

# Recent and upcoming tax changes relevant to retirement funds .

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# Agenda

- Tax issues flowing from Taxation Laws Amendment Act 2020 (enacted 20 January 2021)
- Tax proposals in the Budget Review 2021
- SARS: removal of practice notes - GN18: GN 16
- De minimis amounts

# Taxation Laws Amendment Act 2020

- Annuitisation of Provident funds ( separate session)
- Paragraph 2B of the Fourth Schedule
- Deduction of own contribution to retirement funds (Paragraph 5 and 6 of the Second Schedule)
- Withdrawing retirement funds – Three year rule
- Estate Duty – non deducted contributions on death used to purchase an annuity
- Changes to the definition of living annuity in relation to trusts and the new paragraph 3B
- Textual amendments to section 10C.

# Background to Paragraph 2B of Fourth Schedule

- Postponed to 1 March 2022
- Retirement fund administrators withhold PAYE on pensions
- Insurers withhold PAYE on compulsory annuities and voluntary annuities
- Each administrator applies the tax tables to the pension/ annuity as if it were the taxpayer's only source of PAYE income.
- The rebates are applied to each annuity
- If an annuity is the only source of PAYE income, the annual tax rebates will have been applied once
- Sometimes annuitants have more than one source of PAYE income, such as salary from an employer or two annuities being paid from two different administrators or insurers.
- each administrator deduct PAYE as if it is the Taxpayers only source of income
- The consequence is that the annual tax rebates are applied more than once.
- Shortfall on assessment - rebates and bracket Creep
- Taxpayers have cashflow problems - spent the refund
- Original draft Bill in 209 – intention to alleviate cashflow of surviving spouses

# Paragraph 2B of the Fourth Schedule

- Applies to.... All retirement funds; or
- a person that pays an annuity amount as defined in section 10A (1) shall,
- when deducting or withholding PAYE
- disregard the Rebates
- where the annuitant receives remuneration from more than one employer
- if the Commissioner, pursuant to an application made by that person, issues a directive that the amount must be disregarded,.

# Paragraph 2B of the Fourth Schedule

- Final legislation - applicable to all fund annuities and section 10A annuities
- Technical omission – compulsory annuities from insurers
- How do administrators get the information to determine if another source of PAYE income?
- Which administrator gets to apply the rebate?
- **Para 2(2)** already provides a solution *“taxpayer may ask the administrator in writing to withhold more PAYE than is required to avoid shortfall on assessment*
- Proposed this as a solution
- Awaiting a meeting with SARS – to find a practical solution.

# Estate Duty -non deducted contributions on death used to purchase an annuity

- Section 3(2)(bA) Of Estate Duty Act
- Originally all death benefits from retirement funds were Estate Duty free
- Death bed lump sums to RA funds
- Amendment that lump sums that were not tax deductible were estate dutiable if they were tax free for the beneficiary
- But what if the beneficiary took an annuity?
- In the previous Act - was clarification that if the lump sum was used to purchase an annuity by the beneficiary, then it would not be dutiable.
- Badly drafted so better clarification

# Three - year uninterrupted residence test on ceasing residence from SA

- Effective 1 March 2021
- Introduced following announcements regarding the phasing out of emigration for individuals and replacing emigration with a verification process based on tax, risk and source of funds.
- **The law prior to 1 March 2021 –**
  - members of RA funds could withdraw their funds from an RAF and later a Preservation fund on having officially emigrate from SA; and
  - Expiry of a visa (no Change)

**NB:** It only applies to Preservation Funds where the person has already taken their one allowable pre- retirement withdrawal.

- Does not apply to pension/provident funds
- Deferred members of funds had to transfer to preservation or RAF funds to get an emigration withdrawal benefit.



## After 1 March 2021

- Definitions of Retirement annuity fund; Pension preservation fund: Provident preservation fund

### **New three -year rule**

- On or after 1 March 2021, a member may only withdraw the full amount of the retirement fund as a cash withdrawal benefit if the member is a non-resident for an “uninterrupted period of three years” or longer.

### **Limited retention of emigration status**

Although the concept of emigration is being phased out, a limited acknowledgement of emigration status will be retained in two ways:-

- If a member is or was a resident and that person has officially emigrated from the Republic; and
- If an application for official emigration is received by the SARB on or before 28 February 2021, and it is approved before 28 February 2022;

# Questions on implementation of 3 year- rule

- Much media hype
- Sole motive was phasing out of emigration
- Refused submission on reducing 3 - year rule to non-residency only
- Numerous questions on implementation of 3-year rule
- Meeting held with SARS
- Onus on taxpayer to prove non-residence for 3 years to fund administrator
- Difficulties of proof discussed
- ASISA and IRFA to make submission on suggested declaration and supporting documents
- Submission made on proposed declaration and supporting documents
- Awaiting response – not in updated external guide
- Applicable to non-residents before 1 March 2021 who can prove 3 years non-residence to the fund administrator
- No need to have previously told SARS of their cessation of SA residency? Sufficient to provide proof to administrator.
- Declaration of non-residence only in tax returns since 2019

## External guide '*Tax Directive: Emigration, cease to be resident and expiry of visas – Emigration*

- Guide updated – emigration requirements seem to be the same
- Manual Form B or C
- Emigration withdrawal can still be used if MP 336(b) submitted before 1 March 2021.
- Letter from authorised dealer to confirm that emigration was recognized by the SARB for the purposes of exchange control
- Copy of the TCC iro emigrations issued by SARS or an affidavit indicating why the TCC cannot be provided
- Copy of Tax Compliance Status –Pin issued
- If DTA, certificate of residence from the tax authority in the country of residence
- Immigration and citizenship certificate- If no DTA
- A letter that the DTA must be taken into account.
- Date of emigration

## External guide *'Tax Directive: Emigration, cease to be resident and expiry of visas* Industry

- Certificate of residence not older than 6 months issued by the Tax Authority of the country of residence.
- The fund administrator must ensure that the member was not a resident for an uninterrupted period of three years or longer from date of ceased to be a resident.
- There is a field in the tax directive for date of cessation of residence
- The documents that may be accepted by the Fund for this purpose are passports indicating the entry in and out of SA, assessments issued by the country of residence, **etc.**
- The taxpayer must inform SARS as soon as he / she ceased to be an SA resident. SARS system will be updated with the information. If the member did not inform SARS the application will be rejected. ( unclear )
- Doesn't mention the Tax Clearance Status – but assume that Tax Clearance Status must be applied for and a TCS Pin must be provided to the authorised dealer
- No declaration and doesn't include ASISA submission

# Definition of living annuity relating to trusts and the new paragraph 3B of Second Schedule

**(eA)) inserted in the definition of living annuity as follows”**

*in anticipation of the termination of a trust, the value of the assets referred to in paragraph (a) must be paid to the trust as a lump sum pursuant to that termination .*

## **New Paragraph 3B**

Deems the assets to have accrued to the trust immediately prior to the termination of the trust and taxed in terms of Second Schedule.

## **Submissions**

- Problematic drafting - cannot be paid to a trust, if the trust is terminated.
- Existing living annuity policies, do not provide for benefits to be paid out on the death of the owner/trust who is not the life assured. So, the legislation is at odds with the law of life insurance where benefits pay out when the life assured dies.
- Deemed to have accrued to the trust – what if the policy does not pay out on “death of the trust”
- To put this in perspective, it will apply very rarely, when a trust which owns a living annuity policy, terminates.

# Deduction of own contributions (Paragraph 5 & 6 of the Second Schedule)

- Applies to lump sums on exit from a fund
- Contributions that did not qualify for a deduction in terms of section 11F are tax free
- It's a deduction
- Refers to "the person's own contributions", which inadvertently prevents employer contributions to qualify for deduction.
- "Own contributions" replaced with "any contributions".
- The effective date is 1 March 2016.

# Textual amendments to section 10C

- Same issue
- Also alignment with section 11F –
- Own contributions changed to “any contributions” so that contributions made by an employer on behalf of the member that did not rank for a deduction will be taken into account and not just “own contributions”

# Withdrawal of Practice Notes

- GN 18
- GN 16



# Withdrawal of GN 18

- GN 18 – pursuant to industry agreement
- purchase annuities in the name of the member from an insurer on retirement.

## **Three methods:-**

- An annuity paid by the fund;
- An annuity bought for the member by the fund from an insurer, and
- An annuity bought from an insurer in the name of the member.

only one of the “methods” and not a combination of methods.

- IRFA - Repeated submissions to use a combination
- sections 37A and 37B of the Pension Funds Act to apply to member owned annuities.
- non-commutable and payable for the lifetime of the member.
- On 1 March 2021, GN18 withdrawn because “the notes had become obsolete as a result of the updated legislation”

# ASISA and IRFA submissions

- ASISA asked – what intervening legislation?
- IRFA meeting – questioned SARS – replied Regulation 39?
- Noted that Regulation 39 applied to payment methods only
- SARS asked for a submission
- Concerns whether Pension Funds Act extended section 37A and B to member owned annuities?
- Commutation of Living annuities governed by “living annuity” in the Income Tax Act,
  - Without GN 18, are guaranteed annuities arguably commutable?
- Certainty has been requested in the COFI Bill

# Non- Binding opinion from SARS

- GN 18 followed industry agreement.
- ITA – *the Commissioner may approve a fund subject to such limitations or conditions as **he may determine**,*
- Section 1(1) - permits the Commissioner to prescribe additional limitations and conditions for the approval of rules of retirement funds.
- General Note 18 and 18A was issued in terms of this discretion of the Commissioner.
- The industry agreement still prevails even in the absence of GN 18 and 18A in line with the Commissioner's discretionary power.
- The rules of a fund prevail and may provide for a member owned annuity.

## Non- Binding opinion from SARS – methods of payment

- the rules of retirement funds may provide for –
  - paying the annuity directly,
  - purchasing the annuity in the name of the fund, and
  - purchasing the annuity in the name of a retiring member
- This is in line with Regulation 39 of the Pension Funds Act which requires trustees to have an annuity strategy for members

# Non-Binding opinion from SARS – commutation and creditor protection

The annuity so purchased, as with an annuity in the name of a retirement fund or paid directly by such a fund, must be:-

- compulsory, non-commutable, payable for and based on the lifetime of the retiring member; and
- not be transferred, assigned, reduced, hypothecated or attached by creditors as contemplated by the provisions of sections 37A and 37B of the Pension Funds Act.

## **The Income Tax Act**

- up to 1/3 commuted – “remainder paid in the form of an annuity”
- Doesn't prescribe whether annuity must be provided by the retirement fund/from insurer the nature/characteristics of such an annuity

## **Pension Funds Act- s 37A and B**

- .....including an annuity purchased by the retirement fund from an insurer for a member
- no distinction between member owned and fund owned annuities.
- No reinstatement of GN 18 – even until COFI

# Withdrawal of GN 16

- **Part 1:** not more than 1/3 retirement interest commuted for a single payment, except where two-thirds of the total value does not exceed R50 000 or where the member is deceased; (now R165000 or R247 500)
- In RAF's or pension preservation funds with multiple contracts, the "retirement interest" is the total value of all the policies under the fund on any particular "retirement date"
- Aggregation of all the policies to determine whether the R75 000 will be exceeded
- **Part 2: Guaranteed Annuities:** If no previous commutation, may commute on condition that the total value of the "retirement interest" did not exceed R75 000 on the "retirement date" of the member
- If member commuted before, or unable to determine - R50 000
- Without GN 16 –No commutation?

# De minimis amounts

**De minimis surrender value on RAF's** – from R7000 to R15000 – awaiting Gazette

**De minimis – Living annuities - R125 000**

Per living annuity

SARS aggregating with same insurer

**Removal of GN 16**

- No commutation of guaranteed annuities?

**Retirement funds**

- R247 500
- GN 16 aggregation at fund level
- Without GN 16?
- SARS systems aggregate at fund level

# Proposals in Budget review

- Deemed withdrawal of retirement fund when individual ceases to be a resident
- Transfers between retirement funds by members who are 55 years or older
- Clarifying the calculation of the fringe benefit in relation to employer contributions to a retirement fund
- Allowing members to use a retirement interest to acquire annuities on retirement – **(we think it means allowing different methods as was prohibited in GN 18)**



# Deemed withdrawal prior to becoming non-resident

- When member ceases to be a tax resident, deemed to have withdrawn the day before.
- Reason- Provisions of the tax treaty between South Africa and the new resident country will result in South Africa forfeiting its taxing rights.

## Government proposes:-

- A deemed withdrawal tax
- The deemed withdrawal will incur interest
- Payment of tax and interest deferred until actual payments arising on withdrawal, retirement, death,
- The tax on exit will be calculated based on the prevailing lump sum tables on actual exit or in the form of an annuity
- A tax credit will be provided for the deemed retirement withdrawal tax as calculated when the individual ceased to be a South African tax resident.
- Submission made on concerns expressed in advance of the legislation.

# Transfers between retirement funds by members who are 55 years or older

*Government proposes allowing tax-free transfers into more or similarly restrictive funds by members who have already opted to retire.*

- **paragraph 6A** of the Second Schedule read with paragraph **2(1)(c)**
- Applies to deferred members after retirement from employers but not from the fund
- **Para 2(1)(c)** - *“ 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... para 6A”*
- **Para 6A** is quite restrictive. It only allows the deduction from a pension fund to a pension preservation fund or retirement annuity fund; and
- from a provident fund into a pension preservation , provident preservation fund and or a retirement annuity fund.
- Unclear how they intend to amend it.

# Calculation of the fringe benefit in relation to employer contributions

- From 1 March 2016, all employer contributions to a retirement fund are fringe benefits for employees.
- On defined benefit contributions, the fringe benefit is calculated in accordance with the seventh schedule and the employer must provide the employee with a contribution certificate.
- Sometimes a retirement fund has a defined contribution component and a self-insured risk benefit
- Self-insured risk benefits are not considered a defined contribution component
- It is proposed that self-insured risk benefits be classified as a defined contribution component so that those funds with self-insured risk benefits can provide the fringe benefit value based on the actual contribution

THANK YOU

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