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# Making sense of the revised retirement fund regulations

**EXECUTIVE SUMMARY:** A recent revision in South African pension fund regulations affects your ability to transact on your retirement fund investment account. Ian Barow and Taryn Hirsch look at the regulations and summarise the options available to you.

During the first quarter of this year, the Minister of Finance introduced revised investment requirements for retirement funds (Regulation 28 of the Pension Funds Act). If you are a retirement fund member, these revisions may mean that you need to make changes to your investment accounts.

One of the key objectives of the regulation is to ensure retirement fund investments are adequately diversified and it aims to achieve this by prescribing the maximum exposure that members may have to certain asset classes (e.g. 75% in equities, 25% in property, 25% in foreign assets). Previously Regulation 28 only prescribed maximum limits at retirement fund level. This meant that members could potentially select asset class exposures of their choice outside these limits to make up their investment account, provided that the retirement fund's total holdings complied with the regulation across all of its members.

## Impact on member choice

Members of the Allan Gray Retirement Annuity, Pension Preservation and Provident Preservation Funds (so-called member choice retirement funds) need to select unit trusts as underlying investments for their investment accounts. These members are still able to select underlying investments which best suit their risk profile and investment objectives, but they now need to adhere to the maximum limits set by the legislation on their individual investment accounts.

Some investors prefer 'solution' unit trusts, where the asset allocation decision is delegated to the unit trust investment manager. There are several different types of solution unit trusts – your choice would depend on your investment objectives and risk profile. Most of these types of unit trusts are fully Regulation 28 compliant and, in case of doubt, each unit trust's compliance status is noted on our fund lists and fact sheets. If you invest in Regulation 28 compliant unit

trusts, your account will most likely always be automatically compliant.

There are other investors who, often with the help of a financial adviser, may prefer to select individual asset class unit trusts, such as equities or bonds, and use a combination of these as 'building blocks' to create their own portfolios. These investors will need to ensure that their accounts are Regulation 28 compliant. We have developed simple tools, such as the Regulation 28 calculator available via our website (see text box on page 16), to help these 'building block' investors and their advisers to maintain compliant portfolios.

## What to do if you are a retirement fund member

### 1. If the combination of unit trusts you have selected complies with the regulation, you do not need to do anything.

Many of the unit trusts that you can select as underlying investments already comply with these requirements, e.g. the Allan Gray Balanced Fund, the Allan Gray Stable Fund and the Allan Gray Money Market Fund. Alternatively, you may be invested in a compliant combination of unit trusts. Either way, no action is required.

### 2. If your investment account does not comply, and you have not transacted on your account since 1 April 2011, you do not need to do anything until you transact.

Transacting on your account may require action from you – please refer to **Table 1** to find out what constitutes a transaction. Please read point 3 below if you plan to transact.

### 3. If you transact, you will need to comply with the new limits.

If you wish to transact on your investment account, you will have to make sure your account remains compliant from the point that you transact onwards.

If your investment account does not currently comply with the new limits and you wish to transact, you may keep your account non-compliant, but you will need to direct all new debit orders and/or additional contributions into a new investment account. Your new investment account will need to comply with Regulation 28 but your existing account can then remain non-compliant, as long as you do not transact on it.

If you prefer to keep just one investment account, you are required to make your existing account compliant. To do this, you must switch all or part of your investments and debit order allocations and/or additional contributions in your existing investment account into a combination of unit trusts that complies with the regulation. You can use our Regulation 28 calculator to help you create a compliant account (see text box).

**4. If your investment account does not comply, and you have transacted on your account since 1 April 2011, you will need to 'rebalance' your account before 31 December 2011.**

You will need to switch your debit order allocations and/or additional contributions into a combination of unit trusts that complies with the regulation.

This means you must either:

- Select unit trusts that comply with these requirements, e.g. the Allan Gray Balanced Fund, the Allan Gray Stable Fund and the Allan Gray Money Market Fund, or
- Select a compliant combination of unit trusts.

The deadline for administrators to implement the revised Regulation 28 is 31 December 2011. As many of you take leave towards the end of the year, please provide us with your rebalance instructions before 31 October 2011. To do this you can log into your secure account and complete a switch instruction online, where you will be able to use our Regulation 28 calculator. You can also complete and sign a 'Rebalance instruction' (available from the Forms section on our website or from the Client Service Centre) and return this to us as soon as possible. If you choose to send us a faxed instruction, please use the online calculator described in the text box, or feel free to call our Client Service Centre, to make sure that the outcome of your switch is compliant before instructing us. We recommend that you discuss your fund selection with your financial adviser.

If we do not receive an instruction from you that results in your account becoming compliant, we are required to make your account compliant. We will do this by moving a percentage of your non-compliant investment into the Allan Gray Money Market Fund.

**5. If you open a new retirement annuity, pension preservation and/or provident preservation fund investment account it will need to comply with the new limits.**

For assistance, please contact our Client Service Centre or speak to your financial adviser.

As the regulation is still new, the Regulator has not finalised all the practical issues. We will keep you informed if there are any important developments.

**TABLE 1** | What is a transaction?

Classified as a transaction	Not classified as a transaction
Setting up a debit order*	Existing debit orders
Increasing or decreasing an existing debit order (This is not the same as an annual escalation)	Annual escalations of debit orders
Additional contributions	Distributions that are re-invested
Switches	Cancellation of debit orders
Transfers-in of units	Existing phase-in arrangements
	Withdrawals from preservation funds
	Divorce order payments
	Where a unit trust is no longer available on the platform and a replacement unit trust is selected
	Switches between classes of the same unit trust

\*Debit orders are only relevant for the Allan Gray Retirement Annuity Fund

Source: Allan Gray

**Please use our calculator to create a compliant account**

To help investors 'rebalance' their accounts we have built a calculator, available via the Regulation 28 button under 'Quick links' on [www.allangray.co.za](http://www.allangray.co.za). The calculator is easy to use:

- Simply input your selection of unit trusts and allocation to each.
- The calculator will validate your account (see below).
- If your asset allocation meets the Regulation 28 limits, the calculator will indicate this with a 'yes'; if it does not, the calculator will indicate 'no' and display the areas where your investment does not comply and by how much.

**How we validate Regulation 28 compliance**

We use the following asset classes to validate Regulation 28 compliance: 75% equities, 25% offshore and 25% property.

As many unit trusts have exposure to property assets within their portfolios, we have limited investments in property unit trusts to 15% to manage compliance more effectively. When assessing asset class limits, we use the unit trusts' intended maximum limit (IML). The IML is the expected maximum amount that fund managers will invest in each asset class. This is based on a combination of their investment mandates, past practices and best understanding of the regulations. By using IML, clients are less likely to have their accounts become non-compliant due to fund manager decisions and market movements.

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Ian joined Allan Gray in 2009 as head of the Institutional Legal and Compliance department. He practised Corporate and Commercial Law for five years at Edward Nathan Sonnenbergs, before leaving in 2004 to pursue his career in corporate legal affairs. He is also one of the trustees of the Allan Gray retirement funds.

Taryn is a qualified attorney and certified financial planner. She joined Allan Gray in 2009 and is head of the Retail Legal department. Prior to a stint at an international law firm in Tokyo, Taryn spent eight years at Deneys Reitz (now Norton Rose) where she was a director in the banking and finance department.

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