

Taxation Laws Amendment Act No. 23 of 2018

Summary

The Taxation Laws Amendment Act No. 23 of 2018 (the Amendment Act) was published in Government Gazette No. 42172 on 17 January 2019.

The following changes are of particular relevance for the retirement fund industry:

- 1. Transfer of retirement benefit to preservation fund after reaching normal retirement date:** From 1 March 2019, a member will be entitled to transfer his post-retirement benefit to a preservation fund. The member will not be entitled to the one pre-retirement withdrawal option that is available to a member who transferred his withdrawal benefit to the preservation fund.
- 2. Withdrawal from preservation fund upon emigration or repatriation on expiry of a work or visitor visa:** A member of a preservation fund will be entitled to withdraw his full lump sum benefit from that fund when he emigrates from South Africa and the emigration is recognised by the South African Reserve Bank for the purposes of exchange control, or when he repatriates when his work or visitor visa expires, similar to a member of a retirement annuity fund, even if the member has already made one pre-retirement withdrawal.
- 3. Transfer of surplus between funds in which the same employer participates:** Where an actuarial surplus is transferred between different retirement funds in which the same employer participates, no taxable fringe benefit will be created in the member's hands.
- 4. Provident fund annuitisation postponed:** The implementation of annuitisation requirements for provident funds have been postponed to 1 March 2021, and the tabling of the report by the Minister of Finance in relation to this, to 31 August 2020.
- 5. Other changes to the Income Tax Act:**
 - Definition of pension preservation fund: Allows a pension preservation fund to accept divorce order payments from a provident fund and a provident preservation fund.
 - Section 3(5): Reflects the transformation of the Financial Services Board into the Financial Sector Conduct Authority.
 - Section 10C: Clarifies that only contributions that did not rank for deduction under section 11F in any *prior* year of deduction, and not the current tax year, can be deducted against a compulsory annuity.
 - Section 11F: Section 11F(2) clarifies the ordering rule for claiming deduction in terms of section 11F, foreign tax credits in terms of section 6quat as well as tax deductible donations in terms of section 18A. Section 11F(4) clarifies that not only contributions made for the benefit of the employee, but also amounts paid on behalf of the employee, to a retirement annuity fund, should qualify for deduction under section 11F.

- Paragraph 6 of the Second Schedule: Includes a transfer from a provident preservation fund to a pension fund as a tax-free transfer.
- Paragraph 12D of the Seventh Schedule: Provides for circumstance under which contribution certificates may be updated.

These changes are discussed in detail below.

1. Transfer of retirement benefit to preservation fund after reaching normal retirement date

The Income Tax Act was amended to allow a member to choose from which date he wants to receive his retirement benefit. This applied from 1 March 2015 – refer to [Legal Update 2-2015](#) for more information about this change.

This amendment allowed a member to postpone his retirement date. The General Rules of the FundsAtWork Umbrella Funds were amended from 1 March 2016 to allow a member to postpone his retirement, retrenchment and disability benefits and become an inactive member. Refer to [Legal Update 11-2016](#) for more information on the postponement of a retirement benefit.

The Taxation Laws Amendment Act No. 17 of 2017 amended the Income Tax Act to allow a member to transfer his retirement benefit to a retirement annuity fund from which he can then access it at a later date. Refer to [Legal Update 2-2018](#) for a discussion on this amendment and other amendments under that Amendment Act.

It is important to remember that a member of a provident fund who transfers his retirement benefit to a retirement annuity fund will only be entitled to take one-third of his retirement benefit in a lump sum when he eventually takes his retirement benefit from the retirement annuity fund. He will then have to buy a pension with the rest of his retirement benefit.

Annexure C of the March 2018 Budget Speech pointed out that [P]ension preservation and provident preservation funds were excluded as the administration required to disallow once-off withdrawals from these funds was considered too onerous. Industry consultations indicate that the system changes will not be burdensome, thus it is proposed that transfers to pension preservation and provident preservation funds be catered for in the legislation.

The Amendment Act now includes provisions that allow for post-retirement benefits to be transferred to a preservation fund. The definitions of “pension fund” and “provident fund” have been amended to allow such transfers, and the definitions of “pension preservation fund” and “provident preservation fund” have been amended to accept these transfers. Paragraph 6A of the Second Schedule to the Income Tax Act has also been amended to allow for the following transfers to be tax deductible:

- From a pension fund to a pension preservation fund or a retirement annuity fund, and
- from a provident fund into a pension preservation fund, provident preservation fund or a retirement annuity fund.

In addition, the definitions of “pension preservation fund” and “provident preservation fund” have been amended to make it clear that a member who transferred his retirement benefit to a preservation fund **will not** be allowed to take a *withdrawal* benefit from the preservation fund. The one withdrawal prior to retirement in a preservation fund is only available to a member who transfers his pre-retirement benefit, such as his resignation benefit, to the preservation fund.

Under current legislation, a member cannot stagger his retirement. When he reaches his retirement date¹, he will

¹ “retirement date” means the date on which—

(a) a member of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund, elects to retire and in terms of the rules of that fund, becomes entitled to an annuity or a lump sum benefit contemplated in paragraph 2 (1) (a) (i) of the Second Schedule on or subsequent to attaining normal retirement age”.

have to take his full retirement benefit, whether he remains in the fund as an inactive member or transfers his benefit to a preservation fund or a retirement annuity fund. He cannot for instance decide to keep a part of his retirement benefit in his existing fund and either take the rest of it as a partial retirement benefit or transfer it to a preservation fund or a retirement annuity fund. It's all or nothing.

“Normal retirement age” as defined in the Income Tax Act² is not the *normal* retirement date as defined in most funds’ rules, but rather the earliest date on which a member becomes entitled to a retirement benefit.

Paragraph 2(1)(c) of the Second Schedule to the Income Tax Act provides for the inclusion of *any amount transferred for the benefit of that person on or after normal retirement age, as defined in the rules of the fund, but before retirement date, less any deductions permitted under the provisions of paragraph 6A* to be included in a member’s gross income. SARS has confirmed that the underlined words should be interpreted to correspond with the definition of “normal retirement age” in section 1 of the Income Tax Act, which means that “normal retirement age” will be the earliest retirement date allowed for in the fund rules, as opposed to what most fund rules call their “normal retirement age”.

The FundsAtWork Umbrella Funds have three retirement dates: early retirement (55)³, normal retirement (as defined in the Special Rules of the specific participating employer), and late retirement (for a member who stayed in employment after his normal retirement date, the last day of the month in which he actually retires from employment). For members of the FundsAtWork Umbrella Funds, “normal retirement age” would then be their early retirement date.

This means that a member who elects to retire on his early retirement date, can also transfer his retirement benefit to a preservation fund or a retirement annuity fund. If he chooses to transfer it to a preservation fund, the preservation fund would have to record it as a retirement benefit, and even though the member might only be 55, he would not be able to take it as a withdrawal benefit in the preservation fund. The transferred benefit will have to retain its nature as a retirement benefit.

Effective date: 1 March 2019. If a member retired from employment before 1 March 2019 and left his benefit in his occupational fund, he will be entitled to transfer his post-retirement benefit to a preservation fund after 1 March 2019.

2. Withdrawal from preservation fund upon emigration or repatriation on expiry of a work or visitor visa

Before 2008, a member in a retirement annuity fund was not entitled to withdraw his benefit from that fund if he emigrated. This was changed when the Taxation Laws Amendment Act No. 3 of 2008 introduced the following as paragraph (b)(x)(dd) to the definition of “retirement annuity fund”:

“the payment of a lump sum benefit contemplated in paragraph 2(b)(ii) of the Second Schedule where that member emigrated from the Republic and that emigration is recognised by the South African Reserve Bank for purposes of exchange control;”

This allowed a member who emigrated from South Africa before he retired to withdraw his benefit in the retirement annuity fund before retirement, provided that he paid the full tax on the benefit.

The Taxation Laws Amendment Act No. 25 of 2015 expanded paragraph (b)(x)(dd) of the definition of “retirement annuity fund” to have a similar allowance for a member who departed from South Africa before his retirement

² “normal retirement age” means –

(a) *in the case of a member of a pension fund or provident fund, the date on which the member becomes entitled to retire from employment for reasons other than sickness, accident, injury or incapacity through infirmity of mind or body”.*

³ *Pension: 55. Early retirement prior to the age of 55 may be allowed if the member does not have an outstanding housing loan guarantee, subject to SARS approval.*

Provident: 55. Early retirement prior to the age of 55 may be allowed, subject to SARS approval.

date at the expiry of a visa. The amendment allowed that member to withdraw a lump sum benefit from his retirement annuity fund before his retirement date if he –

- a. ceased to be a resident as defined in the Income Tax Act; or
- b. left South Africa when his work or visitor visa expired.

This means that both a member that emigrates and one that repatriates are entitled to the payment of a lump sum benefit from their retirement annuity fund when they leave South Africa before their retirement date.

A member who transfers a pre-retirement benefit to a preservation fund is allowed to make one withdrawal from that preservation fund before his retirement date. If he leaves South Africa before his retirement date under the same circumstances as those applying under paragraph (b)(x)(dd) of the definition of “retirement annuity fund”, and he has not made that one pre-retirement withdrawal from the preservation fund yet, he can make use of that withdrawal to access his benefit in the preservation fund. If however he has previously made that one withdrawal already, he cannot take the balance of his benefit in the preservation fund until he gets to the retirement date. What’s more, if he is in a pension preservation fund and his total benefit is more than the *de minimus* amount (currently R247 500), he will have to buy a pension with at least two thirds of his retirement benefit.

The Explanatory Memorandum to the Amendment Act states the following:

In order to promote Government’s policy of a uniform approach on the tax treatment of all retirement funds, it is proposed that the tax treatment of different types of preservation fund withdrawals be aligned to allow members of all preservation funds to be able to access and withdraw the full value of the post-tax retirement benefits upon emigration or repatriation on expiry of the work visas.

To achieve this, the Amendment Act amended the definitions of “pension preservation fund” and “provident preservation fund” to allow a member of a preservation fund to withdraw his full lump sum benefit (even if he exercised his previous once-off withdrawal option) when he emigrates from South Africa, if the emigration is recognised by the South African Reserve Bank for the purposes of exchange control, or when he departs from South Africa (repatriates – go back to his country of citizenship) when his work or visitor visa expires, similar to a member of a retirement annuity fund.

Effective date: 1 March 2019. A member who has formally emigrated before 1 March 2019 and who has previously made one pre-retirement withdrawal from his preservation fund will be able to withdraw his full lump sum benefit from that preservation fund from 1 March 2019 if all the administrative requirements are met. A member who is still in the process of emigration and who has previously made one pre-retirement withdrawal from his preservation fund will be able to withdraw his full lump sum benefit from that preservation fund from 1 March 2019 once the formal emigration process is completed and all the administrative requirements are met. A member whose visas expired before 1 March 2019 or whose visa expires on or after 1 March 2019 will be entitled to withdraw his full lump sum benefit from his preservation fund from 1 March 2019.

3. Transfer of surplus between funds in which the same employer participates

Paragraph 2(l) of the Seventh Schedule to the Income Tax Act provides that a contribution for the benefit of an employee to any pension fund, provident fund or retirement annuity fund will be deemed to be a taxable benefit granted by the employer to the employee. The result of that is that the contribution will be subject to fringe benefit tax in the member’s hands.

Paragraph 4 of that same Schedule provides that a benefit provided by any associated institution of the employer will be deemed to have been granted to the employer and would also be subject to fringe benefit tax in the employee’s hands if that benefit would have constituted a taxable benefit if it had been granted directly by the employer to the employee. Paragraph (c) of the definition of “associated institution” in that Schedule includes *any fund established solely or mainly for providing benefits for employees or former employees of the employer or for employees or former employees of the employer*. A contribution made by a retirement fund in which the employer participates to another fund in which that same employer participates for the benefit of the employee can be seen

as a benefit provided by an associated institution, which would result in it being subject to fringe benefit tax in the employee's hands. This includes the transfer of actuarial surplus from a retirement fund in which the employer participates to another fund in which that same employer participates, and even the transfer of an amount from an employer surplus account to the individual members' accounts to for instance fund benefit improvements. Because the member was already taxed on the contributions which made up the surplus, taxing the transfer of that surplus between different funds in which the employer participates or within the same fund would mean that the member would be subject to fringe benefit tax on the same contributions twice.

The Amendment Act now amended paragraph 2(l) of the Seventh Schedule to firstly provide not only for contributions for the benefit of, but also contributions *on behalf* of any employee to a retirement fund to constitute a taxable fringe benefit, and secondly to provide that this does not apply to *the transfer of any surplus as contemplated in section 15E(1)(b), (d) and (e) of the Pension Funds Act*⁴. This includes

- pensions or pension increases to compensate members for the loss of employer provided post-retirement medical aid benefits;
- benefit improvements to all or a category of members, and
- transfers from one employer surplus account to the employer surplus account in another fund, for the same employer.

Effective date: Deemed to have come into operation on 1 March 2017, applying to years of assessment starting on or after that date.

4. Provident fund annuitisation postponed

The annuitisation of provident funds as discussed in [Legal Update 4-2014](#) and [Legal Update 4-2016](#), was initially going to be implemented on 1 March 2016.

The Revenue Laws Amendment Act No. 2 of 2016 postponed the implementation date to 1 March 2018 to allow for further consultations between Government and the National Economic Development and Labour Council (NEDLAC) on social security reform.

The Taxation Laws Amendment Act No. 17 of 2017 postponed the implementation date to 1 March 2019 and provided that the Minister of Finance had to table a report in the National Assembly not later than 31 August 2018.

The Amendment Act now postpones the implementation of the annuitisation requirements for provident funds to 1 March 2021 and provides that the Minister of Finance must table a report in the National Assembly not later than 31 August 2020 in respect of the results of the deliberations on this issue.

6. Definition of pension preservation fund: divorce order payments

Paragraph 1(a)(iv) of the definition of "pension preservation fund" in section 1 of the Income Tax Act has been amended to allow a pension preservation fund to receive a divorce order payment from a provident fund and provident preservation fund, in addition to the already allowed transfers from a pension fund and a pension preservation fund.

⁴ Section 15E(1) *Notwithstanding anything to the contrary in the rules, a participating employer may require the board to use actuarial surplus allocated to the employer surplus account in terms of sections 15B, 15C and 15F for use by that employer for any of the following purposes, namely—*

- (b) *payment of pensions, or an increase in pensions in course of payment, so as to compensate members for the loss of any subsidy from the employer of their medical costs after retirement;*
- (d) *improving the benefits payable to all members, or a category of members as defined in the rules, as determined by the employer;*
- (e) *transferring part, or all, of the employer surplus account in terms of subsection (2) to the employer surplus account in another fund where the employer is a participating employer;*

Effective date: 1 March 2019.

7. Section 3(5): Exercise of powers and performance of duties

From 1 April 2012, section 3(5) allowed the Commissioner for the South African Revenue Service to delegate the function to approve or to withdraw an approval of a retirement fund for tax purposes to the Executive Officer of the Financial Services Board.

The Financial Sector Regulation Act came into effect on 1 April 2018. It *inter alia* resulted in a new regulatory body to be established. The Financial Services Board was transformed into the Financial Sector Conduct Authority. Section 3(5) was amended to reflect these changes.

Effective date: Deemed to have come into operation on 1 April 2018.

8. Section 10C: Deduction of previously disallowed contributions against compulsory annuity

Section 10C(2)⁵ allows for member contributions that did not rank as a deduction under section 11F to be used as an exemption against a compulsory annuity income. This section has now been amended to insert the word “prior” before “year of assessment” to make it clear that the contributions not deducted that are referred to are those that did not rank for deduction under section 11F in any *prior* year of deduction, and not the current tax year. The Explanatory Memorandum on the Amendment Act explains the rationale for this as follows: “*This thereby prevents any circular application that could arise from considering the current year’s contributions as the section 10C exemption occurs before the section 11F deduction.*”

Effective date: Deemed to have come into operation on 1 March 2016.

9. Section 11F: Deduction in respect of contributions to retirement funds

Section 11F(2) has been amended to clarify the ordering rule for claiming deduction in terms of section 11F, foreign tax credits in terms of section 6quat as well as tax deductible donations in terms of section 18A to ensure the correct application of the legislation.

Section 11F(4) has been amended to clarify that not only contributions made for the benefit of the employee, but also amounts paid on behalf of the employee, to a retirement annuity fund, should qualify for deduction in terms of section 11F. Paragraph 2(bA) of the Fourth Schedule to the Income Tax Act has also been amended to allow the employer to allow those contributions or payments as a deduction from the member’s remuneration every month.

Effective date: 1 March 2019.

10. Paragraph 6 of the Second Schedule: Deductions on withdrawal or resignation

Paragraphs 6(1)(a)(i)(dd) and 6(1)(a)(ii)(dd) have been amended to include a transfer from a provident preservation fund to a pension fund as a permitted (tax-free) transfer. This is in alignment with the policy intent explained in the Explanatory Memorandum on the Taxation Laws Amendment Bill 2011 for permitted transfers from less restrictive retirement funds to equally or more restrictive funds.

⁵ (2) There shall be exempt from normal tax in respect of the aggregate of compulsory annuities payable to a person an amount equal to so much of the person’s own contributions to any pension fund, provident fund and retirement annuity fund that did not rank for a deduction against the person’s income in terms of section 11F as has not previously been—

- (a) allowed to the person as a deduction in terms of the Second Schedule; or
- (b) exempted from normal tax in terms of this section, in respect of any year of assessment.

The tax free transfers can now be summarised as follows:

FROM	TO
Pension	Pension
	Pension preservation
	RA
Pension Preservation	Pension
	Pension preservation
	RA
Provident	Pension
	Pension preservation
	Provident
	Provident preservation
	RA
Provident Preservation	Pension
	Pension preservation
	Provident
	Provident preservation
	RA
RA	RA

Effective date: 1 March 2019.

Paragraph 6(1)(b)(v)(bb) has been amended by inserting the word “directly” before “from a fund contemplated in subitem (aa)” to make it clear that only one additional transfer from a public sector fund is allowed. For more information on the tax exempt status of pre-March 1998 built up in public sector funds, refer to paragraph 2 of [Legal Update 2-2018](#).

Effective date: Deemed to have come into operation on 1 March 2018.

11. Paragraph 12D of the Seventh Schedule: Updated contribution certificate

Paragraph 12 D has been amended by inserting two new items, (c) and (d), which provide that updated contribution certificates may be supplied where the fund made an error in calculating the fund member category factor, or where an employee’s fund member category changed during the year. The corrected contribution certificates must be supplied to the employer within one month after the date that the error was discovered or should reasonably have been discovered (item (c)) or after the date on which the change becomes effective (item (d)).

Effective date: Deemed to have come into operation on 1 March 2018 and applies to years of assessment starting on or after that date.

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