By Ina Opperman
Business Journalist
15 May 2024 | 01:37 pm

Beware of these myths about the two-pot retirement system

The two-pot retirement system will come into effect after the enactment of the Pension Laws Amendment Bill.

Image: iStock

Despite wide media coverage of how the two-pot retirement system will work once it is implemented on 1 September, the new way of saving for retirement is still surrounded by various myths that indicate that consumers do not really understand how the system will work.

Privacy

It also does not help that people focus on the money they want to withdraw instead of the main objective of the new two-pot retirement system to preserve your retirement savings to ensure that you can retire more comfortably because you have saved enough.

"The two-pot retirement system is primarily designed to encourage long-term savings and preservation of retirement investments," Gontse Tsatsi, head of Retail Clients at Old Mutual Investment Group, said at the launch of the asset manager's Long Term Perspectives annual publication in Johannesburg recently.

According to the legislation, retirement savings accumulated until 1 September 2024 will go into a "vested component", which will not be subject to the new rules.

ALSO READ: Two-pot retirement system will bring major change in R3.27 trillion industry

READ MORE
Police seize counterfeit goods over R3m and arrest Pakistani national

How the savings component will be funded

Thereafter, one-third of pension fund contributions will flow into the "savings component" and two-thirds into the "retirement component". The two pots refer to how the money will be allocated from 1 September 2024, which is the savings pot and retirement pot. The savings pot will receive once-off "seed capital" from the vested pot of 10% of savings to a maximum of R30 000.

"This means that everything saved in a pension fund until 1 September 2024, except for the seed capital, will be treated as it was in the past, governed by the current Pension Funds Act and Fund Rules," Tsatsi said.

"From 1 September the new system will allow people to access what they have accumulated in the savings pot once a year and investors will not have access to the retirement pot until retirement."

Tsatsi emphasised that the purpose of the new system is to enable South Africans to save enough for a comfortable retirement by preventing them from cashing in all their savings each time they change jobs.

However, he said, there are several myths about the new system circulating among the public that must urgently be debunked:

#Myth 1: I am finally going to get my pension money

"You will only have access to the money in the savings pot, which will include the seed capital of up to R30 000 before tax at a marginal rate. The Act makes this provision so that investors can access their retirement funds once a year in case of an emergency. "

Privacy

However, he said, making a habit of using your retirement fund for emergencies is not recommended, as all your pension assets, including those in the savings pot, should ideally be used for retirement.

ALSO READ: **Two-pot retirement system: these are the risks**

#Myth 2: I can still access my pension money if I resign?

Tsatsi says the only pension money you will have access to if you resign will be the funds that are in the vested component (from original retirement savings before the Act is effective on 1 September 2024), as well as those in the savings pot (after 1 September 2024).

“Money accumulated in the retirement pot after 1 September 2024 will not be available to you if you resign and change jobs. Also remember that if you resign and deplete your component and savings pot, you will have only your retirement pot in the future.”

#Myth 3: There will be no taxes or charges on my withdrawals

There will be a flat administration fee on once-yearly withdrawals from the savings pot, Tsatsi says. However, the major “cost” will come from the taxman.

“The withdrawal will be taxed at your marginal tax rate. For example, if you withdraw R30 000 and your marginal tax rate is 26%, the pension fund will deduct tax of R7 800.” In essence, this means that you lose the tax benefit from your retirement savings.

ALSO READ: **No two-pot retirement system withdrawals already on 1 September**

#Myth 4: I can withdraw money at any time in the case of an emergency

Not true, Tsatsi says. “You can withdraw from your savings pot only once a year. National Treasury initially envisaged the savings pot to be used for emergencies, but the final legislation does not stipulate what the money can or cannot be used for.”

Withdrawals must be a minimum of R2 000 before tax and “once a year” refers to the tax year from 1 March to 28 February of the following year.

#Myth 5: My pension fund will be a great vehicle for financial emergencies

Although the money in the savings pot may be useful in an emergency, such as when you have lost your job or are about to undergo an expensive medical procedure, Tsatsi said you should only use this route as a last resort, not least because of the high tax you will pay on withdrawals.

Privacy

"Our key recommendation is to have a separate emergency fund, which should be the equivalent of at least three months' living expenses, funded from discretionary savings. This can be in a low-risk, interest-bearing unit trust fund. Money can be accessed easily without any hassles or limitations and the only tax charged is on the capital gains," Tsatsi explained.

He pointed out that it is imperative for South Africans interested in withdrawing from the two-pot retirement system to approach it from a well-informed perspective by seeking advice from a qualified financial adviser who can help them plan for the short and long term.

"From our Long-Term Perspectives research, it is clear that to truly build wealth, investors need time and must take advantage of the eighth wonder of the world, compounding interest."

ALSO READ: Two-pot retirement system: Advice can prevent you walking off financial cliff

Consumers must remember withdrawals are only for emergencies

He also urges consumers to remember that although the savings pot should be used for emergencies only, constant withdrawals will mean that your lump sum at retirement is depleted and about a third of the life savings will not enjoy the benefits of investment growth and compounding.

"When you consider it in this way, a third is a huge amount," Tsatsi warned.

He noted that Old Mutual initially, at the end of 2021, analysed the likely withdrawals from a "segment" perspective. "From this viewpoint, Old Mutual Investment Group/Old Mutual Unit Trusts, catering to middle to high-income clientele, anticipated relatively low withdrawals at the time.

"However, over the past three years, there has been a shift, showing the cost burden on clients across all segments, from low to high LSM, due to increases in the prices of fuel, electricity, rates and taxes and interest rates.

"While the assumption focuses on the impact on low LSMs, it is important to note that these increases also affect those with housing loans and vehicle financing agreements. Given the process of the two-pot system over the past three years, the initial and current perspectives differ. We now anticipate withdrawals even from the middle to high LSMs."

He said Old Mutual's analysis shows that R14.2 billion is in play, with R7.9 billion from retail retirement products and R6.3 billion from occupational schemes.

Catch up with the latest news from **The Citizen** on WhatsApp by following our channel. Click here to join.

Privacy