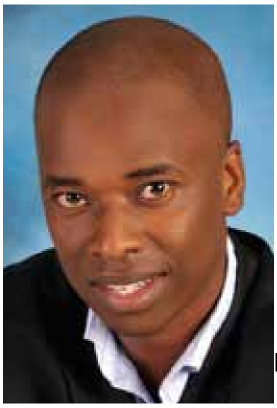
MARCH 2009

Eskom Pension and Provident Fund

Powertalk

THE NEWSLETTER FOR MEMBERS OF THE ESKOM PENSION AND PROVIDENT FUND

Editor's Note



WELCOME to the first edition of PowerTalk for 2009 and my first edition as the new Editor since joining the EPPF in September 2008.

I come from a mainly marketing background, starting out as the communications co-ordinator at Liberty Life, where I was responsible for internal communications and events planning. I then moved to Discovery Vitality, where I did marketing on the Discovery credit card portfolio mainly involved with the loyalty and retail partners on the card. I produced the marketing newsletter – Power Shopping Guide. Although I enjoyed the marketing world, schmoozing and entertaining clients, I was looking for a smaller and closer working environment with growth opportunities - this I found in the EPPF.

Since joining the EPPF I have experienced an amazing growth curve and have so far found my time here very rewarding. I'm responsible for the Fund's communications (including the annual report and newsletters) and I'm now involved with the call centre operations as well as the client service initiative.

In keeping with the vision of the Fund, we aim to firstly streamline the Fund's Communication Strategy and attach it to the current administration processes ensuring that you receive Fund communications timeously. Our intention is that you, our members, are kept informed with information that is up to date and relevant. We are training our call centre staff to improve service delivery to you so that your queries are answered effectively and within reasonable timeframes. The Fund has also embarked on a client service initiative to improve your service experience with face-to-face interaction with the Fund. We are very excited about the developments in the Fund and with the help of the rest of the team and your continued support and feedback, we hope to continue to bring you quality communications and services.

We truly value your feedback – good or bad – so please contact us and have your say.

Wishing you a very happy and successful 2009!

Regards

Themba

Client service … keeping you in the loop

IN an effort to ensure that all your queries and concerns on the Fund are dealt with effectively, the Fund has embarked on a new client service initiative. Our Retirement Fund Consultants will be going around the country to personally address any queries you might have. Mobile offices have already been established in Ladysmith and Newcastle and the expansion of this initiative is proceeding rapidly.

Look out for notification on the dates and times of when they will be in your area.

THIS ISSUE:

YOUR QUESTIONS ANSWERED

The Fund sent out benefit statements during November 2008…
We have since received a number of questions from you about these benefit statements. The Fund's Actuary answers some of these questions …

YOU will be aware from previous communications that in terms of relevant Pension Fund legislation, the Fund must provide a benefit not less than the Minimum Individual Reserve (MIR) to any member who leaves the Fund before retirement age.

What is the MIR?

The MIR is the "market value" of a member's accrued pension at the date on which it is calculated. It must not be less than the accumulated value of a member's own past contributions to the Fund. This ensures that a member will always receive the greater of the value of their own contributions plus interest, or the value of the accrued pension.

How is my MIR calculated?

The Fund must do two separate calculations:

1. The value of the member's accumulated past contributions plus interest. The rate of interest after December 2001 must compare reasonably with the actual rate of investment return that the Fund has earned on its assets.
2. The "market value" of the "accrued deferred pension". In other words, the amount of capital required in current market conditions to buy you the amount of pension that you have earned for past service up to the date of leaving the Fund, based on your salary (as defined) at the date of leaving the Fund.

The MIR is the greater of the above two calculations.

What about my voluntary contributions?

The value of any balance in your Additional Benefits Account is paid in addition to the above amounts.

How do you calculate the "market value" of my accrued pension?

The value of this amount is calculated using financial assumptions, including items such as the rate of future salary increases, future investment returns and pension increases. An allowance is also made for an assumed age difference between spouses, assumed life expectancy and the allowable one-third commutation. While this is a complex calculation, the Law is very strict (or "prescriptive") about the financial assumptions that can be used and the Registrar of Pension Funds sets outs these assumptions for all retirement funds, so that the MIR calculation is broadly consistent between funds.

Does the MIR value change very often?

The MIR value will normally change each month, as you accumulate more service and in line with your salary increases. It will generally tend to increase if asset prices increase. Conversely it can also reduce during a declining investment return cycle such as during a stock-market crash when asset prices drop.

When must it be paid?

The Fund must test the normal Fund benefit against the MIR when a member resigns, is dismissed, retrenched, or transferred to the Fund of another employer (for example as a result of a sale of a business to that employer). The benefits due in these circumstances cannot be less than the MIR. Generally the MIR is paid in circumstances where a member is not entitled to receive a pension in terms of the Rules. In other words it is not payable if a member is retiring or dies in service.

Why can I not get my MIR as a lump sum when I retire?

There are two important reasons why the MIR is not paid as a lump sum on retirement:

- Firstly, the Fund is approved as a "pension fund" by the SA Revenue Service (SARS). In terms of the Income Tax Act, 1962, a pension fund's rules must provide for annuities (pensions) to be paid on retirement from employment (that is, from age 55 in the case of our Fund), only one-third of which can be commuted for a lump sum.
- Secondly, the role of the MIR is to protect members who are not entitled to a pension in terms of the Rules when they leave the Fund. It ensures that a member who leaves the Fund early, receives full value for the accrued pension in terms of the Rules. It has no other function. If you retire, you will receive a pension and will therefore receive the full value (that is, MIR) of the Fund's benefits in terms of the rules.

The payment of the MIR as a lump sum on retirement would jeopardise the SARS approval of the Fund, because it would contravene both the Income Tax Act and the Fund's Rules.

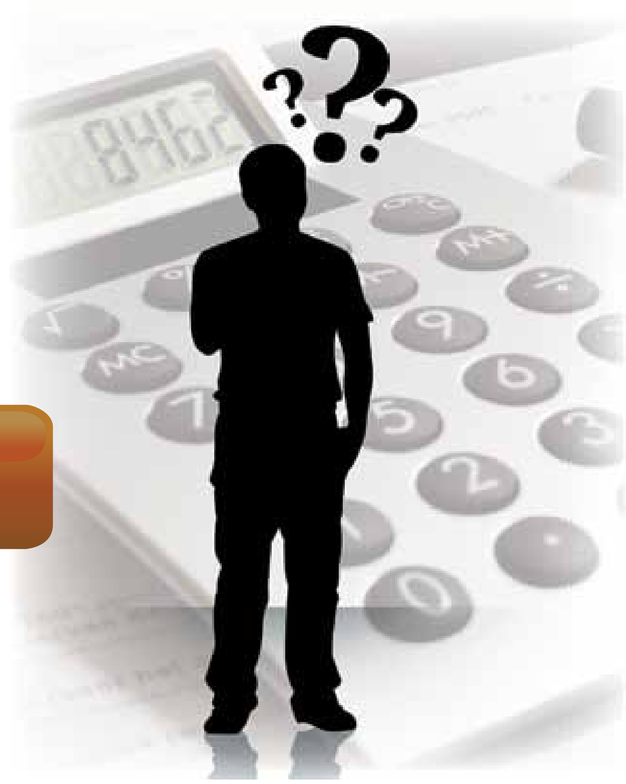
I have heard that the MIR is better than the normal retirement benefits – is this true?

In terms of the Pension Funds Act, 1956, members of pension funds should receive their MIR when they leave their pension funds for any reason whatsoever (on resignation, retrenchment or retirement etc), the only difference would be the method of payment of the MIR depending on the reason for leaving, example, on retirement the benefit (MIR) will be paid 1/3rd as cash and 2/3rd as a pension while on resignation before age 55 the benefit may be paid as a lump sum.

The MIR is quite simply the market value of the pension in terms of the Rules. Because it is based on market-related financial assumptions, its value will tend to move in line with changes in the capital markets. Therefore, there are times when the MIR could appear to be attractive and other times when it could appear to be less attractive. Bear in mind also that, in the MIR calculation, no allowance is made for the state of health of the member. Therefore if the Fund was allowed to pay the MIR as a lump sum to a retiring member, a member in ill-health with a reduced life-expectancy may receive more money than is actually required to secure the pension, and a member in excellent health, with a long life-expectancy, may not receive enough to last a life-time.

Can I resign just before retirement age and get my MIR as a benefit?

SARS will normally scrutinise the taxpayers next tax submission to check if the resignation was not a retirement disguised as a resignation (which is contrary to a General Note GN4 issued by SARS in 1995). In any event you would not gain financially because resignation benefits are taxed more harshly than retirement benefits and the resignation lump sum benefit from the Fund will be taxed heavily.



What happens if I resign just before retirement age, preserve my MIR and then retire?

If you resign and preserve your MIR in the Fund, it will be accumulated with investment returns from your resignation date until your retirement date. At your retirement date you would be able to draw up to 1/3rd of the value as a lump sum and the balance would be used to secure a pension for you and your spouse from the Fund. The pension would be calculated using the Fund's annuity factors, based on your age at retirement.

A comparison of these benefits with the normal retirement benefit in terms of the Rules, is most likely to be financially neutral, because the Fund uses the same annuity factors to convert a lump sum to a pension as they use in calculating the MIR. You would also need to take account of the loss of post-retirement medical aid benefits, which is financially material for most pensioners.

The Fund would be at risk of contravening the Income Tax Act if the date of resignation was close to retirement age, and if it appears that a retirement is being disguised as a resignation.

Spotlight on …
the people in the Fund

Linda Soga joined the EPPF in September 2008 as an Investment Multi-Manager. We chatted to her about her role …

> “… one must be able to analyse the markets and gauge investment performance.”

A little bit about you …
I completed my B.Comm in 1998 at the University of Natal majoring in Economics and Finance. I then completed my B.Comm Honours through UNISA in 2001.

I've been in the Financial Services Industry for nine years now. My previous roles have included working as an Investment Manager for the Transnet Pension Fund and as an Investment Consultant at Fifth Quadrant Actuaries & Consultants.

What type of person best suits the role of an investment manager?
Analytical … one must be able to analyse the markets and gauge investment performance. External asset managers manage the bulk of the Fund's investments and you have to be comfortable to interact with these asset managers regularly. You must be knowledgeable about the Retirement Funds Industry and, of course, investing in general.

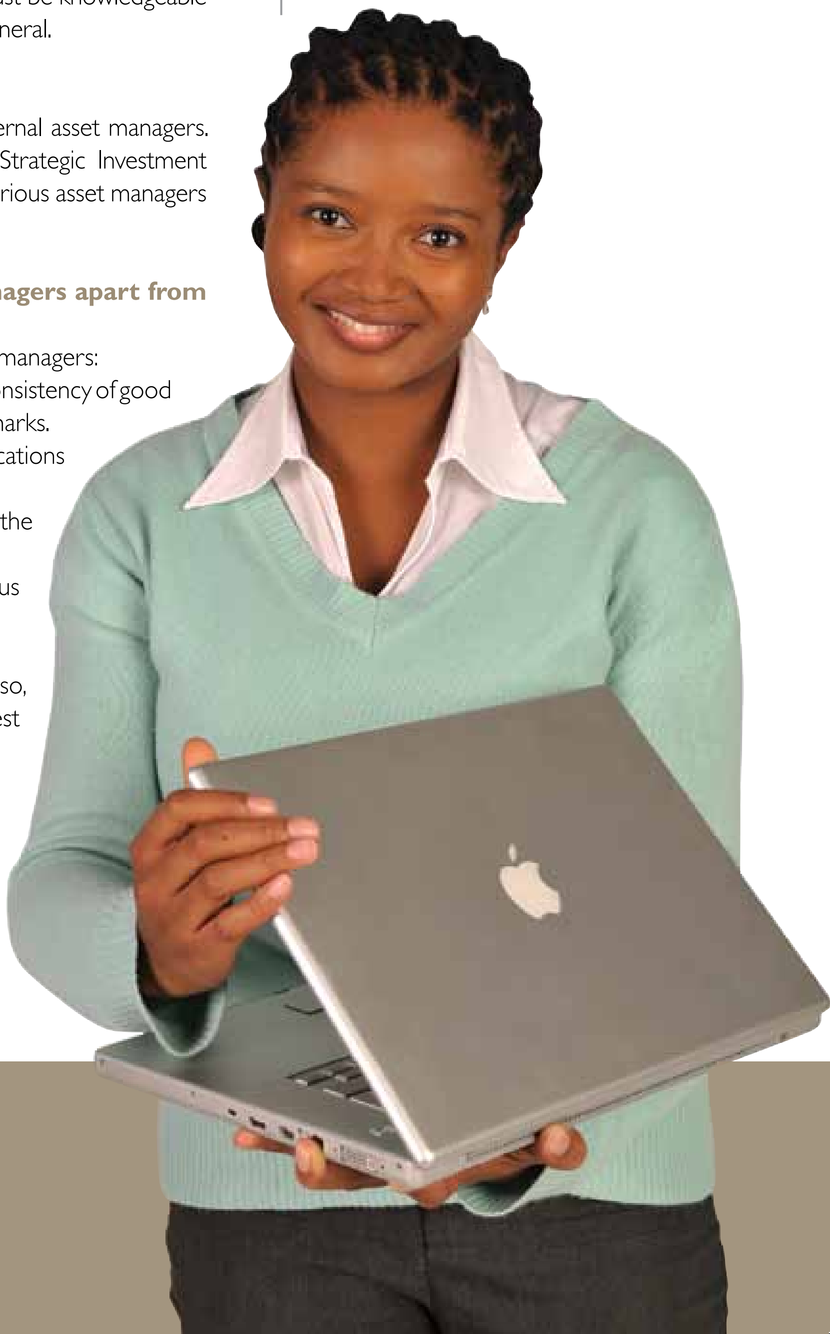
What is your role in the EPPF?
I am an Investment Multi-Manager. This involves selecting the external asset managers. I also monitor their performance and regularly report to the Strategic Investment Committee, which is a sub-committee of the Board. I screen the various asset managers and manage the Fund's relationship with them.

Name the qualities that set successful investment managers apart from the others?
There are basically four criteria that I use to evaluate investment managers:

- Performance – not just performance over the short term, but consistency of good performance – that is, meeting the mandates and set benchmarks.
- People – the quality of the investment team and the qualifications of that team.
- Investment philosophy – how do they go about choosing the assets in which to invest.
- Processes – how they translate their philosophy into the various portfolios.

A good manager must be outstanding on all the above criteria. Also, their ethos and ethics must be in line with, and in the best interest of the Fund and our members.

How do you go about deciding what to invest in and what not to invest in?
The Fund provides broad guidelines to the asset managers. They are given a mandate and a performance target or benchmark – the Fund's Strategic Investment Committee sets these criteria. The manager chooses the assets to invest in but these must be within the mandate that they were given.



Tell us about any good or bad personal investment experiences?

I'm now very conservative with my personal finances. I did, however, make a bad decision in the past – when I left one of my previous employers I took my retirement fund benefit in cash and didn't preserve it. In hindsight it was a poor investment decision because I now have to make up for the loss of future retirement income. Not only did I pay tax on the amount, I've also missed out on the benefit of compound interest on the money. I'm lucky that I'm still young enough to make up some of the loss but if I was older I would never be able to make up the loss. It's definitely something I won't do again.

I used the money to travel – which I enjoyed - but what I actually should have done was saved separately for the trip. I was young and naïve then. One must always remember that the longer you remain invested the more your money will grow – the power of compound interest (interest on interest).

Do you use any technology to help with your job?

I get most of my information through a live feed from I-Net but I do a lot of research myself.

Any major challenges since joining the Fund?

I've had a steep learning curve since joining the Fund. I joined the EPPF in September 2008 and in October 2008 the current global financial crisis hit and the market panic began. It has been challenging and quite stressful to remain focused on the long-term goals of the Fund with all the current short-term volatility. However, we know from experience that we just have to ride out the volatility and that it is the nature of markets to be volatile. As a long-term investor the Fund has to be patient and wait for the upswing.

What projects are currently on the go?

In terms of Black Economic Empowerment … the Board of Trustees of the Fund has decided to make an asset allocation to qualifying emerging black asset managers. We have researched all eligible asset managers and are now in the selection process.

The project entails targeting established asset managers with a minimum of 50% BEE shareholding and with a minimum of 50% black senior professionals. These asset managers will be monitored and will be subject to the same mandates as the Fund's current asset managers. They will have the same performance targets. In short, it means that the Fund will be giving an opportunity to these asset managers but the requirements will remain the same.

> "Remember … always seek the advice of a credible financial consultant when making those important investment decisions."

What kind of advice would you give an investor in the current financial climate?

If you have the time, that is a long-term investment horizon of seven years or more, then you could ride out the current market volatility and wait for the market recovery.

The key is not to panic and switch investment portfolios and lock in the losses. If you are closer to retirement you should seek the advice of a registered financial planner who will be able to assist you in making an informed decision.

Preservation and your retirement savings

IT IS A REALITY that many people will not work for one employer all of their working lives. If you leave the Fund before retirement, that is, if you resign, are retrenched or are dismissed, you will receive a lump sum benefit that will not be less than the minimum benefit in terms of the Pension Funds Act (see article "Benefit statements … Your questions answered" for more on MIR).

You have a number of options available when leaving the EPPF.

- You can preserve your benefit by:
  - Transferring your benefit to your **new employer's retirement fund**.
  - Electing to become a deferred pensioner on the Fund – this benefit reverts to the **Deferred Pension Scheme** and can only be accessed from age 55.
  - Transferring your benefit to any approved **retirement annuity**.
  - Transferring your benefit to a **preservation fund** in which your employer participates.
- Or, your final option is to take the money in cash (you will pay tax on this money).

Research shows that the average working South African will change jobs at least five times during their working life*. So what do people do with their retirement fund money each time they move between jobs? Approximately nine out of ten people cash in their retirement funds and start saving again from scratch in their next job*. This has a huge impact on the amount of the retirement savings you will have when you eventually retire. This is why the average South African is retiring on less than 28% of their final pre-retirement salary*.

Now, if you worked for one company for 40 years (the average working life) and contributed towards your retirement savings every month, you might be able to replace about 70% of your pre-retirement salary at retirement*. Assuming that you are debt free, this might provide you with a comfortable retirement.

The only other way to ensure that you have the same effect that unbroken service would give is to preserve your retirement benefit every time you change jobs.

❖ **A preservation fund** is a retirement fund designed to preserve your money. It is similar to a retirement annuity but has the advantage of allowing one lump sum withdrawal prior to age 55. You can't make ongoing contributions to a preservation fund and must make your election for the transfer before you leave your employer. Also, your employer must agree to participate in the fund before you leave.

Note, if you belong to a **provident fund**, you must transfer to a **provident preservation fund.** Similarly, if you belong to a **pension fund** you must transfer to a **pension preservation fund**.

A member can retire from the **preservation fund** from age 55.

❖ **Retirement annuity funds** can also be used for preserving your withdrawal benefit or for providing a pension with the money that you want to save for your retirement. You may choose to either make monthly contributions, or to pay a once-off premium.

You may retire from a **retirement annuity fund** at any time from age 55. Should you die before retirement, the full value of your contributions, plus the interest provided by the annuity, will be paid to your nominated beneficiary/ dependant (subject to tax).

Note: Transfers to a new employer's fund, a **preservation fund** or **retirement annuity fund**, is tax-free at the time of transfer, provided that the transfer is not from a pension fund to either a **provident fund** or a **provident preservation fund.**

But you might be thinking … What about my life now? Most people don't save ahead for the next year of their lives, let alone for their retirement. After all, with rising food prices, high interest rates and increased cost of living, there are so many things that you need to think about now. When it comes to the option of receiving a lump sum cash payment when leaving your retirement fund it is easy to be tempted to use your withdrawal benefit to settle your short-term debts. Most people feel that they need the money for their children's education or paying off their home loan.

But you have to think about the future … if you retire and your pension is less than 50% of your final pre-retirement salary, you will have a tough time and your lifestyle will definitely not resemble the way you used to live before you retired. On the other hand, if you are debt free and living on a pension equivalent to 70% of your final salary, it will be easier to maintain your quality of life.

To give yourself the best chance of financial success in the long term **always make your financial decisions with the help of a professional financial advisor.** The financial decisions you make today will have an impact (positive or negative) on your long-term financial goals.

(*for more info go to:www.irf.org.za)

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