

PROFICIO

NFB FINANCIAL UPDATE



FROM THE CEO'S DESK

In recent editorial much has been said about diversification, which remains a very powerful, so called, free lunch. This remains true in general but when looking at the last few years, patience hasn't really been rewarded. In actual fact, the top performing asset class locally has been cash and bonds, with preference shares having outperformed over the last year.

Whilst we fully subscribe to the adage which suggests remaining calm and fully invested, this can wear thin after prolonged periods of rather flat or even downward trending markets. Our experience and also advice to those who are exposed to shares, property and other more aggressive, growth focused assets is indeed to stay the chase.

Stripping out the few SA Inc. shares that have propped the market up leaves a vast array of quality companies, many with outstanding management and leadership who have shown amazing resilience in an environment, which has threatened the very survival of business and society at large. Their share prices are at multi-year lows and whilst they haven't grown earnings as in prior years, they are poised and have leaned themselves into a robust shape. Should the market benefit from a positive electoral outcome, these same companies and overseas investors have large cash resources, currently languishing in bank deposits and call accounts, ready to deploy. This point certainly is not a slam dunk, but when markets become buoyant, they run hard. Much research has been done into investors who miss only a dozen or so of the top trading days over a decade and in so doing leave a considerable amount of performance on the table!

Listening to overseas commentary recently had me wondering if we are too close to the playing field? Firstly, a comment from a UK based asset management outfit was: "South Africa is a way more predictable place from the point of view that you have a clear insight into your president and governing party for the next number of years, whilst we (British) haven't got a clue!" The second point was a reflection of the tough economic and political environment and echoes my point above. The focus was on the global market's appetite for emerging market equity (and the commensurate dividend income) and yield from bonds and other debt instruments, issued by corporates, banks and the state and which are trading at a material premium to overseas, developed country debt. Given recent woes at Eskom, state capture in general and the lowering of estimated tax revenues, amongst other

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factors, the premium has widened, making our yields even more enticing. This premium is called a risk premium and reflects a return, which reasonably compensates the buyer for the risk of a blowout. Looking at sectors of our market and the prices of stocks, the yields available on bank issued preference shares, and certain of the larger property REITs, their interest becomes understandable.

The opinion regarding the president retaining his role; the ANC remaining the dominant player, i.e. the status quo remaining, hasn't been shared domestically in conversations I've had with friends, family and institutional contacts. What remains starkly obvious is the rather troubled state of affairs both at home and abroad. Brexit trundles along, President Trump is now adding India to his global trade war conversation, terrorism has raised its horrible head in one of the most unlikely places on earth, and even Boeing seems to be adding to the chaos.

On a more positive note, NFB has been the very proud and fortunate recipient of some remarkable awards over the last few years. The past year is no exception and our Asset Management unit has again bagged a Raging Bull award and two awards from Morningstar for its performance in 2018. In addition, the Private Wealth division was recognised in 2018 as the top Wealth Advisory business in the country. Whilst it is easy to rest on one's laurels, we like to believe we are different. Firstly, we will try even harder in the coming years. Secondly, we are patently aware that the luxury to build businesses into something regarded to be in the top echelon requires clients, customers, ambassadors, products and services. You, our clients, are a critical part of this recipe and we are extremely grateful for your support, networking and remarkable long-term loyalty.

NFB turned 34 on April 1st, 2019. This is quite something, as from very humble beginnings in Port Elizabeth and Cape Town, we expanded to East London and eventually to Johannesburg. We are engaging in some exciting initiatives and our Johannesburg businesses, including Private Wealth Management, Asset Management and NWest Securities are set to move to our beautiful new premises in a few weeks' time. More about this in the next edition. If you are from Johannesburg, we will see you there. If you're visiting from out of town, pop in for a visit. You are welcome. ■

Mike Estment CFP®
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REASONS TO PAY MORE ATTENTION TO YOUR RETIREMENT FUND



One of the first things you are required to attend to after joining a new employer as a permanent employee is completing the forms of the occupational provident or pension fund. For some individuals this is the first and only time they give attention to their retirement fund until their annual statement arrives, or until they resign from the company and cash out the fund value, less tax and move onto the next employer.

Despite the lack of care most employees show towards their occupational retirement funds, these are designed to protect the employees against themselves, insolvency, their employers and any creditors who could see the funds as an asset to attach for funds owed. Current legislation governing retirement funds provides an effective shield from attachment, transfer or cession, and has been tested in various court cases.

The reason for such stringent rules on retirement assets is due to the socio-economic role they play in relieving the state of being overburdened by having to provide financial support to the masses through old age grants when employees are too old to work, and child support grants to the minor children of deceased employees who would now look to these grants to provide for their basic needs.

We will look at the hidden aspects of retirement funds and the special protection afforded to members when they or their beneficiaries need these funds most.

Group risk benefits – approved and unapproved group life policies provide additional benefits which pay out to the member and/or their family. A portion of the retirement fund contribution is directed towards an insurance policy premium on the life of the member so that the death benefit can be paid to the member's nominated beneficiaries at death. Further benefits may include disability and

critical illness benefits as well as education policies that cover minor children's education costs from primary through to tertiary level. The benefits vary from employer to employer.

Pension-backed housing loans – for those who have built up a substantial benefit amount in their retirement fund, and should the rules of the fund allow, a fund may grant a loan to a member or furnish a guarantee to a third party for a loan to purchase a property that will be owned by the member or the member's spouse, occupied by the member or their dependent. The value of the loan may not exceed 90% of the value of the property or exceed the lowest after tax benefit to which the member is entitled in terms of the rules of the fund. This loan can be used for the deposit or towards bond registration costs and fees when acquiring the property, including vacant land. It can also be used for renovations, alteration or repairs of the property and settling an existing home loan. The maximum loan term is 30 years, but can depend on each individual case as the loan has to be settled by retirement age. Should the member fail to repay the loan, or exit the fund, the member's retirement savings will be used to settle the home loan balance. This benefit applies to members of all income brackets of participating funds.

Protection from the employer – it is one of the duties of the trustees of retirement funds to ensure that the interests of the members are protected, as well as avoiding conflicts of interest. Trustees need to act impartially and apply their minds objectively to any request received from the employer to deduct losses suffered by the employer from a member's benefit. Section 37(A) of the Pension Funds Act states that the member's benefits may not be reduced, transferred or otherwise ceded. The provisions of Section 37(D) of the Pension Funds Act only allow the employer to deduct against members' benefits under specific circumstances.

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Compensation for damages or losses to the employer caused by the member due to theft, fraud, dishonesty or misconduct by the member and in respect of which the member had admitted liability in writing or in respect of which the employer has obtained a court judgement.

- (i) The written admission must be made *freely and voluntarily* – so there must not be any form of duress or undue influence to get the confession out of the member.
- (ii) The loss must be due to the said *member's misconduct, dishonesty, theft or fraud*. Losses suffered by the employer due to the employee being negligent or not following procedure or policy do not qualify as an event to claim from a member's benefit. The employee has to be seen to have intentionally done wrong.

If there is no written acknowledgement of guilt of misconduct, theft, fraud or dishonesty, the employer has to obtain a compensation order in terms of Section 300 of the Criminal Procedure Act for the claim to be satisfied by the fund. In *S Ndumiso v Auto Workers Provident Fund and Ascension Trading CC t/a Ascension Motors*, the Pension Funds Adjudicator found that even though the employee was convicted for theft of the employer's money, the employer had to obtain a compensation order in addition to the criminal conviction. The fund having already compensated the employer from the member's benefit, was ordered to pay back the full benefit withdrawn.

Protection of beneficiaries – at times it is not the fund members but their minor beneficiaries that need protection – and current legislation does not let the dependents down in this regard. The Pension Funds Act and the Maintenance Act provide for a parent who does not receive maintenance from the other parent under an existing maintenance order, to approach the maintenance court for an order against the non-paying parent's retirement fund to pay the amount owed from the member's benefit.

In a recent case of a dismissed SAPS official, who was a member of the Government Employees Pension Fund (GEPF), the maintenance court had granted an attachment order in September 2012 against the father's pension held at the GEPF for maintenance arrears of R40,000. The GEPF failed to pay despite continuous follow-ups. In September 2015, the court issued a new order, attaching the father's pension for arrears of R72,000, and the GEPF failed to comply. In November 2016, the persistent mother obtained a further court order for the attachment of outstanding arrears of R104,000 plus R240,000 for future maintenance, totalling R344,000, and yet again the GEPF failed to pay. In 2018, having exhausted all other options, the mother approached the Public Protector to assist in the matter. The Public Protector intervened and the GEPF eventually complied and within five months the owing funds were paid out.

Protection from insolvency – Section 37 (B) of the Pension Funds Act states that should a member's estate be insolvent or sequestrated, their benefit may not be deemed to form part of the assets in the

insolvent estate of the member, and may not in any way be attached or appropriated by the trustee of the insolvent estate or by creditors.

Treasury is continuously working on ways to protect retirement funds against risks of premature depletion. The Minister of Finance issued the Default Regulation to the Pension Funds Act which has three main components to it:

- (i) A Default Investment Strategy – occupational defined contribution funds are to design default portfolios with the members interest in mind. Asset allocation, fees, risk and returns of the portfolio must be transparent.
- (ii) A Default Preservation Strategy – occupational provident and pension funds are to allow members greater opportunity to preserve benefits within the fund on resignation as paid-up members. Retirement benefit counselling must be available when members decide to withdraw their benefit.
- (iii) A Fund Annuity Strategy – all pension, pension preservation and retirement annuity funds to comply and have an annuity strategy for a sustainable income throughout retirement. Members are to have access to retirement benefit counselling no less than 3 months before retirement date on the annuity options available.

Provident funds currently give members the option to withdraw the full benefit at retirement. The annuitisation of provident funds and preservation provident funds remains under discussion at the National Economic Development and Labour Council (NEDLAC).

The Default Regulation legislation does not apply to the Government Employees Pension Fund.

Though employees may show little respect to their retirement fund benefits by withdrawing funds prematurely and neglecting how their money is invested, it's important to remember that a retirement fund is a valuable asset and members should definitely take more time to scrutinise their benefits and not underestimate their rights when it comes to their retirement savings. ■

Sources used:

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DEMYSTIFYING THE OFFSHORE WRAPPER

The offshore investment conversation between investors and private wealth managers has been more prevalent over the past few years and with good reason: state capture, the state of our State Owned Enterprises (SOEs), three different finance ministers in three years, and local equity markets providing investors with very little in the form of real returns over the past four years.

Private wealth managers often suggest the use of a wrapper when advising investors on offshore investments. So, what exactly is a wrapper? A wrapper is a generic term of referring to an endowment. In its simplest form an endowment is an investment product issued by a registered life company and governed by Section 54 of the Long-Term Insurance Act. The product, by virtue of the aforementioned description, has potential benefits which we will discuss further.

The potential benefits of using a wrapper for investors who already have offshore assets or are looking to physically take money offshore, either via their R1 million discretionary allowance or their R10 million foreign investment allowance, cannot be overlooked or underestimated.

Many investors are unaware that their offshore assets could potentially be subject to adverse tax and estate consequences at death:

- **Probate** – probate is a process whereby a will is accepted by a court as a legal document. There are certain offshore jurisdictions which cannot be governed through a local will and, as such, a foreign will would need to be drafted to deal with the assets. In the instances where a local will is accepted, very often the local estate is delayed while the will is sent offshore – this can cause unnecessary delays to the winding up of the estate as well as add to costs as a lawyer would need to be appointed to assist in the winding up of the foreign assets in the country where the asset is held.
- **Situs** – assets held in certain foreign jurisdictions, most notably the UK and the US may be subject to inheritance tax under the law of situs. In the US this results in tax at 40% for asset bases in

the US of over \$60,000 and in the UK, tax at 40% for asset bases in the UK of over £325,000. Local estate duty is levied at a rate of 20% for estates under R30 million and 25% for estates in excess of R30 million.

BENEFITS OF WRAPPING YOUR OFFSHORE INVESTMENT

- Using a wrapper avoids both Probate and Situs. It should be noted that a correctly drafted will in the jurisdiction of your offshore assets could negate some difficulties associated with Probate.
- Having a nominated beneficiary upon death means there will not be executor fees on the asset. This should not be confused with estate duty that could apply.
- The product is tax efficient for investors with a marginal tax rate in excess of 30% as well as trusts (although a trust cannot physically take money out of South Africa via tax clearance; they are able to do so via an asset swap).
- All tax is paid within the product, on the investors behalf, by the issuing company resulting in simple administration. Also, as tax is paid within the product all redemptions are capital in the hands of the investor.

	Income Tax	Capital Gains Tax
Individuals	18% - 45%	18%
Trusts	45%	36%
Endowments	30%	12%

Investing locally or offshore can be challenging with so much more to consider than just market returns and costs. Ensuring the correct structures are in place can save significant costs and reduce the administrative burden both whilst alive and upon death.

If you have any queries please chat to your NFB Private Wealth Manager who has the necessary skill and expertise to optimise your family's portfolio. ■

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