PBO

PARLIAMENTARY BUDGET OFFICE

PARLIAMENT OF THE REPUBLIC OF SOUTH AFRICA

2023 REVENUE LAWS AMENDMENT BILL (RLAB)-Standing Committee on Finance

Proposed amendment to the implementation date of the so-called "two-pots" retirement reforms of the Revenue Laws Amendment Bill (RLAB) **from 1 March 2025 to 1 March 2024**

27 November 2023

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1. Introduction

This brief is a response to a request on the part of Dr Zakhele Hlope, Content Advisor for the Standing Committee on Finance (SCOF), with regard to advice pertaining to the proposed amendment to the Revenue Laws Amendment Bill (RLAB) [B39-2023]. In line with the request, the Standing Committee of Finance has proposed in its draft Report of the Standing Committee on Finance on the Revenue Laws Amendment Bill [B39 - 2023]- November 2023 that the implementation date for the RLAB be changed to the 1 March 2024, as opposed to the current date of 1 March 2025.

Falling within the scope of the same report, the Committee has further recommended that the National Treasury (NT) conduct a thorough impact assessment to determine the feasibility of introducing a staggered approach to the implementation of the RLAB. In addition, the recommendation is that this assessment consider the varying needs and emergency circumstances of fund members alongside the administrative readiness of the various retirement funds concerned with its implementation. With regard to these matters as they currently stand, our understanding is that the Committee has as yet made only one amendment, while the implementation date has been pushed forward from 1 March 2025 to 1 March 2024. With the above recommendation in mind, a proposal to staggering the implementation of the RLAB has been presented for principal consideration on the part of the National Treasury.

In the light of the proposed amendment and acting on behalf of the Committee, Chairperson Hon. M J Maswanganyi wrote a letter on the 21 November 2023 notifying the Minister of Finance about the proposed amendment to the RLAB implementation date. The Committee further noted that the proposed amendment;

> *"does not impact the fiscus negatively. The Committee has thoroughly examined the fiscal implications and is confident that this adjustment aligns with the broader economic considerations and financial goals of the government."*

In the name of providing clarification on this matter, the SCOF's Content Advisor has since requested that the Parliamentary Budget Office (PBO) advise with regard to the Committee Report on the RLAB [B39-2023] as to whether or not;

- The proposed change to the implementation date of the RLAB [B39-2023] is in line with section 11 (3) of the Money Bills Amendment Procedure and Related Matters Act of 2009.

Falling within the same Report, the Committee has made other recommendations[1] which do not impact directly upon the implementation of the RLAB. Furthermore, in preparing this brief the Parliamentary Budget Office has relied upon the Money Bills Amendment Procedures and Related Matters Act of 2009.[2] The Office has also drawn upon the Committee's various deliberations on the RLAB and engagement with numerous stakeholders, as well as direct and informal interaction with some of the key stakeholders or their representation in the National Treasury, the South African Revenue Services (SARS), the Congress of South African Trade Unions (COSATU) and Retirement Industry Experts amongst others.

Given the pressing nature of the Standing Committee of Finance's request, the Office has then decided to focus its recommendations on addressing two specific matters. First, whether or

[1]The Committee notes the proposal for a staggering mechanism to address liquidity concerns and market pressures. While acknowledging NT's concerns about administrative complexities, the Committee recommends that the government conduct a thorough impact assessment to determine the feasibility of introducing a staggered implementation approach. This assessment should consider the varying needs, the emergency circumstances of fund members and the administrative readiness of the different retirement funds.

[2]Money Bills Amendment Procedures and Related Matters Act of 2009 is used interchangeably with Money Bills and Related Matters Act in the brief

not the proposed amendment is in line with section 11 (3) of the Money Bills and Related Matters Act in relation to the change in implementation date. Second, in consideration of the advice given about the various options presented for the Committee's deliberation in finalising its report on Revenue Laws Amendment Bill [B39-2023] for November 2023.

2. Revenue Laws Amendment Bill – the context of this brief

The Revenue Laws Amendment Bill was tabled in Parliament by the Minister of Finance on 1 November 2023, together with the 2023 Medium-Term Budget Policy Statement (2023 MTBPS). The RLAB is a section 77 of the Constitution Bill. The tabling of this Bill was preceded by the publication of its draft version (Draft RLAB) on 9 June 2023 to solicit public comments.

The RLAB focuses on pre-retirement preservation where, in accordance with the current retirement regime, individuals are able to make full withdrawals from their pension or provident fund when they cease employment. The RLAB then addresses the two main weaknesses of the current retirement regime. Firstly, the lack of preservation pre-retirement.[3] Secondly, the reality that households in financial distress have assets within their retirement fund(s) that are not accessible in the case of emergencies or financial hardship. The RLAB thus introduces the so-called 'two-pots' retirement system, which seeks to retain the current principle of exempting contributions and growth thereon while taxing the withdrawal of benefits.

The primary objective of introducing the so-called "two-pots" retirement system is to provide flexibility for fund members to access their retirement savings during emergencies but without necessitating resignation from the fund. The rationale behind this system is that in principally focusing upon long-term savings, traditional retirement systems often lack the adaptability necessary to address immediate financial crises. Hence the "two-pots" reform strives for a balance between long-term security and immediate needs in recognising the unpredictability of life and the challenges thrown up in difficult periods. The new system thus permits fund members to access a portion of their savings during crises that may arise, such as the financial challenges presented by the COVID-19 pandemic.

The RLAB consists of eight clauses which introduce the 'two-pots' retirement system. The changes presented here will ensure that the retirement system remains responsive to diverse financial needs. The hope is that the reformed system will support both long-term financial security and immediate assistance during emergencies.

3. SCOF Amendments to RLAB – the proposed implementation date

One of the significant areas of disagreement between the various stakeholders involved in the reform is the proposed implementation date for RLAB. Some stakeholders have argued that the original timeframe is insufficient to accommodate the necessary preparations as regards the proposed date of implementation (1 March 2024). They propose in its place a transition period of 12-18 months following the promulgation of legislation which will be crucial for undertaking essential changes, such as updating systems, staff training and communication while educating fund members about the intricacies of the two-pot system. On the other hand, opposing voices urge the original date of 1 March 2024 to remain effective, citing the pressing financial needs of individuals who do not want to face deferral of the reform due to the delay

[3]The ability of pension and provident fund members to access their retirement interest when terminating employment can create an incentive for fund members to terminate employment as a means of gaining access to those funds, thus prematurely terminating the ability to preserve these funds until normal retirement age is, per the fund rules, reached.

in implementing the legislation. However, the National Treasury opted for deferral and extended the implementation date to 1 March 2025.

The SCOF notes the concerns raised by various stakeholders regarding the proposed implementation date of 1 March 2025. The Committee further recognizes the pressing financial needs of individuals and households awaiting these changes and proposes that the date of implementation be brought forward to 1 March 2024 as suggested by some stakeholders. The Committee has proposed this amendment in line with its roles and responsibility in terms of the Money Bills Amendment Procedures and Related Matters Act of 2009.

The Committee has further noted the suggestion that a staggering mechanism be implemented to address liquidity concerns and market pressures. While acknowledging NT's concerns about administrative complexities, the Committee recommends that the government conduct a thorough impact assessment to determine the feasibility of introducing this staggered approach to implementation. This assessment should consider the varying needs, emergency circumstances of fund members and the administrative readiness of the different retirement funds.

4. Context of the RLAB and Money Bills Act Amendment

The Money Bills Amendment Procedures and Related Matters Act, provides for a procedure to amend money Bills and the Division of Revenue Bills and related fiscal instruments before Parliament. It does so through the following functions:

- Representing the interest of the people on public finances
- Ensuring public participation in the budget process
- Providing norms and standards for amending money bills and for matters connected therewith

Section 11 (3) of the Money Bills and Related Matters Act requires the relevant committees to follow specific criteria when considering the amended revenue Bills and revenue proposals. The proposed amendment to the RLAB requires approval or amendments that relate to the tax treatment of contributions, alongside different rules for withdrawals in terms of the retirement-fund vehicles available to individuals, including pension funds, provident funds, retirement annuity funds, pension preservation funds and provident preservation funds. However, most of the requirements of section 11(3) under consideration fall outside of the proposed amendments to the RLAB, which addresses concerns such as:

- The lack of preservation before retirement
- The lack of access, even in cases of emergency, of some households in financial distress which have assets within their retirement funds

However, the stipulations of sections 11 (3) clauses (b) and (e) are broad enough to warrant the Standing Committee on Finance engage in oversight and propose the amendment under review.

As required by section 4 of the Money Bills and Related Matters Act, the Committee:

(4) (a) Held public hearings on the Revenue Bill

(b) Consulted with other committees

To address the afore-mentioned concerns, the government of South Africa has proposed reforms to the retirement savings regime as part of the ongoing changes introduced since

2012. The proposed 2023 reforms will introduce a 'two-pots' retirement system which, amongst other benefits, makes provision for a "savings component" and "retirement component" available to savers and their existing pot of funds. It also makes provision for the creation of seed capital where, upon the implementation date of the "two-pots" retirement system, this new "seed capital will make available immediate access to an allowable balance within the retirement fund. Here the seed capital refers to the starting balance in the "savings component" of the new "two-pots" retirement system which, from 1 March 2025, should be available to members of the retirement fund for withdrawal on or after this implementation date. In addition, on or after 1 March 2025, retirement funds will be required to create another component (or pot) known as the "retirement component" which will be housed within the current retirement fund.

A proposed date of 1 March 2024 for amendment and implementation of the proposed "two-pots" system has thus been set to give retirement fund members access to a portion of their accumulated benefits in the "vested component" of their funds. However, with the process of reform having started in 2021, the proposed current proposed implementation date has delayed this process by another year with regard to introducing the "two-pots" system. Hence, for stakeholders, this delay of an additional year is one of the significant areas of contestation.

On the one hand, retirement industry representatives argue that the industry requires a transition period of 12-18 months after the promulgation of legislation for the smooth and efficient implementation of the new system. On the other hand, representatives of the unions and civil society argue that many individuals are under severe pressure and require more immediate access to the funds. They argue that the proposed changes to the system had already been announced as part of the programme of Covid-19 support for citizens.

After considering the proposals by the National Treasury and inputs from stakeholders and the public, the Committee proposed an amendment of the RLAB to push forward the implementation date of the two-pots retirement system from 1 March 2025 to 1 March 2024. The Minister of Finance has been given fourteen days to respond to the proposed amendment, which is in line with section 5 of the Money Bills Amendment Act of 2009.

5. Discussion – the various perspectives and challenges to consider

5.1. Proposed amendment and Section 11 of the Money Bills and Related Matters Act

The amendment aims to address inconsistencies and complexities in the existing retirement fund system, which has an impact on tax collection as reflected in Section 11(3)(a) of the Money Bills and Related Matters Act. By introducing the "two-pots" retirement system, the reforms strive to harmonise tax treatment, enhance preservation, reduce charges and improve governance. These objectives align with the broader fiscal framework by promoting efficiency, equity and consistency in tax treatment.

Furthermore, the reforms consider the impact upon individuals' and households' financial behavior, encouraging preservation before retirement and providing flexibility for withdrawals in emergencies. However, the system puts a strict government regulation limit on the amount that individuals can withdraw. The NT is of the view that the proposed "two-pots" system addresses concerns related to access, immediate needs and financial distress, fostering responsible financial choices. However, this may stem from the fact that government may well raise concerns that it may have to provide more social support in the future if household can access their retirement funds, while the private sector is worried that their funds under management may decline, resulting in decreasing profits. Accordingly, the NT is of the view that the proposed "two pots" system tackles concerns related to access, immediate needs, and financial distress, fostering responsible financial choices In the light of the cost-of-living crisis and concerns about immediate financial needs, this solution will work to alleviate some of the pressure within the constraints of the current operation and governance of the pension system. Moreover, this approach is unlikely to impact negatively upon development, investment, employment and economic growth being that it establishes a more flexible and responsive retirement system in alignment with Section 11(3)(e) of the Money Bills and Related Matters Act.

The "two-pots" system will provide relief to pension fund members. However, the effect and size of the impact of this relief on the economy is unknown at this stage. The NT may have to provide appropriate estimates in the near future. However, it is unlikely that "two pots" system and related fund withdrawals will negative impact on the economy.

In terms of equity and fairness, the NT is thought to be balanced and fair. Hence, through approval of the system, the Committee has concurred that the suggested amendments offer a balanced approach. The "two-pots" system enables individuals to access a portion of their retirement savings before retirement and in doing so, the RLAB initiative addresses the lack of motivation for preservation before retirement.

The introduction of "seed capital" and the division into "savings" and "retirement" components in RLAB has as its objective to balance immediate needs with long-term financial planning, ensuring fair treatment for members as advocated for in Section 11(3)(b) of the Money Bills and Related Matters Act. Overall, it seems that the SCOF-proposed change in date for the amendment aligns with the overarching principles and objectives outlined in section 11 of the Money Bills Amendment Procedure and Related Matters Act of 2009.

5.2. Key retirement industry concerns about the proposed implementation date

Administrators in the retirement industry have noted that meeting the deadline of March 1 2024 depends upon the finalization and gazetting of the 2023 Draft Revenue Laws Amendment Bill, along with realisation of the necessary Pension Fund Amendments governing the 'two-pots' system. The completion of this legislation (RLAB) is thus crucial for pension funds to prepare adequately for implementation of the impending system.

The retirement industry is clear that successful implementation of RLAB is also contingent upon the South African Revenue Service and the Financial Services Conduct Authority (FSCA) updating their operations in order to be fully prepared for the new two-pots system. The retirement industry emphasizes their heavy reliance on SARS to provide guidance on the requirements for processing early withdrawal claims. Without this essential information, they will be unable to carry out the necessary system modifications to facilitate these transactions.

In addition to these regulatory challenges, industry stakeholders have expressed the need for an extended timeline to address several critical aspects adequately. These elements of implementation include

- testing their systems against irregular and fraudulent claims
- seamless integration of SARS processes with their systems
- training of staff and members and communication with them, and
- education of customers about impending changes.

However, assuming that the RLAB is passed by both Houses of Parliament in December 2023 and that the President accents the law within the same period, the industry has underlined how they will be confronted with a limited two--month window for implementation of the "two-pots system. This compressed timeframe adds pressure to the already intricate process of preparing for implementation of the two-pots system and executing it. Such concerns are concrete about the feasibility and effectiveness of meeting the proposed deadline of 1 March 2024, with industry representatives emphasizing the need for a more realistic and accommodating timeline to ensure a smoother and more successful implementation process.

6. SCOF Considerations – Parliamentary Budget Office Advise

In the draft Report of the Standing Committee on Finance on the Revenue Laws Amendment Bill [B39 - 2023], the Committee has proposed that the implementation date for RLAB be restored to the original date, 1 March 2024 as opposed to the National Treasury implementation date of 1 March 2025. The Committee's Content Advisor has subsequently requested that with regard to the Committee's action, the Parliamentary Budget Office clarify whether or not the proposed amendment has fulfilled the requirement of the section 11 of Money Bills and Related Matters Act related to amendments to revenue bills. Secondly, the Parliamentary Budget Office should advise as to whether the Committee is required to give any further consideration of this proposed amendment.

The PBO advice to SCOF is then as follows:

A. Having looked at the specific requirements of section 11 (3) addressing the amending revenue bills and revenue proposals in Parliament, it is clear that the Committee's decision to effect this specific amendment (restoring implementation to the original date, 1 March 2024 as opposed to the National Treasury implementation date of 1 March 2025) will not have direct if limited implications for the approved 2023 fiscal framework and Division of Revenue Bill.

B. The proposed amendment addresses concerns related to access, immediate needs and financial distress within a context of fostering responsible financial choices. Consequently, this amendment is likely to impact positively upon development, investment, employment and economic growth by establishing a more flexible and responsive retirement system in alignment with section 11(3)(e) of the Money Bills and Related Matters Act.

C. Without undermining paragraphs "A" and "B" above that the SCOF-proposed implementation change is in line with section 11 (3), the Parliamentary Budget Office further recommends that SCOF consider and seek to address some of the stakeholders' concerns and tackle the challenges related to implementation dates by considering the following options:

   i. **Middle Ground:** In this approach, 1 March 2024 remains the effective date of implementation. However, a provision is made in the Bill that if the stakeholders still require time to prepare then they should be given a grace period of six months after the date of implementation until the 1 September 2024. In that case, 1 September 2024 will be the date when all stakeholders are required to comply fully with RLAB. or

   ii. **Phase-in or Staggering Approach:** This approach allows for a smoother transition from 1 March 2024 until the 28 February 2025. Thereafter, the Act should be fully implemented. This phase-in approach should aim to limit the quantity of withdrawals by also acting as a pilot process for the new system. It may also be considered a way to limit the amount of the withdrawals from 1 March 2024. In addition, the phase-in period would help to improve communication strategies and so educate stakeholders more effectively about the forthcoming changes, thereby mitigating potential confusion and user resistance. or

iii. **Extending the implementation date:** Despite the SCOF-proposed amendment being in line with section 11 (3), and in light of the some of the key stakeholders' concerns, the Committee may consider moving the full implementation to a later date in the 2024 calendar year. One proposed date is 1 September 2024 or any date considered reasonable by the Committee. In doing so, the stakeholders will be afforded more space to address current concerns raised about their readiness to establish the requisite systems.

D. In light of the complexities and contestations around the implementation of the "two pots" system, the Committee may consider recommending for the establishment for task team within government and affected stakeholders to oversee the initial implementation process. Such task team may be requested to provide Parliament with regular update about the progress of the implementation of the "two pots" system.

The Parliamentary Budget Office has brought it to the Committee's attention that the legislation should first be enacted in order for the industry to conduct a comprehensive and thorough assessment of their readiness to implement the reforms. It is thus crucial for Parliament to ensure that its process is concluded as per planned in December 2023. In this way, the Presidency and government alike will play a role in ensuring the act is gazetted within a reasonable timeframe.

The Parliamentary Budget Office recommends the adoption of the Standing Committee on Finance Draft Report on the Revenue Law Amendment Bill [B39 - 2023]. However, its adoption should be accompanied with the provision that Observations and Recommendations 5.3 be updated in consideration of the PBO advise outlined in this brief.