Legal Services
FINANCIAL SERVICES

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ON THE SCALES 6 of 2018

Taxation Laws Amendment Act, 2017, signed on 18 December 2017

The President has signed the Taxation Laws Amendment Act 2017 (‘the TLAA’) and the Tax Administration Laws Amendment Act 2017 (‘the TALAA’) and they are now law.

These Acts provide clarity on certain technical issues and also introduce new administrative requirements for tax purposes.

As a reminder, we covered the provisions of the TLAA when it was still a Bill in *On the Scales 12 of 2017.*

Summary

In the Taxation Laws Amendment Act 2017 (‘the TLAA’) the following items are of interest to retirement funds and their members:

1. The annuitsation requirements for provident funds will be postponed to 1 March 2019.
2. Retiring members of occupational funds, will now be given the option of preserving their retirement benefits in a retirement annuity fund.
3. The tax exempt status in respect of pre-March 1998 benefits, will apply in cases where one additional transfer occurs to a different fund of the benefits which originate from a public sector fund.
4. The 12-month limitation on employees joining a newly established pension or provident fund has been removed from 1 March 2018.
5. Technical correction to section 11 of the Income Tax Act (‘the ITA’) to deal with deductions in respect of contributions to retirement funds.
6. Partial repeal of the foreign income employment exemption (section 10(1)(o)(ii)) of the ITA) with effect from 1 March 2020. Foreign income earned by residents will no longer be fully tax exempt, excepting for the first R1million of remuneration each year.

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1. Postponement of annuitisation requirements for provident funds to 1 March 2019

The annuitisation requirements for provident funds has been postponed for 1 year from 1 March 2018 to 1 March 2019 and will apply in respect of the years of assessment commencing on or after that date.

2. Transferring retirement fund benefits after reaching a retirement age

Currently, on reaching a retirement age in terms of the rules of the fund, members can elect when to retire. The date on which the lump sum benefit accrues to members (for tax purposes) is the date on which members elect to retire and receive the payment of their benefit from the fund and not on the retirement age. This change came into effect when paragraph 4 of the Second Schedule was amended with effect from 1 March 2015. [refer to *On the Scales* 1 of 2015]

From 1 March 2018, changes have been made to the ITA to allow retiring members to transfer their benefits into a retirement annuity fund, after retiring from employment but before the date on which a member elects to retire from the fund.

Comment: While members may retain benefits within their funds, they may no longer make contributions to these funds. Retiring members have the option to transfer their retirement interest in their occupational fund to a retirement annuity fund, which may allow for further contributions to be made by these members if the rules of the retirement annuity fund permit this.

3. Tax exempt status of pre March 1998 buildup in public sector funds.

The Second Schedule of the ITA, currently allows for the determination of amounts to be included in gross income for lump sum amounts arising from public sector funds in terms of the prescribed formula.

It further allows for the tax free withdrawal of pre-March 1998 benefits:

- when they are withdrawn from a public sector fund, and
- when they are withdrawn from the fund to which they were transferred, that is, the pre –March 1998 benefits that were transferred from the public sector fund to a private sector fund.

Where employers decide to merge or consolidate with other employers forming new funds, the exemption applying to pre- March 1998 benefits no longer applies as that exemption only applies as mentioned above.

From 1 March 2018, the Second Schedule will allow for the exemption, in respect of pre-March 1998 benefits, to apply in cases where one additional transfer to a different fund occurs if the benefits were originally coming out of a public sector fund. This change is aimed at addressing the issue of unfairness.

4. Removing the 12-month limitation on joining a newly established pension or provident fund

Previously there was a limit of a12-month period for joining a newly established pension or provident fund.

To encourage employees to contribute towards their retirement and remove practical difficulties, from 1 March 2018, the limit of a 12-month period is removed so that employees are allowed to join a newly established pension or provident fund at any time, subject to the rules of the fund.

5. Deduction in respect of contributions to retirement funds

On 1 March 2016 the tax deductibility of contributions to retirement funds was harmonized across all retirement funds through the replacement of section 11k, where the same deduction now applies to both the employer and employee contributions to pension funds, provident funds and retirement annuity.

The inclusion of the deduction in section 11(k) has created technical complications. The opening proviso states that deductions under section 11 relates to taxable income derived from the carrying on of a trade.

However, not all allowable contributions to retirement funds relate only to income generated from the carrying on of a trade.

Before 1 March 2016 the ITA contained specific exemption for retirement annuity funds under 11(n)(i)(ff), seeing that contributions to retirement annuity funds did not relate to income that is generated from carrying on a trade.

The provision dealing with deductions for contributions to retirement funds under section 11(k) has created some anomalies such as generating an assessed loss from contributions to retirement funds that are above the allowable limit when taxable capital gains are a part of the higher limit.

Section 11k has been deleted to remove the inconsistencies and anomalies created by provisions in the ITA that allow for a limited deduction for retirement fund contributions under section 11(k).

A new section 11F has been inserted into the ITA to allow for a tax deduction for contributions to all retirement funds, harmonizing tax deductibility to retirement funds and this includes contributions that are made to retirement annuity funds. [refer *On the Scales* 2 of 2016]

The amendment is deemed to have come into effect on 1 March 2016.

6. Repeal of the foreign income employment exemption-section 10(1)(o)(ii) of the ITA postponed to 1 March 2020

From 1 March 2001 South Africa moved to a residence based system of taxation (previously source based). This means that South African tax residents are subject to tax on their worldwide income.

Section 10(1)(o) of the ITA exemption was extended to include South African residents who are rendering services outside South Africa for a period which, in aggregate, exceeds 183 full calendar days during any period of 12 months commencing or ending during a year of assessment.

The exemption does not apply in respect of remuneration derived from services rendered outside South Africa if the taxpayer's employer is the government or any public or municipal entity or the taxpayer holds a public office position.

South Africa has concluded double taxation agreements ("DTAs") with many countries. The main purpose of a DTA is to eliminate double taxation of the same income, by allocating taxing rights between the source state and the residence state.

When the section 10(1)(o)(ii) exemption was introduced in 2001, the main purpose of this exemption was to prevent double taxation of the same employment income between South Africa and the foreign country.

The current exemption creates opportunities for double non-taxation in cases where the foreign country does not impose income tax on the employment income or taxes on employment income are imposed at a reduced rate.

The current section 10(1)(o)(ii) exemption will be amended with effect from years of assessment commencing on or after 1 March 2020 and foreign income earned by residents will no longer be fully tax exempt. An amount of R1million of remuneration will remain exempt from tax each year.