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RETIREMENT PROVISION

Child care

Fairheads promotes Beneficiary Funds

NOT ENOUGH SOUTH AFRICANS KNOW about beneficiary funds, which are a cost-effective alternative to setting up a testamentary trust to care for your children if you die, says Giselle Gould, business development director of Fairheads Benefit Services. She spoke at the Institute of Retirement Funds conference in Durban on 18th August 2014.

She said that anyone who is a member of a retirement fund could state on their nomination form that the trustees should consider the use of a beneficiary fund to accept death benefits on behalf of their minor dependants, should the member die while in service. Members should also nominate a guardian for their minor children. "Beneficiary funds are tightly regulated by the Pension Funds Act and were introduced in 2009, yet very few people know about them and retirement funds are not doing enough to communicate their existence to members.

"Beneficiary funds are cheaper than setting up a testamentary trust to care for your children if you die. They benefit from economies of scale as one fund can comprise thousands of minors' sub-accounts." As a result, institutional fees apply. They are tax efficient too, with no tax paid in the beneficiary fund and any payment out of a beneficiary fund, whether capital or income, is also tax free.

In many instances, it is preferable for retirement fund trustees to pay lump-sum death benefits into a beneficiary fund instead of directly to the guardian. By paying into a beneficiary fund, the assets are in the child's own name and carefully invested and managed until they turn 18. If they were paid to the guardian and the guardian should die, the assets would form part of his or her estate and not necessarily be used to pay for minors' expenses such as education.


Giselle Gould

Gould called on retirement funds to appoint beneficiary fund service providers and ensure that members were aware of their benefits.

About Beneficiary funds

Beneficiary funds are aligned with the Pension Funds Act and are designed to receive lump-sum death benefit payments in terms of section 37c of that act. Upon the death of a retirement fund member, the trustees identify the dependants and use their discretion whether to pay the money into a beneficiary fund, administer it within the retirement fund or pay it directly to the guardian. They are guided in this complex decision by service providers such as Fairheads which has developed tools such as a guardian assessment process to assess whether a guardian is financially literate and capable of investing and administering minors' assets for their benefit.

Once in a beneficiary fund, the trusteeship of the assets passes to the board of the beneficiary fund. Beneficiary funds are structured similarly to retirement funds. They offer greater protection for minors as they are regulated by the Pension Funds Act and all stakeholders have recourse to the Pension Funds Adjudicator; there are strict corporate governance requirements; and investments are prudentially managed in line with regulation 28. When the minor turns 18, he or she is entitled to the remaining assets in the beneficiary fund.

Once the funds are in a beneficiary fund, the trustees of the beneficiary fund take over the fiduciary duty from the retirement fund trustees. In consultation with the guardian who needs to draw up a budget, the trustees assess the income needs of the minor and, taking into account the capital amount and the age of the child, conduct an asset allocation exercise, inserting the child into a specific asset allocation matrix.

In Fairheads' experience, the average beneficiary fund account is around R100 000 which, carefully managed, can provide a monthly income and finance an entire education through to tertiary level. When the member turns 18, the account is terminated and the funds paid out unless the member requests they remain in the beneficiary fund.

Fairheads has found that over 70% of all special requests for capital payments from beneficiary funds are education-related, be this for school or tertiary education fees, books, uniform etc.

In line with best practice, Fairheads outsources the investment of beneficiary funds to a number of leading investment houses. The investment strategy for a beneficiary fund is distinctly different from that of a retirement fund. Individual members of a beneficiary fund have very different needs and this requires an asset allocation matrix for each category of members. Essentially this is a type of life-stage investment model, but determined by the trustees in consultation with asset consultants. For example, a one-year old member will have very different needs from a 16-year old member in high school and therefore would fit into a separate asset allocation matrix.