momentum

Consolidated legal updates
2014

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FundsAtWork

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Legal update

No. 1 of 2014 • 17 January 2014

Payment of death benefits on employer-owned insurance policies

From 1 March 2012, an employer who is the policyholder of a lump sum death benefit insurance policy can claim an income tax deduction in terms of section 11(*w*)(i) of the Income Tax Act for the premiums paid *only if* the amount is included in the taxable income of the employee concerned. For that reason, the premium must be added to the employee's remuneration as a fringe benefit and taxed accordingly without further deduction. Furthermore, the premiums paid by the employer have to be for an insurance policy *directly or indirectly for the benefit of the employee or his or her spouse, child, dependant or nominee* (refer paragraph 2(*k*) of the Seventh Schedule of the Income Tax Act). If these requirements are met, the proceeds from the insurance policy will be paid out tax-free to the employee, dependant or nominee in terms of section 10(1)(*g*G) of the Income Tax Act.

Following these changes, Momentum Employee Benefits has changed the wording for all new lump sum death benefit insurance policies to provide as follows with regards to the payment of the death benefit:

On production of a death certificate satisfactory to Momentum and such other information as Momentum may require in respect of a Member, Momentum shall pay the Death Benefit to the Policyholder for the benefit of the natural person nominated, in writing, by the Member or failing such nomination (or part thereof) to the estate of the Member.

This means that Momentum will pay the benefit to the employer as the policyholder. The employer must then ensure that the benefit is paid to the member's nominated beneficiaries, who must be a natural or living person. If the member did not make a nomination (or the nomination does not distribute 100% of the benefit), then the employer will have no alternative but to pay the whole or a portion of the benefit to the member's estate. The employer does not have any discretion. The employer cannot for instance decide to distribute the benefit to the member's beneficiaries in the proportions they consider appropriate and ignore the member's nomination.

We recommend that the employer makes sure that each member completes a beneficiary nomination form for the lump sum death insurance benefit and keep these nominations up to date. The nomination of beneficiaries made by a member in respect of his / her pension / provident fund cannot be used for these death benefit insurance policies. The employee must complete a separate nomination form for each of the benefits. For example if the employee belongs to a pension fund and has group life cover from the pension fund (approved benefit) and from an employer-owned insurance policy, they need to complete two beneficiary nomination forms. This will result in their rightful beneficiaries receiving the death benefit. The employer can click here for the beneficiary nomination form. All FundsAtWork forms are available on www.momentum.co.za/fundsatwork.

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Legal update

No. 2 of 2014 • 17 January 2014

Taxation of group insurance premiums and benefits

Summary

The Taxation Laws Amendment Act No. 31 of 2013 that was published in Government Gazette No. 37158 on 12 December 2013 brings a change to the taxation of employer-provided disability income benefits. From 1 March 2015, a member will no longer be able to claim a tax deduction on the premium paid for a disability income benefit and the benefit will be paid out tax-free.

Current position for the employer-provided (unapproved) insurance benefits that have been set up for the benefit of the employee or their spouse, child, dependant or nominee

	Death, disability, severe illness lump sum	**Disability income**
Employer	Deduction for premiums paid on behalf of the employee.	Deduction for premiums paid on behalf of the employee.
Member	Premiums taxed as fringe benefit. No deduction for premiums paid.	Premiums taxed as fringe benefit. Deduction for premiums paid.
Benefit	Tax-free – exemption will apply.	Taxed – included in gross income, no exemption.

Currently, the premiums paid by an employer on self-standing insurance benefits such as death and disability for the benefit of the employee or their spouse, child, dependant or nominee, are deemed to be a taxable benefit granted by the employer to the employee. This means that these premiums have to be taxed as fringe benefits in the hands of the employee.

A lump sum benefit is paid out tax-free to the employee or their dependants or nominees in terms of section 10(1)(*gG*) of the Income Tax Act. When the benefit is paid to the employer, it is included in the employer's gross income. If the employer then on-pays this amount to the employee or their dependants or nominees, the employer must ask for a section 11(*a)* deduction for this payment. The employer's tax position is ultimately neutral, but they first need to account for the accrual and subsequent deduction in their own records.

Employer-provided disability income benefits on the other hand are treated differently. The employee is entitled to claim a tax deduction for the premium on which they paid fringe benefit tax. The employee's tax position for the premium is neutral – they pay fringe benefit tax, but get a deduction for that. If the employee receives a benefit, it is taxed.

Position from 1 March 2015 for the employer-provided (unapproved) insurance benefits that are set up for the benefit of the employee or their spouse, child, dependant or nominee

	Death, disability, severe illness (whether the benefit is paid as a lump sum or annuity)
Employer	Deduction for premiums paid on behalf of the employee.
Member	Premiums taxed as fringe benefit. No tax deduction.
Benefit	Tax-free – exemption will apply.

National Treasury has set out to align the tax position of lump sum disability and income disability insurance benefits. From 1 March 2015, an employee will no longer be able to claim a deduction on the premiums paid for disability income insurance benefits. These benefits will be treated the same as employer-provided lump sum insurance benefits – the premiums will be taxed as fringe benefits in the hands of the employee and the benefit will be paid out to the employee tax-free. The premiums will still be deductible for the employer as long as the premiums have been taxed in the hands of the employee as a fringe benefit. The employer deduction will fall under section 11*(w)*(i) of the Income Tax Act. Section 11(*w*)(i) only relates to cover for employees or directors of the employer. If any other person is covered, the employer should ask for a deduction under the general deduction formula.

Impact on FundsAtWork members

These changes will have an effect on the take-home pay of members who are covered for disability income insurance benefits provided by their employers, as they will no longer be able to claim a tax deduction on the premiums. On the other hand, the benefit will no longer be taxed.

The following simplified example, which does not take any probabilities or interest into account, illustrates the difference between having to pay tax on the premium and paying tax on the benefit.

Mark is 25 years old. His disability income benefit is equal to 100% of his annual insurance salary of R165 000. The premium for this benefit is R1 732.50 per year. The termination date for the benefit is when Mark turns 65. His tax rate is 18%. We assume that neither his insurance salary nor his premiums change. He becomes disabled when he is 50. By that time he paid R43 312.50 (R1 732.50 per year X 25 years) in premiums. His total benefit at age 65 would be R2 475 000 (R165 000 per year X 15 years).

If the benefit is taxed, Mark would pay tax of R445 500 in total during the 15 years. If the premiums are taxed, Mark would pay tax of R7 796.25 over the period of 25 years. In this example, the tax on the benefit is much higher than the tax on the premium and therefore Mark will be better off under the new dispensation.

However, if Mark did not become disabled, he would have paid tax on the premiums without ever receiving the tax-free benefit. Most members do not become disabled before retirement. Most members would therefore not be subject to the benefits of the tax saving on the benefit payments.

From 1 March 2015 all employer-provided insurance benefits will be tax-free, even if the premiums were previously deductible. Members who were claiming a tax deduction on disability income premiums will be in the fortunate position of having had a tax neutral position for the premiums up to 1 March 2015 and getting their benefit paid out to them tax-free if they claim after this date.

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Legal update

No. 3 of 2014 • 17January 2014

Retirement fund contributions

Summary

The Taxation Laws Amendment Act No. 31 of 2013 that was published in Government Gazette No. 37158 on 12 December 2013 changes the tax treatment of contributions and aligns the annuitisation requirements between pension, provident and retirement annuity funds. This Legal Update addresses the taxation of retirement fund contributions. Legal Update 4 of 2014 sets out the post-retirement alignment between retirement funds.

From 1 March 2015, employer contributions will be taxed in the hands of the member and the member will get a tax deduction on the total contribution towards retirement funds, subject to an annual percentage and monetary limits.

Current position for retirement fund contributions

There are three types of retirement funds with recurring contributions: pension and provident funds, which are employment-based, and retirement annuity funds, which are retirement funding vehicles for individuals. There are different tax deductions that apply for the contributions to these funds.

	Pension fund	**Provident fund**	**Retirement annuity fund**
Deduction on member contribution	Up to 7.5% of *“retirement-funding employment”.	None	Up to 15% of non-*“retirement-funding employment”.
Deduction on employer contribution	Up to 10% of **“approved remuneration”. In practice SARS allows up to 20%.	Up to 10% of **”approved remuneration”. In practice SARS allows up to 20%.	N/A

* “Retirement-funding employment” is defined as income consisting of “remuneration” as defined; it is the income taken into account in determining the contributions made by the employee or employer for the benefit of the employee to a pension fund or provident fund.

**Approved remuneration” is defined as follows in section 11(*l*)(iii) of the Income Tax Act: *so much of the total remuneration accrued to such employee during such year of assessment in respect of his employment by the employer concerned as the Commissioner considers to be fair and reasonable in relation to the value of* *the services rendered by such employee during such year of assessment to the employer and having regard to other benefits, if any, derived by him from his employment by the employer.*

Position from 1 March 2015 for retirement fund contributions

	All retirement funds (pension, provident, retirement annuity)
Deduction on member contribution	Up to 27.5% of the greater of ***remuneration or taxable income, subject to an annual monetary limit of R350 000.
Deduction on employer contribution	Unlimited deduction. Employer contributions taxed as a fringe benefit in employee's hands and deemed to be employee contributions.

***Remuneration refers to the payment made to an employee (their salary) and for the purposes of this calculation will exclude any retirement fund lump sum, lump sum withdrawal benefit or severance benefit. Taxable income is a person's total income, from all sources, less the allowable deductions and exemptions. An employee, who receives a salary from their employer but also has other sources of income, can potentially have a taxable income that is higher than their remuneration. In that case, the maximum deduction will be based on their taxable income instead of just their remuneration.

<u>Employee contributions</u>

From 1 March 2015, the contributions paid by an employer for the benefit of their employee to a retirement fund will be deemed to be an employee contribution and will be taxed in the employee's hands. These contributions however, together with the member's other retirement fund contributions, will qualify for a deduction of up to 27.5% of their remuneration or taxable income, whichever is the higher, subject to an annual maximum of R350 000. By implication, the maximum amount that can be taken into account for calculating the maximum retirement fund contributions in a specific year is R1 272 727. Any contribution over that amount will not qualify as a deduction in that year of assessment, but will be carried forward to future years of assessment, once again subject to the annual limits. Whatever the member is not able to claim as a deduction before leaving the fund, can be claimed as a deduction in terms of the Second Schedule to the Income Tax Act when they leave the fund or alternatively, as a reduction in taxable annuity income. This can be illustrated by way of the following example.

Mark earns a salary of R1 500 000 per annum. He also lets out his property and receives rental of R120 000. His deductible expenses in relation to the property are R150 000. His taxable income of R1 470 000 (R1 500 000 + R120 000 – R150 000) is less than his remuneration of R1 500 000. For purposes of calculating the maximum tax deduction for his retirement fund contributions, he will use his remuneration of R1 500 000.

Mark's defined contribution pension fund's rules provides for an employer contribution of 15% and an employee contribution of 7.5% of his salary. Mark also contributes 5% of his salary towards a retirement annuity fund.

Mark will pay tax on 27.5% (15% employer pension fund contribution + 7.5% employee pension fund contribution + 5% retirement annuity fund contribution). He will pay tax on R412 500 (27.5% of his salary of R1 500 000). He can deduct a maximum of R412 500 or R350 000, whichever is the lowest. He will accordingly only be able to deduct R350 000 in the year of assessment, with the balance of R62 500 rolling over until the next year of assessment. If Mark's taxable income remains the same and the monetary cap does not increase, it will mean that the amount to be rolled over each year will increase by the excess of the specific year of assessment. The total amount rolled over by the time the member leaves the fund, can be deducted from his lump sum before the tax paid on the lump sum is calculated. If the total amount rolled over exceeds the lump sum, the deduction can be made against the member's pension.

While the deduction of employer contributions in a defined contribution fund is fairly straight-forward (being equal to the value of the amount contributed by the employer for the benefit of the employee – the employer contribution), that is not the case in a defined benefit fund. In the latter, the cash equivalent of the amount that the employee can deduct is the total of the value of the employer contribution to the defined contribution component of the fund and the employer contribution to the defined benefit component of the fund in accordance with the formula X = Y ((A x AF) + (L x LF)) – V as set out in the newly introduced paragraph 12D of the Seventh Schedule to the Income Tax Act.

<u>Employer contributions</u>

The deduction of the employer contribution is still allowed. In fact, the employer's position as far as the deductibility of contributions towards a retirement fund will be even better from 1 March 2015. The 10% limitation is section 11(*l*) of the Income Tax Act has been removed. This means that the employer has an unlimited retirement fund contributions deduction; they can deduct whatever they contribute for the benefit of their employees to a pension, provident or retirement annuity fund.

In the example above, Mark's employer will be able to deduct the employer contribution of 15%.

Impact on FundsAtWork

The impact on the average member should not be different from the current position. The combined contribution rate on the FundsAtWork schemes is in the region of 12% and most members' remuneration fall below R1 272 727. Although all members will have to pay tax on their employer contributions from 1 March 2015, and given that these contributions are below the deduction threshold as outlined above, they are expected to qualify for a full tax deduction for those contributions. Their tax position is therefore expected to be tax neutral. Instead of taking out a separate retirement annuity to boost their retirement savings, members may even decide to make additional voluntary contributions to their FundsAtWork Umbrella Pension or Provident Fund and make optimal use of the maximum tax deduction on their retirement fund contributions. Members may even find that making an additional voluntary contribution of 5% does not necessarily mean that their take-home pay will decrease by 5%. Take the following as an example. A member with an annual salary of R240 000 with a marginal tax rate of 25% contributes 10% (R24 000) towards his pension fund. He does not have any other taxable deductions. His taxable income after the deduction of R24 000 is R216 000. The tax payable on that is R54 000, which leaves him with a net salary of R162 000. If that member decides to increase his contribution to 15% (R36 000), his taxable income is R204 000. The tax on that is R51 000, which leaves him with a net salary of R153 000. Although his contribution went up by R12 000 (from R24 000 to R36 000), his take-home pay only dropped by R9 000 (from R162 000 to R153 000), resulting in a tax benefit of R3 000. Members are encouraged to take full advantage of the maximum tax deductions for contributions.

In light of the increased tax deduction on contributions, employers might choose to increase contributions or even to restructure the scheme to only have employer contributions. This will lead to an increase in the number of Special Rules that require amendment. The suggestion is that if employers want to increase their contributions or restructure the contribution rates, they don't wait until 2015 to do so, but rather request the amendments sooner (perhaps towards the last quarter of 2014).

The contribution deductions apply to all contributions made to a fund. They therefore include the administration costs and the costs of the insurance benefits provided by the fund. Where members need a higher percentage of their salary to be allocated towards retirement savings and also need the maximum deduction to apply to their retirement savings, rather than fund-provided insurance benefits the employer might decide to rather choose insurance benefits outside of the fund.

Where an employer does provide separate insurance benefits to their employees, and the premiums for those benefits are included in the employer contribution to a pension or provident fund (otherwise referred to as an inclusive scheme), the employer must make sure that the insurance premium portion of the contribution is taxed correctly. In these cases, the employer cannot allow the employee to claim the total employer contribution to the fund as a deduction under section 11(*k*) of the Income Tax Act; the portion of the employer contribution that relates to the employer-provided insurance benefit must be taxed as a fringe benefit in the hands of the employee in terms of paragraph 12C of the Seventh Schedule, with no corresponding deduction. Refer to Legal update 2/2014 for more information on the taxation of employer-provided (group) insurance premiums and benefits.

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Legal update

No. 4 of 2014 • 17 January 2014

Provident fund post-retirement alignment

Summary

The Taxation Laws Amendment Act No. 31 of 2013 that was published in Government Gazette No. 37158 on 12 December 2013 changes the tax treatment of contributions and aligns the annuitisation requirements between pension, provident and retirement annuity funds. Legal Update 3 of 2014 addresses the taxation of retirement fund contributions. This Legal Update explains the post-retirement alignment between retirement funds.

The following three major changes about the post-retirement alignment will come into effect on 1 March 2015:

1. A member of a provident fund will no longer be able to take their whole retirement benefit in a lump sum. They will only be able to take 1/3rd in a lump sum, while the rest of the benefit must be used to buy a pension (annuity), the same as with a pension and a retirement annuity fund. However, the member's vested rights will be protected and they will still be able to take the portion of their benefit that built up before 1 March 2015, plus the growth, in a lump sum. The 1/3rd restriction will not apply to a member who is over the age of 55 on 1 March 2015, unless the member transfers to another retirement fund. It also does not apply to paragraphs (a) and (b) pension funds.

2. The *de minimus* threshold has been increased from R75 000 to R150 000. This means that if a member's total benefit at retirement in a specific fund is less than or equal to R150 000, they can take their whole benefit in a lump sum. It will then not be necessary for them to take 1/3rd of the benefit in a lump sum and buy a pension with the rest. The current *de minimus* threshold applies to pension, pension preservation and retirement annuity funds. The new threshold of R150 000 will apply to pension, pension preservation, provident, provident preservation and retirement annuity funds.

3. Following the post-retirement alignment, a member will also be able to transfer between a pension and provident fund and *vice versa* without incurring any tax liability.

Current position for benefit pay-outs

	Pension / Retirement Annuity Fund	Provident Fund
Retirement payout / annuitisation	At least 2/3rds must be used to buy a pension (annuity).	Member may take entire benefit as a lump sum.
Taxation of retirement payout	Lump sum taxed according to retirement tax tables. Pension taxed at member's marginal tax rate.	Lump sum taxed according to retirement tax tables.
De minimus exception	If the total benefit is less than or equal to R75 000, the entire benefit can be taken as a lump sum.	N/A

Current position for tax-free fund to fund transfers

From	To
Pension Fund	Pension Fund Pension Preservation Fund Retirement Annuity Fund
Pension Preservation Fund	Pension Fund Pension Preservation Fund Retirement Annuity Fund
Provident Fund	Pension Fund Pension Preservation Fund Provident Fund Provident Preservation Fund Retirement Annuity Fund
Provident Preservation Fund	Pension Preservation Fund Provident Fund Provident Preservation Fund Retirement Annuity Fund
Retirement Annuity Fund	Retirement Annuity Fund

The general rule for fund-to-fund transfers is that if the member transfers from a fund that is less restrictive to a fund that is more restrictive, the transfer will be tax-free. For example, if a member transfers from a provident fund (where they are allowed to take their whole retirement benefit in a lump sum) to a pension fund (where they can only take 1/3rd of the retirement benefit in a lump sum), the transfer will be tax-free.

It is Government's policy to encourage a secure post-retirement income in the form of a mandatory pension to make sure that retirees do not spend their retirement fund benefits too quickly and then outlive their retirement savings and become dependent on the State. To do this, provident fund members will become subject to the same annuitisation requirements as those applying to members of pension and retirement annuity funds.

Position from 1 March 2015 for benefit pay-outs in provident funds

	Pre-1 March 2015 portion of benefit	**Post-1 March 2015 portion of benefit**
Retirement: Member younger than 55 years on 1 March 2015	Benefit plus growth may be taken as a lump sum.	Member is required to buy a pension with at least 2/3 rds of the benefit. Up to 1/3rd of the benefit may be taken as a lump sum.
Retirement: Member older than 55 years on 1 March 2015	Entire benefit can be taken as a lump sum upon retirement.	Entire benefit can be taken as a lump sum upon retirement for contributions to the same retirement fund as at 1 March 2015.
De minimus exception	N/A	If amount subject to annuitisation is less than or equal to R150 000, member can take entire benefit as a lump sum.

From 1 March 2015, a member who retires from a provident fund will have to buy a pension with at least 2/3 rds of their benefit. The same requirement already applies to pension and retirement annuity funds. The member will however still be able to take that part of their benefit that accrued up to 1 March 2015, plus the growth, in a lump sum. This protection of their vested rights will apply even if they transfer to another fund. In practice this means that a provident fund will have to maintain two records for each member – one for the benefit that accrued before 1 March 2015, plus the growth, and one for the benefit that accrued after 1 March 2015, with the growth. The following example illustrates what will happen from 1 March 2015.

Facts:

Mark is a member of P Provident Fund on 1 March 2015.

Mark's benefit on 1 March 2015 is R400 000. The growth on this is R50 000 per year.

Mark continues to contribute R100 000 to his benefit every year. The annual growth on this is also R50 000 per year.

On 1 March 2017 Mark transfers to T Pension Fund.

On 29 February 2020 Mark retires from T Pension Fund.

Result:

P Provident Fund has to keep two records for Mark – one for the R400 000 benefit that Mark accrued before 1 March 2015, plus the growth, and one for the benefit that accrued after 1 March 2015, with the growth.

On 1 March 2017 the amount in Marks's pre-1 March 2015 account is R500 000 (R400 000 + [R50 000 x 2]). On that same date, the amount in Mark's post-1 March 2015 account is R300 000 ([R100 000 x 2] + [R50 000 x 2]).

When P Provident Fund transfers Mark's benefit to T Pension Fund, P Provident Fund must indicate the value of the two accounts.

T Pension Fund in turn must also have two records for Mark. Record 1 will reflect Mark's pre-1 March 2015 benefit plus growth, and record 2 will be for Mark's post-1 March 2015 amount. T Pension Fund will put the R500 000 transferred from Mark's pre-1 March 2015 account at P Provident Fund to Mark's pre-1 March 2015 account in T Pension Fund and the R300 000 transferred from Mark's post-1 March 2015 account at P Provident Fund to Mark's post-1 March 2015 account in T Pension Fund.

When Mark retires on 29 February 2020, the amount in his pre-1 March 2015 account will be R650 000 (R500 000 + [R50 000 x 3]). Mark can take this benefit in a lump sum. The amount in his post-1 March 2015 account will be R750 000 (R300 000 + ([R100 000 x 3] + [R50 000 x 3]). Mark will only be able to take R250 000 of his benefit in a lump sum and will have to buy a pension with the remaining R500 000.

The Taxation Laws Amendment Act provides that the 1/3rd restriction will not apply to a person who is a member of a provident fund and who is 55 years or older on 1 March 2015, as long as that member stays in the same fund. He will lose his vested rights with regards to the contributions made after 1 March 2015 in another fund.

A member of a provident fund who is 55 years at 1 March 2015 will be able to take the following in a lump sum at retirement: the benefit that accrued before 1 March 2015, plus the contributions made by him after 1 March 2015 to that same provident fund, together with the growth on both the pre- and the post-1 March 2015 contributions. If this member stays in the same provident fund, he will be able to take his whole benefit at retirement in a lump sum. If he however transfers to another fund, only the benefit that accrued to him while he was a member of the provident fund of which he was a member on 1 March 2015 plus subsequent growth on that portion can be taken in a lump sum. For example, if Mark in the earlier example was 55 years old on 1 March 2015, he would be able to take the R800 000 that was transferred to T Pension Fund on 1 March 2017, plus growth, in a lump sum when he retires in 2020. The balance of his benefit must be used to buy a pension, subject to the *de minimus* exemption. T Pension Fund will have to keep two records for Mark – one for the amount that was transferred from P Provident Fund on 1 March 2017, plus growth, and another one for the contributions made to T Pension Fund after the transfer, plus growth.

The 1/3rd restriction will also not apply to a pension fund as defined in paragraphs (a) and (b) of the definition of "pension fund" in section 1 of the Income Tax Act. Such a pension fund, which is defined as a provident fund in the Second Schedule to the Income Tax Act, is allowed to have a retirement lump sum benefit in excess of the 1/3rd restriction. A member of for example a municipal pension fund whose rules currently allow for their members to take their whole retirement benefit in a lump sum will therefore still be able to take their whole retirement benefit in a lump sum after 1 March 2015.

The *de minimus* exemption amount will be increased from R75 000 to R150 000 on 1 March 2015. That means that if the retirement benefit of a member of a retirement fund is R150 000 or less, the member would be able to take their whole benefit in a lump sum; he will not be required to buy a pension with at least two-thirds of his benefit. This rule applies per fund, in other words a member who has three fund benefits, each of which is less than R150 000, will be able to take all three benefits in a lump sum.

Position from 1 March 2015 for tax-free fund to fund transfers

From	To
Pension Fund **Pension Preservation Fund** **Provident Fund** **Provident Preservation Fund**	Pension Fund Pension Preservation Fund Provident Fund Provident Preservation Fund Retirement Annuity Fund
Retirement Annuity Fund	Retirement Annuity Fund

From 1 March 2015, transfers between all occupational retirement funds (pension, pension preservation, provident and provident preservation funds) and transfers from any occupational fund to a retirement annuity fund will be tax-free. A member in a retirement annuity fund will still only be able to transfer to another retirement annuity fund. The reason for this restriction is that a retirement annuity fund has a restriction that no other retirement fund has – a member in this fund cannot withdraw from the fund before retirement.

Impact on FundsAtWork

Members younger than 55 on 1 March 2015: FundsAtWork will have to keep separate records / accounts for all members in a provident fund in order to separate pre-1 March 2015 contributions and growth from post-1 March 2015 contributions and growth. This will enable FundsAtWork to determine what part of the member's benefit must be subject to annuitisation rules on retirement. It will also enable FundsAtWork to advise the receiving fund of a member transferring from the provident fund which part of the member's benefit is pre-1 March 2015. It does not mean that separate record-keeping will be restricted to provident funds; pension funds should also be able to accommodate dual record-keeping to enable the splitting of the pre- and post-1 March 2015 records of members under the age of 55 transferring into the pension fund from a provident fund.

Members 55 or older on 1 March 2015:

1) ***Existing members***: FundsAtWork will not be required to have separate record-keeping for members in a provident fund that are 55 or older on 1 March 2015 as the whole benefit for these members can still be taken as a lump sum.
2) ***New members***: FundsAtWork will have to keep separate records / accounts for all new members that come from a provident fund and who are 55 or older on 1 March 2015. The amount transferred from the provident fund of which the member was a member on 1 March 2015, plus the growth, must be separated from the contributions and growth after the transfer. The member will be able to take the pre-transfer amount in a lump sum on retirement; the post-retirement benefit must be used to buy a pension, unless the *de minimus* exemption applies.

The administration system will apply the *de minimus* exemption on provident funds from 1 March 2015. It will allow a member whose post-1 March 2015 benefit is less than R150 000 to take that benefit in a lump sum.

Switch forms and the system supporting switching will be changed to distinguish between the pre- and post-1 March 2015 portion of a member's retirement savings account as members may wish to apply different investment strategies to the two portions of their savings.

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Legal update

No. 5 of 2014 • 14 February 2014

Changes to the Pension Funds Act: Payment of benefits

Summary

The Financial Services Laws General Amendment Act No.45 of 2013 was published in Government Gazette No. 37237 on 16 January 2014. It amends the Pension Funds Act and creates a number of new requirements regarding the payments of benefits. The effective date of these provisions is 28 February 2014.

1. Payment of a benefit where the member does not have a bank account

<u>Current position</u>

A fund is not allowed to pay a benefit to anybody other than a member or beneficiary. Funds are often faced with the situation where a member or beneficiary who is entitled to payment from the fund does not have a bank account and is not able to open one. Some members only have joint bank accounts with their spouses. Banks generally don't allow a member to open a bank account if they only want to do so to receive payment of their benefit and then immediately withdraw the total benefit.

<u>Position from 28 February 2014</u>

From 28 February 2014, the fund will be permitted to pay a member's or beneficiary's benefit into the bank account of a third party, if they can give sufficient proof that they are not able to open a bank account.

Payment to the third party will be regarded as a payment made directly to the member or beneficiary and the fund will have discharged its duties in relation to that member or beneficiary.

<u>Impact on Momentum FundsAtWork</u>

FundsAtWork will change its process to accommodate payment to a third party as foreseen by the amendment. Once the member or beneficiary can prove that they cannot open a bank account, they will be required to sign a document authorising payment to the third party and indemnifying Momentum against any claim resulting from such payment.

However, this amendment still does not allow a fund to pay a member's or beneficiary's benefit into a joint account. Where a member or beneficiary only has a joint account, FundsAtWork will not be able to make the payment into the joint account. FundsAtWork will allow payment to a third party if the conditions set out in the previous paragraph are met.

2. Payment of death benefits where no dependants can be traced

Current position

A fund has 12 months from the member's death within which to trace dependants of a deceased member. If the fund is unable to trace any dependants and if the member has not nominated a beneficiary, or if the member nominated a beneficiary to receive only a portion of the benefit, the benefit or remaining benefit must be paid into the estate of the deceased member. If there is no estate, the benefit must be paid into the Guardian's Fund.

Position from 28 February 2014

Section 37C is amended to also allow for payment into an unclaimed benefit fund. From 28 February 2014, a fund will be able to pay a death benefit in the circumstances above into an unclaimed benefit fund if, after 12 months from the member's death, the fund has been unsuccessful in tracing a dependant, there are no nominees and there is no estate.

Impact on FundsAtWork

FundsAtWork goes to great lengths to trace dependants in order to avoid payment of a member's death benefit to the Guardian's Fund. FundsAtWork will still do their best to trace beneficiaries in order not to pay a benefit to the Guardian's Fund or an unclaimed benefit fund. However, if there is no beneficiary, FundsAtWork will pay the benefit to an unclaimed benefit fund rather than to the Guardian's Fund, as the trustees of the unclaimed benefit fund has an obligation to trace beneficiaries on a regular basis.

3. Unclaimed benefits and unclaimed benefit fund

Current position

The definition of "unclaimed benefit" *excludes* a death benefit not paid within 24 months from the date of the member's death. It is not clear from the definition exactly when a death benefit would be included as an unclaimed benefit. It also does not provide for the amount payable to a non-member spouse following a deduction under a divorce order under section 37D to qualify as an unclaimed benefit.

The current Pension Funds Act does not define an unclaimed benefit fund.

Position from 28 February 2014

The definition of "unclaimed benefit" has been amended to *include* a death benefit payable to a beneficiary under section 37C that is not paid within 24 months from the date on which the fund became aware of the death of the member, or a longer period as long as the board can reasonably justify it in writing.

The definition has also been expanded to include any amount that remains unclaimed or unpaid to a non-member spouse within 24 months after the date on which a section 37D deduction was made.

A new definition for "unclaimed benefit fund" has been included. An unclaimed benefit fund is a preservation fund set up to receive unclaimed benefits.

Impact on FundsAtWork

If one reads this amendment together with the amendment to section 37C which is discussed under paragraph 2 above, FundsAtWork will be able to deal with death claims as follows:

- Pay to the member's dependants or nominated beneficiaries.
- Pay to the estate if there are no dependants or nominated beneficiaries.
- Pay to an unclaimed benefit fund where, 12 months after the member's death, no dependant or nominated beneficiary could be found, and there is no estate.

- If the benefit has not been paid within 24 months after the fund became aware of the member's death, pay the benefit into an unclaimed benefit fund. This will generally be the case where a dependant or nominated beneficiary that has been identified (and awarded a portion of the benefit) cannot be traced.

FundsAtWork will change its death claims payment process to take these changes into account.

It will also change its process to allow for the payment of the amount deducted in favour of a non-member spouse under a divorce order into an unclaimed benefit fund if it has not been paid 24 months after the deduction has been made.

4. Beneficiary fund can receive unapproved benefits

Current position

A beneficiary fund is defined as a fund referred to in paragraph (c) of the definition of "pension fund organisation", which in turn refers to a fund established with the object of receiving, administering, investing and paying benefits referred to in section 37C on behalf of beneficiaries, payable on the death of a member of a pension fund. In short, a beneficiary fund can only receive death benefits payable from a pension fund.

Position from 28 February 2014

Paragraph (c) of the definition of "pension fund organisation" has been changed by substituting the phrase "referred to in section 37C" with "in terms of the employment of a member". This means that any benefit payable to a beneficiary that became payable in terms of the member's employment can be paid to a beneficiary fund. An employer would therefore be able to pay a benefit payable under a free-standing, employer-owned death benefit (unapproved) policy into a beneficiary fund.

An unforeseen consequence of this change is that a beneficiary fund cannot receive a death benefit that did *not* become payable in terms of the member's employment, such as a benefit from a retirement annuity fund and a preservation fund. This is in conflict with section 37(2)(iii), which allows for payment to a beneficiary fund. The anomaly is that a preservation fund for example would be able to pay the benefit to the beneficiary fund, but the beneficiary fund will not be allowed to receive that payment. It is expected that this discrepancy will be corrected soon.

Impact on FundsAtWork

FundsAtWork is in the process of investigating the impact of this change on the wording of the lump sum death benefit insurance policies with the view to allow employers to pay unapproved benefits into a beneficiary fund. The impact of this change on the payment method of fund provided (approved) death benefits will be investigated at the same time. A communication in this regard will be sent to all employers who have unapproved policies with FundsAtWork as soon as possible.

5. Deductions allowed from a pension benefit

Current position

The Pension Funds Act allows a fund to make certain deductions from a member's benefit or minimum individual reserve. The fund is restricted to making these deductions from the member's benefit and is not permitted to make any deductions from a deferred pension or from a living annuity.

In terms of section 37D(1)(d) the fund is permitted to make the following deductions from a member's benefit or individual reserve:

- any amount awarded to a non-member spouse under a divorce order;
- any amount payable in terms of a maintenance order, and
- income tax resulting from the deduction.

For amounts awarded to a non-member spouse, the wording of section 37D(1)(d) read together with the definition of "pension interest" in the Divorce Act seems to imply that the deduction must be made only from the benefit that a member would have been entitled to receive had they resigned on the date of the divorce. This would mean that the fund cannot deduct any such amounts from a deferred pension or a living annuity.

The Pension Funds Act only allows for deductions in favour of a non-member spouse following a divorce order under the Divorce Act.

Section 37D(4)(b) of the Pension Funds Act stipulates the following periods applicable to divorce orders:

1. Within **45 days** of the submission of the court order to the fund, the fund must request the non-member spouse to elect if the amount to be deducted must be paid directly to them or if it must be transferred to a fund on their behalf.
2. Within **120 days** of being requested to make an election, the non-member spouse must inform the fund of their election. If they elect that the amount must be paid to them directly, they must provide the fund with the details of how payment must be made. If they elect that the amount must be transferred to a fund on their behalf, they must provide the fund with the details of that pension fund.
3. If the non-member spouse makes an election, the fund must within **60 days** of being informed of how the amount must be dealt with, pay or transfer the amount.
4. If the non-member spouse does not make an election, the fund must within **30 days** of the expiry of the 120 day period, pay the amount directly to the non-member spouse.
5. If the fund cannot reasonably ascertain how the payment to the non-member spouse must be effected, it must retain the amount as well as the interest on the amount in the fund until details of how the payment must be effected is provided to the fund by the member, the non-member spouse or any other person.

The non-member spouse is only entitled to fund return (interest) on their benefit from the expiry of the 120 day period referred to in paragraph 2 above until date of payment.

<u>Position from 28 February 2014</u>

Section 37D has been expanded to include a deduction in favour of a non-member spouse following a divorce order under Islamic law.

It further allows for the deductions provided for in section 37D(1)(d) to be made from either a member's or deferred pensioner's benefit or a member's interest or minimum individual reserve, or the capital value of a pensioner's pension after retirement.

This provision means that a fund may deduct from a pensioner's or deferred pensioner's benefit any amount awarded by the court to a non-member spouse, any amount in respect of maintenance or any employees' tax due as a result of the deduction.

Section 37D(4)(c) has been amended to change the period from which the non-member spouse is entitled to interest on their benefit. From 28 February 2014, interest will be calculated from the date of the deduction, which is the date on which an election is made or, if no election is made within the 120 day period referred to in paragraph 2 above, the date on which that 120 day period expires.

<u>Impact on FundsAtWork</u>

FundsAtWork will make deductions to non-member spouses if there is a valid divorce order, both under the Divorce Act and under Islamic law.

The Rules of the FundsAtWork Umbrella Pension and Provident Funds do not provide for deferred pensions or annuities. The changes with regards to the deduction from a pensioner's or deferred pensioner's benefit accordingly currently do not have any direct impact on FundsAtWork.

With regards to the calculation of fund return on the non-member spouse's portion of a divorce benefit, FundsAtWork will make the necessary system changes to give effect to the change.

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Legal update

No. 6 of 2014 • 14 February 2014

Changes to the Pension Funds Act: Trustees

Summary

The Financial Services Laws General Amendment Act No. 45 of 2013 was published in Government Gazette No.37237 on 16 January 2014. It amends certain provisions of the Pension Funds Act (the Act) relating to the composition of the board and the duties and obligations imposed on the individual board members (trustees). The effective date of these provisions is 28 February 2014.

1. Requirements for a properly constituted board

Current position

Every fund must have a board consisting of at least 4 trustees. The members of the fund have the right to elect at least 50% of the trustees. Umbrella funds, preservation funds and retirement annuity funds can apply for exemption from this last requirement. They must then have at least one independent board member, and 3 other members. The election procedures, terms of office, procedures at board meetings, voting rights of trustees, the quorum for a board meeting, deadlock breaking mechanisms and the powers of the board must all be set out in the rules of the fund.

Position from 28 February 2014

In addition to the above requirements, the Act now requires that the composition of the board must at all times comply with the requirements contained in the rules of the fund and that any vacancy on the board must be filled within such period as prescribed.

This means the rules of the fund must at all times reflect the correct number of employer appointed and member elected trustees that comprise the board.

A vacancy on the board must be filled within the period prescribed by the registrar.

If there are any changes to the board composition, for instance if the board decides to increase or decrease the number of trustees, the rules must be amended to reflect the new board composition.

If the board composition does not comply with the requirements in the rules, or if a vacancy on the board is not filled within the prescribed period, the board will not be properly constituted and any resolutions or decisions made by that board will be void.

Impact on FundsAtWork

The Rules of the FundsAtWork Umbrella and Preservation Funds (the Funds) already reflect the exact number of trustees that make up the board.

The Rules will be amended to align with the prescribed period for the filling of a vacancy on the board. If there are any changes in the board composition, the Rules will be amended accordingly.

2. New obligations on trustees

The Amendment Act imposes a number of new duties on trustees:

a. The registrar may prescribe the level of skills and training that a trustee must attain. These requirements will be published in the Government Gazette and trustees will have 6 months from the date of their appointment or election to attain the necessary skills and training. In addition to this, trustees must ensure that they retain those skills throughout their time on the board.

b. A trustee who is removed from office must submit a written report to the registrar. The report must be submitted within 21 days of the trustee's removal and must explain why the trustee thinks that their appointment was terminated. This requirement is not applicable where the trustee resigns voluntarily or where their term of office expires.

c. There will be a 'whistle-blowing' obligation on trustees. A trustee must inform the registrar, in writing, of any information relating to the affairs of the fund, which in their opinion may seriously prejudice the financial soundness of the fund or its members. This obligation arises as soon as the trustee becomes aware of any such information.

d. Trustees are required by law to act independently. They must exercise their powers in a manner that is impartial and not influenced by inappropriate considerations. A failure to act independently will result in a contravention of the Pension Funds Act.

e. In addition to the duties of due care, diligence and good faith, the Act imposes a fiduciary duty on trustees. Trustees have a legal obligation to act in the best interests of the members and beneficiaries for accrued benefits or any amount accrued to provide a benefit. This duty extends not only to active members, but to deferred pensioners, pensioners and any other person deriving a benefit from the fund.

f. The trustees also have a legal duty to the fund to ensure that the fund is financially sound, responsibly managed and governed in accordance with its rules and the Act.

g. In addition to ensuring that adequate and appropriate information is communicated to the members of the fund informing them of their rights and benefits, this duty now extends to beneficiaries of the fund as well. The trustees must ensure that beneficiaries of a fund are informed of their rights, duties and benefits.

h. The board is permitted to delegate its functions under the Act to a person or committee, subject to any conditions as the board may decide. The delegation must be in writing and must be in line with the system of delegation laid out in the rules of the fund. The rules should specify whether or not the board is required to ratify any decisions or actions taken by a delegate or subcommittee.

i. The board is not relieved of its functions once delegated and remains responsible for any decisions taken by the delegate or committee. The board may withdraw the delegation any time.

<u>Impact on FundsAtWork</u>

The trustees on the Funds are already well versed in pension fund and other related matters. Once the required level of skills and training that a trustee must attain has been published, FundsAtWork will do a gap analysis to see whether the trustees of the Funds need any additional training and arrange for the required training. FundsAtWork will also put a training program in place to ensure that the trustees maintain the required level of skills.

FundsAtWork will include communicating to beneficiaries in the Funds' Communication Strategy and Plan as well as the Communication Policy Statement and will make sure that they are informed of their rights, duties and benefits.

FundsAtWork already has a system of delegation in place in terms of which functions and duties of the board are delegated.

3. Liability of a trustee

Prior to the amendment, the Pension Funds Act did not contain any provisions specifically relating to the liability of a trustee. A new section 7F is inserted which changes the position as follows from 28 February 2014:

a. In proceedings brought against a trustee the court may relieve the trustee of any liability, either wholly or partly, if the court is of the view that the trustee acted independently, honestly and reasonably, or if after considering all the circumstances of the case, the court is of the view that it would be fair to excuse the trustee.

b. In relieving the trustee of liability the court may impose any terms or conditions that it considers to be fair in the circumstances.

c. The provisions of this section only apply in cases where the court is of the view that there was no wilful misconduct or wilful breach of trust on the part of the trustee.

4. New requirements for appointments made by the board

A. <u>Principal officers</u>

<u>Current position where a principal officer is unable to perform their duties</u>

Where a principal officer is outside the country or otherwise unable to perform their legal duties, the fund has 30 days to appoint a new principal officer. However, the Act is silent on when this period starts.

The fund may appoint only one principal officer and is not permitted to appoint a deputy principal officer.

<u>Position from 28 February 2014</u>

The 30 days that the board has to replace a principal officer is removed. The registrar will prescribe the period within which a new principal officer may be appointed. The board must appoint a new principal officer within the prescribed period after the commencement of a continuing absence or inability to discharge any duty by the principal officer.

The fund will be permitted to appoint a deputy principal officer. Further, the principal officer of the fund may delegate any of their duties to the deputy principal officer. Such delegation must be done in writing and must be done according to the rules of the fund. The principal officer is not relieved of any of their functions and may withdraw the delegation at any time. The deputy principal officer does not replace the principal officer but acts as the principal officer until the fund appoints a new one.

Impact on FundsAtWork

FundsAtWork will amend the Rules of our Umbrella and Preservation Funds (the Funds) to provide for the appointment of a deputy principal officer and to set out the system of delegation in terms of which the principal officer delegates duties to the deputy principal officer. The principal officer of the Funds will also be asked to set out the delegation of her duties in writing to comply with the new requirement.

B. Valuator

The Pension Funds Act is amended to provide that the valuator must be a natural person who is resident in South Africa. If the valuator resigns or is unable to discharge their duties, the fund must appoint a new valuator within the period prescribed by the registrar.

Impact on FundsAtWork

FundsAtWork will ensure that all documents relating to the appointment of the valuator reflects the name of the individual that is appointed as the valuator and not the partnership or company to which the valuator belongs.

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Legal update

No. 7 of 2014 • 14 February 2014

Changes to the Pension Funds Act: "Whistle-blowing" protection

Summary

The Financial Services Laws General Amendment Act No. 45 of 2013 was published in Government Gazette No. 37237 on 16 January 2014. It amends the Pension Funds Act by extending the application of the Protected Disclosures Act to disclosures made by officers of a fund. The effective date of these provisions is 28 February 2014.

Current position

The Pension Funds Act imposes a "whistle blowing" obligation on the principal officer and auditor of a fund. This means that principal officers and auditors have a legal duty to inform the registrar of any matter relating to the affairs of the fund that may seriously prejudice the financial soundness of the fund or its members.

The Act does not specify how these disclosures should be made nor does it provide expressly for the protection of the person making the disclosure.

Position from 1 February 2014

The "whistle-blowing" obligation is extended to trustees, valuators, deputy principal officers and employees of the fund or administrator. A disclosure by any one of these parties will automatically be regarded as a protected disclosure.

What is a "disclosure"?

A disclosure is any information communicated to the registrar regarding any conduct of a pension fund, an administrator, trustee, principal officer, deputy principal officer, valuator or employee of the fund or administrator, made by any of these parties, which relate to the business of the fund and which may prejudice the fund or its members.

Under the Protected Disclosures Act, any information disclosed by an employee for unlawful or irregular conduct of their employer or fellow employees is considered a protected disclosure. The person making such a disclosure is protected from any occupational detriment or victimisation that they may suffer as a result of making the disclosure.

The amendment to the Pension Funds Act extends the application of the Protected Disclosures Act to disclosures made by a trustee, principal officer, deputy principal officer, auditor, valuator and any other employee of the fund or administrator.

A disclosure by any one of these parties will be considered a protected disclosure and the party making the disclosure will be protected in terms of the Protected Disclosures Act.

The amendment also imposes an obligation on the registrar to establish a process for the submission and protection of disclosures.

Impact on FundsAtWork

FundsAtWork will ensure that the principal officer, deputy principal officer, auditor, valuator and every employee of Momentum Employee Benefits are aware of their legal duty to inform the registrar, in the manner prescribed, of any matter relating to the management or administration of the FundsAtWork Umbrella and Preservation Funds, which in their opinion may prejudice the financial stability of the Funds or their members.

Natasha Marhye
Legal Adviser
Momentum Employee Benefits – FundsAtWork

Legal update

No. 8 of 2014 • 14 February 2014

Changes to the Pension Funds Act: General amendments

Summary

The Financial Services Laws General Amendment Act No.45 of 2013 (the Amendment Act) was published in Government Gazette No. 37237 on 16 January 2014. This document deals with some of the more general amendments while other specific amendments are dealt with in Legal Updates 5 – 7 of 2014. The effective date of these provisions is 28 February 2014, except for the amendments discussed in paragraphs 4 and 9.

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1. Personal liability of employers for payment of contributions

Current position

The Pension Funds Act (the Act) requires that the employer pays the employer and the member contributions, as stipulated in the fund rules, to the fund. The contributions must be paid into the bank account of the fund or transmitted directly to the fund by no later than 7 days after the end of the month, for which the contribution is payable.

While the Act imposes legislative duties on the employer, it does not single out any particular person within the employer's organisation who is responsible for the timeous deduction and payment of contributions.

Position from 28 February 2014

The Amendment Act takes things a step further. The newly inserted section 13A(8) imposes personal liability on certain parties within the employer's organisation. These persons will be held personally responsible for ensuring that contributions are deducted and paid to the fund within the prescribed period.

These parties are:

- If the employer is a company, every director who is regularly involved in the management of the company's overall financial affairs.
- If the employer is a close corporation, every member who controls or is regularly involved in the close corporation's overall financial affairs.
- In respect of any other employers, every person according to whose directions or instructions the governing body or structure of the employer acts, or who controls or is regularly involved in the management of the employer's overall financial affairs.

The fund must ask the employer for the names of the persons referred to above. If the employer fails to give this information to the fund, all the directors, members of the close corporation or the governing body of the employer will be held personally liable.

This means that any person falling into any one of the above categories is legally responsible and accountable for ensuring that the contributions of both the members and the employer are paid to the fund within the 7 day period. Since this is a legal duty, non-compliance with section 13A of the Pension Funds Act may have serious repercussions for the person charged with ensuring compliance.

Impact on FundsAtWork

The FundsAtWork Umbrella Pension and Provident Funds (the Funds) will soon embark on a campaign to obtain the names of the persons that can be held personally liable. All new installation documents from 1 March 2014 will require this information.

2. Administrator

Current position

Every person involved in administering investments or benefits on behalf of a pension fund has to obtain approval from the registrar.

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Position from 28 February 2014

The amendment introduces several new requirements for the approval of an administrator by the registrar.

One significant change is that persons administering only investments on behalf of a pension fund, no longer require approval from the registrar. They will be regulated under the Financial Advisory and Intermediary Services Act and not the Pension Funds Act. Persons involved in the receipt of contributions or the disposition of benefits on behalf of a pension fund still need approval by the registrar.

The amendment provides for the information that must accompany an application for a section 13B licence. The information, to be prescribed by the registrar should satisfy them that the applicant is a fit and proper administrator. It includes information giving evidence of the honesty and integrity of the applicant, their competence and operational ability to fulfil the duties imposed by the Act and their financial soundness. The registrar may request additional information and may take into consideration information regarding the applicant from any source including any other regulator or supervisory authority.

New requirements for administrators

a. The administrator will be required to maintain such financial resources as prescribed by the registrar to meet its commitment and manage its risk. Previously there were no prescribed financial resources and the administrator was only required to maintain adequate financial resources.

b. If after conducting an inspection, the registrar directs that the administrator withdraw from the administration of the fund and requires the board to arrange for the administration of the fund to be taken over by another administrator, the current administrator could be liable for the costs of appointing the new administrator.

c. There are specific requirements for an administrator when dealing with records, documentation and information relating to the fund and its members. All records and information belong to the fund. This includes information that the administrator has created, possesses or controls. The administrator must maintain the information in an orderly format and may not destroy or dispose of any information without the consent of the fund.

d. The administrator will have “whistle-blowing” duties. The administrator must inform the registrar of any material matter relating to the affairs of the fund which, in their opinion, may prejudice the fund or its members.

3. Valuations

The definition of “valuation exempt” has been changed to refer to a fund which has been exempted from sections 9A (the appointment of a valuator) and 16 (submitting a statutory actuarial valuation report), as opposed to just referring to exemption from the requirement to submit a valuation report. Section 17, which dealt with modifications where investigations by a valuator are unnecessary, has been deleted. These provisions have, where required, been incorporated in section 16.

4. Fund registration – effective from 30 May 2014

Section 4 has been amended to require a fund to apply for registration and be provisionally or finally registered before it can commence any pension fund business. It also provides that the registrar may ask the fund for further information about its application or to verify information provided in the application. If the fund fails to give or verify the information as requested within 60 days from the date of the request, the application will lapse.

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Section 31 has been changed to provide that the period for carrying on business as a pension fund subsequent to application is no longer 12 months, but instead a period prescribed by the registrar.

5. Rules

Currently, the definition of “rules” includes various documents pertaining to the fund. The amended definition refers only to the rules of a fund registered in term of the Act.

The requirement that amendments be submitted to the registrar within 60 days of the passing of the resolution adopting the amendment remains in place.

A fund may consolidate its rules. Consolidated rules are a collation of the existing rules and amendments. The current Section 12(5) provides that if the registrar is satisfied that the consolidated rules are not substantially different from the existing rules of the fund, the registrar will register the consolidated rules. The word “substantially” has been removed in the amendment. The effect of this is that consolidated rules will now only be registered if they are exactly the same as the existing rules. No changes will be allowed.

The registrar in considering whether to register an amendment may request any additional information. The fund has 180 days to respond to the registrar’s queries failing which the application to have the amendment registered will lapse.

FundsAtWork already complies with these requirements.

6. Section 14 transfers

The requirement that the scheme for a transfer must be submitted to the registrar within 180 days of the effective date has been removed. The registrar will prescribe the period within which a scheme may be submitted.

The new section 14(2)(c) specifically provides that transferred assets must be increased or decreased with fund return from the effective date of the transfer until date of payment.

Another new provision is found in section 14(6)(c). The registrar can withdraw or amend a section 14 certificate if, as a result of legislative changes, members would be prejudiced by the implementation of the transfer. An example of such prejudice would be a change in tax laws, resulting in a transfer from a pension fund to a provident being taxable.

Section 14(7)(b) is amended to clarify that no fees or commission of any nature, whether directly or indirectly, payable by any party or any agent, mandatory or representative of such party, are allowed for a transfer between retirement annuity funds.

Section 14(9) is also new. This allows the registrar to exempt any transaction from the requirements of section 14 subject to the requirements and conditions prescribed by the registrar.

7. Surplus

The definition of “actuarial surplus” has been changed to enable the registrar to prescribe the basis on which a valuator must calculate the value that they place on the fund’s assets.

The definitions of “employer surplus account” and “member surplus account” have been amended to clarify that these accounts must be provided for in fund rules.

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Various amendments have been made to sections 15A, 15B, 15C, 15D, 15E, 15F and 15K relating to surplus. These amendments are:

- Section 15A(2) and 15C(2): existing and future surplus can be distributed directly to members and former members.
- Section 15B(10) deleted: this section obliged the registrar to refer a surplus apportionment scheme to a special *ad hoc* tribunal where –
    - the trustees did not submit a surplus apportionment scheme,
    - the registrar is not satisfied that the scheme is reasonable and equitable,
    - the registrar considers that unresolved complaints require investigation which may lead to a review of the scheme,
    - the statutory actuarial valuation as at the surplus apportionment date of the fund for the purpose of determining the actuarial surplus in the fund is unacceptable to the registrar, or
    - the board or the former member representative requested it.

  Instead, section 15K now deals with the circumstances under which the registrar *may* appoint a specialist ad hoc tribunal. These include the registrar not agreeing with the result of the surplus apportionment investigation or where a nil return is submitted, the registrar not being satisfied that a nil return is justified.
- Section 15B(13): the registrar can withdraw the surplus apportionment certificate on application by the fund trustees, subject to the conditions prescribed by the registrar.
- Section 15D(1)(a) and (b): the balance in the member surplus account can now be used to improve benefits for all members (as opposed to only existing members), and where reasonable and equitable, to improve benefits paid to or amounts transferred for former members who exited the fund after the surplus apportionment date.
- Sections 15E(1)(a) and (i): a participating employer can require (as opposed to request) that the trustees use the surplus in the employer surplus account for the purposes allowed. An additional purpose has been added: repaying part or all of the surplus utilised improperly by the employer.
- Section 15E(2): all or a portion of the employer surplus account can be transferred to the employer surplus account in another fund. Currently only a portion can be transferred.
- Section 15F(2)(b): a transfer of the credit balance in an existing reserve account to the employer surplus account is allowed if the allocation was negotiated between the stakeholders. In addition, the registrar must now also be satisfied that the allocation of actuarial surplus to the existing reserve account was reasonable and equitable.
- Section 15K: various changes with regards to the specialist tribunal have been made, one of which relates to the specialist tribunal's right to decide in favour of the fund submitting a surplus apportionment scheme where they estimate that the costs of the tribunal performing the surplus apportionment exercise will exceed the actuarial surplus.

8. Pension increase policy

The amendment to section 14A requires that a pension increase must be granted to pensioners and deferred every 3 years, with effect from the valuation date on which the increase is based. This increase must not be less than the minimum pension increase, starting with the first actuarial valuation following the commencement date.

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FundsAtWork currently does not pay pensions. Members of the FundsAtWork Umbrella and Preservation Funds are required to use their retirement benefits to buy a pension in their name from an insurer. The pension increase policy is therefore currently not applicable to FundsAtWork.

9. Financial soundness – effective from 29 August 2014

Section 18 has been amended to provide for the registrar's power to prescribe criteria for the financial soundness of a fund. Where the fund is not in a sound financial position, the registrar may direct the fund to submit a scheme setting out the arrangements which the fund has made or intends making to bring the fund into a financially sound condition, within the period and subject to the conditions determined by the registrar.

10. Registrar's powers

The definition of "registrar" has been amended by deleting the references to "Registrar or the Deputy Registrar" and merely referring to the "person" mentioned in section 3. Section 3 in turn specifies that the person appointed as the executive officer is the Registrar of Pension Funds, while the person appointed as the deputy executive officer is the Deputy Registrar of Pension Funds. It goes further to state that the Deputy Registrar will exercise the powers delegated to him which he is authorised to perform under the Financial Services Board Act.

Section 3B, which deals with the establishment and functioning of the Pension Funds Advisory Committee, is deleted. This enhances the independence and impartiality of the registrar.
There are various amendments which refer to the registrar having to prescribe requirements or conditions. Before the Amendment Act, this would have entailed publication in a Government Gazette, which is an expensive and lengthy process. The newly inserted definitions for "official web site", "prescribe" and "publish" will allow the registrar to publish these prescriptions on the Financial Services Board's (FSB) website, unless it is specifically required that they must be Gazetted.

The definition of "this Act" has also been expanded to include any matter prescribed by the registrar by notice in a Government Gazette, in addition to any regulation.

Section 14 allows the registrar to now also address enquiries relating to fund matters to an approved administrator or third party, in addition to the fund.

Section 25 has been amended to allow the registrar to direct the person concerned to take certain actions following an onsite-visit or inspection.

Section 26 allows the registrar to declare that a specific practice or method of conducting business is unacceptable, irregular or undesirable and that the fund, administrator or person must refrain from that practice.

The registrar is also allowed to intervene in the management of a fund where the fund cannot constitute a board properly or the trustees are unable to attain or maintain the required levels of skills and training. Where the registrar believes that a trustee is not fit and proper to act as such, the registrar is allowed to replace that trustee.

A new section 29A has been inserted. This section deals with the winding-up of an unregistered fund and allows the registrar to apply for the sequestration or liquidation of the person concerned and the unregistered fund.

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11. Changes relating to voluntary liquidation

Section 28 of the Act has been amended to provide that a liquidator in discharging the liabilities of the fund must give full recognition to minimum benefits referred to in section 14A.

The amendment also allows the liquidator to transfer benefits to an unclaimed benefit fund if he is satisfied that the benefits will remain unclaimed.

12. Complainant

The definition of “complainant” has been amended to include a spouse or former spouse of a member or former member of a fund. This addition clarifies that spouses or former spouses have the right to lodge complaints with the adjudicator.

13. Companies Act

A definition for “Companies Act” has been inserted, referring to the new Companies Act of 2008. Various changes have been made in the Act, taking the impact of the Companies Act into account. For instance, the Amendment Act includes a new section 18A, dealing with the business rescue of a fund, and a new section 19(5D), which states that a fund may not acquire or hold shares or any other financial interest in another entity which results in the fund exercising control over that entity without the registrar’s prior approval.

14. Contingency reserve account

The definition for “contingency reserve account” has been amended to clarify that this account must be provided for in the fund rules, and must provide for a specific category of contingency. The implication of this is that there has to be an account for each category of contingency.

15. Defined contribution category of a fund

This definition provides that a member’s interest in the fund must be at least equal to a minimum benefit throughout his membership of the fund, and not only at his retirement.

This amendment will also allow a fund to deduct reasonable expenses even where there are no contributions payable, for instance in a paid-up fund or a preservation fund. The amendment to section 14B confirms that reasonable expenses can be deducted in calculating the individual account of a member in a defined contribution category of a fund.

16. Fund return – deemed to have come into operation on 7 December 2001

The definition of “fund return” will allow trustees to use a reasonable approximation, made in the prescribed manner, to allocate a fund return if an exact allocation cannot be made. This will assist funds that do not smooth fund returns and who are faced with mismatches due to timing differences between actual transactions taking place and these transactions being deemed to have taken place for purposes of calculating benefits or costs or accruing investment returns.

This amendment is deemed to have come into operation on 7 December 2001.

FundsAtWork is already complying with this amendment.

17. Member

The definition of “member” has been expanded to include a member and former member of a beneficiary fund.

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18. Preservation funds

Definitions for “pension preservation fund” and “provident preservation fund” have been added. These definitions cross-reference to the definitions in the Income Tax Act.

Impact for FundsAtWork

These changes will apply regardless of whether or not our Rules are amended to include each provision specifically.

19. Pension Funds Adjudicator

The Act has been amended to make the board of the FSB the accounting authority of the Pension Fund Adjudicator’s office. It also stipulates that that board must comply with the Public Finance Management Act.

Whereas the penalty for anyone who:

- insults the Adjudicator;
- tries to bribe the Adjudicator;
- interrupts proceedings conducted by the Adjudicator or misbehave themselves, or
- does anything that is similar to contempt of court

is currently limited to imprisonment of up to 3 months, section 30V has been amended to increase this to a fine of up R1 million or imprisonment of up to one year, or both.

20. Communication

A new section 32A has been inserted. This deals with the registrar’s powers in respect of for communication and provides that the registrar may prescribe what must be communicated to the stakeholders of a fund and when. It further states that any fund-related advertisement, brochure or similar communication may not be misleading, confusing or contain any incorrect factual statement.

21. Penalties

A new section 37(1) has been included in the Amendment Act. This subsection criminalises the inducement or attempted inducement of any person to become a member of or to contribute to an unregistered fund. The penalty for this and the other offences listed in section 37(1) is a fine of up R1 million or imprisonment of up to one year, or both.

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Legal update

No. 9 of 2014 • 27 February 2014

Changes to the Pension Funds Act: Effective date

The Financial Services Laws General Amendment Act No.45 of 2013 was published in Government Gazette No. 37237 on 16 January 2014. The amendments to the Pension Funds Act that have an impact on FundsAtWork have been discussed in Legal Updates numbers 5 to 8, issued on 14 February 2014.

The effective date for most of these amendments is **28 February 2014.**

There are only two exceptions. The first is the amendment to section 4, which requires a fund to apply for registration and be provisionally or finally registered before it can commence any pension fund business. This amendment is effective from **30 May 2014**. The second is the amendment to section 18, which provides for the registrar's power to prescribe criteria for the financial soundness of a fund. This amendment is effective from **29 August 2014**.

The Legal Updates have been updated to reflect the effective dates and are accessible via the links below.

Legal Update No. 5 of 2014 – Changes to the Pension Funds Act: Payment of benefits
Legal Update No. 6 of 2014 – Changes to the Pension Funds Act: Trustees
Legal Update No. 7 of 2014 – Changes to the Pension Funds Act: "Whistle-blowing" protection
Legal Update No. 8 of 2014 – Changes to the Pension Funds Act: General amendments

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Legal update

No. 10 of 2014 • 17 April 2014

Legal Update – Budget Update on Retirement Reforms

Introduction

Following the 2014 Budget Speech, National Treasury released a document titled "2014 Budget update on retirement reforms" on 14 March 2014. This paper is a continuation of the 2013 paper and discusses the retirement reform process first announced by the Minister of Finance in 2012. The paper recaps the overall policy objectives of retirement reform and divides these into short term and long term reforms. It also provides an update on the progress made to date in terms of implementing the proposed reforms.

The Broad Policy Goals of the intended reform

1. Implementing a mandatory system of retirement (auto-enrolment)

   Problem: It is not compulsory for employers to provide their employees with any type of retirement plan. Given the high costs and complexity associated with providing an employer-sponsored scheme, many employers opt not to facilitate retirement funding for their employees. This results in a large number of employees having no access to any retirement planning.

   Reform measures: Implementing a mandatory system of retirement savings will make it compulsory for all employers to provide a retirement fund for their employees. This will go a long way in improving the coverage of retirement funds.

2. Improving Preservation

   Problem: A person resigning from their employer, or withdrawing from their pension or provident fund for any other reason, may opt to take their retirement savings as a lump sum instead of preserving it. Due to financial hardships, many people would rather have their retirement savings paid to them as a lump sum. The problem is that while the lump sum payment may provide some short term relief, in the long term it results in inadequate retirement savings and a potential burden on the state. Having a large number of active members consistently withdraw from the retirement system has a knock on effect on the costs in the retirement system because the costs now have to be shared by the remaining members. The more people participating in the system, the lower the costs will be.

   Reform measures: Implementing compulsory pre-retirement preservation. Upon withdrawing from a fund, a member will no longer have the option of taking his retirement savings as a lump sum. Instead, he will be required to transfer it into another fund.

3. Improving fund disclosure

Problem: There is currently no prescribed format or procedure that funds must follow when disclosing fees or charges to their members. Statements are complex, at times not all charges are disclosed and members are not always aware of what they are paying for. This also makes it very difficult to compare retirement products.

Reform measures: National Treasury has conducted intensive research on charges and charge disclosure in the retirement system. Their findings reveal that the required level of charge disclosure to members in both commercial and non-commercial retirement funds is low. With the proposed reforms, National Treasury intends to improve the way in which charges are communicated to members, by mandating specific disclosure requirements for funds.

4. Getting defaults right

Problem: Members are usually given the opportunity to select the portfolio in which their retirement savings will be invested. There are a number of factors influencing this decision, such as the member's age, years to retirement and risk appetite and the current economic landscape. When members exercise their choice, it is taken that they have done so after taking into account all relevant factors. But what happens when members fail to choose an investment portfolio? Their retirement savings are automatically invested in what is called a default portfolio. There are currently no regulations in South Africa that require funds to create a default portfolio or that lay out the requirements that defaults should comply with. This results in the default portfolio not always being the correct portfolio to meet a particular member's needs and optimise their retirement investment.

Reform measures: Choosing the correct default options is important. These default options must form part of the fund's investment strategy. There are intended reforms that aim to prescribe specific requirements with which defaults should comply to guide trustees when choosing a default option.

5. Fund Consolidation

Problem: There are currently over 3 000 active retirement funds in South Africa. Most of these funds are small and lack the economies of scale and strong governance required to operate effectively. The high degree of diversity makes it both difficult and costly to transfer retirement savings between schemes and increases the need for clients to seek professional financial advice.

Reform measures: National Treasury will implement reforms aimed at consolidating and increasing the degree of standardisation in the structure, investment and benefit offerings between funds. Consolidation and standardisation will ensure that funds are able to achieve greater economies of scale and make it easier to transfer from one scheme to another.

6. Simplifying retirement savings products and making them portable between providers

Problem: The high costs associated with retirement planning are driven by the complexity of the retirement products on the market. Providers seem to compete on the basis of complex product designs instead of creating simple, value for money products. Currently members are not able to transfer to a new service provider with their existing products and packages. This makes it difficult for them to shop around and negotiate the same products at a more reasonable cost.

Reform measures: National Treasury will implement reforms aimed at simplifying retirement products and increasing the portability of products between different providers. Simpler, more portable products will mean increased competition between providers and will incentivise market innovations that lower costs.

7. Ensuring effective intermediation

Problem: Products are designed taking into account the remuneration paid to intermediaries selling insurance products like retirement annuities. This contributes to the complexity and high costs of retirement products. Insurers usually pay the intermediary's commission upfront but spread the costs of the commission over the lifespan of the policy. When policyholders surrender the policy prematurely, they are charged a penalty in order for the insurer to recoup the costs of the commission. High upfront commission may also create conflicts of interests between the financial adviser and member.

Reform measures: National Treasury intends to replace sales commission on insurance policies with transparent fees negotiated between intermediaries and their clients. There are indications that rebates in investment platforms will be phased out, simplifying the layered charging structures on investment platforms.

8. Providing tougher market conduct regulation and more effective supervision

Problem: The 2008 Global Financial Crisis has heightened the need for more effective financial regulation. As with recent global reforms to the banking and insurance sectors, the regulatory system governing the retirement industry will also need to undergo reform making it tougher and more intrusive.

Reform measures: The Registrar of Pension Funds is preparing various draft regulatory instruments intended to implement changes to the Pension Funds Act, aimed at improving fund governance and promoting the consolidation of funds.

Progress on the implementation of retirement fund proposals in 2013

Five technical discussion papers were released during 2012 and 2013. Some of the proposals suggested in these papers were implemented during 2013 after consultation with industry stakeholders.

1. Amendments to the Pension Funds Act

There were a number of amendments made to the Pension Funds Act. The relevant amendments were discussed in Legal Updates 5 – 8 of 2014. These amendments stemmed from proposals made in the paper titled '*Preservation, portability and governance of retirement funds*' released in September 2012. The amendments are aimed at strengthening the governance of retirement funds by empowering the Registrar to impose fit and proper requirements on pension fund trustees, requiring that all trustees undergo prescribed training, clarifying that a trustee owes a fiduciary duty to both the members of the fund and the fund and imposing a 'whistleblowing' obligation on trustees. Employers will be held personally liable for the non-payment of contributions.

2. Tax Reforms

There have been a number of changes to the tax treatment of retirement benefits, particularly from a provident fund. These changes are aimed at encouraging preservation and annuitisation. These changes have been discussed in Legal Updates 3 and 4 of 2014.

From 1 March 2014, the tax free lump sum amount paid on retirement has increased from R315 000 to R500 000, whilst the tax free pre-retirement benefit has increased from R22 500 to R25 000.

The 2013 Charges Paper

National Treasury conducted an investigation into the charges associated with retirement planning and published their findings in a paper titled '*Charges in South African Retirement Funds'.* The paper proposed measures for lowering costs that are in keeping with the broad policy objectives of reform. A mandatory retirement system and automatic preservation are seen as key factors that will reduce costs in the retirement system, while improved disclosure and effective intermediation will raise awareness around issues relating to charges.

After considering the submissions from the industry, the National Treasury has concluded that the high costs in the retirement system are driven by a combination of fundamental economic factors (the high unemployment rate and low participation rate), the current structure of the retirement system (lack of preservation and the large number of small funds) and poor market conduct practices (lack of transparency around charges, potential conflicts of interest).

Reform timeline

National Treasury announced the following draft time line for the implementation of the outstanding reform proposals. They will consult after the publication of each policy measure.

What?	**By whom?**	**When?**
Report on the Retail Distribution Review: draft proposals regarding intermediary remuneration and rebates on investment platforms.	Financial Services Board (FSB)	**May 2014**
Draft regulations on fund default investment portfolios, annuity products & preservation products for consultation.	National Treasury (NT)	**May 2014**
Policy report on extending retirement system coverage with an emphasis on vulnerable workers.	NT	**Late 2014**
Draft regulatory instruments on trustee training, 'fit and proper' requirements, improved fund governance – particularly for multi-employer funds, unclaimed benefits funds and beneficiary funds - and consolidation and harmonisation of funds. Draft regulatory instruments to improve legacy products.	FSB	**Late 2014**
Draft regulations on charge quantification and disclosures for retirement funds.	NT	**Early 2015**
Draft amendments to Income Tax Act and Pension Funds Act to implement pre-retirement preservation proposals.	NT	**Early 2015**
Draft regulatory instruments to improve coverage of the retirement system, with an emphasis on vulnerable workers.	NT	**Early 2015**
Draft regulatory instruments to improve product simplicity and portability. Draft regulatory instruments to rationalise public pensions.	NT & FSB	**Late 2015**

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Legal update

No. 11 of 2014 • May 2014

Non-retirement savings: tax free savings accounts

A. Introduction

The concept of tax free savings accounts was first proposed by National Treasury in the 2012 Budget Review as part of the non-retirement savings reform. Treasury has indicated that it will go ahead with plans to implement tax exempt savings accounts in 2014 and in a paper published in March 2014, provided an overview of their proposal.

Non-retirement savings reforms together with the reform on the retirement system, already underway, represent National Treasury's efforts to encourage household savings with the broader benefits of reducing excessive debt and reliance on the state.

B. The current position

The current mechanism to incentivise non-retirement household savings is an annual interest tax exemption of R23 800 for individuals below 65 and R34 500 for individuals over 65.

C. The proposed reform

Following comments received on the discussion document 'Incentivising non-retirement savings", National Treasury has revised their original proposal on tax free savings accounts.

1. Key features:

- Individuals will be allowed to open two tax exempt savings accounts per year.
- Each account may have interest or equity products, or both.
- Total contributions to each account is limited to R30 000 per tax year.
- Any amounts withdrawn from the account cannot be replaced.
- Taxpayers will be responsible for ensuring that their contributions do not exceed the annual limit.
- The total lifetime contribution limit will be R500 000. The accumulated savings (contributions plus interest) can exceed R500 000.

2. Who may offer products through tax free savings accounts?

- Institutions with a banking licence.
- Institutions with a collective investment scheme licence.
- Government.
- Stockbrokers registered with the Financial Services Board (FSB) and the Johannesburg Stock Exchange.

National Treasury will develop a framework that makes it attractive for firms to participate in this initiative.

3. <u>What types of products may be offered?</u>

- Products that are:
  - *simple* and easy to understand,
  - *transparent* with regard to the disclosure of costs, and
  - *suitable* for the "average" person's portfolio.

- Products that permit flexible contributions and do not bind individuals into any future contribution schedules.

- Eligible products that are included:
  - collective investment schemes (CIS,
  - bank savings accounts,
  - fixed deposits,
  - REITs[1],
  - retail savings bonds,
  - insurance investment products that meet the above requirements,
  - exchange traded funds (ETFs) that are registered as CIS, and
  - investing in ETF's or similar pooled investments through a stockbroker.

- Products that are excluded:
  - Products that require –
    - fixed monthly deposits or premiums;
    - penalties for the non-payment of premiums, or
    - early termination charges that decrease the pay-out of the investment below the market value of the underlying assets at the time of withdrawal,
  - direct share purchases, and
  - insurance products that include death, disability and other risk benefits.

D. Regulating tax free savings account

The FSB will be responsible for monitoring product providers to ensure compliance with the principles and requirements set out in the draft regulations. In extreme cases of market misconduct, the product may be excluded for the purposes of tax free savings accounts.

E. Transfer of funds

To promote competition amongst service providers, National Treasury has proposed that the full balance in a tax free savings account be transferable between service providers without affecting the annual or lifetime limits. With regard to collective investments, the fair market value of the underlying assets will be transferable. In the case of fixed deposits and insurance policies, service providers must transfer the market value of the claim and may charge a reasonable exit penalty.

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[1] "REIT" is defined as follows in the Income Tax Act:

"REIT" means a company—

(a) that is a resident; and

(b) the shares of which are listed—

(i) on an exchange (as defined in section 1 of the Securities Services Act, 2004 (Act No. 36 of 2004), and licensed under section 10 of that Act); and

(ii) as shares in a REIT as defined in the JSE Limited Listings Requirements.

F. Administration of tax free savings accounts

1. Dividends tax

All earnings within the account will be free from tax. No dividends tax will be payable on dividends in the account.

Service providers will have to indicate either to the company or to the withholding agent that the shares in respect of which the dividend has accrued is linked to a tax free savings account and is therefore exempt from tax.

2. Reporting requirements

Service providers offering tax free accounts and individuals investing in these accounts will be required to provide information to SARS in their annual returns. SARS will consolidate the information to ensure that the annual limits have not been exceeded.

The South African Revenue Service (SARS) will also submit a report to National Treasury to enable them to monitor the progress of the non-retirement savings initiative.

Draft amendments to the Income Tax Act, introducing tax free savings accounts, will be published in the 2014 Taxation Laws Amendment Bill.

3. Contributions that exceed the annual limit

While individuals will be responsible for ensuring that their contributions do not exceed the overall annual limit, service providers will also be charged with the duty of checking that annual limits have not been breached.

National Treasury has proposed two possible ways of dealing with “over-contributions”.

Option 1: The contributions in excess of the annual limit together with any growth on that amount will be withdrawn from the account and taxed correctly. This option may create an administrative burden on the service provider who has to reverse the transaction, and on SARS, as they may have to contact service providers to ensure that reversals are done correctly. There is no penalty that could be applied to this type situation that would discourage over-contributions. As an alternative, National Treasury has proposed a penalty charge on contributions exceeding the annual limit.

Option 2: The simpler option would be to apply general tax rules to the amount that is in excess of the annual limit. No withdrawals or reversal will take place. A proportion of the interest, dividends, other receipts and accruals and unrealised capital gains will be taxed at the marginal tax rate for that individual. Applying the general tax rule will mean that the tax paid on the over-contributions would be higher than if the over-contributions were generated outside a tax free savings account.

National Treasury has requested comments on these options.

G. Other reforms to encourage savings

The introduction of tax free savings accounts is the first in a series of proposals from National Treasury that aim to reform the non-retirement retail savings landscape. The RSA retail savings bond is another reform measure intended to simplify and encourage saving. National Treasury intends to explore the possibility of an Islamic retail bond to expand the product offering.

National Treasury is working with the FSB to explore further issues affecting non-retirement savings.

National Treasury has requested that the Ministers of Trade and Industry, Justice and Finance work together to develop a programme to deal with the reckless and exploitative lending practices in the retail lending market.

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Legal update

No.12 of 2014 • June 2014

Legal Update: Tax Administration Laws Amendment Act 39 of 2013

The Tax Administration Laws Amendment Act ("the Act") was promulgated on 16 January 2014. The Act amends the Transfer Duty Act, Income Tax Act, Customs and Excise Act, Value-added Tax Act, Skills Development Levies Act, Unemployment Insurance Contributions Act, Securities Transfer Tax Act, Mineral and Petroleum Resources Royalty Act, Mineral and Petroleum Resources Royalty (Administration) Act and Tax Administration Act.

This Legal Update highlights some of the amendments to the various tax Acts.

Unless otherwise indicated, the changes to the Tax Administration Act No.28 of 2011 are deemed to have come into operation on 1 October 2012. Other amendments effected by this Act came into operation on the date of promulgation, which was 16 January 2014.

1. Transfer Duty Act

The Commissioner has the power to determine the liability of any party entering into a transaction that results in an undue tax benefit (section 20B(1)). The Act has now been amended to provide that any decision by the Commissioner is subject to the dispute resolution procedures set out in Chapter 9 of the Tax Administration Act.

2. Income Tax Act

The following amendments have been made:

- The Commissioner has discretion to extend the period to qualify for the exemption in respect of debt waivers in anticipation of liquidation or deregistration, as he had before.

- The definition of ''return'' has been amended to ensure consistency between the Income Tax Act and the other Tax Acts, so as to only use the defined term of ''return'' where mention is made of any document that forms the basis of an assessment to be submitted to SARS.

- The date of submission of returns for purposes of dividends tax has been clarified. The amendment also provides for returns to be submitted by persons that receive exempt dividends as specified.

- SITE has been made obsolete by the increased tax threshold. The tax threshold for 2014 (with regard to persons under 65 years) is R67 111 and the SITE threshold is R60 000. Taxpayers below R60 000 are not liable for SITE and PAYE. The amendment deletes the age verification requirement.

- As a result of the pre-population of IRP5 certificates in individuals' tax returns, the withholding of tax certificates to directors is no longer required. This provision was deleted.

- The employer now has the option to deliver a tax certificate to an employee in various ways, including electronically.

- The amendment clarifies that all lump sums are excluded from PAYE withholding.

3. Customs and Excise Act

The following amendments have been made:

- The amendment curbs the power of officers to search premises by specifying that an officer may only enter premises on the authority of a warrant except in the following circumstances:

  - Premises licensed or registered in terms of the Customs and Excise Act, business premises of licensed or registered persons, premises that are part of a port, airport, railway station or land border post, and premises entered with the consent of the owner or person in physical control of the premises;

  - Warrantless entry to premises is allowed in circumstances where an officer believes that a warrant would have been issued if applied for, but that the delay in obtaining one is likely to defeat the purpose for which entry is sought.

- Requirements are provided for the conduct of officers when they enter and search premises.

- The amendment also sets out the requirements for obtaining a warrant.

- Clarifies SARS officers' powers relating to criminal investigations.

- Provides for Customs Controlled Areas in industrial development zones. Operators and enterprises could import goods under rebate of duty and exempt from value-added tax. The operator must comply with legislation regulating Special Economic Zones.

4. Mineral and Petroleum Resource Royalty (Administration) Act 2008

- As the payment of royalties in terms of the Royalties Act is a deductible expense for normal income tax purposes, the finalisation of the income tax return is dependent upon the annual royalty return. The amendment aligns the dates of submission of the two returns, i.e. 12 months after financial year end.

5. Tax Administration Act 2011 ("the TAA")

The following amendments have been made:

- The insertion of the definition of ''outstanding tax debt'' and amendment to the definition of ''tax debt'' clarify what is regarded as a ''tax debt'' and what is an ''outstanding tax debt'' recoverable under the TAA.

  - A ''tax debt'' is an amount of tax due or payable in terms of a Tax Act as set out in section 169(1) of the TAA, e.g. a tax debt may be payable but not due in a situation where a tax debt is disputed, but remains payable pursuant to the pay-now-argue-later rule.

  - A disputed tax debt will only be ''due'' if a tax court or higher court finally determines the dispute in favour of SARS.

- Clarifies that there must be a connection between material requested by SARS and the administration of the Tax Act for purposes of which the material is required.

- Clarifies that a return by the taxpayer only constitutes one basis on which an assessment by SARS is based, and not the only basis.

- Under the common law, a *delegation* is a unilateral act that does not require the written acceptance of the person so delegated. The delegation becomes effective when signed by the delegating person. The amendment aligns section 10 with the common law approach.

- Seeks to avoid unnecessary and costly litigation by stipulating that no legal proceedings may be instituted in the High Court against the Commissioner unless the applicant has given the Commissioner written notice of at least one week of the applicant's intention to institute legal proceedings. The notice of legal proceedings must be served at the address specified by the Commissioner by public notice. This provision allows for the possibility of matters or complaints being settled without costly and protracted legal action.

- Affords the Commissioner the power to require returns other than those specifically referred to in a Tax Act.

- Allows SARS to disclose such information to the taxpayer in the performance of its duties without having to obtain the prior consent of the relevant third parties.

- Relates to information on which the taxpayer's assessment is based. This information forms part of the reasons that SARS should provide to justify the assessment and must be given to the taxpayer as a matter of course. The taxpayer should not have to pay for copies of this information.

- Allows for the withdrawal of assessments in certain circumstances.

- Provides that a senior SARS official may agree with the taxpayer to the amount of tax properly chargeable for the relevant tax period and subsequently issue a revised original, additional or reduced assessment pursuant to such agreement, which assessment would then not be subject to objection and appeal.

- Extends the grounds on which an assessment should be made as an exception to include assessments made pursuant to a withdrawal.

- Enables the Commissioner to prescribe the form of documents required under the dispute resolution rules.

- Affords the tax court jurisdiction to hear and decide procedural matters instituted under the dispute resolution rules. It also clarifies the difference between interlocutory applications and applications in a procedural matter.

  A tax court comprises a judge or acting judge of the High Court, an accountant selected from a panel of members and a representative of the commercial community selected from a panel. The Act previously required that where a matter relates to the business of mining, the representative of the commercial community will be a registered mining engineer. This requirement has been amended to allow for an engineer with experience in mining to represent the mining community.

- Enables the president of the tax court to sit alone to deal with interlocutory and procedural matters instituted under the dispute resolution rules.

- Protects a third party compelled to pay amounts owed to or held on behalf of a tax debtor to SARS, from recovery actions by the tax debtor.

- Clarifies that ''tax debt'' is an ''outstanding tax debt'' in respect of which SARS may initiate recovery proceedings.

- Clarifies the main purpose of a preservation order, namely to deal with both the situation where a taxpayer subject to, for example, an audit, takes steps to transfer assets to avoid payment of the tax properly chargeable, and where the taxpayer takes such steps once there is a quantified tax liability. If the audit is not completed and the tax debt not yet quantified, a senior SARS official on reasonable grounds must be satisfied that tax may be due or payable.

- Provides that the disputed amount under an assessment may be partially suspended, rather than an all or nothing approach.

- Clarifies that recovery proceedings may only be instituted in respect of an ''outstanding tax debt''.

- Clarifies that a separate application by SARS is not required before it may institute recovery proceedings under this section in respect of a disputed tax debt for which no suspension was requested or exists.

- Clarifies that a refund may only be set off against a tax debt if no suspension request of the debt is pending or if no suspension exists.

- Provisions with regards to understatements

  - Clarifies that the tax period is relevant to calculating the shortfall under sections 222(3) and (4) and not whether there is prejudice to SARS or the fiscus as referred to in the definition of ''understatement''.

  - Clarifies when an ''understatement'' does not result in a penalty by excluding bona fide inadvertent errors.

  - The purpose of the amendment is to avoid an unnecessarily onerous penalty. If more than one understatement is made in a return, the applicable behavioural category in respect of each understatement must be separately or individually determined. The amendment clarifies that the higher percentage for gross negligence would apply in respect of understatements where there is more than one.

  - Reduces the applicable percentages of the penalty in the case of ''substantial understatements'', ''reasonable care not taken'' or ''no reasonable grounds for tax position taken'' to align them with comparative tax jurisdictions. The percentages for gross negligence or intentional tax evasion remain the same.

  - Clarifies that for purposes of a remittance request for a ''substantial understatement penalty'', the opinion in issue must have been given by a tax practitioner that is independent from the taxpayer. Opinions by e.g. in-house tax practitioners, do not qualify.

  - Clarifies that if an understatement penalty cannot be imposed, additional tax may be imposed.

  - The understatement penalty scheme includes a ''substantial understatement penalty'' which is strictly imposed if the shortfall resulting from an understatement amounts to the greater of 5% of the amount of tax properly chargeable or refundable, or R1 000 000. The TAA provides for the remittance of these penalties if certain requirements are met.

- Enables taxpayers who make voluntary disclosures before the commencement date of the TAA, to qualify for relief on an understatement penalty if the audit of their affairs was concluded after the commencement date.

- Allows a senior SARS official who considers an objection by the taxpayer against an understatement penalty imposed as a result of an understatement in a return before the commencement date of the TAA, to reduce the penalty if there were extenuating circumstances.

- The additional tax scheme under the VAT Act and the understatement penalty scheme differ in the sense that an understatement made in a VAT return submitted before the commencement date of the TAA only results in additional tax if there was intent to evade tax. Under the understatement penalty scheme, a penalty may also be imposed if reasonable care was not taken, no reasonable tax position existed or gross negligence existed. The amendment provides that a senior SARS official who considers an objection against an understatement penalty imposed as a result of an understatement in a VAT return, must reduce the penalty in whole if the penalty was imposed under circumstances other than the circumstances referred to in item (v) of the understatement penalty table, i.e. an intent to evade tax.

Section 235 sets out the different criminal offences relating to tax evasion. This section has been amended to specify that only a senior SARS official may lay a complaint with the SAPS or the National Prosecuting Authority.

Section 246 sets out the requirements for public officers of companies. It stipulates that the public officer must be a senior official of the company who also resides in South Africa. However, the Act has been amended to provide that if there is no senior company official residing in the country, another suitable person may be designated as the public officer. This section has been amended further to provide that if no public officer is appointed, the public officer is the director, company secretary or other officer of the company that SARS designates for that purpose.

- Aims to align the terminology used with that of the Companies Act, 2008.

- Under the additional tax legislation the amount of the penalty was subject to an open-ended discretion as a taxpayer could incur a penalty anywhere between 0 to 200%.

- Clarifies the original purpose of the exception under subsection (6), namely that additional tax may be imposed if capable of being imposed.

6. Impact on FundsAtWork

The changes to the Income Tax Act are part of the broader retirement reform aimed at standardising the way in which the contributions to, and benefits paid from the different types of retirement funds are treated.

Paragraph 2 of the Fourth Schedule to the Income Tax Act has been amended to include contributions to a provident fund.

This paragraph places a duty on the employer to deduct or withhold employee's tax from the remuneration paid by the employer to his employees.

Paragraph 2(4) sets out how this amount should be calculated.

Prior to the Amendment Act, this Schedule provided that the amount to be withheld must be calculated on the balance of the remuneration remaining after deducting any contribution by the employee to a pension fund, or any contribution by the employee to a retirement annuity fund where the proof of payment for such contribution has been furnished in the employer contribution or any contribution made by the employer to a retirement annuity fund.

Paragraph 2(4) has now been amended to include contributions to a provident fund and to specify that the deductions in paragraph 2(4) are subject to the maximum deduction that the employee would have been entitled to under section 11(k) having regard to the remuneration and the period for which it is payable. In future, any contributions made by an employer to an approved South African retirement fund for the benefit of an employee-member will be taxed as a fringe benefit in the hands of the member. The value of the fringe benefit for tax purposes will depend on whether the contributions are made to a defined benefit fund or a defined contribution fund. If the contributions are made to a defined contribution fund, the contribution allocable to the employee will be includible as a taxable fringe benefit for that employee as at the cash value of the contribution. If the contributions are made to a defined benefit fund, the value of the fringe benefit will be determined through a special formula.

Any contributions made by an employer for the benefit of an employee will be deemed to have been made by the employee, thereby being potentially deductible subject to percentage and monetary limits outlined below.

- Percentage limit: deductions in respect of contributions made by the member will be allowed up to 27.5 per cent on the greater of “remuneration” or “taxable income” (excluding retirement lump sums). Potential reliance on taxable income means that self-employed individuals can make deductible contributions (or that formally employed individuals can make individual contributions based on amounts above remuneration if earning income from other sources).

- Monetary limit: no member may deduct contributions in excess of an annual limit of R350 000. This limit ensures that wealthy individuals do not receive excessive deductions (vis-à-vis lower income individuals who do not have the means to contribute much to these funds).

Contributions in excess of the annual limits may be rolled over to future years where the amounts will again be deductible together with contributions made in that year, but subject to the limits applicable in that year.

Employer contributions to all approved South African retirement funds will be deductible against income under a specific deduction provision.

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Legal update

No.13 of 2014 • June 2014

Notice on Valuation Exemption, 2014

A. Summary

The Registrar of Pension Funds has issued Board Notice 59 of 2014, setting out the requirements and conditions that a fund must comply with in order to qualify for an exemption from the provisions of section 9A and 16 of the Pension Funds Act (valuation exemption). This Board Notice replaces Board Notice 61 of 2011 with effect from 6 June 2014.

B. The Format and submission of an application for valuation exemption

- A valuation exemption means that the fund does not have to appoint a valuator or submit a valuation report on the financial condition of the fund to the Registrar every 3 years.

- The exemption is subject to certain conditions and the fund must comply with all those conditions for the entire period of the exemption.

- A valuation exemption is valid for a maximum period of 3 years. Thereafter the fund must reapply to the Registrar for the renewal of the exemption.

- The exemption must start on the same date as the financial year end of the fund.

- An application for a valuation exemption must contain the following documents:

  - A signed statement by the board applying for the exemption. In this statement, the board must confirm that the fund is properly administered in terms of its rules and that the fund does not operate any contingency accounts. The board must undertake to inform the Registrar, if in their opinion, the fund no longer qualifies for the exemption.

  - A certification by a valuator stating the start date of the exemption and confirming that the fund complies with the conditions as set out in the Board Notice.

  - If the fund is already valuation exempt and is applying for a renewal of the exemption, any valuator may complete and sign the certificate.

  - If the fund previously had to submit valuation reports and is applying for an exemption for the first time, then only the fund's valuator may complete and sign the certification.

- Examples of the statement required by the Board and the certification required by the valuator have been included in the Board Notice as Annexures A and B respectively.

- The application must be submitted to the registrar electronically via the official website www.fsb.co.za.

C. Conditions for valuation exemption

- At the effective date of the exemption, the fair value of assets must equal or exceed the liabilities of the fund.
- All existing pension payments and any future pension payments must be fully secured by one or more annuity policies purchased from one or more registered long term insurers.
- The amount used to secure a living annuity for members upon retirement must be limited to the amount available per member in the fund at the date of the member's retirement and at any point thereafter. This means that at any given time a member will only be entitled to his share of the fund.
- All members of the fund, other than pensioners must belong to a defined contribution category of the fund.
- Where any benefit payable to a member exceeds the value of the member's individual account, the excess must be fully insured with one or more registered insurers.
- Where the fund has a contingency reserve account in terms of the rules of the fund, the rules must provide that such an account can never have a negative balance. This condition does not apply to a Processing Error Reserve Account.
- The fund must have complied with the provisions of section 15B of the Act. If the fund had to submit a surplus apportionment scheme to the registrar, then that scheme must have been approved or a nil scheme must have been noted before the exemption can be granted.
- Unless the fund was valuation exempt before its surplus apportionment date, the statutory actuarial valuation as at its surplus apportionment date must be accepted by the registrar.

D. Withdrawal of Valuation Exemptions

- Annexure C of the Board Notice contains a list of valuation exempt funds and the dates on which their exemptions expire.
- The termination date reflected in Annexure C was calculated as follows:

  - If the date on which the valuation exemption expires was specified by the registrar in writing, then that is the date on which the valuation exemption will terminate.
  - If no expiration date was specified, the exemption will expire on the date after 1 January 2015 on which the earliest of 3, 6 or 9 or 12 years since the effective date of the amendment will expire.
  - However, if the fund was granted a valuation exemption and then amends its rules to change its financial year end date, the exemption will terminate on the initial year end date and not the new amended date. If that date has already passed, then the exemption will expire on the next financial year end.

    For example: Fund A's financial year end date is 31 December.
    Fund A applies for and is granted a valuation exemption effective from 31 December 2010.
    The exemption letter does not specify the date on which the exemption will terminate.

    Fund A then amends its rules to change its financial year end to 30 June.

    The exemption will terminate on the earliest of the 3rd, 6th, 9th or 12th year from the effective date. In the case of Fund A, the 3rd year would already have ended on 31 December 2013. The 6th year ends on 31 December 2017. Fund A's valuation exemption will expire on 31 December 2017 and not 30 June 2018.

E. Duty on the Board to notify the Registrar

The board must notify the registrar without delay and in writing in the following circumstances:

- if the fund fails to comply with any of the conditions on which the exemption was granted;
- if any party (including the board, principal officer, chairperson, auditor, administrator or any other person acting in an advisory capacity) is of the opinion that the fund no longer complies with any of the conditions;
- if the fund amends it rules and no longer qualifies for a valuation exemption; or
- if the fund no longer requires a valuation exemption.

F. When will the registrar withdraw a valuation exemption?

- The registrar may withdraw a valuation exemption after receiving a notification from the board referred to in paragraph E above.
- The valuation exemption may be withdrawn where the registrar becomes aware of facts that demonstrate that the find is no longer eligible for the exemption.

G. Consequences of the Registrar withdrawing a valuation exemption

- The registrar may withdraw wholly or in part any valuation exemption by notice on the FSB website.
- The valuation exemption will cease on the date it is withdrawn.
- The fund must within 90 days of the date of withdrawal appoint a valuator in terms of section 9A.
- The fund must submit a statutory actuarial valuation report as at the first financial year end following the date of withdrawal.

H. Impact on FundsAtWork

The FundsAtWork Umbrella Funds currently do not have valuation exemption. It is expected to get such exemption soon.

The valuation exemptions in respect of the FundsAtWork Preservation Funds are effective from 30 June 2013 until 30 June 2016.

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Legal update

No. 14 of 2014 • September 2014

Retirement and insurance benefits during temporary absence from employment

We often get questions about the impact of temporary absence from employment on a member's retirement benefits and whether he continues to be covered for insurance benefits. This legal update discusses the implications of temporary absence and whether or not cover continues during such time.

Provisions of the General Rules of the FundsAtWork Umbrella Pension and Provident Funds (the Funds)

The General Rules of the Funds provide for different scenarios. These scenarios can be illustrated as follows:

<u>Scenario 1: If a member is absent from employment *with pay*</u>
The employer must continue paying full contributions to the Fund. The Fund will continue debiting the relevant expenses, fees and costs from the member's retirement savings account. All insurance cover remains intact.

<u>Scenario 2: If a member is absent from employment *without pay*</u>
The employer must decide whether or not the member's insurance benefits should continue during the member's absence from employment and whether to continue with or stop paying retirement benefit contributions.

1. Employer chooses that insurance benefits must continue

   a. If the employer decides to continue with the payment of retirement fund contributions during the member's absence, the employer must pay both his and the member's contributions toward the member's retirement benefits, as well as all the fund expenses, fees and costs. This includes the costs of the insurance benefits.

   b. If the employer decides not to continue with the payment of retirement fund contributions, the employer must still pay all the fund expenses, fees and costs, including the costs of the insurance benefits.

2. Employer chooses that insurance benefits must not continue

   a. If the employer decides to continue with the payment of retirement fund contributions during the member's absence from employment, the employer must pay both the employer's and member's contribution towards the member's retirement benefits, as well as all the fund expenses, fees and costs, less the costs of the insurance benefits.

b. If the employer decides not to continue with the payment of retirement fund contributions, the employer must still pay all the fund expenses, fees and costs, less the costs of the insurance benefits.

As a general rule, should the employer not choose one of the options above, then option 2b will apply.

The different scenarios are illustrated on the last page.

Where the Fund contribution includes standalone (unapproved) insurance benefit premiums

Where the employer contribution to the Fund includes the premiums for unapproved insurance benefits provided through a separate Momentum insurance policy, the Fund will only pay over the premiums for the unapproved insurance benefits to Momentum if they have actually received the premiums from the employer. The Fund cannot deduct the premiums for unapproved insurance benefits from the member's retirement savings account and pay it to Momentum. The member will then effectively lose his cover for the unapproved insurance benefits. The Fund merely acts as an agent for the employer and has no responsibility to pay the premiums should no premiums have been received. Most importantly, the Fund is not responsible for the paying of the unapproved insurance benefits when there is a claim.

Unapproved insurance benefit provided by Momentum

A member will continue to be covered for 12 consecutive months at the level at which he was covered immediately before his absence, as long as Momentum receives payment of the premiums and the member has not yet reached the age at which the cover terminates. After 12 consecutive months' absence, the member's cover will automatically terminate, unless Momentum has agreed to a longer period of absence, subject to the conditions as specified by Momentum. If a member's cover has terminated and he returns to work, his cover will start again as if he were a new member. If a member is absent from work more than once, and there is not at least 3 consecutive months between his absences, it will be deemed that those periods of absence are continuous. This means that those periods of absence will be added together to determine whether it is more than 12 months. If it is, then the member's cover will terminate.

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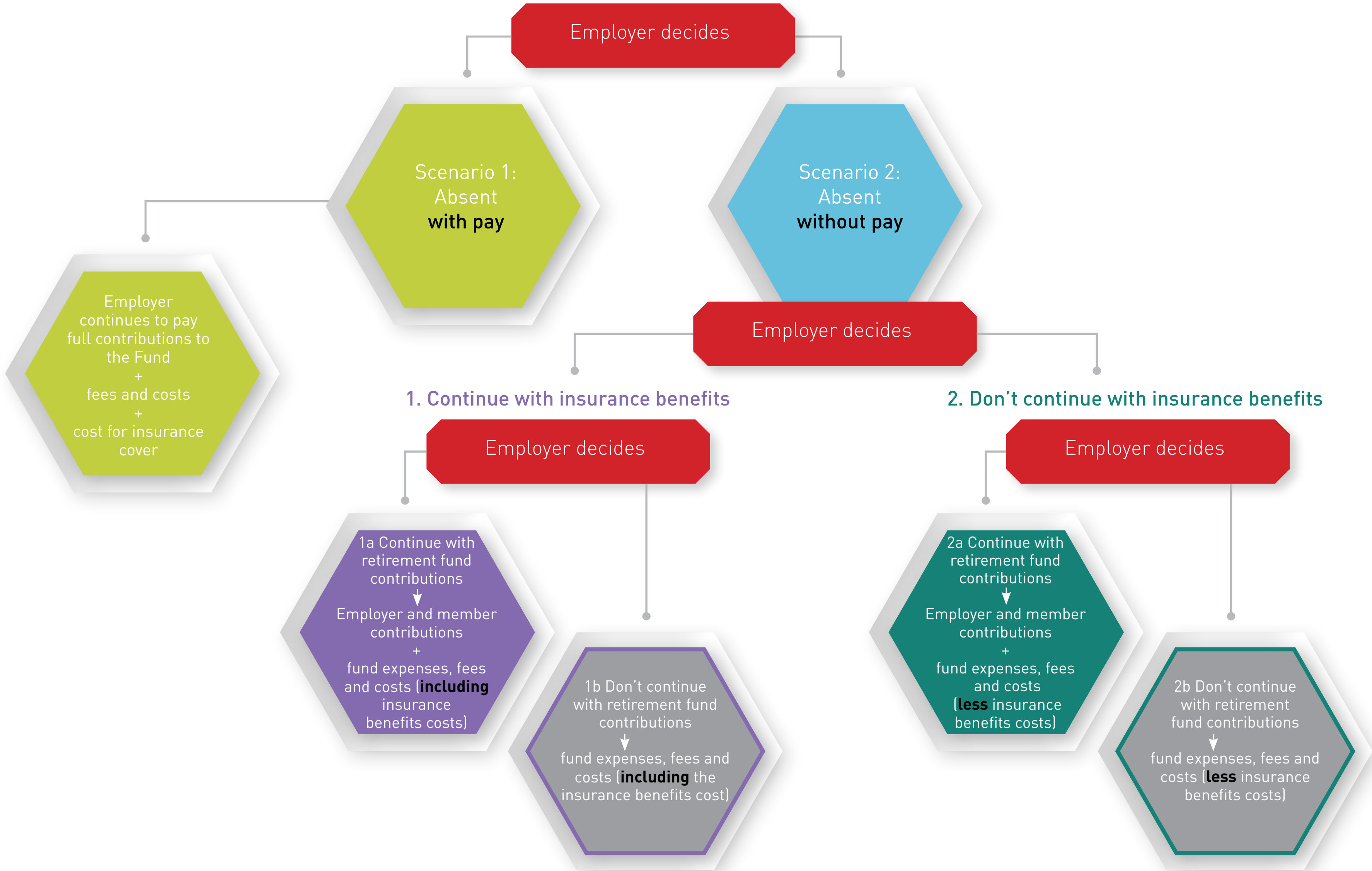
Continuation of retirement and insurance benefits during temporary absence from employment

Provisions of the General Rules of the FundsAtWork Umbrella Funds



As a general rule, should the employer not choose one of the options above, then option 2b will apply.

Legal update

No.15 of 2014 • September 2014

Employment Equity Amendment Act 47 of 2013

The Employment Equity Amendment Act (the Act) was passed by the National Assembly on 24 October 2013 and signed by the President on 14 January 2014. The Act is effective from 1 August 2014.

The Act amends the Employee Equity Act so as to prohibit unfair discrimination in the workplace and strengthens enforcement mechanisms. It recognises that there are disparities in employment, occupation and income within the labour market. It aims to promote equality, eliminate unfair discrimination, ensure the implementation of employment equity and achieve a diverse representative workforce.

The changes

- The definition of "designated groups" is amended to restrict affirmative action to citizens of South Africa (either by birth, descent or naturalisation).
- Discrimination will not be permitted on any listed ground, or any other arbitrary ground.
- A difference in the terms and conditions of employment of employees doing the same or similar work or work of equal value based on any listed ground is seen as unfair discrimination. The employer would have to show that any differences are based on fair criteria such as experience, skill and responsibility.
- The Minister may publish a code of good practice for assessing work of equal value.
- Only psychometric tests that have been certified by the Health Professions Council of South Africa, or another authorised body, may be used.
- In the following instances disputes may be referred to the CCMA and appealed in the Labour Court:
  - unfair discrimination due to sexual harassment;
  - employees earning below the threshold amount, currently R205,433.30;
  - by consent of the parties involved.
- Burden of proof:
  - If unfair discrimination is alleged on a listed ground, the employer will have to prove that the discrimination:
    - did not take place as alleged, or
    - was rational and not unfair, or was justifiable.
  - If unfair discrimination is alleged on an arbitrary ground, the complainant must prove that:
    - the conduct was not rational;
    - the conduct amounts to discrimination, and
    - the discrimination is unfair.
- Fines can be imposed if:
  - reports are not submitted;
  - no valid reasons are provided;
  - an employment equity plan is not prepared, and
  - an employment equity plan is not implemented.

- Should the employer not have submitted a report he can give sufficient notice to the Director General explaining the reasons for failure to submit. Reasons must be credible and only if found not be credible will a fine then be imposed.
- Compliance orders by labour inspectors may now be made an order of court.
- In assessing compliance, the reasonable steps taken by a designated employer to train suitably qualified people from the designated groups will be taken into account.
- The Minister may issue regulations which are to be taken into account in determining if an employer is implementing employment equity.
- The Director General may apply for an order directing an employer to comply with a request, failing which, a fine may be imposed.
- An award by a Commissioner of the CCMA may include an order or an award.
- Fines have been increased and should be paid into the National Revenue Fund.
- The Minister may publish a code of good practice to assess an employer's compliance.

Turnover thresholds applicable to designated employers have been increased as indicated below:

Sector or subsectors in accordance with the Standard Industrial Classification	**Total annual turnover**	
	Previous	**New**
Agriculture	R2m	R6m
Catering, Accommodation and other Trade	R5m	R15m
Community, Special and Personal Services	R5m	R15m
Construction	R5m	R15m
Electricity, Gas and Water	R10m	R30m
Finance and Business Services	R10m	R30m
Manufacturing	R10m	R30m
Mining and Quarrying	R7,5m	R22,5m
Retail and Motor Trade and Repair Services	R15m	R45m
Transport, Storage and Communications	R10m	R30m
Wholesale Trade, Commercial Agents and Allied Services	R25m	R75m

Designated employers are required to submit employment equity plans and reports to the Department of Labour and will receive an assessment of compliance report following a labour inspection.

The Act serves to further prohibit unfair discrimination in the workplace and strengthen the enforcement mechanisms of the Employment Equity Act.

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Legal update

No16 of 2014 • September 2014

Estate duty and death benefits

Introduction
Estate duty refers to a tax of 20% that is levied on the estate of a deceased person in accordance with the provision of the Estate Duty Act (the Act). Estate duty is levied on the *dutiable* portion of the deceased estate.

The Act lists the assets that will attract estate duty and therefore must form part of the dutiable estate and those assets which are excluded from the estate for the purposes of calculating estate duty.

This Legal Update focuses on whether or not approved and unapproved death benefits form part of the estate of a deceased member for the purposes of calculating estate duty.

What constitutes an "estate" for the purposes of calculating estate duty?
In terms of the Act, all property belonging to a person at the date of his death, together with all property *deemed* to belong to that person as at the date of his death, forms part of his estate for the purposes of calculating estate duty.

"Deemed property" is any benefit received because of the death of the deceased. Domestic policies on the life of the deceased are deemed to be the property of the deceased and form part of the deceased estate for the purposes of estate duty.

Unapproved death benefits
Unapproved group life policies are life policies grouped together and owned by the employer. The benefits provided by these policies will become due and payable on the death of the person insured. For this reason; the proceeds of an unapproved group life policy will be deemed to form part of the estate of the deceased member for the purposes of calculating estate duty.

Deduction if surviving spouse is the beneficiary of the unapproved GLA
The value of any benefit received by the surviving spouse as a result of the death of the deceased is deducted from the estate before estate duty is calculated. So, if the surviving spouse is the beneficiary of the unapproved GLA policy or a portion thereof, that amount will not form part of the dutiable estate.

Approved death benefits
These policies are held in the name of the retirement fund to which the member belongs and are subject to the rules of the fund. In terms of section 37C of the Pension Funds Act, the trustees of the fund must determine who becomes entitled to the proceeds of a member's death benefit.

Section 3(2)(c)(i) of the Estate Duty Act states that a death benefit paid from a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund does not form part of a person's property for purposes of determining what constitutes his estate. This effectively exempts an approved death benefit from estate duty.

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Legal update

No. 17 of 2014 • September 2014

Withdrawn SARS General Notes

The following SARS General Notes (GN) have been withdrawn to date.

1. **General Note 3 - Preservation funds and the "N-factor"**

   Issued: 15 February 1995.

   The Second Schedule to the Income Tax Act sets out the formulae used in calculating gross income derived by way of lump sum benefits. The "N-factor" represented the years of service or years of membership. The question addressed by this GN was whether "N" will continue to grow for as long as the member remains a member of a preservation fund.

   It was decided that since a preservation fund can never receive contributions from either members or employers, "N" will never be greater than the value transferred into the preservation fund.

   Status: Withdrawn - 29 March 2012.

   Reason for withdrawal: GN became obsolete due to legislative changes.

2. **General Note 3 – Addendum A – Legislative changes affecting the "N-Factor"**

   Issued: 28 September 2007.

   This addendum clarified certain provisions relating to the "N-factor" and specified with that effect from 1 October 2007, the number of years of employment was no longer a factor when determining the deduction afforded in the case of lump sum benefits payable on retirement or death.

   Status: Withdrawn - 29 March 2012.

   Reason for withdrawal: GN became obsolete due to legislative changes.

3. **General Note 5 – Determination of death benefits**

   Issued: 20 February 1995.

   This GN clarified that where benefits are payable on the death of a member, SARS would only take into account the number of years of membership to the fund from which the benefit is payable in respect of a deceased member for the purposes of formulae A and B of the Second Schedule to the Income Tax Act. The number of years of service or employment was irrelevant.

   Status: Withdrawn - 29 March 2012.

   Reason for withdrawal: GN became obsolete due to legislative changes.

4. **General Note 5 – Addendum A – Determination of death benefits**

Issued: 27 November 2007.

This GN replaced GN 5 with effect from 1 October 2007 and specified that the number of years of membership to a retirement fund was no longer a parameter in determining the deduction afforded where lump sum benefit were payable on death.

Status: Withdrawn - 29 March 2012.

Reason for withdrawal: GN became obsolete due to legislative changes.

5. **General Note 6 – Formula B: Maximums**

Issued: 20 July 1995

This GN provided consistency on how symbol “C” in the definition of formula B in the Second Schedule to the Income Tax Act was interpreted.

Status: Withdrawn - 29 March 2012.

Reason for withdrawal: GN became obsolete due to legislative changes.

6. **General Note 6 – Addendum A – Formula B**

Issued: 28 September 2007.

Replaced GN 6 in respect of benefits accruing on or after 1 October 2007.

Status: Withdrawn - 29 March 2012.

Reason for withdrawal: GN became obsolete due to legislative changes.

7. **General Note 7 – Source of Income**

Issued: 20 July 1995.

This GN confirmed that the provisions of section 9(1)(g) of the Income Tax Act will be applied on the taxable portion of the lump sum benefit, after allowing the deductions determined in accordance with the Second Schedule.

Status: Withdrawn - 5 November 2012.

8. **General Note 8 – Purchase of annuities at retirement**

Issued: 20 July 1995.

This GN made it possible for a pension or provident fund to purchase a life annuity from a registered insurer on a member’s retirement. The fund may not pay more than one pension per member.

Status: Withdrawn: 29 March 2014.

Reason for withdrawal: GN became obsolete due to legislative changes.

9. **General Note 1- Source of Income**

Issued: 20 July 1995.

This GN dealt with the application of section 9(1)(g)(ii) of the Income Tax Act to a paid up member of a pension or provident fund, where there member claims his benefit, but was not a South African citizen for at least 2 years of the last 10 years in which the benefit was accumulated.

Status: Withdrawn 05 November 2012

Reason for withdrawal: Retracted from 5 November 2012.

10. General Note 14 – Housing loans and guarantees

Issued: 24 April 1995.

A retirement fund granting a housing loan or guarantee in terms of section 19(5) of the Pension Funds Act will not be considered to hold moneys on behalf of a member for the purposes of section 99 of the Income Tax Act.

Status: Replaced with issue 2, 12 September 2007.

11. General Note 15 – Approval of fund registered in former TBVC states

Issued: 20 February 1995.

This GN sets out the criterion that the Commissioner must use when considering the approval of funds registered in the former TBVC states. It provided that the Commissioner must look at whether or not the fund in question complies with the definitions of either "benefit fund", "pension fund", or "provident fund". If the fund does not comply with the requirements of one of the relevant definitions, the deemed approval will be withdrawn.

Status: Replaced with issue 2, 12 September 2007.

12. General Note 16 – Commutation of small annuities

Issue 2: 15 September 1995.

This GN replaced the original GN 16 and confirmed that not more than one-third of a member's interest in the fund may be commuted for a lump sum unless the full benefit does not exceed R75 000. Where a member or former member commuted before, or where the administrator is unable to determine whether a previous commutation occurred, the annuitant may commute the remaining annuity for a lump sum if two-thirds of the retirement interest does not exceed R50 000.

Status: Replaced with issue 2, 31 March 2010.

13. General Note 17 – Standard Rules

Issued: 15 February 1995.

This GN made provisions for institutions submitting rules for approval to the Commissioner, to submit a model set of rules, together with standard variations to SARS. This submission should follow the normal procedure.

Status: Replaced with issue 2, 12 September 2007.

14. General Note 24 – Retirement from employment

Issued: 6 October 2000.

This GN served as a reminder that the distinction between the age of a female member and a male member of a provident fund was removed with effect from 1 March 2000. Paragraph 4(3) of the Second Schedule to the Income Tax Act now applies to all lump sum benefits paid to a member who is under the age of 55, regardless of whether the member is male or female.

Status: Withdrawn – 29 March 2012

Reason for withdrawal: GN became obsolete due to legislative changes.

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Legal update

No. 18 of 2014 • November 2014

Sectoral determinations and how they may influence retirement fund membership – focus on the private security sector

This Legal Update clarifies the position with regards to employers whose operational activities fall within the ambit of a sectoral determination.

What is a sectoral determination?

Section 55 of the Basic Conditions of Employment Act entitles the Minister of Labour to make a sectoral determination that governs the basic employment conditions of employees employed in a specific sector. Sectoral determinations are legally binding on employers and employees operating within these sectors. There are various industries where sectoral determinations exist and which govern business entities operating within those sectors, for example hospitality, mining, security, cleaning and other industry sectors. The sectoral determination typically regulates the employer's basic conditions of employment, including, but not limited to, the payment of employees' remuneration, hours of work, leave, and employee benefits such as membership and contributions to retirement funds. A sectoral determination may require membership of an industry specific retirement fund. This means that an employer will not be allowed to associate itself and contribute to a retirement fund of its choice, unless they have been granted exemption as outlined in the sectoral determination.

The sectoral determination establishes the minimum employee benefits that an employer must provide to employees. The employer can however, in addition to contributing to the bargaining council fund, provide additional benefits, over and above those set out in the sectoral determination, to his employees; there is nothing prohibiting him from doing so. The provision of top-up benefits will be completely separate from and unrelated to any collective agreement or sectoral determination. These benefits will be provided outside the bargaining council structures. The employer must be guided by the terms and conditions of the collective agreement and must be careful not to duplicate benefits already provided for.

When Momentum is requested to provide quotations on any business, it would be important to consider whether a sectoral determination applies to the employer.

How do we establish if an employer falls within the ambit of a sectoral determination?

Typically employers operating within a particular sector should be aware of the sectoral determination that governs the employment conditions. All sectoral determinations are published in the Government Gazette and on the Department of Labour's website.

The sectoral determination will stipulate whether or not membership of an industry retirement fund is compulsory. In this note we will focus on the sectoral determination for the private security sector. Please keep in mind, however, that there are sectoral determinations that relate to the other sectors too, with each sectoral determination laying down the requirements applicable to that sector.

The Sectoral Determination for the Private Security Sector and the Private Security Sector Provident Fund (the PSSPF).

Employers of the private security sector must comply with Sectoral Determination 6 of 2001 published on 30 March 2001. This requires, amongst other things, membership of the PSSPF. This fund started on 1 November 2002.

The rules of the PSSP define an Employer as follows:

> "… *any person (excluding an Employer who has been granted an exemption to participate in the Fund by the Trustees in terms of Rule 3.3) who employs or provides work to any person in the Private Security Sector and remunerates him or who permits any person in any manner to assist him in the carrying on or conducting of his business;* …"

Therefore in terms of the rules of the PSSPF, if a private security employer meets the above criteria, they are eligible and, in fact, required to become a participating employer of the PSSPF. This includes an employer -

- who employs or is providing work to any person in the private security sector and remunerates such person; or
- who allows any person in the private security sector to assist him in any manner in carrying on or conducting of his business; and
- that has not been granted an exemption from the PSSPF under Rule 3.3.

PSSPF's Rule 3 and Sectoral Determination 6 of 2001 allows for the following two instances where an employer, who employs an employee for whom minimum wages are prescribed, may apply to be exempted from membership of the PSSPF:

1. where the employer *already* had an existing pension or provident fund in place for his employees prior to the publication of the determination on 30 March 2001; and
2. where the employer did not have an existing pension or provident fund in place on 30 March 2001, but had before that date consulted, in writing, with his employees to commence negotiations towards establishing a pension or provident fund.

Essentially this means that all employers that were not participating in any existing pension or provident fund prior to the publication of the determination on 30 March 2001, or shortly thereafter, and those employers that came into existence after the publication, are obliged to join and contribute to the PSSPF. Should such employer not have joined the PSSPF, that employer is non-compliant with the sectoral determination unless it obtained exemption from the PSSPF.

The PSSPF's board of management will consider all properly motivated applications for exemption from the PSSPF, as outlined in the determination, subject to conditions as laid down by the PSSPF's board. If there is a dispute, it will be referred to the Department of Labour.

Security sector employers participating in the FundsAtWork Umbrella Funds that have not been granted exemption by the PSSPF, may be required to transfer to the PSSPF as referred to in section 14 of the Pension Funds Act.

Financial planners and intermediaries will therefore need to be mindful of applicable sectoral determinations when considering joining FundsAtWork.

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Legal update

No. 19 of 2014 • October 2014

T-day postponed

On 16 October 2014, National Treasury published a media statement, the revised draft Taxation Laws Amendment Bill 2014 (TLAB), the revised draft Tax Administration Laws Amendment Bill 2014 (TALAB) and the draft Response Document that was presented to the Standing Committee on Finance (SCOF) in Parliament on 15 October 2014. These documents are available on the National Treasury website http://www.treasury.gov.za/legislation/bills/2014/TLAB-TALAB/.

What is changing?

Without going into the details of all the amendments proposed in the Bills, the following changes are of immediate interest to Momentum FundsAtWork, its clients and their employees.

1. Retirement fund contributions

   The effective date for the changes to the way in which retirement fund contributions would be taxed has been delayed for a year. These changes were discussed in Legal Update 3-2014.

2. Valuation of defined benefit fund contributions

   The valuation of defined benefit fund contributions will only be applicable when the changes to retirement fund contributions come into effect. These changes have accordingly also been delayed by a year.

3. Provident fund post-retirement alignment

   The effective date for the changes to the taxation of provident fund benefits to be in line with pension funds and retirement annuity funds has also been delayed for a year. These changes were discussed in Legal Update 4-2014.

According to the media statement, the implementation of these changes will be delayed for a year to allow for further consultations between Government and NEDLAC on social security reform. Should there be no agreement at NEDLAC by 30 June 2015, the implementation date may be moved out for another year, to 1 March 2017.

What stays the same?

1. Disability income benefits

   The effective date for the changes relating to the taxation of employer-provided disability income benefits, as discussed in Legal Update 2-2014, is still 1 March 2015. From 1 March 2015, a member will no longer be able to claim a tax deduction on the premium paid for a disability income benefit and the benefit will be paid out tax-free.

2. Tax free savings

   The effective date for the provisions on tax free investments, to an annual maximum of R30 000 and a lifetime maximum of R500 000 remains 1 March 2015.

What is new?

1. Right to elect when to retire

   The amendment to the definition of "retirement date" which aims to allow the member to elect when he wants to retire will come into effect on 1 March 2015.

As soon as the legislation incorporating the changes referred to above has been finalised, a further Legal Update will follow.

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