Unpacking the Two Component (Pot) System

ETFSA RA Fund Webinar – 13 August 2024

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What is the “Two Pot” System?

- Amendment Bill by the Government to enforce:
  1. Immediate **access** to a portion of your retirement funds.
  2. Retirement funds **preservation.**

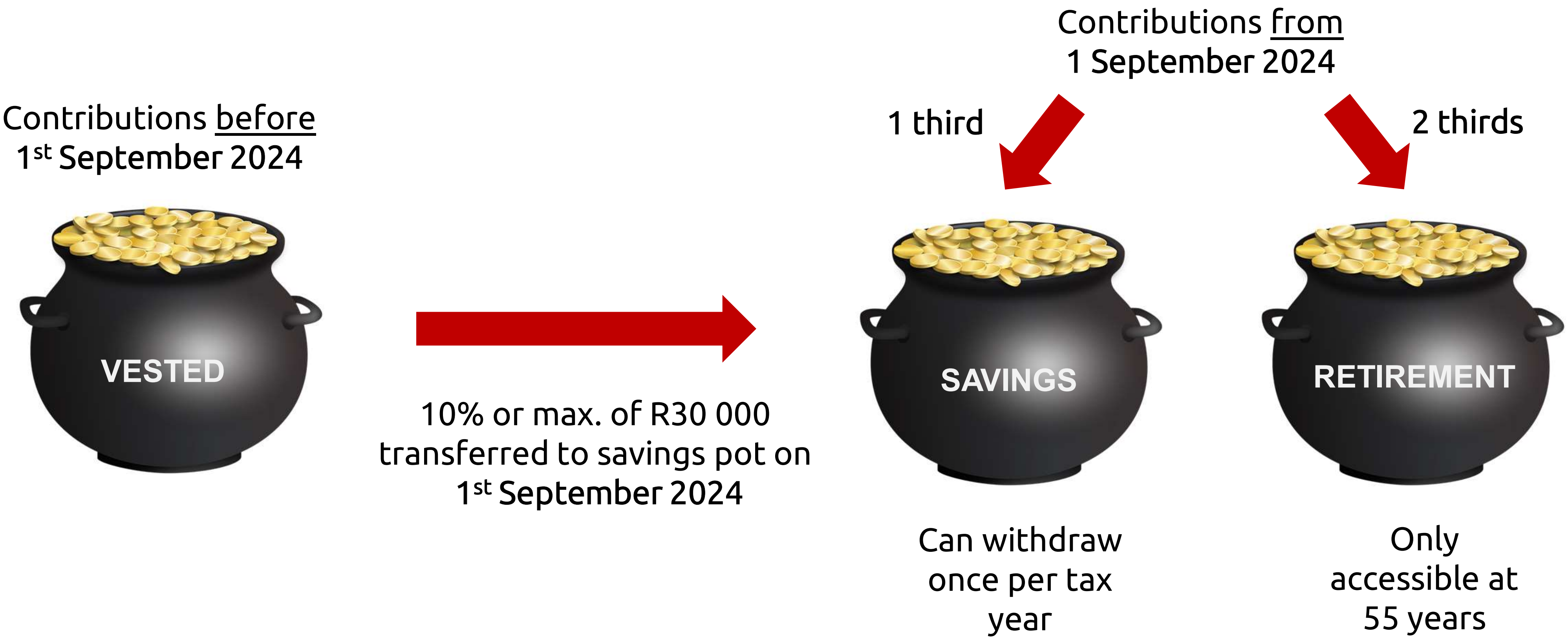
- Applies to ALL retirement funds

- Scheduled to take effect on 1st September 2024

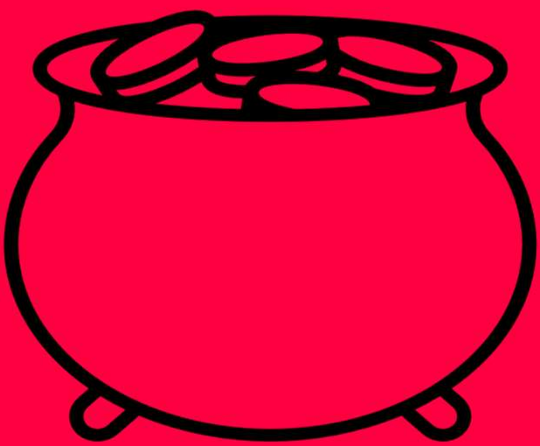
- It will consist of the following three components:

1. **Vested Component** – Any retirement funds accumulated before 1st September 2024
2. **Savings Component** – Allocation of 1/3rd of new contributions after 1st Sept (accessible)
3. **Retirement Component** - Allocation of 2/3rd of contributions after 1st Sept (only accessible at 55 years or older)

“Two Pot” System Illustration

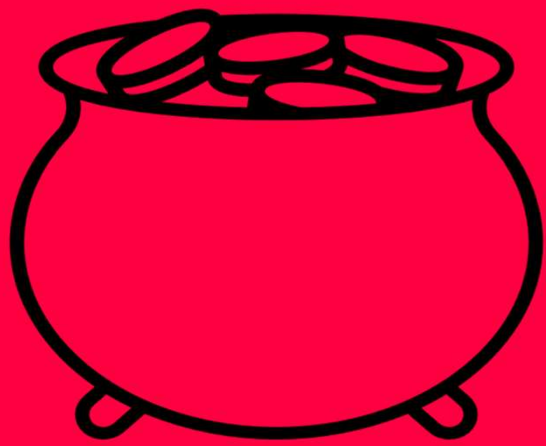


Pot 1 – Vested Component



- All accumulated retirement contributions until 31st August 2024
- Vested component = vested rights (will not be affected by the new system).
- At 55 years or older, you can use your vested benefits to retire – in accordance with existing retirement rules..
- Balance less than R247 500, you can take the whole amount as a cash lump sum.
- Accessibility will ONLY be at retirement – unless your vested component is a Pension/Provident Fund or Preservation Fund.
- At retirement, you can take one-third in cash as a lump sum – the R550 000 tax-free withdrawal rate and post-retirement tax tables apply.
- The balance is used to purchase a Living Annuity.

Pot 1 – Vested Component



Transfer of seed capital to your Savings Pot from 1 September 2024

- 10% of your vested pot, up to a <u>maximum</u> of R30 000 per retirement fund will be seeded to your Savings Pot.

<u>Seeded capital examples:</u>

R10 000 balance (vested component): Only R1 000 will be seeded but <u>not accessible</u>

R120 000 balance (vested component): Only R12 000 will be seeded and <u>accessible</u>

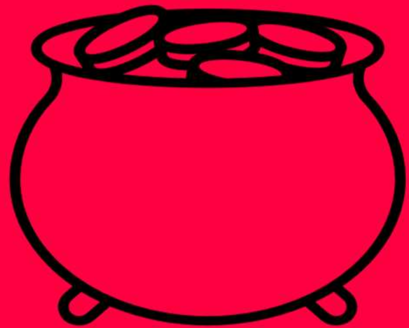
R950 000 balance (vested component): Only R30 000 will be seeded and <u>accessible</u>

Pot 1 – Vested Component

Accessing your Seed Capital

- You can withdraw the seed capital at any time.
- Important to note before withdrawing:

1. Tax – Administrator obtains Directive from SARS and deducts tax upfront.
2. Administration processing charge (maximum of R200 per withdrawal).
3. Outstanding tax at SARS is deducted before payment.
4. You can keep your seed capital in your savings pot to increase the cash available at retirement.



<u>Tax calculation:</u>

Salary – R800 000 (your marginal tax rate – 39%)
Withdrawal amount – R30 000 (savings component)
R5 500 – owned to SARS for non-payment of tax (IT88)

Withdrawal process from 1 September 2024:

1. <u>Once all documentation received, the claim process will commence.</u>
2. <u>Withdrawal amount = R30 000 – R11 700 (Tax) = R18 300.</u>
3. <u>Outstanding tax (IT88) = R18 300 – R5 500 = R12 800</u>
4. <u>Processing charge = R12 800 – R200 = R12 600</u>

<u>Therefore, the amount to be paid to the member is R12 600</u>

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Pot 2 – Savings Component

- From 1^{st} September 2024, $1/3^{rd}$ of contributions will be received in this component

- Monthly <u>contributions of R6 000</u> will be distributed as below:

  Savings component: $1/3^{rd}$ = R2 000

  Retirement component : $2/3^{rd}$ = R4 000

- Your seed capital (maximum R30 000), plus your new contributions, make up the savings pot.

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Pot 2 – Savings Component - withdrawals

- Withdrawals are limited to <u>one</u> per tax year.
- No withdrawals less than R2 000 will be permitted.
- Any withdrawals before retirement are taxed at your normal (marginal) tax rate.
- At retirement, the balance in your savings pot can be drawn as a lump sum – will be taxed at post-retirement rate.

At 56 years, Sharon decides to retire with the following balances:

Savings Component = R450 000
(R550 000 tax-free lump sum at retirement).

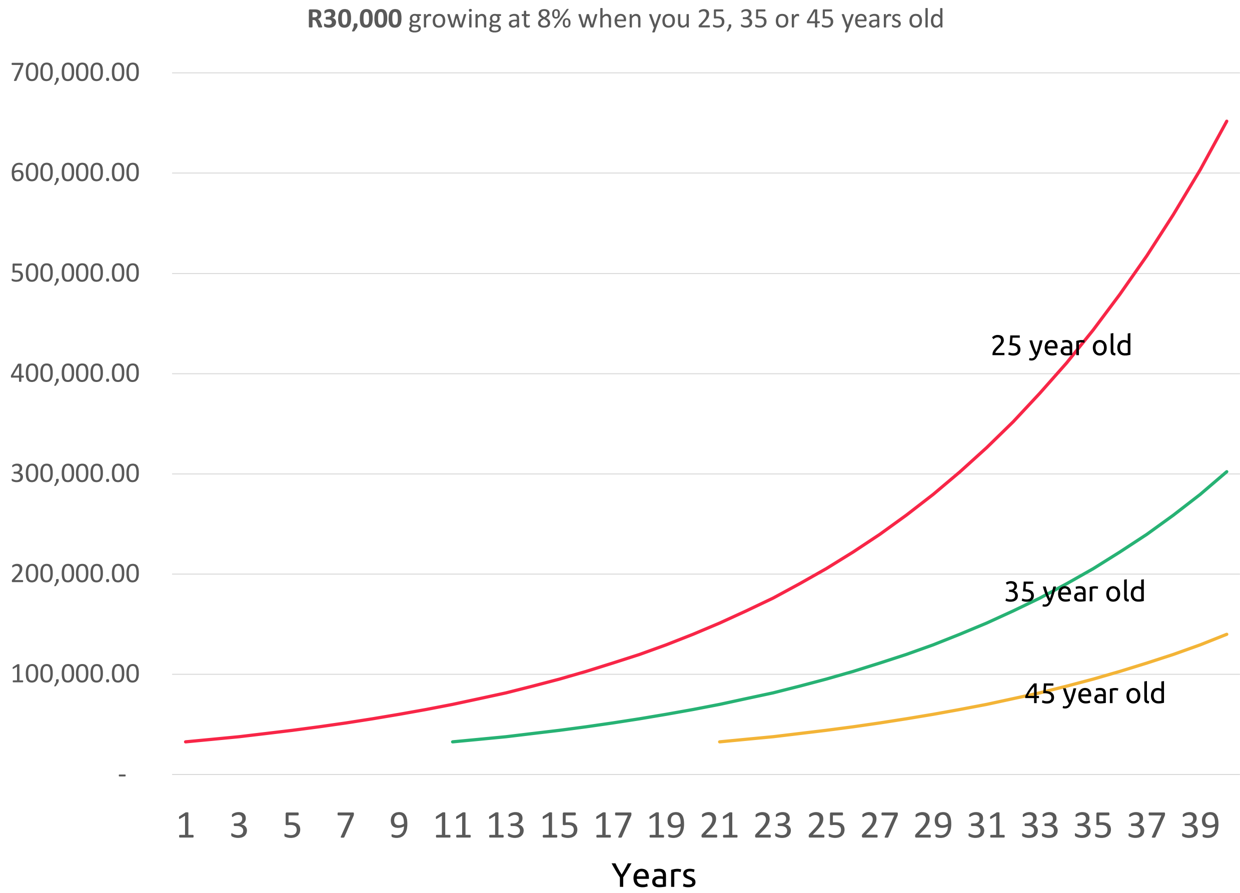
Retirement Component = R980 000
(Purchase a living annuity policy that will pay her a pension).

You can Transfer your Savings Component to your Retirement Pot (once a year) but will then lose <u>access</u> to this money.

Should you access your savings pot?

- When should I access my savings pot?
  - Accessing savings pot = case of emergency.
  - Accessing even a small portion = Loss of compounding effect.
  - Aim to meet near-term liabilities and costs with near-term earnings/cash flow and not fund with retirement assets.

The power of compounding



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Pot 3 – Retirement Component

- From 1^{st} September 2024, $2/3^{rd}$ of contributions will be transferred into this component.

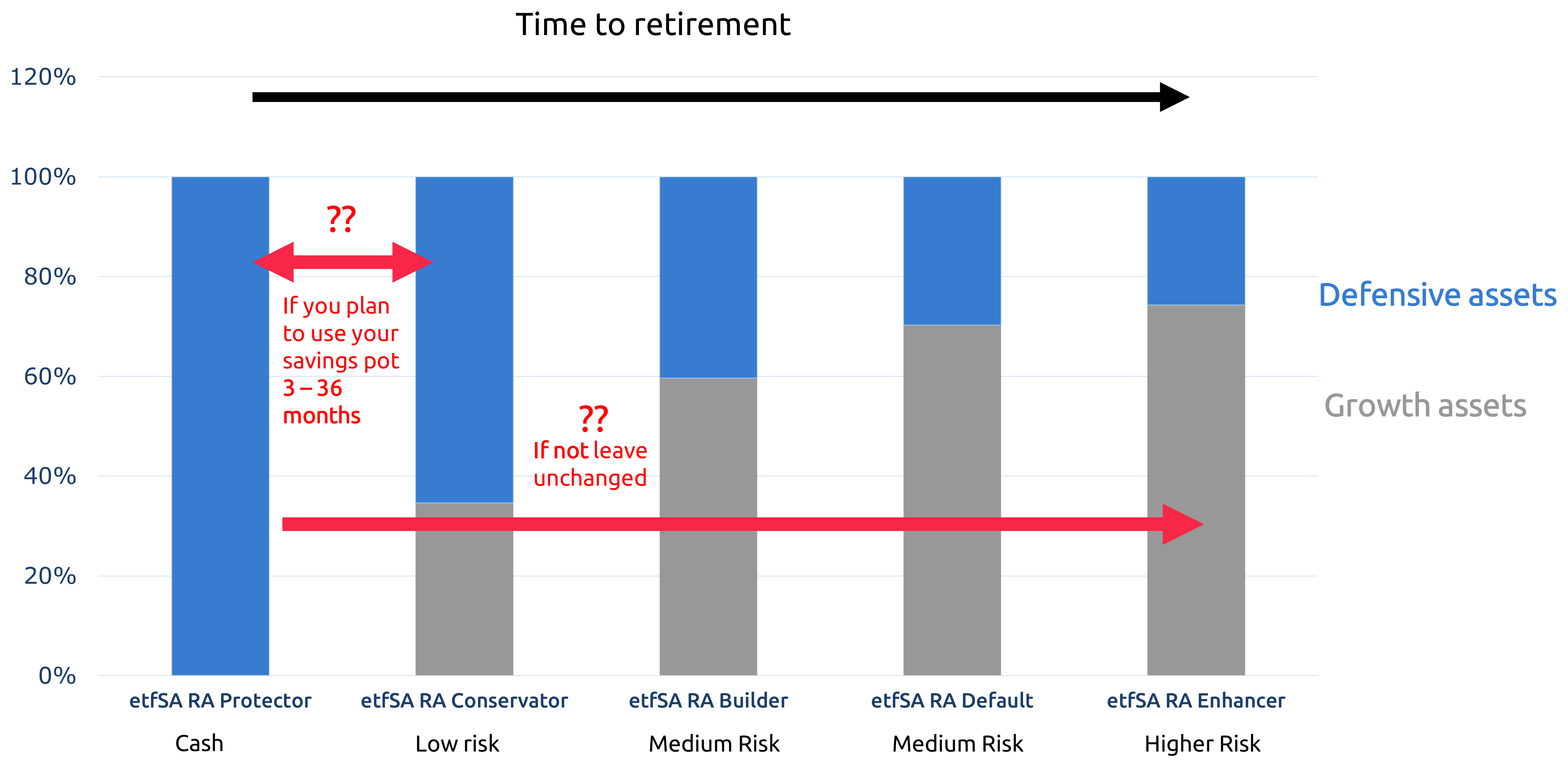
  Monthly contributions of R6 000 will be distributed as below:

  Savings component: $1/3^{rd}$ = R2 000

  Retirement component : $2/3^{rd}$ = R4 000

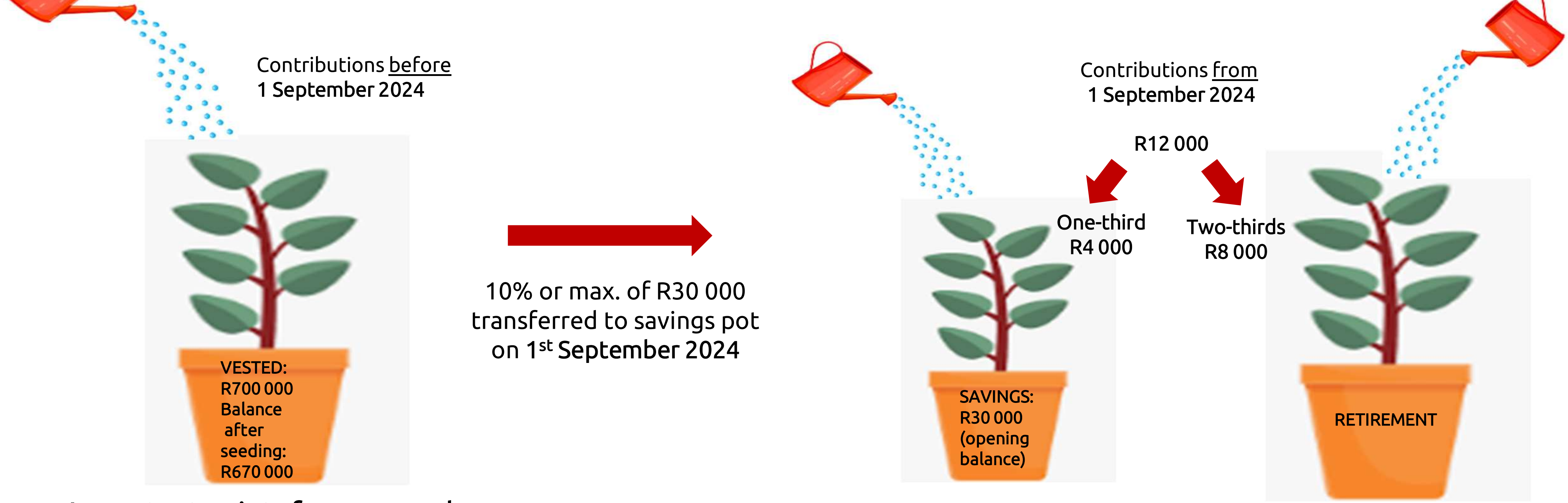
- No accessibility will be granted to this component until 55 years or older.
- This component will be used to purchase a living annuity policy on retirement.
- Contributions from the savings component can be transferred into this component but not vice versa.
- All funds held in this pot have to be used to purchase an annuity on retirement.

Investment decisions based on two pots?



"Two Pot" System example

Gareth is 42 years old and is on a marginal tax rate of 39%.
He has a Pension Fund **valued at R700 000** and **contributes R12 000 per month**:



Important points from example

1. **Vested component** – at retirement, he can take R223 333 plus return, cash and R446 667 plus return, to a living annuity product.

2. **Savings component** – he has <u>immediate access</u> to withdraw these funds, subject to tax, once a year.

3. **Retirement component** – money in this retirement pot will be used to purchase a living annuity product which will provide him with a pension.

What changes “POST” Two Pot System?

ETFSA Retirement Annuities

	CHANGE	NO CHANGE
Contributions	1. Contributions received after **1 September 2024** will be split into the Savings and Retirement component. 2. Any excess contributions (more than 27,5% or R350 000) will be automatically allocated to the retirement component.	Current contribution limits of 27,5% or a maximum of R350 000 of taxable income per financial year, will remain unchanged.
Retirement age		55 years or older.
Accessibility	1. Access to cash before retirement only in the savings component. 2. The balance has to be preserved for retirement.	Vested component still allows you to cash in before retirement, but, taxed at pre-retirement tax rates.
Transfers	The transfer will be actioned per component: Old vested component: >**New vested component.** Old savings component: **>New savings component.** Old retirement component: **>New retirement component**	You can still do transfers (e.g. Section 14 transfers) from one provider to another, tax free.
Resignation	If you resign (leave) your employer your vested rights apply for contributions made before 31 August 2024. After that, your contributions are split between savings and retirement pots.	When leaving an employer, you can transfer/consolidate your benefits in an existing policy or transfer to a Preservation Fund.

What changes "POST" Two Pot System? continued..

	CHANGE	NO CHANGE
Divorce	Each component will be proportionally allocated as per the divorce decree.	
Death	Once the death claim process is finalised, distribution will be executed per component instead of actioning from one fund.	Section 37C of the Pension Funds Act still needs to be followed and distributions will be executed per component.
Taxation	1. Any withdrawal from the savings component will be taxed at your marginal tax rate (maximum tax rate = 45%). 2. SARS will deduct any outstanding tax (IT88) before payout.	1. Retirement lump sums (at 55 years or older) will be taxed according to the retirement tax table. 2. Tax free lump sum (R550 000) applicable at retirement.
Investment Portfolios	You can invest in one portfolio across all components or select different portfolios for each component at no additional cost.	All portfolios need to abide by Regulation 28.
Fees	Withdrawals from the savings component will incur a maximum administration charge of R200 per withdrawal.	The composite fee on the ETFSA RA Fund, of 1,00% per annum, will **NOT** change and will be charged per RA policy and **NOT** per component.
Return/Investment	Returns will be allocated per component depending in which portfolio you are invested.	
Emigration	Your vested pot and savings pot can be fully withdrawn on formal emigration – taxed at pre-retirement tax rate.	Retirement Annuity capital can only be withdrawn 3 years after formal emigration.

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