Vickers & Peters
LIFESTYLE AND ASSET PLANNING

Around the Table with Vickers & Peters Financial Planning

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Tax changes – Effective: 01 March 2014

Reforms to retirement savings

Individuals' contributions to pension and retirement annuity funds are and will remain tax deductible. However, the deductibility of such contributions, as well as contributions to provident funds and employer contributions (that will constitute fringe benefits) will be increased to **27.5%** of the greater of remuneration or taxable income (excluding retirement annuity or lump sum income). An annual cap on deductible contributions of R350 000 will be applied.

Tax treatment of contributions to pension, retirement annuity and provident funds will be standardised, allowing provident fund members to receive a tax deduction on their own contributions. Vested benefits will be protected as balances in provident funds at the date of implementation and subsequent growth will not be required to be annuitized (purchase a compulsory pension).

It is proposed, however, that future contributions made to provident funds (after an agreed date) be subject to the same annuitisation requirements applicable to retirement annuity and pension funds (one third lump sum and two third's a compulsory pension). This requirement will not apply to provident fund members older than 55 years at the date of implementation. New employees can still join and contribute to existing provident funds, and new funds can be created subject to the same tax and annuitisation rules. This will reduce the complexity of the retirement system significantly.

Contributions in excess of the annual caps may be rolled over to future years. Any non-deductible contributions remaining at retirement will be set off against any lump sum or annuity income before tax is calculated to avoid double taxation. Specific provisions will need to be made for defined-benefit pension plans and will require further engagement with industry.

Employer contributions: Contributions by employers to retirement funds are to be fringe benefit taxed.

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Unapproved (i.e. non retirement fund owned) disability or income protection policies: SARS has traditionally allowed deductions for income protection rather than income capacity policies. This has lead to much confusion and debate as regards to whether the deduction was available or not. In response to this, it is proposed that the premiums paid in respect of all unapproved risk policies will be non-deductible, with the proceeds of these policies being tax free.

Review of long-term insurance taxation

Policies representing the risk business of long-term insurers (assets which underpin the liabilities) will no longer be taxed in the individual policyholder funds (30%) but in the corporate policyholder fund (28%). The result is a higher level of tax savings for individuals invested in these products with marginal tax rates above 28%.

Example:

John has an individual tax rate of 35% and cannot decide whether he should invest his R5 million inheritance into a Unit Trust Fund or into an Endowment Fund.

Capital	R 5,000,000.00	Portfolio asset allocation
Total Return	12.00%	
Interest Yield	6.00%	50%
Dividend Yield	2.00%	50%
Marginal Tax rate	35.00%	
4 Fund tax rate (corp.fund)	28.00%	
Dividend Withholding Tax	15.00%	
Interest exemption pa	R 22,800.00	

Endowment	Year 1	Year 2	Year 3	Year 4	Year 5	
Capital Value	R 5,000,000.00	R 5,501,000.00	R 6,052,200.20	R 6,658,630.66	R 7,325,825.45	
Total return	R 600,000.00	R 660,120.00	R 726,264.02	R 799,035.68	R 879,099.05	
Interest earned	R 300,000.00	R 330,060.00	R 363,132.01	R 399,517.84	R 439,549.53	
Tax paid on interest portion	R 84,000.00	R 92,416.80	R 101,676.96	R 111,865.00	R 123,073.87	
Dividends earned	R 100,000.00	R 110,020.00	R 121,044.00	R 133,172.61	R 146,516.51	
Tax paid on dividends earned	R 15,000.00	R 16,503.00	R 18,156.60	R 19,975.89	R 21,977.48	
Total tax paid	**R 99,000.00**	**R 108,919.80**	**R 119,833.56**	**R 131,840.89**	**R 145,051.34**	**R 604,645.59**
Capital Value	**R 5,501,000.00**	**R 6,052,200.20**	**R 6,658,630.66**	**R 7,325,825.45**	**R 8,059,873.16**	**R 8,059,873.16**

Unit Trust	Year 1	Year 2	Year 3	Year 4	Year 5	
Capital Value	R 5,000,000.00	R 5,487,980.00	R 6,022,806.08	R 6,608,975.46	R 7,251,417.11	
Total return	R 600,000.00	R 658,557.60	R 722,736.73	R 793,077.06	R 870,170.05	
Interest earned	R 300,000.00	R 329,278.80	R 361,368.36	R 396,538.53	R 435,085.03	
Interest exemption pa	R 22,800.00	R 22,800.00	R 22,800.00	R 22,800.00	R 22,800.00	
Taxable interest	R 277,200.00	R 306,478.80	R 338,568.36	R 373,738.53	R 412,285.03	
Tax paid on interest portion	R 97,020.00	R 107,267.58	R 118,498.93	R 130,808.48	R 144,299.76	
Dividends earned	R 100,000.00	R 109,759.60	R 120,456.12	R 132,179.51	R 145,028.34	
Tax paid on dividends earned	R 15,000.00	R 16,463.94	R 18,068.42	R 19,826.93	R 21,754.25	
Total tax paid	**R 112,020.00**	**R 123,731.52**	**R 136,567.35**	**R 150,635.41**	**R 166,054.01**	**R 689,008.29**
Capital Value	**R 5,487,980.00**	**R 6,022,806.08**	**R 6,608,975.46**	**R 7,251,417.11**	**R 7,955,533.15**	**R 7,955,533.15**

5 yr Endowment tax saving	R -84,362.69
5 yr difference in capital value	R 104,340.01

Notes: Assumed no Capital Gains Tax as investment is held for full term without selling or switching portfolios.

Assumed 50% of portfolio invested in equity and 50% invested in interest bearing assets

Assumed balance of total equity return 4.00% is due to share price re-rating

The above investment analysis illustrates the tax liable of the endowment Fund versus a unit trust fund and its direct impact on future capital values. Ignoring the liquidity restraints of the endowment, John would be better served investing his inheritance in the endowment fund and not the unit trust fund.

Research will be undertaken during 2013/14 on a number of topics, including:

- The effectiveness of various tax incentives.
- The taxation of various innovative financial instruments.
- A single unified treatment of dividend cessions and dividend compensation payments.
- Certain anti-avoidance rules to eliminate the shifting of income from taxable parties to exempt parties are also considered.
- An exemption for shipping income to attract international shipping.
- Debt relief to assist distressed debtors (such as business rescue) from VAT input tax claw-back provisions.
- The default application of the turnover apportionment method to non-financial sectors for VAT purposes.
- The alignment of new pension margin requirements with related tax rules.

VPFP will keep you updated on these proposals in future editions of Around the Table.

The value of a properly structured Buy and Sell Agreement

Buy and Sell agreements should be reviewed on a regular basis and updated whenever there has been a change within the company or your personal circumstances. These are the 10 basic mistakes that can occur in Buy and Sell agreements, and the policies used to fund the agreement.

1. No signed Buy and Sell agreement

This means that there is no obligation to buy or sell on death or disability. There is no value for the partner's share of the business if it is eventually sold. There is no exemption for Estate Duty, as there is no proof that the life assurance policy was intended for buy and sell purposes.

2. Policies are company owned

This will mean that the proceeds are Estate Dutiable. If done as a conforming policy, you will lose Income tax of 28%. Therefore, 20% lost for Estate Duty, 28% for Income tax, 15% for DWT (Dividend Withholding Tax). If no provision for this was made upfront, you sit with a real shortage of cash to buy the shares.

3. Premiums are claimed as a tax deduction

If the policies are not company owned, policies are non-conforming, then premiums are NOT tax deductible. If your policy has been set up in error as a conforming policy, you would need to replace it.

4. Company pays premiums , loan accounts are not set up properly

In this situation, the individual partners own the policies and the company decides to pay the premiums for the policies on their behalf. This causes individuals to have a debit loan account with the company that should be settled EVERY month. If this is left to year end, they have effectively received a taxable fringe benefit. If the situation continues over a tax year, then the company has paid the premiums and not the individual, this is definitely a tax problem.

5. The shares are overvalued in the Buy and Sell agreement

The purchase price of the deceased's equity in the company shall be the greater of:
an amount equal to the total net proceeds (after allowing for payment of any tax, duty or levy that may be due) of the policies of assurance; or the value placed on the deceased's equity by the auditors.

If the purchaser pays more for the shares than they are worth, he will be making a donation. As the donor, he will have to pay Donations tax of 20%, even though he has paid over the proceeds. The South African Revenue Service could also look to disallow part of the policy for estate duty exemption, as it could be argued that the policy is not a legitimate buy and sell policy**.**

6. The shares are undervalued in the Buy and Sell agreement

This happens when the parties to the Buy and Sell agreement cannot afford the cost of the life and disability cover. In this situation, the Deceased's estate would be making a donation and would have to pay Donations Tax, this is in addition to the heirs receiving

less than the business is worth. A way to structure this situation is that the outstanding amount be paid off over a period of time. This must be specified in the agreement.

7. What if you become disabled, and don't die?

Allow for disability in the Buy and Sell agreement and the policy. Make sure that the definition of disability matches between the policy and the agreement. If partial disability is allowed via the policy, you need to consider if it will trigger a pro-rata buying of shares?

8. The share values are not updated, there is no clause in the Buy and Sell obliging parties to do this

This could lead to the heirs only being paid what the Buy and Sell values the shares at, unless there is a clear clause in the agreement stating otherwise. It is important that you value the business accurately and that the values are updated at least yearly. If not your heirs payout could be seriously undervalued.

9. Shareholders agreement contradicts the Buy and Sell agreement, no provision for Interest on purchase

Most shareholders agreements contain a short clause on buy out of shares on death and disability. To avoid contradictions, you should consider removing it when the Buy and Sell is signed.

Every Buy and Sell should have an interest clause provision, for late payment. This should relate to late payment of outstanding purchase price, as well as late payment to purchase shares after receipt of the policy proceeds.

The Buy and Sell agreement should ensure that the partners buy each other out pro-rata to their current interests, in case the ownership percentage is not reflected properly.

10. No need for a Buy and Sell agreement, will be sorted out in the Will

There is a risk here... Wills can be changed at any time, the agreement cannot. Consider... if the business goes to one family member... how do the others get compensated?

In Summary

What should a buy and sell agreement determine?

- Who will buy and who will sell?
- What is bought or sold?
- When?
- At what price?
- How was value determined?
- How will the purchase price be paid?
- How will the purchase price be funded?

There is no place for an option to buy shares in continuation planning for a business. Don't let an option destroy your succession planning. We recommend that the buy-and-sell agreements and the life assurance policies underlying these agreements be subjected to a regular legal audit in order to ensure, not only their validity, but also their relevance to your overall estate plan.

Home Employees and Domestic Worker Retirement Savings

For many of us in South Africa, our domestic workers play an important role in our families, and often are considered more than just staff members. And as their employer we have the same obligations to assist our home staff with their savings for retirement as any big corporation or business does with their staff, especially in South Africa, where government assistance in terms of Retirement Savings is close to zero.

At VPFP, our Employee Benefits division, headed by Chris Ellis, has found a reliable and cost efficient product offering retirement savings for your domestic and home employed staff. The Absa Home Employees Provident Fund is an employee benefits package that offers participating employers the means to provide their employees with a Retirement Savings Fund. The fund provides retirement and withdrawal benefits, with the option for associated separate group risk schemes offering death, disability and funeral benefits. The fund comprises several plans, each offering unique benefits at affordable monthly contributions.

The final retirement savings amount is not a guaranteed amount; rather it is the total of all contributions, less fees and costs, plus investment returns. With this in mind the earlier you begin saving for your staff, the more the staff will have accumulated at retirement.

The Absa Home Employees Provident Fund is designed specifically with the domestic employers and body corporate in mind and there is no minimum number of employees you need to have in your employment before you can participate in the fund. The Absa Home Employees Provident Fund is a provident fund and is registered with the Financial Services Board. As per the below table, this product caters for all contribution options, and is a cost effective and simple solution. **It is important to note that the normal retirement age is 65 and that risk benefits cease at the age of 65.**

Membership of the fund is simple and done through you the employer. Your staff have the option to take their accumulated savings only on termination of your employment contract, be that through dismissal, resignation, retrenchment or retirement.

Should wish to receive more information on this simple yet vital retirement savings product, please contact the Employee Benefits team at Vickers and Peters on 011 803 3663 or 011 803 7399.

Absa Home Employees Provident Fund Fees as from 01/08/2012

Plan		A	C	D	E	F	G	H	I	J
Contribution		R 127.00	R 127.00	R 171.00	R 248.00	R 342.00	R 589.00	R 826.00	R 1,155.00	R 1,391.00
Death & Capital Disability Cover	Cover	R 0.00	R 10,000.00	R 15,000.00	R 25,000.00	R 5,000.00	R 75,000.00	R 100,000.00	R 150,000.00	R 200,000.00
	Premium	-	R 9.70	R 14.55	R 24.25	R 48.50	R 72.75	R 97.00	R 145.50	R 194.00
Funeral Cover	Cover	R 0.00	R 7,500.00	R 10,000.00	R 10,000.00	R 10,000.00	R 10,000.00	R 10,000.00	R 10,000.00	R 10,000.00
	Premium	-	R 13.50	R 18.00	R 18.00	R 18.00	R 18.00	R 18.00	R 18.00	R 18.00
Admin Fee	Admin ACA	R 17.10	R 17.10	R 17.10	R 17.10	R 17.10	R 17.10	R 17.10	R 17.10	R 17.10
	Admin Intermediary	R 7.24	R 7.24	R 9.75	R 14.14	R 15.00	R 15.00	R 15.00	R 15.00	R 15.00
Less Total Cost		R 24.34	R 47.54	R 59.40	R 73.49	R 98.60	R 122.85	R 147.10	R 195.60	R 244.10
Net Contribution		R 102.66	R 79.46	R 111.60	R 174.51	R 243.40	R 466.15	R 678.90	R 959.40	R 1,146.90
% of Contribution		80.84%	62.57%	65.26%	70.37%	71.17%	79.14%	82.19%	83.06%	82.45%

Admin fee is split as follows:

a) Admin ACA is R17.10 (incl. VAT), plus

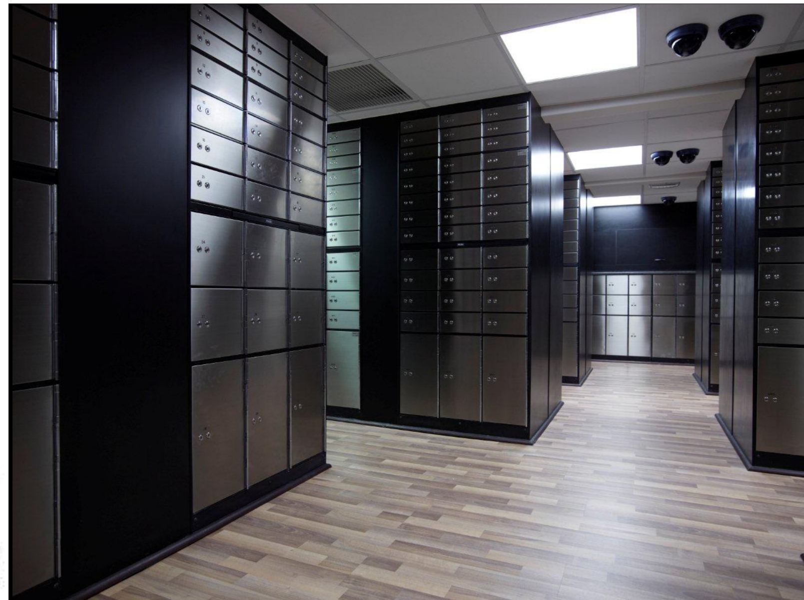
b) Admin intermediary is based on 5.7% of actual contributions (incl. VAT) **MAX of R15.00**

Death/disability cover rate = R0.97 per R1000

Funeral cover rate = R1.80 per R1000

Clients looking for safe deposit boxes and off-site safety vaults

High valued jewelry and specified personal valuables that are kept at home are vulnerable assets which can be safe-kept at an attractive, cost effective Safe Deposit company, called Knox Titanium Vault Company. Knox offers an alternative option to keeping your assets in a safe at home. They will offer VPFP clients a 20% discount to retail. Please contact Wayne Becker on 011 646 1919 for further information. **www.knoxvault.co.za**



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Macro Overview

Global markets experienced extreme volatility in the first quarter of 2013, beginning the year with many stock markets around the world reaching multi-year highs on the back of a last minute agreement out of the US to avoid the impending Fiscal Cliff. However, the positive mood subsided after minutes from the January US Federal Open Market Committee (FOMC) meeting suggested a possible scaling back of the Fed's quantitative easing programme, causing fear around the effect on the already sluggish US economic recovery and triggering a 19% spike in the Volatility Index (VIX) (a measure of implied volatility and often referred to as Wall Street's "fear gauge"). Fed Chairman Ben Bernanke later dispelled fears, confirming the Central Bank's commitment to its quantitative easing programme.

The Italian government elections in February added to fears of European political uncertainty. Furthermore, in mid-March, Cyprus became the fifth of the euro's 17 member states to request a bailout. Despite being the third smallest Euro economy, the proposed bailout plan (to tax Cypriot bank deposits) raised concerns over the stability of Euro Zone financial institutions, in addition to apprehension surrounding the potential precedent that has been set for future sovereign bailouts in the region. The Italian elections and Cypriot bailout request again demonstrated how sensitive markets are to Europe's debt problems and their destabilisation capability.

Notwithstanding the increased levels of investor anxiety throughout the quarter, equity markets ended the period on a positive note, with particularly strong performance out of the US and Japan.

Performance – *what added and what detracted?*

The largest contributor to performance of the funds was the 10% weakening of the rand to the US dollar, coupled with strong performance from global equity markets.

In addition, local equity fared well, with particularly strong performance out of industrial stocks.

- Local property was another winner over the quarter.
- The primary detractor of performance was resource stocks.
- Both local and global bonds were relatively flat over the quarter.

Position going forward

The funds remain cautiously positioned, given the significant swings of volatility across markets, asset classes and sectors. We prefer equities to fixed interest on a relative valuation basis, but remain cautious in local equity, choosing to be positioned marginally underweight versus our benchmark. Within the fixed interest space, we favour income-enhancing strategies to cash and pure bond exposure.

Offshore, we remain overweight equities and underweight fixed interest, although we have increased our fixed interest exposure through active mandates. In general, we have moved away from a predominantly passive investment strategy to a more active and index-enhanced strategy as we believe the current market conditions and economic environment are conducive to active management, which can add considerable value from a performance and risk management perspective. We are confident that this will enhance the fund returns going forward.

VPFP Fund Performance for the Period Ending 28 March 2013

Fund or Benchmark	3 Month	6 Month	1 Year	2 Years	3 Years	4 Years	Inception	
	Return	Return	Return	Return	Return	Return	Return	Risk
VPFP CPI + 2	**3.74%**	**7.16%**	**15.74%**	**28.13%**	**38.32%**	**54.79%**	**56.45%**	**4.43**
Investment Objective (CPI + 2%)	2.05%	4.37%	7.93%	16.83%	23.60%	33.20%		
VPFP CPI + 4	**4.37%**	**8.82%**	**16.94%**	**27.21%**	**38.35%**	**61.45%**	**51.55%**	**6.28**
Investment Objective (CPI + 4%)	2.54%	5.39%	10.05%	21.46%	31.01%	43.96%		
VPFP CPI + 6	**4.57%**	**10.25%**	**18.14%**	**27.70%**	**40.01%**	**72.84%**	**45.51%**	**9.20**
Investment Objective (CPI + 6%)	3.03%	6.40%	12.16%	26.17%	38.72%	55.36%		
JSE All Share Index	**1.56%**	**11.47%**	**18.80%**	**23.78%**	**38.66%**	**95.74%**	**24.00%**	**17.85**

Inception 12/05/2008 *(CPI Benchmark as at 28 February 2013)*

Source: MoneyMate

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Our services include…

- Pre and Post Retirement Planning
- Local and Global Investments
- Business Assurance – Key person and Partnership
- Personal and Group Life Assurance
- Employee Benefit Advice and Products
- Tax and Estate Planning

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