Why a retirement annuity is a good choice to boost your savings

For clients looking to boost their retirement savings an investment Retirement Annuity is an excellent choice. Although you cannot access the money before age 55 (which could be also seen as a good thing), an investment RA allows the investor greater flexibility and choice. There are no contractual terms, as it is in most cases with your traditional life product RA, which means there are no penalties if you decide to stop contributing. In addition you can make ad hoc contributions when you like or reinstate your regular contributions at the same, higher or lower rate (subject to product minimums). There are also no maturity dates beyond the legislative retirement age 55, which means you are not locked in for extended periods or penalized for early exit. In terms of fund manager selection your investment choice is unrestricted with full access to the VPFP managed portfolios.

Reasons to investment in an investment Retirement Annuity

- Disciplined approach to create wealth for a financially secure retirement – access your investment funds from age 55.
- Ideal opportunity to expose your investment to growth assets, which are essential to generate inflation-beating returns.
- Ideal opportunity to capitalise on the power of compound growth.
- Tax concessions you just cannot afford to ignore:
    - Contributions are tax deductible* – money you would have paid to SARS can now generate investment returns for you.
    - No income tax, Interest, Capital Gains Tax or dividend withholding tax (DWT) on investment returns – your investment can grow faster than most other investment vehicles.
    - Favourable tax treatment at retirement – if you select a one-third lump sum, at least R500 000 may be tax free.
    - No tax on two-thirds used to purchase a compulsory annuity to provide income after retirement – more money in your pocket.
    - Income after retirement is taxed as normal income (higher rebates from age 65).
    - Retirement funds are exempt from estate duty – all your RA money goes to your dependants.
- Protection against claims from creditors, with certain exceptions – nobody other than you or your loved ones can touch your retirement money.
- Any contributions to a RA that did not qualify for a tax deduction will be allowed to be offset against taxable income at retirement – **please see article "Reducing your Tax Rate at Retirement" for details.**

Note* from March 2015 employer contributions to retirement funds will be taxed as fringe benefits in the hands of employees. Employees may deduct up to 27,5% of remuneration or taxable income in respect of contributions to pension, provident and retirement annuity funds, subject to an annual cap of R350 000.

A product example and summary is provided below

Scenario

Client aged 40 runs his own business and is not a member of a pension or provident fund. He has made very little provisions for retirement, and is therefore not making use of the generous tax concessions for taxpayers contributing to retirement funds. The client is reluctant to take out a Retirement Annuity because he has other investments.

Solution

By not investing at least some of his money in a retirement annuity, the client is passing up the following benefits:

- In terms of Section 11(n) of the act (see above) the client would be able to claim a tax deduction of the premium (up to 15% of his taxable income (increasing to 27.5% in 2015/16), as it would all be non-retirement funding, seeing as he is not a member of a pension/provident fund).
- The investment will be untaxed.
- When the client retires, he will be able to draw a lump sum of up to R500 000.00 tax free.
- Finally, the retirement annuity will generally (assuming no intent to defraud creditors) be protected on insolvency, and is a nice "nest egg" for the self employed client.

Benefits

The client has an investment where the contributions were tax deductible at his marginal rate of up to 40%, there was no tax within the portfolio, and when he retires, he is able to draw up to R500 000 tax free. In addition, the investment is protected on insolvency! What other investment has these benefits?

Conclusion

All self employed and people not contributing to a retirement fund should be allocating at least part of their investment contributions to a retirement annuity. By failing to do so they are simply not utilising major tax benefits allowed in the Income Tax Act. Due to the compounding effect of the untaxed investment returns, the effective rate of return generated by a RA is unmatched.

Retirement Annuity	
Investment Income (Interest, Dividends, Rental Income)	Non Taxable
Capital Gains Tax (CGT)	Non Taxable
On death	CGT exempt & estate duty exempt
Creditors claim on insolvency	Protected
Tax deductable	RA - up to 15% of non retirement funding income* see note
Liquidity	RA - can only access at age 55 or disability
Retirement	RA can access up to 1/3 with R500 000.00 tax free
Income payment	Income from annuity is taxable income
Regulation 28	Needs to be compliant (can only invest up to 75% in equity)

Reducing your Tax at retirement

Before 01 March 2014, any disallowed contributions that did not rank for deduction in terms of section 11 of the Income Tax Act could be offset against any taxable **lump sum** taken at retirement. However, members that elected to use their entire benefit to purchase a compulsory annuity and receive a monthly income, did not benefit from this exemption. Section 10C was promulgated to rectify this and to encourage members not to take a lump sum, or to take a smaller lump sum, at retirement.

The change to Section 10C of the Income tax Act therefore states any aggregate of a person's own contributions to a retirement fund that did not rank for a tax deduction against that persons income, shall:

- Firstly, be deducted against any retirement fund lump sum, and
- Any remaining amount can then be applied in respect of the aggregate of compulsory annuities* payable to a person during any year of assessment.

This section is applicable from 1 March 2014 and applies in respect of amounts received or accrued on or after that date.

Note*'compulsory annuity' means the amount of the remainder of the retirement interest of a person payable in the form of an annuity as contemplated in –

a. annuity from pension fund; or

b. annuity from pension preservation fund; or

c. annuity from retirement annuity fund

Example:

John received an inheritance of R5 million. He decides to invest this amount in a retirement annuity for reasons highlighted in the previous article. John is 55 years old.

Later that year John decides to retire from the retirement annuity, before claiming any tax deduction in respect of the contribution made to that retirement annuity.

John has a few liabilities he would like to settle and has elected to access a portion of his retirement annuity as a lump sum.

He takes a lump sum of R1 000 000 and transfers the rest of the funds to a living annuity. His living annuity income is R500 000 per annum.

Lump sum at retirement of RA	R1 000 000.00
Less previously disallowed contributions limited to lump sum amount	(R5 000 000.00)
Taxable amount	R0
Therefore not necessary to apply retirement tax table	

Unused deductions (R5 000 000 – R1 000 000.00)	**R4 000 000.00**
2014/2015 year of assessment	
Annuity received	R500 000.00
Section 10C exemption limited to annuity	(R500 000.00)
Taxable income	R0
Unused deductions remaining (R4 000 000.00 – R500 000.00)	**R3 500 000.00**
During the 2015/2016 year of assessment, John decides to retire from his Pension Preservation fund (R6m) and takes a lump sum of R2 000 000.00.	
Lump sum taxation:	
Lump sum	R2 000 000.00
Less previously disallowed contributions limited to lump sum amount	(R3 500 000.00)
Taxable amount	R0
Therefore not necessary to apply retirement tax table	
Unused deductions remaining (R3 500 000.00 – R2 000 000.00)	**R1 500 000.00**
2015/2016 year of assessment:	
Annuity received	R500 00.00
Section 10C exemption	(R500,000)
Taxable income	R0
Unused deductions remaining (R1 500 000.00 – R500 000.00)	**R1 000 000.00**
2016/2017 year of assessment	
Annuity received	R500 000.00
Section 10C exemption limited to annuity	(R500 000.00)
Taxable income	R0

Unused deductions remaining (R1 000 000.00 – R500 000.00)	**R500 000.00**
2017/2018 year of assessment	
Annuity received	R500 000.00
Section 10C exemption limited to annuity	(R500 000.00)
Taxable income	R0
Unused deductions remaining (R500 000.00 – R500 000.00)	**R0.00**

This benefit is only available to the person that actually made the contributions to the fund and will not be carried forward to a beneficiary of an annuity upon the death of that person.

Submitting your tax returns – 2013/2014

The 2014 tax season starts on 1 July 2014 and ends on 21 November 2014. During this time you will need to submit your income tax return to the South African Revenue Service (SARS). To help you with your tax submission, we have put together the answers to some frequently asked questions.

Who needs to register for income tax?

SARS requires everyone who receives taxable income above the tax threshold to register for income tax.

What are the tax thresholds?

For the 2013/2014 tax year, the taxable income thresholds for individuals are as follows:

- Below age 65 (R67 111)
- Age 65 and below 75 (R104 611)
- Age 75 and over (R117 111)

How to register for income tax?

You will need to complete the SARS IT77 form. This is available from the SARS website (www.sars.gov.za) or by contacting SARS. Once completed, you will need to hand the form in at your local SARS branch together with the following information:

- A certified copy of your ID, passport or drivers licence
- Your bank details (either a cancelled cheque, a certified and original copy of your account statement or an original letter from the bank confirming your bank details)
- Income details for the last three years (e.g. copies of your IRP5)
- Proof of your residential address (e.g. your rates/electricity bill not more than three months old)

What is an income tax return?

This is a declaration of income earned and capital gains or losses realised in a tax year.

Who is required to submit an income tax return to SARS?

You are liable to pay income tax if you earn more than R67 111 in the 2014 year of assessment, and are younger than 65 years of age. If you are 65 years of age or older, the tax threshold (i.e. the amount above which income tax becomes payable) increases to R104 611. For taxpayers aged 75 years and older, this threshold is R117 111.

Where taxpayers receive remuneration which is less than R250 000, they may elect not to submit an income tax return, provided the following criteria are met:

- Their remuneration is from a single employer;
- Their remuneration is for a full year of assessment (1 March – 28/29 February);
- No allowance was paid, from which employees' tax was not fully deducted;
- No further deductions need to be claimed or income declared

How do you submit an income tax return?

There are various ways to submit your income tax return. You can:

- Submit your submission online via eFiling or via your mobile device using the SARS app

- Submit your return manually by going into a SARS branch and requesting assistance from a SARS consultant
- Post your submission to SARS
- Place your submission in the drop box at a SARS branch
- The easiest and most efficient way is directly via eFiling or the SARS app. For more information on eFiling, please visit www.sarsefiling.co.za.

What happens if you do not submit your income tax return by the SARS deadline?

SARS will charge you non-compliance penalties for each month that your return is outstanding. If you do not submit your income tax return and pay your penalty, SARS may deduct the penalty from your salary/income or bank account.

What information does your investment administrator (Sanlam, Momentum, Old Mutual, Liberty ect..) report to SARS?

To verify the information that tax payers provide SARS and to pre-populate certain sections on tax payers' income tax returns, SARS requires third parties (investment administrators) to provide it with certain information. Third parties must report the following client information to SARS twice a year:

- Investment income (e.g. dividends and interest)
- Capital gains/losses
- Living annuity income
- Retirement annuity fund contributions

How do you use your investment tax certificate(s) when completing your income tax return?

Depending on the product you are invested in, you will be sent directly from the administrator a tax certificate at the end of each tax year. The table below highlights the different tax certificates issued for each product.

Tax certificate or statement	Tax certificate description	Product
IRP5	This certificate reports all annuity income.	Living Annuity or Retirement Income Option
IT3(b)	This certificate reports interest and dividends for local and offshore investments.	Unit Trust or Flexible Investment Option (Offshore and Local)
IT3(c)	This certificate reports capital gains and losses for local and offshore investments.	Unit Trust or Flexible Investment Option (Offshore and Local)
Retirement annuity fund contribution certificate - code 4006	This certificate reports all retirement annuity fund contributions made during the tax year.	Retirement Annuity Fund

How will you receive your tax certificates?

The investment administrator (Sanlam, Momentum, Old Mutual, Liberty ect..) will send you your tax certificates according to your communication preference (i.e. email or post). For clients with offshore investments please request your tax information by contacting your VPFP financial advisor.

If you would like to change your communication preference please send an e-mail to clientservicing@vpfp.co.za

Who to contact for more information?

For more information regarding your tax submissions, please contact SARS directly on 0800 007 277 or visit www.sars.gov.za .If you require assistance with your tax certificate/s, please contact your VPFP financial advisor or our Client Service Centre clientservicing@vpfp.co.za

Market & Fund Performance Update

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1. Macro Overview

Despite a few dismal first quarter GDP figures, the global economy seems to be improving. With better jobs reports, manufacturing data and consumer confidence out of the US, the S&P 500 continues to reach record highs. In addition, global central banks continue to back lower interest rates for longer.

US growth contracted at an annual pace of -2.90% in the first quarter this year, lower than previous estimates of -1.00%. The economy grew +2.60% in the fourth quarter of last year. The decrease in real GDP for the first quarter was primarily a result of negative contributions from private inventory investment, a downturn in exports and a rise in imports, and a deceleration in private sector credit as the difficult winter caused consumers to postpone spending, disrupted production, led businesses to hold off on investment, and caused construction delays. The decline in growth in Q1 appears to be an outlier, given that most other data is signalling an improvement in the economy. Most importantly the labour market remains solid.

In other indicators US inflation has been ticking up to the Federal Reserve's (Fed's) 2.00% target, from a reading of 1.50% in March to 2.10% in May. The Fed has continued with the tapering of its quantitative easing (QE) programme, cutting an additional US$10 billion in April and US$10 billion again in June. The Fed continues to purchase a total of US$35 billion per month (US$20 billion in US Treasuries and US$15 billion in Mortgage-backed securities), from total monthly purchases of US$85 billion worth of bonds before tapering began in December 2013. At the most recent FOMC meeting, Fed Reserve Bank Chair, Janet Yellen reiterated that even after employment and inflation are near mandate-consistent levels, economic conditions may, for some time, warrant keeping the target federal funds rate below levels the Committee views as normal in the longer run, thereby entrenching the view that interest rates will remain lower for longer.

In the EU, the ECB cut benchmark interest rates to 0.15% from 0.25% at its policy meeting in June and announced further policy easing measures to combat low inflation and growth, including a cut in the marginal lending facility to 0.40% from 0.75% and a cut in the deposit facility rate to -0.10% from 0.00%. This is the first time a major global central bank has cut rates to negative. EU inflation dropped to 0.50% in May.

European bond yields have come off substantially. Italian bonds reached their lowest level in history at the end of June, following the ECB's cut in key lending rates. After reaching over 7.00% at the end of 2011 the Italian 10 year government bond traded at 2.73% on 30 June 2014.

The local economy also experienced a dismal drop off in economic activity in the first quarter, falling by a disappointing -0.60% (well below expectations of a -0.20% decline) compared to growth of 3.80% in the fourth quarter of 2013 (SA's worst quarterly growth performance since Q2 2009). The decline in local growth could largely be attributed to the platinum strikes which became far more of a burden than originally expected, lasting five months in total before an agreement was finally reached on 23 June 2014. The drop in GDP was largely driven by the sharp decline in mining production, which fell a massive 24.70% for the quarter as a result of the extensive and prolonged platinum strike. Manufacturing activity also took a knock, losing 4.40% for the quarter.

SA CPI rose to 6.60% in May from 6.10%, the second month above the 6.00% upper inflation band target. This is the highest level of inflation in nine months. The increase has been mainly as a result of rising food inflation which jumped 8.80%, its highest level since April 2012. Transport inflation also contributed significantly, rising 8.90% from 6.90%.

The SARB has kept interest rates on hold at each of the two meetings following the first interest rate hike in January and may only begin raising rates further once local growth prospects improve and after developed economies begin raising interest rates.

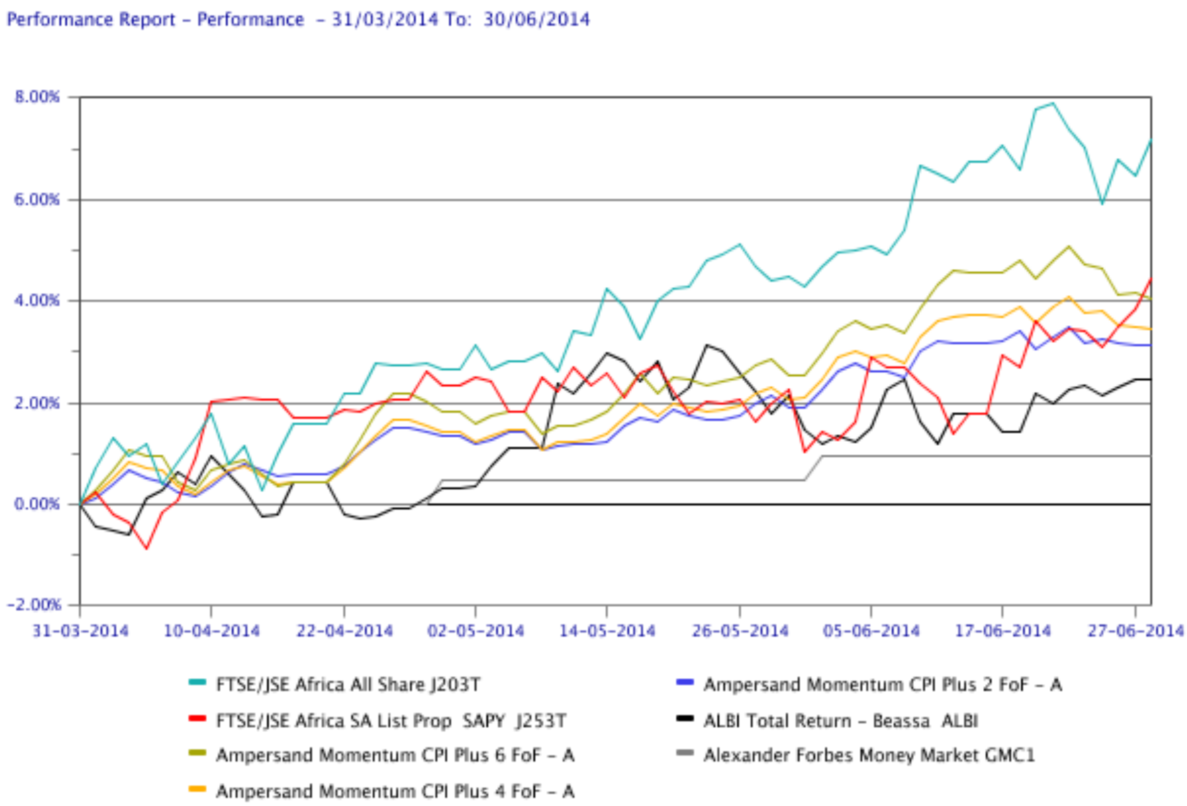
2. **Performance** – *what added and what detracted?*

Market performance has improved further since last quarter.

Local equities were once again the biggest gainer for the quarter, with global equities not far behind. The JSE All Share Index extended gains by 7.18% for the second quarter reaching an all-time high of 51,322.67 on 20 June 2014. The star performer for the quarter has been Industrials, which gained 8.30%. Financials also grew a substantial 6.80%. Global equity gained 5.04% in US dollar terms (6.25% in rand terms). Local listed property and bonds also provided reasonable performance, returning 4.43% and 2.46% respectively.

The rand weakened by a further 1.00%, extending gains on our US dollar-based assets.

Overall it was a positive quarter and we are pleased with performance and comfortable with where we are positioned.



3. Position going forward

Locally, we have considerably decreased our nominal fixed interest exposure (government and corporate bonds). We favour local listed property and other alternative income-generating fixed interest instruments and seek to expand in this space going forward.

Offshore, we maintain our long equity stance but we are considering a more cautious approach in this space. We seek to increase the ability of our underlying managers to protect the client.

We expect volatility to continue in markets and across the globe and thus believe diversification is even more paramount at this time. Our portfolios remain well diversified across assets, geographies, investment strategies and asset managers.

4. Fund Performance for the Period Ending 30 June 2014

Fund or Benchmark	3 Months Return	1 Year Return	3 Years Return	4 Years Return	5 Years Return
Ampersand Momentum CPI + 2% FoF	**3.14%**	**11.94%**	**40.93%**	**54.57%**	**70.41%**
Investment Objective (CPI + 2%)	2.46%	8.75%	26.16%	34.52%	43.56%
Ampersand Momentum CPI + 4% FoF	**3.46%**	**16.29%**	**46.62%**	**62.03%**	**80.71%**
Investment Objective (CPI + 4%)	2.96%	10.87%	33.69%	45.33%	58.13%
Ampersand Momentum CPI + 6% FoF	**4.06%**	**20.66%**	**53.19%**	**72.44%**	**96.19%**
Investment Objective (CPI + 6%)	3.44%	12.99%	41.51%	56.78%	73.86%
Alexander Forbes Money Market	**0.96%**	**5.03%**	**17.02%**	**24.21%**	**33.42%**

Source: MoneyMate (A Class, ZAR) *(CPI Benchmark as at 31 May 2014*