VERBATIM
March 2021
ISSUE 60

RETIREMENT FUNDS AND EMIGRATION – RECENT TAX CHANGES

Tax legislation is changing for certain types of funds for members that leave South Africa. Amended legislation will become effective on 1 March 2021 (the Taxation Laws Amendment Act, 2020) that will affect how members of *preservation funds and retirement annuity funds* access benefits when they leave South Africa.

In the past…

Before the change to legislation, if a member of a retirement annuity fund completed 'financial emigration' the member could then withdraw from a retirement annuity fund before the age of 55, pay the tax and take the money with them when they left South Africa. Without this exception, a member of a retirement annuity fund (other than in limited circumstances) may only access their benefits from the age of 55.

Understanding the meaning of 'financial emigration'
This is where a South African citizen changes their residence status from 'resident' to 'non-resident' with the South African Reserve Bank for exchange control purposes. It is an administrative process through the South African Reserve Bank to cease being a South African exchange control resident.

TAX RESIDENCY

In the 2020 National Budget, Government, as part of the modernising of the foreign exchange control system, announced the phasing-out of the concept of financial emigration and referred to the fact that emigration is not automatically a factor that results in cessation of tax residency.

It is important to distinguish between being a tax resident on the one hand and being an exchange control resident on the other. If a member wants access to their retirement annuity fund benefits, under the amended legislation, it will be tax residency that will determine whether they get access to these benefits.

THE POSITION FROM 1 MARCH 2021

From 1 March 2021, *a member will only be able to access their retirement annuity fund benefits once they have ceased to be resident for tax purposes and have been a non-resident for tax purposes for three consecutive years following 28 February 2021.*

How the amended legislation will work in practice is yet to be seen but it is likely that stricter verification procedures will be put in place.

It is arguable, that if a person has been overseas for a while and, thus, has been a non-tax resident for three years already, then they will not have to emigrate for exchange control purposes and may access their retirement annuity fund benefits now.

VERSO®
FINANCIAL SERVICES (PTY) LTD
Tel: (021) 943 5300 or 0861 88 88 81 | Fax: (021) 917 4600
E-mail: info@verso.co.za | Web: www.verso.co.za
An authorized Financial Services Provider. License number 14985

SOME LEEWAY

If a South African finalises their financial emigration or has submitted a full application to the South African Reserve Bank, before 1 March 2021, then they may still take their retirement annuity fund or preservation fund benefits under the old rules and will not have to wait the three year period.

PRESERVATION FUNDS

The permitted once-off withdrawal from preservation funds remains unchanged and may be taken prior to normal retirement date and after the payment of tax. Thus, members of preservation funds may continue to use this mechanism to obtain access to their preservation fund benefits as a cash lump sum. The remainder of preservation fund benefits are then locked in until retirement

Preservation funds will be subject to the same amended tax legislation. From 1 March 2021, a member will only be able to access their preservation fund benefits once the member has ceased to be resident for tax purposes and has been a non-resident for tax purposes for a period of three consecutive years following 28 February 2021.

PENSION AND PROVIDENT FUNDS UNAFFECTED BY THIS CHANGE

Pension and Provident funds remain unaffected by the amended legislation referred to above, as a member who leaves employment always has the option to take benefits as a cash lump sum (after paying the tax) and use their foreign exchange allowances to move the money out of South Africa.

We do, however, expect to see amendments affecting pension and provident funds and members leaving South Africa in proposed legislation going forward.

Tel: (021) 943 5300 or 0861 88 88 81 | Fax: (021) 917 4600
E-mail: info@verso.co.za | Web: www.verso.co.za
An authorized Financial Services Provider. License number 14985

Financial Inclusion Paper

At the same time the Medium-term Budget Policy Statement was published, National Treasury published the first draft of the Financial Inclusion Policy Paper, "An Inclusive Financial Sector for All" ("the Paper") for public comment. It aims to establish a policy framework for financial inclusion in South Africa. Treasury is of the view that financial systems have substantially developed in South Africa in the past 20 years, however, financial systems have not sufficiently closed the gap that exists in access to financial services by individuals and small, medium and micro enterprises (SMMES). In addition, international and domestic factors such as the pandemic, low economic growth, continuing high unemployment levels, increasing consumer prices, and greater household dependency on credit, impact negatively on household and business financial health.

The Paper explores what needs to be done to:

a) deepen the financial inclusion of individuals,

b) extend access to financial services for SMMES; and

c) to leverage a more diversified provider and distribution base for financial services in South Africa.

Budget 2021 stated that 20 institutions provided comments on the Paper and that National Treasury will facilitate workshops with stakeholders to discuss these comments before finalising the Paper this year. It will also work with industry and civil society working groups and forums to develop a financial inclusion strategy, including a monitoring mechanism, to assess the state of financial inclusion and the impact of this policy.

The Conduct of Financial Institutions Bill

The first draft of the Conduct of Financial Institutions Bill (COFI) was published for public consultation in December 2018. The second draft was published on 29 September 2020 for public consultation.

As a reminder:

- COFI is a key pillar in government's Twin Peaks financial sector regulatory reform process that aims to entrench better financial customer outcomes in the South African financial sector. It is a financial institution-facing law that mostly sets conduct principles for financial institutions to meet (principle–based legislation).
- The overall approach is the application of overarching principle-type requirements to categories of activities and financial institutions. However, it is acknowledged that more detailed requirements, delivered by way of conduct standards, are necessary to support the overarching principles in certain circumstances.
- COFI will significantly streamline the legal landscape (i.e. the laws that financial institutions are currently subject to) for conduct regulation of financial institutions and others.
- One of the aims of COFI is to give legislative effect to the market conduct policy approach, including implementation of the Treating Customers Fairly (TCF) principles. COFI ensures that the TCF principles are legally binding and enforced on all financial institutions.

The National Treasury is engaging stakeholders to discuss and clarify comments received and a revised draft of the Bill will be tabled in Parliament in 2021.

Transformation and financial inclusion

The Financial Sector Transformation Council established seven subcommittees to review the targets in the Financial Sector Code to strengthen transformation. The subcommittees are developing targets for management control and skills development, socioeconomic development and consumer education, *retirement funds and ownership*, access to financial services, preferential procurement and empowerment financing.

It was stated that this tax year the subcommittees will finalise and submit the revised targets to the Financial Sector Transformation Council for approval and then to the Department of Trade, Industry and Competition to publish for public comment.

Access to retirement fund monies by members

In the Medium-term Budget Policy Statement, the Minister recognised that retirement funds are designed primarily to promote life-cycle savings, and encourage individuals to save while working to provide an income when they retire. However he stated that Treasury had received a number of proposals to enable limited pre-retirement withdrawals from retirement funds, especially during times of a disaster like the COVID-19 pandemic. He went on to state that Treasury has consulted with NEDLAC partners to introduce the necessary legislative amendments next year to allow for limited withdrawals under certain circumstances, but linked to mandatory preservation requirements.

Continuing with this theme, in Budget 2021 the Minister recognised that the Covid-19 pandemic had influenced many other countries to allow members of retirement funds to access their retirement savings. He reiterated what was stated in the Medium-term Budget Policy Statement and further that Government continues to engage with trade unions, regulators and other stakeholders to discuss how to allow these withdrawals, together with mandatory preservation requirements.

The long-awaited Levies Bill

This Bill is still awaited. The Minister stated that with the implementation of Twin Peaks, regulated institutions in the financial sector will be expected to pay a levy towards regulatory costs. It was stated that the Bill is expected to be tabled in Parliament in "early 2021" and the resulting revenue will fund the Prudential Authority, the Financial Sector Conduct Authority and other entities and activities outlined in the Financial Sector Regulation Act.

RETIREMENT FUNDS – THREE TECHNICAL AMENDMENTS TO THE INCOME TAX ACT

The Budget Review includes four proposed technical amendments in order to correct anomalies in the Income Tax Act. Given the information currently available, the amendments are not yet fully understood and consideration will be given to the final wording of the proposed amendments, once available.

Annuities on retirement

The first proposed amendment refers to the circumstance when a member retires and can commute an amount for cash and take the rest as an annuity. Depending on the rules of the fund, that annuity can be provided by the fund, purchased from an insurer in the name of the fund or purchased from an insurer in the name of the member. Treasury referred to the aim of increasing flexibility for a retiring member and maximising the retirement capital available to provide for an annuity by expanding the amount of retirement interest that may be used to acquire annuities.

Non tax residents who retire from a fund or who die

Treasury provides background to the effect that if a member of a fund ceases to be a tax resident and later retires from the fund or dies, the Income Tax Act deems such amounts to be from a South African source, thus remaining within the South African tax jurisdiction, despite the member no longer being a South African tax resident. However the member is already a tax resident of another country and the benefit may be subject to tax in that country and not South Africa as a result of a tax treaty.

Thus, government proposed a change to the Income Tax Act such that when the member ceases being a tax resident in South Africa the member will be deemed to have withdrawn from the fund on the day before he/she ceases to be a South African tax resident.

What appears to be proposed is that if the member then leaves their monies in the fund until retirement or death then the tax (and interest) on the deemed withdrawal will be deferred until the monies are paid out of the fund or the member retires. When payments are actually received from the fund the payments will then be taxed.

Transfers between retirement funds of retiring members who are 55 years or older

Government refers to members who have already opted to retire and want to transfer their fund benefits to another fund and are considering an amendment to ensure that such members can transfer tax-free to a similarly restrictive or more restrictive fund.

Clarifying the calculation of the fringe benefit for employer contributions to a retirement fund

Treasury provides the following background:

"From 1 March 2016, all employer contributions to a retirement fund on behalf of employees were considered taxable fringe benefits for the employees. If the contribution contains a defined benefit component, the fringe benefit is calculated and the employer must provide the employee with a contribution certificate. An anomaly arises in instances where a retirement fund provides both a retirement benefit in relation to the defined contribution component and a self-insured risk benefit. The current interpretation of the legislation would result in the classification of the total contribution to the fund as a defined benefit component because self-insured risk benefits are not considered a defined contribution component."

Thus, Treasury has proposed that:

"… self-insured risk benefits be classified as a defined contribution component to ensure that retirement funds that provide both defined contribution component retirement benefits and self-insured risk benefits can provide the fringe benefit value based on the actual contribution".

UNEMPLOYMENT INSURANCE FUND (UIF) CONTRIBUTION CEILING

The ceiling for contributions to UIF has not been increased in the last four years, despite the increase in the benefit ceiling. The contribution ceiling will therefore return to be in line with the benefit ceiling and set at R17 711.58 per month from 1 March 2021.

FUEL LEVY, ROAD ACCIDENT FUND LEVY AND SIN TAXES

- An inflation-linked general fuel levy increase of 15c per litre for petrol and diesel.
- An above-inflation increase of 11c per litre for the Road Accident Fund levy.
- Smoking and drinking will be 8 per cent more expensive.