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## LEGAL UPDATE 13/2010: TRANSFERS TO PRESERVATION FUNDS

The Income Tax Act No. 58 of 1962, as amended by the Taxation Laws Amendment Act No. 17 of 2009, allows for the following transfers to preservation funds:

From	To
Pension Fund	Pension Preservation Fund
Pension Preservation Fund	Pension Preservation Fund
Provident Fund	Provident Preservation Fund
Provident Preservation Fund	Provident Preservation Fund

Momentum often has queries as to whether members of pension and provident funds may transfer their benefits to preservation funds even though they have already reached normal retirement age.

Furthermore, members who have reached normal retirement age sometimes submit withdrawal forms requesting that we withdraw rather than retire them in order to enable them to transfer their withdrawal benefits to preservation funds. Employers also attempt to amend the normal retirement age in the Special Rules in order to allow members who have reached normal retirement age to withdraw and transfer their benefits to preservation funds.

This is not allowed, for the reasons given below.

Paragraph (a) of the definition of “pension preservation fund” in the Income Tax Act No. 58 of 1962 provides that:

- (a) *membership of the fund consists of—*
  - (i) *former members of a pension fund whose membership of that fund has terminated due to—*
    - (aa) *resignation, retrenchment or dismissal from employment and who elected to have any lump sum benefit that is payable as a result of the termination transferred to that fund;*

**Allowable transfers to preservation funds**

**Can a member transfer their benefits to a preservation fund after reaching normal retirement age?**

**Definition of pension preservation fund in the Income Tax Act**

- (bb) *the winding up of that fund, if the member elects or is required in terms of the rules to transfer to this fund; or*
- (cc) *a transfer of business from one employer to another in terms of section 197 of the Labour Relations Act, 1995 (Act No. 66 of 1995), and the employment.*

This applies *mutatis mutandis* to a provident preservation fund.

The General Rules of the FundsAtWork Umbrella Pension and Provident Funds define WITHDRAWAL as follows:

*WITHDRAWAL means a MEMBER'S leaving the FUND as a result of –*

- (a) *his resignation or dismissal;*
- (b) *him no longer being an ELIGIBLE EMPLOYEE as contemplated in RULE 6.2.2.3;*
- (c) *the liquidation of his PARTICIPATING EMPLOYER, or*
- (d) *his PARTICIPATING EMPLOYER terminating its participation in the FUND in terms of RULE 4.3,*

***provided that such MEMBER has not already reached the NORMAL RETIREMENT AGE.***

From this, it is evident that a member who has already reached the normal retirement date as specified in the Special Rules cannot claim a withdrawal benefit.

Rule 10.6.6 of the General Rules of the FundsAtWork Pension Fund provide as follows with regards to withdrawal benefits:

*WITHDRAWAL benefits will be paid as a lump sum. Subject to the requirements of the COMMISSIONER and the INCOME TAX ACT, a withdrawing MEMBER may elect to –*

- 10.6.6.1 *take his WITHDRAWAL benefit in cash;*
- 10.6.6.2 *transfer his WITHDRAWAL benefit to an APPROVED FUND;*
- 10.6.6.3 *take a portion of his WITHDRAWAL benefit in cash and transfer the balance to an APPROVED FUND;*
- 10.6.6.4 *transfer a portion of his WITHDRAWAL benefit to an APPROVED RETIREMENT ANNUITY FUND and the balance to an APPROVED PENSION PRESERVATION FUND, or*
- 10.6.6.5 *transfer his gross WITHDRAWAL benefit, reduced only by a deduction in terms of section 37D of the ACT, to an APPROVED PENSION PRESERVATION FUND.*

**Definition of withdrawal in the FundsAtWork Umbrella Pension and Provident Funds**

Rule 10.6.2 in turn deals with retirement benefits as follows:

*RETIREMENT benefits and disablement benefits will be used to purchase a pension in the name of the MEMBER from an INSURER. A MEMBER may prior to his RETIREMENT elect to commute so much of this pension as is permitted in terms of the INCOME TAX ACT to a lump sum.*

The General Rules of the FundsAtWork Umbrella Provident Fund have similar provisions.

A withdrawing member in the FundsAtWork Umbrella Pension and Provident Funds would be able to transfer their withdrawal benefit to an approved pension or provident preservation fund, as the case may be. However, a retiring member would have to purchase a pension / commute as much of their retirement benefit as permitted by the Income Tax Act. The retiring member would therefore not be able to transfer to a preservation fund.

This has been confirmed by SARS, who advised that in terms of the current tax legislative framework, only withdrawal benefits from pension and provident funds are transferable to preservation funds. Benefits due to retirement should not be transferred to preservation funds. Once a member of a fund has reached retirement age in terms of the rules of the fund, the member must retire and receive a retirement benefit.

SARS has also confirmed that should either the "transferring (employer) fund" or "receiving (preservation) fund" or both be found to have acted contrary to any of the conditions subject to which their rules were approved for tax, the approval status of such a fund will summarily be withdrawn. This will have adverse tax consequences for the remaining members of such an offending fund.

In line with this, once members of pension and provident funds reach normal retirement age in terms of the rules of the fund in which they belong, members will only be entitled to a retirement benefit and may not transfer their retirement benefit to a preservation fund.

Carlo Subban  
Legal Adviser  
Momentum BenefitsAtWork

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**A member who has reached normal retirement age may not transfer the benefit to a preservation fund**

**SARS confirmation**