Sanlam

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Insurance | Financial Planning | Retirement | Investments | Wealth

Newsletter of Sanlam Corporate: Legal

1. Taxation Laws Amendment Act, 2020 (“the Amendment Act”)

The Amendment Act was published in the Government Gazette on 20 January 2021. The amendments affecting retirement funds are as set out below. All references to “the Act” are to the Income Tax Act.

Annuitisation of retirement benefits from provident funds and provident preservation funds

[Applicable provisions: The definitions of the various types of retirement funds in section 1 of the Act]

The Amendment Act confirms that the compulsory annuitisation of provident fund and provident preservation fund retirement benefits, also known as T-day, will go ahead on 1 March 2021. From T-day members of provident funds and provident preservation funds will be compelled to annuitise at least two thirds of their retirement benefits (excluding vested benefits), as is currently the case with pension funds, pension preservation funds and retirement annuity funds.

Should the member retire early or due to ill health, the same rules as with normal retirement would apply, i.e. the early or ill health retirement benefit is subject to compulsory annuitisation, with the exclusion of vested benefits.

Vested benefits, as referred to above, refers to that part of a benefit that is not subject to annuitisation upon retirement, and that can in other words be taken in cash. A member’s vested benefit depends on his/her age at 1 March 2021.

If the member is younger than 55 on 1 March 2021, his/her vested benefit is his/her contributions to a provident fund prior to 1 March 2021, plus growth. At least two thirds of all contributions (plus growth) after 1 March 2021 will have to be annuitised, except if the value thereof does not exceed the commutation threshold of R247 500.

If the member is 55 or older on 1 March 2021, contributions made to a provident fund, or transfers made to a provident preservation fund, on or after 1 March 2021 (and growth thereon) can also be taken in cash, provided that the member remains a member of the provident fund or provident preservation fund of which he/she is a member on 1 March 2021. If the member transfers to another fund after 1 March 2021, all contributions to the provident fund of which he/she was a member on 1 March 2021, plus growth, up to the date of transfer will remain exempted from annuitisation. At least two thirds of all contributions to the transferee fund (plus growth thereon) will however have to be annuitised, except if the value thereof does not exceed the commutation threshold of R247 500.

If a member's fund value consists of a vested and non-vested portion, any deduction in terms of section 37D of the Pension Funds Act will be recovered proportionately from the vested and non-vested portions.

Withdrawing from a preservation fund or retirement annuity fund upon emigration

[Applicable provisions: The definitions of "Pension Preservation Fund", "Provident Preservation Fund" and "Retirement Annuity Fund" in section 1 of the Act]

Currently the definitions of "pension preservation fund", "provident preservation fund" and "retirement annuity fund" in section 1 of the Act make provision for payment of lump sum benefits when a member of any of these funds withdraws from the fund due to him/her emigrating from South Africa, on condition that such emigration is recognised by the South African Reserve Bank for exchange control purposes.

As stated in the 2020 Budget Review, the government will be modernising the foreign exchange control system, and one of the changes will be the phasing out of the concept of emigration for exchange control purposes. In terms of the Amendment Act the definitions of the aforesaid funds are amended to replace the requirement that the emigration must be recognised by the Reserve Bank for exchange control purposes with a new test. The new test will allow payment of lump sum benefits when a member ceases to be a South African tax resident (as defined in the Act), and such member has remained non-tax resident for at least three consecutive years. The implementation date of these amendments is 1 March 2021.

Postponement: Disregarding tax rebates if pensioner has other source of remuneration

[Applicable provision: Paragraph 2B of the Fourth Schedule to the Act]

Paragraph 2B briefly entails that if a taxpayer receives remuneration from more than one source (including a pension from a retirement fund or insurer), the tax rebates applicable to the taxpayer are not to be taken into account by the retirement fund or insurer when calculating the taxes to be withheld on the pension. Any pay-as-you-earn (PAYE) excessively withheld will be refunded by the South African Revenue Service (SARS) upon assessment.

In terms of the Amendment Act the implementation of paragraph 2B is postponed from 1 March 2021 until 1 March 2022.

Clarifying deductions in respect of contributions to retirement funds

[Applicable provisions: Paragraph 5(1)(a) and 6(1)(b)(i) of the Second Schedule to the Act]

Paragraphs 5(1)(a) and 6(1)(b)(i) of the Second Schedule to the Act make provision for a deduction of retirement fund contributions that did not qualify for a deduction in terms of section 11F of the Act, when calculating the amount of lump sum benefits to be included in the member's gross income. These paragraphs until now referred to "own contributions", which inadvertently prevented employer contributions to a retirement fund on behalf of employees (made on or after 1 March 2016) from qualifying for a deduction under either paragraph. This anomaly is removed by replacing the reference to "a person's own contributions" with a reference to "contributions". The effective date of the amendments is 1 March 2016, which aligns with the effective date of section 11F.

Deduction of previously non-deductible contributions from qualifying annuities

[Applicable provision: Section 10C of the Act]

Previously non-deductible retirement fund contributions, which were also not used as a deduction against retirement fund lump sums, can be deducted from a "qualifying annuity", which is a compulsory annuity paid upon retirement.

"Qualifying annuity" with regard to a provident fund and provident preservation fund is currently defined as "the amount of the retirement interest of a person payable in the form of an annuity (including a living annuity) by a provident fund or provident preservation fund". This is accordingly limited to a pension paid directly by a provident fund and provident preservation fund, and does not include a pension purchased from an insurer. This has been corrected by defining "qualifying annuity" in the case of a provident fund and provident preservation fund as "an annuity (including a living annuity) as contemplated in paragraph (b)(iv) of the proviso to the definition of 'provident fund'" and "an annuity (including a living annuity) as contemplated in paragraph (e) of the definition of 'provident preservation fund'". "Qualifying annuity" with regard to a provident fund and provident preservation fund will therefore now include a pension purchased from an insurer.

Section 10C further currently only refers to "own contributions", which inadvertently prevents employer contributions to a retirement fund on behalf of employees (made on or after 1 March 2016) from qualifying for a deduction in terms of section 10C. Section 10C is amended to remove this anomaly, by replacing the reference to "own contributions" with "any contributions".

The above amendments will apply from 1 March 2021.

Living annuity paid to a trust

[Applicable provisions: The definition of "living annuity" in section 1 of the Act and a new paragraph 3B of the Second Schedule to the Act]

A new paragraph (eA) is added to the definition of "living annuity" to allow for a lump sum payment to a trust when a trust in receipt of a living annuity is in the process of being terminated. This means that the lump sum will be taxed on the retirement fund tax table for retirement and death. A new paragraph 3B is also added to the Second Schedule, in terms of which the lump sum shall, on the date of payment thereof, be deemed to have accrued to the trust immediately prior to the date of termination of the trust.

The above applies from 1 March 2021.

Previously non-deductible contributions deducted from death benefit: deemed asset for estate duty purposes

[Applicable provisions: Section 3(2)(bA) of the Estate Duty Act and a new section 3(3)(e)]

Section 3(2)(bA) of the Estate Duty Act up till now included as property of the deceased previously non-deductible contributions to a retirement fund that were allowed as a deduction from the deceased's death benefit. Section 3(2)(bA) is deleted, and replaced by a new section 3(3)(e), the effect of which is that the aforesaid amount is for estate duty purposes no longer regarded as property, but as deemed property.

The above is deemed to have come into operation on 30 October 2019, and applies in respect of the estate of a person who dies on or after that date, and in respect of contributions made on or after 1 March 2016.

2. Deduction from a benefit to compensate the employer for damages suffered because of theft or fraud by a member

The Board of Trustees of a retirement fund ("the Board") is empowered to withhold a member's benefit so as to enable the employer to obtain judgment against the member in respect of damages caused by theft or fraud on the part of the member. The Western Cape High Court has in 2019 in the matter of *SA Metal Group (Pty) Ltd v Deon Jeftha and 2 Others* ruled that before the Board can decide to withhold a member's benefit, "*the employer's case, as related to the fund, must be put to the employee to afford him an opportunity to respond thereto*".

The above decision was confirmed in a recent decision of the Financial Services Tribunal ("the Tribunal") in the matter of *FundsatWork Umbrella Provident Fund v Elvis Eliah Ngobeni and Another*. The Tribunal further ruled that "*the mere satisfaction by the trustees of a fund that the employer has placed allegations before them which, if true, would show damages arising from dishonest conduct by the employee, would not on its own be sufficient*". The Board can only resolve to withhold a member's benefit if they are satisfied that there is "*a well-grounded apprehension of irreparable harm or loss*".

When the Board receives a request from the employer to withhold a member's benefit so as to enable the employer to obtain judgment against the member, the Board must, in view of the above, give the member the *opportunity* to respond to the employer's allegations. The Board would further have to consider all the information before them, and would only be able to withhold the member's benefit if they are satisfied that the employer has a reasonable chance of succeeding with its claim against the member, and that the employer will suffer "*irreparable harm or loss*" if the benefit is not withheld.

The Tribunal has further ruled in the above matter that a deduction can only be made from a member's benefit in the case of a civil judgment, and that a member's benefit may accordingly only be withheld in the case of a civil action, and not in the case of a pending criminal case against the member. This is *somewhat* concerning because, although a mere conviction is not sufficient, the Pension Funds Adjudicator ("the Adjudicator") has on several occasions held that a deduction can also be made from a member's benefit if the criminal court has ordered the member to compensate the employer in terms of section 300 of the Criminal Procedure Act. It remains to be seen whether the Adjudicator will in future cases follow the same approach as the Tribunal. In the meantime the Boards of retirement funds will have to be aware of the risk that the Adjudicator may, in accordance with the Tribunal's decision, rule that a member's benefit may not be withheld pending a criminal case against the member.

3. FSCA Guidance Notice 2 of 2020 (RF): Guidelines on the release of assets backing unpaid surplus liabilities

The Financial Sector Conduct Authority (FSCA) has issued the above Guidance Notice (“the Guidance Notice”), containing *certain* guidelines which a fund should follow when considering the release of a proportion of the assets backing unpaid surplus liabilities in terms of section 15B of the Pension Funds Act, i.e. surplus allocations to former members who cannot be traced.

The background is that the Supreme Court of Appeal has on 2 November 2020 declared regulation 35(4) of the *Pension* Funds Act invalid. Regulation 35(4) provided that where the board of a retirement fund is able to determine the surplus allocation due to a former member, but is unable to trace that former member, the board must place the amount allocated into a contingency reserve account, and the amount may not be released except when making payment to the former member.

The following is *stated in the Guidance Notice regarding the guidelines which a fund should follow when considering the release of a proportion of the assets backing unpaid surplus liabilities:*

“It would be prudent for funds to only take decisions to release any assets having regard to the following:

(a) The board should be able to illustrate the steps taken to identify and trace unclaimed former members within a reasonable period prior to the release of the assets. The Authority considers that reliance on historic and outdated tracing exercises may not be sufficient;

(b) The Board should be able to motivate the assumptions used in determining the assets to be held in respect of the unpaid surplus allocations;

(c) Given that the full obligation remains but that the assets held will be reduced, there is the risk that the assets retained will be insufficient to cover the claims of possible members coming forward in the future. Boards should, therefore, provide for the manner in which the liability will be met, which should be reflected in the rules of the fund; and

(d) Boards are reminded that in the event that the fund may need to transfer the obligation and assets in respect of unclaimed benefits to an unclaimed benefit fund, the unclaimed benefit fund may not be prepared to accept a transfer where the value of assets is less than the full value of unclaimed assets. The board should in such an event indicate its plan of action at the time of submitting the valuation report in term of section 16 of the PFA to the Authority for its consideration.”

4. FSCA Information Request 6 of 2020 (RF): Request for information related to pending transfers in terms of section 14 of the Pension Funds Act

In terms of the above Information Request all retirement funds and administrators that have pending or overdue *section 14 transfers must provide the following information to the Financial Sector Conduct Authority (FSCA) by not later than 31 March 2021 -*

(a) a list of all the pending section 14 transfers on their books; and

(b) a brief project plan of how the fund intends on actioning and finalising each of these section 14 transfers in a structured and prudent manner.

The background to the Information Request is that the FSCA has identified that there are numerous retirement funds that have a backlog of section 14 transfers on their books, which has the potential of impeding fair outcomes for members.

A retirement fund or administrator that fails to provide the above information commits an offence and is liable on conviction to a fine not exceeding R1 000 for each day during which the offence continues.

5. FSCA Communication 56 of 2020 (RF): Supervisory concerns about industry practices related to submission of statutory returns

It is stated in the above Communication that the Financial Sector Conduct Authority (FSCA) is increasingly concerned about the lack of adherence to submission deadlines in terms of the Pension Funds Act for the following statutory returns:

- Annual financial statements;
- Section 14 transfers;
- Valuation reports;
- Surplus apportionment schemes;
- Schemes to bring the fund into a financially sound condition;
- Rule amendments to comply with the default regulations.

According to the FSCA "*funds and administrators have instead opted to submit a large volume of extension applications for matters that can be better managed through improved planning, strengthened* internal controls at administrator level and increased governance oversight by boards and principal officers". It is further stated in the Communication that in order to ensure that funds are the ones requesting an extension, and not the service providers, the FSCA will, as of 1 March 2021, only accept applications signed by the Principal Officer or Deputy Principal Officer and/or a duly authorised member of the Board.

The FSCA will further only under exceptional circumstances consider granting a further extension in respect of the same statutory return submission. The fund would in such a case need to clearly explain the reason the extended deadline has not been met.

It is stated in the Communication that experience has shown that applications for extensions are caused by inter alia poor planning or governance, lack of internal controls, lack of co-operation between the relevant parties and tax directives being declined by the South African Revenue Service (SARS). According to the FSCA these are matters that are within the control of the board of trustees, and the necessary remedies or recourse should be contained in the administrator's service level agreements and administration agreements.

Funds and administrators should further ensure that they are in a position to provide basic information requested by SARS for tax purposes. Funds and employers should ensure that employees and members are on-boarded with all the correct personal information, including identity numbers and income tax numbers, and should verify that they have up-to-date information for all existing employees or members.

The FSCA also reminds funds that failure to submit statutory returns by the due date constitutes non-compliance, and may result in administrative action against the fund, including penalties.

6. FSCA Communication 57 of 2020 (RF): Application forms to be used when applying for extensions

To ensure consistency, and in order to streamline the application processes, the Financial Sector Conduct Authority (FSCA) has developed standardised forms for use by funds and administrators when applying for an extension of any period contemplated in the Pension Funds Act. The forms are annexed to the above Communication. Form II must be used for extensions relating to section 14 transfers and Form I must be used for extensions relating to any other matters.

7. Extension for compilation of manual in terms of the Promotion of Access to Information Act, 2000

In terms of section 51 of the Promotion of Access to Information Act, 2000 ("PAIA"), all public and private bodies (including retirement funds) must prepare a PAIA manual, containing among others the following information:

- address and contact details of the head of the body;
- a notice regarding the categories of records of the body which are available without a person having to request access in terms of PAIA;
- a description of the records of the body which are available in accordance with any other legislation;
- sufficient detail to facilitate a request for access to records;
- a description of the subjects on which the body holds records and the categories of records held on each subject.

A copy of the manual must be submitted to the South African Human Rights Commission. A copy must also be available for inspection at the registered office of the body (e.g. retirement fund). The manual must be updated on a regular basis.

The date of commencement of section 51 was 15 February 2002, but the Minister of Justice and Constitutional Development has granted an exemption from the requirement of submission of the manual and has from time to time extended the exemption. The last extension would have expired on 31 December 2020. The Minister of Justice and Correctional Services has however on 18 December 2020 further extended the exemption for all private bodies, except for certain categories of companies, until 30 June 2021. Retirement funds accordingly now have until 30 June 2021 to comply with the requirements regarding the manual.

8. Consultation Paper on Open Finance

The Financial Sector Conduct Authority (FSCA) has published a consultation paper ("the paper") on Open Finance for public comment. The purpose of the paper is to obtain input in order to develop the FSCA's policy position on Open Finance.

It is stated in the paper that "*Open Finance is a framework to allow consumers and enterprises to access and share their financial data with third party providers who can then use that data to develop innovative products and services with consent*". It is further stated that it relates to all consumer financial services data held by inter alia retirement funds, insurers and intermediaries.

There are three key parties involved in Open Finance:

- financial institutions which collect and store customer data;
- third parties that collect customer data from financial institutions to offer value added services to customers;
- customers whose information is collected and stored with financial institutions during onboarding and product usage.

The paper proposes a set of recommendations that will serve as a basis for licensing, supervision, and enforcement procedures around Open Finance:

- Before consumer financial data is shared, informed consent between the consumer, financial service provider and third-party provider needs to have been obtained. Consumers need to be fully aware of terms and conditions of what they are consenting to and how their data will be used to serve them.
- The financial service provider and third-party provider should have a complaints management process in place to enable them to process and address any customer complaints or issues raised.
- Open Application Programming interfaces (APIs) are proposed as the standard mechanism for data sharing.
- It is recommended that financial service providers share consumers' financial data with third party providers without charging a fee.
- To address data privacy breaches and data misuse without consent, it is recommended that a liability framework is introduced to hold financial service providers and third-party providers accountable. The liability framework should align to chapter 11 of the Protection of Personal Information Act (POPIA).

Sanlam will provide comments on the paper via industry bodies.

Retirement funds or other clients requiring more information should not hesitate to contact their consultant.