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Asset Management

A New Paradigm in Pension Planning – Introducing the Two (Three) Pot Retirement System

In a landmark move aimed at revolutionising retirement planning, South Africa is gearing up to implement a pioneering "two-pot retirement system." This framework marks a significant departure from the traditional pension model and promises to provide greater flexibility and security for retirees nationwide. The revamped system will apply universally to all retirement funds, spanning both private sector and public sector funds. However, certain exceptions apply. Specifically, the system will not extend to old generation or legacy retirement annuity policies, nor to funds without active participating members. These exceptions include funds undergoing liquidation, beneficiary funds, closed funds, or dormant funds.

South Africa's alarming savings rates are widely publicised. According to the most recent findings from the Sanlam Benchmark Survey, less than 10% of retirees manage to maintain their pre-retirement standard of living—a sobering statistic. Moreover, the latest Baseline Survey reveals that 46% of adults prioritise current spending over saving for their future, with a third having no retirement plan in place at all. Old Mutual's statistics further underscore this trend, revealing that more than 90% of retirement fund members exercise the option to withdraw all their retirement savings when changing jobs (or resigning), instead of transferring the money to a preservation fund, a new fund or simply leaving it invested with the original fund.
Preserving the bulk of retirement contributions will undoubtedly be a positive development. However, it's important to note that this will primarily benefit individuals actively contributing to their retirement funds. While this change may not directly address the broader issue of poor savings rates, it represents a step in the right direction.

POT 1: The Vested Pot
Under the new legislation, retirement benefits accrued prior to September 1, 2024, will be safeguarded in a separate entity known as the "vested pot." Governed by regulations outlined in the Pensions Funds Act, 24 of 1956, access to this pot will only be granted upon reaching the retirement date. However, with the updated pensionable salary, individuals will have a retirement pot and a savings pot.
Within the revamped system, members will have the opportunity to transfer up to 10% of their accumulated benefits, with a maximum cap of R30,000, into the savings pot post-implementation of the Two-Pot System. This provision aims to ensure that the savings pot doesn't start with a zero balance, providing a financial buffer for unforeseen expenses. Notably, the 10% and R30,000 limit applies per member, per fund, allowing individuals with multiple pensions to withdraw multiples of the R10% of accumulated benefits.

POT 2: The Retirement Pot
Dedicated to securing long-term financial stability, this pot serves as the designated destination for both monthly and lump-sum retirement annuity fund contributions. Two-thirds of these contributions are allocated to this pot, aiming to preserve them until retirement. This segment is specifically earmarked for the acquisition of an annuity.

POT 3: The Savings Pot
One-third of the pensionable salary will be allocated to the savings pot. Within this pot, withdrawals are limited to once a year during employment, with a minimum withdrawal of R2 000 annually. Members do not lose the funds in their savings pots if they refrain from making withdrawals within a year. Rather, any unwithdrawn amounts, coupled with additional contributions, will continue to accumulate within the savings pot. Funds withdrawn from the savings pot will be included in a member's income and subject to taxation at their marginal rate.

The potential economic ramifications of increased access to retirement funds are still unfolding, with ongoing debates about its implications. Nevertheless, one foreseeable consequence is the potential boost to consumer spending in the short term. This is due to the likelihood that a significant portion of individuals will tap into their "savings pot" as they gain access to it. Withdrawal behaviour within the savings pot will be segmented by income bracket, with an expectation that maximum withdrawals can be primarily applied to the lowest income brackets (deemed to be most in need of accessing their savings). According to estimates from the National Treasury, there is an anticipated additional tax collection of R5 billion in the fiscal year 2024/25, resulting from members accessing their initial or seed capital pot. Assuming a marginal tax rate of 25%, this would imply total withdrawals of R20 billion (equating to 0.4% of total industry assets based on the 31 Dec 2023 SARB Bulletin) for the year.

The National Treasury's estimate falls on the conservative end of the spectrum, as industry experts project a broader range. Without access to all member funds, experts foresee withdrawals ranging from 2-3% of industry assets, potentially surpassing R100 billion, indicating a significant potential impact on the retirement savings industry.

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