

Demand for tax-efficient retirement and savings vehicles on the up

After another unexpected and eventful year, the festivities have officially ended, bringing us back to square one - outlining future goals and saving plans for a start.



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For those who were fortunate enough to receive additional income in the form of a bonus or '13th cheque' - now is the time for them to consider saving a portion of their income for their retirement.

When considering how to optimise their retirement savings, investors should consider the following insights on Retirement Annuity products versus Tax-Free Savings Accounts and how they can maximise the tax benefits available to them as they approach the tax year-end on 28 February 2022.

The role of RAs and TFSAs in retirement planning

Retirement Annuity (RA) products have been around for many years, and are specifically designed as a vehicle focused on saving for retirement. Tax-Free Savings Accounts (TFSAs) were introduced in 2015, and though not designed specifically for retirement, they do provide unique rules around tax treatment which can be leveraged to supplement retirement savings.

While both products provide tax incentives to save, and benefits when creating a long-term financial plan, appropriate product choices will depend on your individual circumstances. A combination of the two may also be a suitable way to achieve desired outcomes by leveraging the benefits of each to achieve your retirement and savings goals.

Key considerations when balancing investments between RAs and TFSAs

Tax on investment income

Both products offer investors a tax advantage as they attract no tax on interest, dividends and capital gains while funds are invested. Note that even without these tax treatments, SARS allows certain annual tax exemptions on investments outside of these products, namely a R23 800 annual interest income allowance and a R40 000 annual capital gains tax exemption.

So, if you receive less than R23 800 in interest income or less than R40 000 of capital growth, you will not owe any tax on your investments. You will, however, still be charged dividends tax of 20% on all shares which have paid you a dividend.

Contributions

There are no contribution limits in an RA. You can contribute and deduct up to 27.5% (capped at R350 000) of your total annual taxable income in any given tax year, and excess contributions can be claimed as deductions in the following year of assessment.

By contrast, TFSAs have a maximum contribution limit of R36 000 per tax year and R500 000 over the lifetime of the product, and contributions exceeding these limits are penalised at a 40% tax rate. Annual contributions are not tax deductible and do not carry over to subsequent tax years, so it's important to use as much of each year's TFSA allowance as possible.

Contributions to both products can be made on a lump-sum, monthly or ad hoc basis, but the exact payment arrangements vary between product providers. For example, the RA and TFSA offered by PSG (the PSG Wealth Retirement Annuity and PSG Wealth Tax Free Investment Plan) have minimum lump-sum contribution amounts of R20,000 and R6,000 respectively, and the minimum debit-order amounts for both products are R500 a month, R1,500 a quarter, R3,000 half-yearly and R6,000 yearly.



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Accessing your savings

RA savings can generally only be accessed at retirement, at which stage a maximum of one third of the withdrawal amount can be taken as a lump sum, and the remainder must be invested in a retirement income product. On withdrawal from an RA, the lump-sum portion will be taxed according to the retirement lump-sum tax tables or the withdrawal lump-sum tax tables (depending on the event). Income from the retirement income product will be taxed at your marginal income-tax rate.

TFSA savings can be accessed at any time and there is no tax payable on the amount withdrawn. There is also no limit on the amount you can withdraw, but you cannot replace the withdrawn amounts, as TFSA contribution limits apply, regardless of withdrawals.

Investment choices

RAs are subject to certain restrictions on asset classes, prescribed by Regulation 28 of the Pension Funds Act. Broadly

speaking, these limits are 75% equity, 30% offshore assets and 25% property. These limitations do not apply to TFSAs, so a significant benefit of TFSAs is that they allow investors an opportunity to achieve almost 100% offshore investment exposure – for example, by investing in a unit trust feeder fund. These funds – denominated in rands but mostly invested in foreign currency funds – are available through local product providers (such as PSG Wealth). This approach also significantly simplifies the offshore investment process, and you don't need to use your own offshore investment allowance.

TFSAs are ideal vehicles to use to supplement retirement savings, as they provide additional flexibility and diversification. However, finding the right balance between an RA and a TFSA may not always be a simple task. It is important that you engage with a financial adviser to support you through this process.

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