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What you need to know about pensions offered by retirement funds

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THE Default Regulations, which become effective for all retirement funds from March next year, require every retirement fund to develop a trustee-endorsed annuity strategy. By using their scale and bargaining power, bigger retirement funds can potentially offer more cost-effective annuity solutions to retiring members than currently available retail annuity products, although the differences are expected to narrow as providers adapt to the changing retirement landscape.

In a presentation at the recent annual conference of the Actuarial Society of South Africa in Cape Town, David Gluckman and Danie van Zyl, respectively head of special projects and head of guaranteed investments at Sanlam Employee Benefits, examined the advantages and disadvantages of in-fund living annuities versus retail living annuities for retiring members.

Gluckman said that although there was still a demand for guaranteed, or life, annuities, there has been a huge move among retiring South Africans over the past several years to living annuities. (A life annuity is a pension product you buy from a life assurance company, which pays a pension for life. A living annuity is an investment product in which you can choose the underlying investments and the amount you draw down as a pension each year. However, you risk running out of money before you die.)

Gluckman says boards of trustees can choose any annuity products to be part of the trustee-endorsed annuity strategy. "Options include both living annuity and life annuity products, or hybrid life/living annuity solutions, or combinations, such as a life annuity for one segment of members and living annuity for another segment. All of these can either be structured on an In-fund basis or an out-of-fund basis," he says.

In addition to the differences in legal structure, holders of in-fund living annuities are likely to pay less in administration, advice and investment costs.

Says Gluckman: "It's desirable that financial advisers advising members retiring from large retirement funds familiarise themselves with these in-fund products and that they begin putting these options on the table."

DIFFERENCES BETWEEN IN-FUND AND OUT-OF-FUND LIVING ANNUITIES

In-fund living annuity	Out-of fund living annuity
Subject to the Pension Funds Act (PFA)	Subject to the Long Term Insurance Act
Governance overseen by board of trustees	Individual insurance contract
Section 37C* of PFA applies on death	Beneficiary nomination prevails on death
Regulation 28 of PFA governing investment asset allocation applies	Reg 28 does not apply (yet)
Can be converted to an out-of-fund annuity	Cannot be converted to in-fund annuity
Asisa standards on costs and disclosure: good practice	Asisa standards on costs and disclosure: mandatory
Differences in who can advise on these products.	
Fica requirements less burdensome	Fica applies
PFA offers significant protection from creditors	Less certain protection from creditors

*Section 37C of the PFA places a duty on the fund trustees to identify the dependants and nominees of the deceased member and effect an equitable distribution of the benefit among those dependants and nominees.