

Tax Developments

-Retirement Funds & Other

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Key Changes

- Retirement Fund Contributions
- Fringe Benefits
- Distinction between Pension Funds & Provident Funds
- Tax-free threshold in relation to Lump Sums
- The provision of Living Annuities

Retirement Fund Contributions

Current Position

- Employees – 7.5% of retirement funding income (Pension Fund)
- Employers – 20% of approved remuneration
- Retirement Annuities – 15% of non-retirement funding income

Proposed*

- Employees – 22.5% of taxable income for pension, provident & retirement annuity funds
- Minimum Deduction – R12 000
- Maximum Deduction – R200 000

*With effect from 1 March 2012

Example

- Annual Taxable Income – R900 000
 - 22.5% of R900 000 = R202 500
 - Maximum deduction = R200 000 [Clear that threshold is to discourage the use of retirement annuities to reduce taxable income for high income earners]
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- Annual Taxable Income – R51 000
 - 22.5% of R51 000 = R11 475
 - Minimum deduction = R12 000 [Tax relief directed at lower income earners]

Threshold

- As soon as the “cap” of R200 000 is reached, higher income earners will suffer a negative income tax effect

$$R888\ 888 @ 22.5\% = R200\ 000$$

Fringe Benefit

- From 1 March 2012 Employer's contribution on behalf of an Employee – deemed to be fringe benefit in Employee's hands
- Not clear what is meant by “on behalf of”
- In context of employer contributions to medical scheme, fringe benefit arises in relation to contributions made for the “benefit of” the employee
- In the case of medical aid scheme where employer contribution cannot be attributed to particular employee – apportionment method

Fringe Benefit

- Will effect salary sacrifice mechanisms – employer contribution to provident fund taxable as fringe benefit

Pension v Provident Funds

- Lump sum benefits from Provident Funds to be subject to one-third limit
- Rationale: “To protect workers’ savings”
- Existing rights protected, implementation subject to consultation with Trade Unions & other interested parties

Tax Free Threshold

- Increase tax-free lump sum on retirement from R300 000 to R315 000 w.e.f 1 March 2011
- Trend: More attractive tax benefits on retirement than withdrawal
- Assumed disallowed contributions (over the 200K threshold) will rank for deduction on retirement in terms of the Second Schedule

Living Annuities

- Currently only provided by Long-term insurers
- Proposal to broaden list of service providers
- “To encourage competition”
- Collective Investment Schemes
- National Treasury’s Retail Savings Bond Scheme

Other Developments

Commissioner for the South African Revenue Service v NWK Limited (SCA)

- Changed the landscape in relation to transactions lacking in commercial substance
- Most extreme judgment in the so-called “substance over form” cases incl. Erf 3183/1 Ladysmith (Pty) Ltd & Ano v Commissioner for Inland Revenue & Relier (Pty) Ltd v Commissioner for Inland Revenue

CSARS v NWK Limited

- Facts involved a financing transaction using maize as the means to repay loan
- Use of SPVs (Momentary role played)
- Circular flows of maize
- Set-off contemplated at the outset
- Fiction of delivery still took place
- Essence: Enhanced “Loan” of R96m : True Loan of R50m
- Claimed deductions on artificial loan

CSARS v NWK Limited-The Crux

Lewis JA “In my view the test to determine simulation cannot simply be whether there is an intention to give effect to a contract in accordance with its terms. Invariably where parties structure a transaction to achieve an objective other than the one ostensibly achieved they will intend to give effect to the transaction on the terms agreed. The test should thus go further, and require an examination of the commercial sense of the transaction: of its real substance and purpose. If the purpose of the transaction is only to achieve an object that allows the evasion of tax, or of a peremptory law, then it will be regarded as simulated. And the mere fact that parties do perform in terms of the contract does not show that it is not simulated: the charade of performance is generally meant to give credence to their simulation.”

CSARS v NWK Limited

- Commerciality principle not confined only to tax
- Taxpayers can no longer argue that tenor of agreements were given effect to in the absence of proper commercial rationale
- New layer of commerciality introduced
- SARS can now question and attack transactions that lack commercial substance on more aggressive basis than ever before
- Commissioner for Inland Revenue v Conhage (Pty) Ltd – Real commercial substance