savings vehicles;
- there are synergies between a robust pension environment and the development of financial markets that in themselves have further economic development benefits; and
- retirement savings institutions provide a stable long-term flow of funds, directed primarily to domestic investment, because funds seek to match their long-term liabilities with appropriate assets.

International evidence indicates that front-loaded tax benefits – that is, the favourable tax treatment of contributions to retirement funding vehicles – is the most effective way of stimulating savings. This treatment is available to members of pension funds, is not available to members of provident funds, and is available on a restricted basis to members of retirement annuity funds. Therefore, it is likely that the reform of retirement funding taxing arrangements will see more equitable tax treatment of contributions towards pension, provident and retirement annuity funds and the national social security fund with such contributions being wholly or partially tax-deductible and, in the case of low-income workers, paid by means of the wage subsidy.

Higher-income earners have benefited disproportionately from tax incentives in the past without this serving any particular public purpose, so it is likely that there will be some form of monetary cap on tax relief on contributions to retirement funding vehicles.

There are a number of options in regard to the tax treatment of contributions that could be considered. These include granting full or partial tax deductibility at marginal rates, or a tax credit system. The tax credit system is roughly equivalent to allowing a tax deduction at a standard rate.

Hunter (2009:13) opines that a special consideration will have to be given to the tax treatment of contributions of those with volatile incomes or periods of unemployment and those who have started contributing to a retirement fund late in life. The tax on certain forms of retirement fund investment income has been scrapped to enhance the adequacy of funds available in retirement, to simplify the tax treatment of retirement savings and to minimise tax-driven investment decisions.

Finally, it is proposed that some tax relief on lump sums paid on retirement be retained but the basis for determining it this will have to be simplified. Withholding tax on benefits paid to persons with taxable income of less than R43 000 a year will be abolished.

The 2013 budget speech has indicated that the government intends to proceed with the implementation of tax-preferred savings and investment accounts. Accordingly, Tax-preferred savings and investment accounts will be introduced in 2015. The tax treatment of pension, provident and retirement annuity funds will be simplified and harmonized. However, with effect from 1 March 2013, tax-free interest-income annual thresholds has been increased from R33 000 to R34 500 for individuals 65 years and over, and from R22 800 to R23 800 for individuals below 65 years old.

7. CONCLUSIONS

The wide-range of proposals to reform social security and retirement fund is an indication that Government is committed in increasing the financial security of all citizens. The introduction of preservations is a step in the right direction. A quite substantive number of South Africans reach retirement financially unprepared. Only half the country’s workers belong to a retirement fund. Only a small fraction (10%) of the country’s workers is able to maintain their pre-retirement level of consumption after retirement, largely because of a lack of preservation of retirement fund assets when members leave their jobs. Although the preservation requirement is not yet implemented, it is recommended that its implementation of should be fast-tracked, but done correctly within a reasonable time frame and thorough consultations.

The South African pension industry is one of the largest contributors to the country’s economy and we submit that its proper governance is of paramount importance. The 2007 PF Circular 130 on good governance of retirement funds issued by the Financial Services Board is welcomed as it aims to strengthen fund governance.

One of the features of the PF Circular 130 is to introduce the statutory requirement that trustees be "fit and proper", with no criminal history. In this regard, the trustees will be declared prohibited persons by the regulator if they are found to have been involved in past transgressions of good pension fund governance. It is also proposed that the trustees adhere to governance principles and continually undergo training to increase their knowledge and to equip them to carry out their duties more effectively.

The population size of South Africa has increased noticeably from 40,5 million in 1996, to 44,8 million in 2001, and then to 51,8 million in 2011 . The time is right for bold new steps in improving income security of the poor and strengthening the fabric of social solidarity that binds all South Africans together.

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