Hotline

No 19 / 2011

DRAFT TAXATION LAWS AMENDMENT BILL, 2011

DESCRIPTION OF ISSUE

National Treasury has released the draft 2011 Taxation Laws Amendment Bills for comment.

SOURCES

Draft Taxation Laws Amendment Bill 2011, Explanatory Memorandum on the draft and the Media Statement: www.treasury.gov.za.

BACKGROUND

National Treasury has released the draft 2011 Taxation Laws Amendment Bill, 2011 for comment. This will be followed by briefing of the parliamentary Statutory Committee on Finance (SCOF) and public hearings on the draft Bill. National Treasury then submits comment to SCOF before the drafts are revised and introduced in Parliament. This is expected to be in September. Some of the proposals are mentioned below.

Retirement Income Draw Down Account (RIDDA)

- The definition of living annuity will from 1 March 2012 be removed and replaced by a definition of retirement income draw down account. References in fund definitions, the Second Schedule and other areas of the Act are appropriately amended.
- The RIDDA can be issued by a qualifying person. This is undefined but the intention stated in the memorandum is to extend providers beyond insurers and retirement funds. Encouragement of combining RIDDAs from various sources is aimed at.
- The current maximum draw down rate of 17,5% is in the definition, but there is no minimum. Annual variation is provided for. On transfer from one provider to another, the rate can be varied and thereafter at each anniversary of the transfer. No splitting is allowed in transfer.
- Payments on death have been clarified. They can be in lump sum or draw down account form, or both, where the nominee is a natural person. Only a lump sum is allowable to a non-natural nominee.
- Agreements (presumably this is meant to cover living annuity agreements) concluded after 21 Feb 2007 must contain a provision on these maximum draw down and annual variation limits.

Medical Scheme Tax Credit

- The proposal is to convert the current deduction regime to a tax credit regime to facilitate more equality in the system[1].
- The motivation behind the proposal is that the current dispensation is worth more to higher earners as their marginal tax rates are higher.
- The proposed credit would be R216 per member and R216 per the first dependant and R144 for each additional dependant. An additional R216 would apply to those over 65 or those with a disability.
- For this tax year the contribution deductions have been increased as announced in the Budget: R720 per member and R720 per the first dependant and R440 for each additional dependant.

Long-Term Insurance[2]

Changes made in 2010 to the regulation of employer-owned long-term insurance policies elicited much industry comment. Further revision is proposed to clarify the general principle that

- after-tax premiums generate tax-free proceeds
- pre-tax premiums result in taxable proceeds.

As part of these changes:

- The Seventh Schedule has been changed to include from 1 January 2011 as a taxable fringe benefit: any direct or indirect payment by the employer to an insurer for the benefit of the member, his spouse, child, dependant or nominee. A new paragraph 12C defines the cash equivalent of the fringe benefit.
- The previous CGT exemption for business assurance in paragraph 55 of the Eighth Schedule has been replaced to provide exemption to risk only policies.

The impact of the proposals in respect of group risk policies:

PHI:

- In the current dispensation for group unapproved PHI arrangements, the EE would pay fringe benefit tax on the ER paid premium and then also be taxed on the proceeds of the policy if they became entitled to a disability income benefit (as these benefits are paid as regular income and so fall within a specific provision of gross income catering for payments of an annuity nature).
- The new changes propose to afford the EE a deduction for the ER paid premium that was included in their taxable income as its purpose was to fund an income replacement policy (and individuals are normally afforded these deductions if they had taken out these policies in their own names)

GLA:

- In the current dispensation for group unapproved GLA arrangements, the EE would pay fringe benefit tax on the ER paid premium and not be able to claim a deduction therefore. It was raised via the ASISA tax committee that in this case the EE / dependant should not pay tax on the lump sum proceeds.
- The new changes propose to make it clear that this would be the tax outcome.

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[1] See Did You Know 4/2011 for the effect of tax credit vs a deduction.

[2] See Hotline 28/2010 and Did You Knows 15/2010, 17/2010 and 3/2011.

Severance Benefits

- Severance benefits as defined in the Act, such as retrenchment benefits paid by an employer, must with effect from 1 March 2011, be aggregated with lump sum benefits from retirement funds and be taxed according to the appropriate scale. This confirms the current practice endorsed in correspondence between SARS and ASISA.

Retirement Scale

- As notified in the 2011 Budget Review, the tax scale brackets applicable to retirement fund lump sum benefits derived on retirement, death or retrenchment (and now also to severance benefits from the employer) have been improved from 1 March 2011, with the maximum nil tax rate moving from R300 000 to R315 000.

Transfers of retrenchment benefits to preservation funds

- An amendment to the definitions of preservation funds allows a member to transfer part of a retrenchment benefit from an occupational fund to a preservation fund and derive the retirement tax scale benefits on the cash portion.
- This takes effect from the commencement of years of assessment commencing on or after 1 January 2012.

Transfers from preservation funds

- Changes to paragraph 6 of the second schedule allow tax free transfer from preservation funds to retirement annuity funds from the commencement of years of assessment commencing on or after 1 January 2012[3].
- Another change to “pension preservation fund” contemplates transfers in from a provident fund, a provident preservation fund and another pension preservation fund[4].

Miscellaneous retirement fund changes

- There are also minor clarificatory changes to the definitions of funds and to paragraph 4 of the Second Schedule, inter alia.

VAT Act

- Reference to preservation funds has been included in the definition of superannuation scheme. This confirms that the management of such schemes falls into the VAT net.

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[3] The definition of retirement annuity fund appears to need an accommodating change too.
[4] This has not been carried through to the tax concessions in paragraph 6 of the Second Schedule, however.

Source

The draft Bill proposes a unification of source rules. Section 9 will be replaced to this end. A pension, annuity or RIDDA will be deemed to be from a source in the Republic if it was received or accrued in respect of

- an office held by appointment of statute.
- services performed for a Government department, parastatal or municipal entity.
- services rendered in the Republic. A proportional calculation will apply for services rendered inside and outside the Republic.

No specific provisions have been proposed to apply to lump sum benefits.

CONSULTATION ISSUES

The 2011 Budget Review contained proposals on limits to retirement fund contribution deductions and the cash allowance at retirement for provident funds [see Hotlines 9/2011 and 12/2011]. Discussion documents on these topics will be published in July. A discussion document will also be released soon on conversion from medical scheme deductions to tax credits.

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