Legal Update – Tax Free Investments

A. Background

Amendments to the Regulations in terms of Section 12T(8) Income Tax Act, which relate to Tax Free Savings and Investment Accounts (“TFSAs”), were published in Government Notice No. 40758 on 31 March 2017. A summary of TFSAs was discussed in Legal Update 4 of 2015.

The amendments set out the process for transfers and clarify the position on performance fees in underlying funds. The amendments also provide guidance on disclosing returns to fixed deposit tax free savings accounts, give powers to the regulator to oversee product offerings, align the rules of access for fixed deposits and include Postbank as a product provider. In this summary, a provider of a TFSA is referred to as a product provider.

B. Summary of amendments

1. Product providers

The South African PostBank Limited has been added to the list of entities that are allowed to issue TFSAs.

If a product provider advertises a TFSA that is for a fixed term and a guaranteed return, then the product provider must clearly state in the advertisement the rate of return as calculated by the formula set out in the regulations.

2. Contributions

A product provider may not accept any contributions from an investor that are more than the annual and lifetime contribution limits, which are presently limited to R33 000 and R500 000 respectively.

When determining whether contributions over the limits have been made, the exempt amount received by or accrued in a specific tax year or previous tax years for the TFSA is not taken into account. The transfer of a TFSA to another TFSA for the same investor and any amount received or accrued for a TFSA are also not taken into account. A product provider may accept these amounts but cannot accept any other amounts as a contribution to the TFSA.

This, in practice, means that penalties will only be applied where an investor has contributed amounts over the annual and lifetime limits. The contributions over the annual and lifetime limits will be subject to normal tax at a rate of 40%.

For example, A had a TFSA of approximately R100 000. A passed away and her child B inherited the proceeds of the TFSA. B later got his own TFSA. When calculating whether B made contributions over the annual and lifetime limits, the R100 000 will not be taken into account. If B contributed R40 000 in a tax year to his TFSA, only the amount above the annual limit, namely R7 000, will be taxed at 40%.

3. Transfers

From 1 March 2018, transfers of an amount from one TFSA to another will be allowed. The transfer will have to be completed within 10 business days after the maturity date or the date on which the investor requested the transfer. A product provider will not be obliged to make more than two transfers in one tax year for the same investor.

When a product provider transfers a TFSA to another product provider, the transferring product provider will have to issue a certificate and provide or send a copy of the certificate to both the investor and to the receiving product provider. The certificate will have to contain information such as:

- The name, identity number, passport number or tax reference number of the investor.
- The amount in cash that is transferred or the market value of any asset of the TFSA where the amount to be transferred is an asset other than cash.
- The name, registration number and tax reference number of the transferring product provider.
- The name, registration number and tax reference number of the receiving product provider.
- The total amount of contributions for the TFSA that is being transferred and the total amount of contributions from other TFSAs that were made during the tax year into the TFSA that is being transferred.
- The total amount of contributions for the TFSA that is being transferred and the total amount of contributions from other TFSAs that were made in the years before that year in which the TFSA is transferred.
- The words “transfer of tax free savings account”.
- A description of the assets of the TFSA where the amount being transferred relates to an asset other than cash.
- The number of assets that are being transferred for an asset other than cash.

4. Fees and returns

If a product provider is required to recover any fee for the TFSA, the product provider may only recover such fee from the TFSA. A product provider may also not charge performance fees, whether charged as part of the TFSA or in an underlying fund into which the TFSA contributions are invested.

Formulas for calculating the rate of return of a TFSA with a fixed term and a guaranteed return were introduced. The maturity date of a TFSA has now been limited to a maximum of five years from the date on which the TFSA was issued.

Where a TFSA has a maturity date, the product provider must pay the amount due to the investor within seven business days after the maturity date or after the date on which the investor requested payment. If the TFSA has no maturity date, then the product provider must pay the amount within seven business days after the investor has requested payment.

A product provider may refuse to pay any amount if the TFSA continues to exist after the payment is made and the remaining amount is lower than the minimum amount required to be invested in terms of the agreement between the product provider and the investor.

5. Registrar's powers

The Registrar of the Financial Services Board (Registrar) has been granted powers to act when a TFSA does not comply with any regulations or legislation. The Registrar may require the product provider to:

- stop advertising the TFSA;
- stop inviting members of the public to invest in the TFSA; and
- transfer any existing TFSAs or amend any of the benefits, terms and conditions and marketing material of the TFSA.

If the Registrar objects to the proposed implementation of a TFSA, the product provider may not implement the TFSA until the grounds for objection have been resolved.

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