

Legal Update

5 of 2021:

Artificial withdrawals



The FundsAtWork Umbrella Funds (the Funds) are receiving an increased number of requests from participating employers to grant employees access to their retirement savings by allowing them to resign “artificially” with the express purpose of accessing their withdrawal benefit, then immediately reinstating them. As part of their fiduciary duties, the Trustees of the Funds would like to make all participating employers aware of the stance of the South African Revenue Service (SARS) regarding artificial resignations for employees to access their withdrawal benefit, and the possible consequences thereof.

Participating employers must note the following:

- Allowing access to retirement savings withdrawal benefit through artificial resignation could have serious implications for both the Funds and the participating employer’s scheme. SARS views this type of transaction as a serious violation of the provisions of the Income Tax Act. It could result in SARS revoking the income tax approval of the Funds or of the special rules of the participating employer, or of both.
- To prevent such income tax approval being revoked, the employee’s Fund membership will have to be fully reinstated, as if such artificial resignation never took place. This means the member will have to repay in full the withdrawal benefit paid to them.

Having the Funds’ income tax approval status or that of the special rules of the participating employer revoked will mean that:

- Contributions to the Funds will no longer be tax-deductible;
- The Funds’ investments and the growth thereon will be taxed; and
- The more beneficial basis on which lump-sum benefits are taxed will no longer apply.

These factors combined would make the continued existence of the Funds or the continued participation of the employer in the Funds an unattractive proposition. Furthermore, if the employee has to fulfil the requirement to repay the unlawfully accessed benefit to the Funds, it could result in severe financial hardship for the employee.

When SARS becomes aware of a questionable termination of employment and immediate reinstatement, they will investigate whether there was any circumvention of the provisions of the Income Tax Act. They are then likely to find that although the exit from employment was formally structured as a legitimate resignation, the real intention was deliberately disguised to allow the employee early access to their retirement savings withdrawal benefit.