

disability cover be mandated as one of the benefits from a retirement fund. The level could be of the order of pensions of 20% of income for orphans, and 50% of income in the event of disability.

If such compulsory benefits are introduced, a strong argument could be made for the abolishment of the Road Accident Fund and the various forms of compulsory coverage for employment accidents – as they would be redundant. The Committee was divided over whether such a recommendation could be made, with some members being convinced a public system should remain to provide benefits over and above the minimums suggested.

9.2.2 Administration

9.2.2.1 Boards of management

Most boards are now equally divided between employer and employee appointed trustees, whose primary fiduciary duties are to members. Not many trustees are financial or legal experts, and they are largely reliant on expert help for the administration of their funds and the investment of assets. This has led to proposals that funds appoint professional trustees to ensure their boards have adequate expertise. This has apparent advantages, but clearly weakens the position of the lay trustees in board meetings. If trustees want independent advice, they would be advised to contract others to provide it, rather than surrender some of their powers.

The Committee recommends that the principle of lay trustees, with democratic accountability to the members, be encouraged. All funds, including those umbrella funds and retirement annuity funds currently exempted, should be required to have elected trustees. Payment to trustees for services rendered should not be permitted.

9.2.2.2 Administration costs

Smaller retirement funds are considerably more expensive to administer, and less likely to be able to afford expert advice.

The Committee recommends that responsibility for rationalising the over 15 000 retirement schemes be left in the hands of trustees. It is further recommended that provincial Governments, together with unions and local business organisations and retirement fund administrators, investigate the possibilities of establishing regional funds, which will allow for both democratic election of trustees and greater efficiency.

9.2.2.3 Allocating benefits to dependants

The process of allocating benefits to dependants on death and divorce is problematic from the point of view of efficiency and equity.

The Committee recommends that the matter be given a high priority by the Financial Services Board (FSB). The rights of divorced spouses require particular attention.

9.2.2.4 Fiduciary duties

The fiduciary duties of trustees and directors of insurance corporations require ongoing monitoring. Conflicts of interest arise frequently in the choice of service providers, of investments and in the allocation of benefits. The Committee recommends that the FSB be required to include in its annual report the steps it has taken to ensure higher standards are met.

9.2.3 Retirement fund investment

The Committee recommends that Government explore wage-linked bonds as a measure that is possibly more appropriate to the needs of retirement funds, and to its own risk management strategies.

The Committee recommends that retirement funds initially be required to invest a proportion of their assets within a defined socially desirable investment universe. The initial yield on these investments should be in line with the return on marketable investments.

The Committee recommends that no further increases in international investments be permitted until a performance index divided into local and foreign exposure, for both foreign and locally listed equities, is created, and trustees are able to gauge the exposure of the funds to foreign currency risks.

Trustees' lack of expertise makes it difficult for them to judge the appropriateness of investment performance benchmarks. The Committee therefore recommends that the FSB develop appropriate investment benchmarks for use by retirement funds, and investment managers be required to measure their performance against these benchmarks.

The Committee recommends that trustees, or their delegated agents, be required to apply their minds to the major issues of corporate governance such as full accountability to shareholders, the appropriate structure and

functioning of the board, and the control of management remuneration, and to use the vote attached to their shares.

The Committee also recommends that all companies be required to amend their articles of association in order to achieve representation of significant minority shareholders (including minorities indirectly held through pyramids and cross holdings) on their boards of directors. As both Government and union controlled funds are significant investors, they will be entitled to representation on a number of boards. This will therefore boost the representivity of boards of directors.

9.2.4 Taxation of retirement funds

The Committee is of the view that the current tax structure should be retained. It can however be significantly simplified.

9.2.4.1 Deductibility

The Committee recommends that total deductible contributions should be limited to 20 per cent of the employee's taxable income. The allowance for arrear contributions should be scrapped as representing an unnecessary complication.

9.2.4.2 Tax on investment income

The Committee recommends that the taxation of retirement funds be brought within the ambit of the Income Tax Act and that income could be taxed in the same manner as insurance funds. Generous deductions for administration expenses could reduce criticism that such a tax falls heavily on the poor, without opening opportunities for much tax planning.

The current basis of taxation allows for the tax paid to exceed real earnings. This can be the case with tax on interest-bearing instruments and with CGT. This significantly undermines the security of all saving, and views were expressed within

the Committee that the basis should be amended to prevent this occurring. The opinion was expressed that government was obtaining inappropriate tax advice from low inflation OECD countries.

Some members of the Committee felt that abolishing STC and CGT on realised share profits, and increasing the corporate rate to compensate, could significantly simplify the taxation of investment income and increase the liquidity of the market. No agreement was reached on this matter.

9.2.4.3 Tax on benefits

The current tax position encourages lump sum withdrawals, lump sum death benefits and the commutation of pensions on retirement. It is inconsistent to prevent people from withdrawing most of their savings from retirement funds and then give them tax incentives to withdraw the maximum possible.

Consideration should be given to according lump sums with no special status and taxing them as income in the year in which they are received. This approach is simple and would mean that people would pay more tax when they chose lump sums over pensions, and is preferred by the Committee.

9.2.4.4 Tax on life assurance

The taxation of life assurance benefits also leads to a preference for lump sum rather than annuity benefits.

The Committee recommends that benefits paid out of the taxed life assurance fund be explicitly freed from taxation as annuities in the hands of beneficiaries.

9.2.5 Defined benefit vs defined contribution

The Committee did not wish to take a position on this issue. It was however concerned that

Table 10
Summary statistics on the retirement industry

	Funds	Members (000's)	Contributions (R'billion)	Assets
Self-administered	2 682	2 963	18 987	278
Under-written by Insurers	13 127	6 416	20 339	132
Government	7	1,438	14 888	194
Industrial	8	76	100	1
Total	15 824	10 893	54 314	605

greater attention be paid to finding appropriate investments for retirement funds. The investment recommendations set out on page 96 derive from this concern. It is also concerned that members are fully informed of the present value of their benefits.

It therefore recommends that all funds be required to inform their members annually of the present value of contributions made by employers on their individual behalf, and of the increase (or reduction) in value of their retirement benefits. It also recommends that an employer guarantee of the benefits payable from the fund or of its investment returns be the subject of a separate contract between the fund and the employer.

The Committee's brief also requires it to consider question of impact on government as employer. It is recommended that, if the GEFP were converted into a DC fund, the assets should primarily be inflation and wage linked bonds. It would be inappropriate for government to have too large an influence on private sector businesses should the GEFP become a major shareholder in local companies.

9.2.6 Consumer protection issues

Powerful vested interests control the insurance and related industries. There is limited regulatory capacity to monitor compliance with trustee laws across 15 000 funds. Consumer protection is sometimes inadequate, and there is little real competition. The following suggestions are made.

9.2.6.1 Excessive sales and lapses, but few complaints

The Committee has not been able to obtain definitive statistics, but it appears that about half the working population appear to have little personal insurance, while the other half appear over-insured. Thirty per cent of life policies result in a lapse, causing loss to the policyholder. The Committee's research suggests that most policyholders do not appreciate the losses they suffer, and believes that the problem lies with the current commission system.

The Committee recommends that commission could continue to be payable to agents of an insurer, who make it clear that they are selling policies, not giving advice. Such contracts should either offer a defined set of

insurance benefits, or be investment products with restricted charges - as with stakeholder pensions in the UK.

9.2.6.2 Competition

The Committee was concerned at the apparently low level of competition in the financial services markets - with four or five groups dominating the insurance and banking industries. Evidence from the UK was that even their much larger and open markets were not regarded as sufficiently competitive. Responsibility for regulating these industries is divided between the FSB, the South African Reserve Bank (SARB) and the Competition Commission. It seems that there might be inadequate coordination and insufficient monitoring of possible abuses of market power.

The Committee recommends that the regulating bodies be required to perform a regular review of competition within these markets and investigate ways of increasing competition. Suggestions were made that life insurance companies be compelled to make comparable expense and performance statistics available. The publication of investment performance statistics also needs monitoring. In particular, all costs should be fully disclosed. Other possibilities are that more encouragement should be given to smaller mutual societies to develop into real competitors in the market.

9.2.6.3 Low-cost national savings scheme

Representations to the Committee have included suggestions for a low-cost national savings scheme that can cater specifically for the growing numbers of workers excluded from formal, regular employment retirement funds. Such a scheme, preferably administered through a non-profit public entity, would cater specifically for workers with unstable incomes and irregular contribution patterns. It is not clear, however, that such a scheme would be able to function at a lower cost level than existing savings arrangements offered by banks and insurers. It might well however compete with existing schemes and so promote much needed competition in the industry.

The Committee therefore recommends that such a national scheme be investigated. This investigation should be carried out jointly or in consultation with the state development finance institutions, the FSB, and SARB, Development Bank of South Africa, Department of Labour and