Sanlam

Legal Report

March 2023

1. Bulking payments to former members of deregistered funds

Certain retirement fund administrators previously engaged in a practice called bulking, which entailed that the administrator treated individual retirement fund bank accounts as one account in order to negotiate a higher interest rate. The administrator did however not disclose the additional interest to the relevant retirement funds, resulting in the administrator making so-called secret profits. When this practice came to light, the Financial Sector Conduct Authority's predecessor, the Financial Services Board, during 2007 informed all administrators that it expects them to pay these profits to the affected funds.

The Minister of Finance on 1 March 2009 published a notice in terms of which bulking settlement payments by retirement funds to former members are tax-free. When this notice was issued, some of the affected retirement funds were no longer registered. Fund administrators could therefore not pay the bulking settlement payments to the fund to be distributed to its former members. These bulking settlement payments are currently still held by the respective fund administrators.

The Minister has in view of the above issued a draft notice making provision for the tax-free payment of bulking settlement payments to former members of deregistered retirement funds, provided that the following requirements are met:

- the bulking settlement payments relate to amounts that became due and payable by the administrator to the relevant retirement fund before 1 January 2008; and
- such bulking payments have not been allocated due to the fact that the fund has been deregistered; and
- the administrator has entered into an agreement with the Financial Sector Conduct Authority to make such bulking settlement payments directly to the former members of the deregistered fund.

It is made clear in the explanatory memorandum and media statement accompanying the draft notice that this will be the last opportunity for administrators to rectify the situation.
The draft notice is open for public comment until 6 April 2023.

2. Two pot retirement system

The two pot retirement system, which will give members access to a portion of their retirement fund benefits before termination of service, will come into effect on 1 March 2024. The retirement fund industry is however still awaiting the final legislation in this regard, which makes it very challenging to prepare for the implementation of the system. National Treasury, at the recent Pension Lawyers Conference, provided the following feedback regarding the current status.

According to National Treasury the second draft of the two pot legislation (hereinafter referred to as “the revised two pot bill”) will be issued before the normal taxation laws amendment bills are published. The taxation laws amendment bills are usually published during July of each year, and it can accordingly be expected that the revised two pot bill will be issued before the end of July 2023.

The revised two pot bill will again be in draft form, and the retirement fund industry and general public will be given the opportunity to comment on the bill. Workshops on the bill will also be held.

It was stated in the 2023 Budget Review that the following areas still require additional work:

- a proposal for seed capital, in other words that members should have immediate access to a portion of their fund values on the implementation date of the two pot system, despite the fact that they have not yet built up a savings pot;
- legislative mechanisms to include defined benefit funds;
- legacy retirement annuity funds;
- the possibility of withdrawals from the retirement pot if a member is retrenched and has no alternative source of income.

National Treasury stated at the Pension Lawyers Conference that the revised two pot bill will not necessarily include the above issues, and that these aspects may possibly only be addressed at a later stage. Consideration will further be given to an exemption for legacy retirement annuity funds not able to implement the two pot system for some of their members. As far as defined benefit funds are concerned, the proposal from National Treasury is to reduce the period of service to provide for early withdrawals, or a fund may choose a methodology verified and acceptable to the Financial Sector Conduct Authority (FSCA).

It was also confirmed that if a member has withdrawn an amount from the savings pot, and resigns within 12 months of such withdrawal, the member will have to wait until 12 months after the withdrawal before a further withdrawal may be made.

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Consequential amendments to the Pension Funds Act to cater for the two pot system, will be released soon after the revised two pot bill is published.

3. Deregistration of inactive retirement funds

The Financial Sector Conduct Authority (FSCA) has published a report on the deregistration of inactive retirement funds.

The publication of the report is pursuant to a deregistration project initiated in 2007 to deregister any retirement funds that no longer had members, assets or liabilities, or a properly constituted board of trustees. The project was put on hold in 2013 due to various court actions. The aim of the report is to provide a comprehensive overview of the deregistration project. The report also clarifies the requirements for the deregistration of funds going forward.

It is inter alia confirmed in the report that when application is made for the deregistration of an orphan fund, i.e. one without a board of trustees, the administrator must also make application for the appointment of an interim board in terms of section 26(2) of the Pension Funds Act. The administrator is required to nominate a minimum of two persons, one being an employer representative and the other nominee being a member representative or former member of the fund. If only one of these is available, the FSCA will request the fund to nominate an independent trustee to act alongside the employer or member representative.

It is also stated in the report that the FSCA does not accept employees of the administrator as section 26(2) nominees or appointees, save for umbrella funds where an exemption in terms of section 7B of the Pension Funds Act should be renewed. However, even in those instances, it is required that an independent trustee be nominated. Where the employer is no longer in existence and there are no members left in the fund, or where any remaining members are unwilling to serve as trustees, the administrator would be required to nominate two independent trustees. Where the fund has assets to pay for the independent trustees' remuneration, the fund bears the costs. Where the fund has no assets and cannot afford this expense, the administrator is required to fund the independent trustees' remuneration.

It is also stated in the report that the FSCA's Retirement Funds Conduct Supervision Department, as part of the deregistration project, liaises with administrators and section 26(2) trustees on a quarterly basis. The purpose of these engagements is to provide a platform where section 26(2) trustees and administrators may voice difficulties encountered in bringing funds closer to cancellation, and where possible, the FSCA also provides guidance on particular issues. This project is ongoing and will continue for the foreseeable future, given the inherent and unique complexity of issues besetting terminating funds.

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The report also, inter alia, contains the following statement:

"*The FSCA's Retirement Funds Supervision Department has held meetings with Liberty, Old Mutual, Sanlam, Alexander Forbes and MMI to discuss cancellations of terminating funds, section 26 appointments, and reinstatements relating to historic cancellations and any other burning issues. With regard to historic cancellations, the engagement with these administrators focused on the need to verify from membership data available to them any cancelled fund that still had assets and members. As membership data lies in the domain of the administrator and not the FSCA, administrators were required to self-report any errors. However, the FSCA utilised the information at its disposal to direct attention to specific funds and guided administrators' focus in this regard. From the FSCA's general engagement with administrators, it was apparent that they not only appreciated their statutory duties, but also that they carried reputational risk. The administrators voluntarily undertook to conduct internal investigations and report their findings to the FSCA as and when any case was uncovered.*"

Retirement funds or other clients requiring more information should not hesitate to contact their consultant.

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