

# WHAT YOU NEED TO KNOW ABOUT PROPOSED TAX CHANGES IN INVESTMENTS

Treasury has proposed some important changes to the tax regulation in the investment industry. Below, are some of the key issues you need to be aware of.



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## ACCESS TO PRESERVATION FUNDS UPON FORMAL EMIGRATION


The definition of a retirement annuity (RA) allows a member to withdraw their full benefit prior to reaching retirement - provided they have formally emigrated from South Africa and that emigration is recognised by the South African Reserve Bank for the purposes of exchange control. Access to this benefit would be a withdrawal benefit and will therefore be taxed as such.

However, the same allowance does not apply to preservation funds. Members of preservation funds are allowed one full or partial withdrawal from their fund benefit prior to retirement. Had they taken a partial withdrawal prior to retirement, they would only be able to access the benefit again, either as a lump sum, compulsory annuity or a combination of the two at retirement. This means that if a preservation fund member emigrates and has already accessed their one withdrawal, they would have to wait until age 55 to access their fund benefits again. This allowance now not only works for South Africans who formally emigrate but also applies, upon expiration of their work visa, to expatriates who had invested in an RA while working in South Africa.

Treasury has now proposed aligning the treatment of preservation fund members to allow a preservation fund member to withdraw from their fund upon formal emigration or the expiration of a work VISA. If this proposal is passed then it will come into effect on 1 March 2019.

## TRANSFERS TO PRESERVATION FUNDS AFTER REACHING EMPLOYMENT RETIREMENT AGE

In the 2017 tax amendments, Treasury allowed a pension or provident fund member who reached employment retirement age to defer retiring from the fund itself and transfer to an



RA. An allowance to transfer to preservation funds was not included at the time. This is because a preservation fund allows a member one (full) withdrawal which would bypass annuitisation requirements. Treasury indicated that they assumed the administration of restricting these withdrawals from preservation funds would be unduly burdensome on preservation funds.

However, after consultation with industry, Treasury is satisfied that preservation funds will be able to administer and restrict the one withdrawal from preservation funds if the benefit was transferred in from a pension or provident fund after reaching retirement age. Practically, this means preservation funds will need to obtain information to confirm whether a transfer is as a result of resignation or retirement from employment. This proposal is also scheduled to be effective 1 March 2019.

#### ANNUITISATION OF PROVIDENT FUNDS

In the Taxation Laws Amendment Bill media statement, Treasury indicated that the legislation forcing members to annuitise at least two thirds of their provident fund contributions made after 1 March 2019 was still scheduled for the above-mentioned date. They did however indicate that the process of consultation within NEDLAC was taking longer than anticipated following the release of the paper on comprehensive social security on 25 November 2016 and that they may introduce changes to the start date of 1 March 2019.

In the response document to industries comment dated 12 September 2018 Treasury has indicated that they intend to introduce further legislative amendments shifting the effective date of 1 March 2019 by one or two years in line with the NEDLAC constituencies' recommendation. What is interesting to note is that while annuitisation keeps being postponed, provident fund members continue to benefit from the contribution tax deductions introduced in 2016.

#### PROPOSED TAX CHANGES TO COLLECTIVE INVESTMENT SCHEMES

In the Taxation Laws Amendment Bill 2018 (TLAB) explanatory memorandum, Treasury indicated that "it has come to Government's attention that some collective investment schemes (CIS) are, in effect, generating profits from the active frequent trading of shares and other financial instruments. These CIS argue that the profits are of a capital nature. They base this argument on the intention of long term investors in the CIS."

It has long been accepted that collective investment schemes are long term investments and are therefore capital in nature. When an investor decides to withdraw from a unit

trust, such withdrawal would be capital in nature and any gain will be liable for capital gains tax (CGT), regardless of whether the withdrawal was made in a month, a year or 10 years from the initial investment date.

Due to Treasury's concerns that some CIS's are frequently trading shares they proposed the following:

##### *A. ONE-YEAR HOLDING PERIOD RULE*

It is proposed that distributions from CIS to unit holders derived from the disposal of financial instruments within 12 months of their acquisition should be deemed to be income of a revenue nature and be taxable as such in the hands of the unit holders if distributed to them under current tax rules relating to distributions.

##### *B. FIRST-IN-FIRST-OUT METHOD*

It is proposed that where a CIS acquired financial instruments at various dates, the CIS will be deemed to have disposed of financial instruments acquired first. The first in first out method will be used to determine the period the financial instruments were held for the purposes of the one year holding period rule.

##### *C. TREATMENT OF LOSSES*

Deductions and allowances do not flow through to unit holders and amounts deemed to have accrued to unit holders are limited to amounts of gross income reduced by deductions allowable under section 11.

Source: Explanatory Memorandum on the Taxation Laws Amendment Bill, 2018 (Draft) 16 July 2018

Over the last few years Treasury has focused on improving the savings culture amongst South Africans. Tax-free Investments were introduced in 2015 and we have seen from the take up of the product that this initiative has had success. Such a proposal would undo some of the good work done to promote savings in South Africa and could have a detrimental effect on local unit trusts. This concern was communicated to Treasury via the invitation to comment on TLAB 2018. Fortunately, in their Draft Response Document to industry's comments, Treasury has indicated that they have partially accepted industry's concerns and have indicated that Government along with industry be given more time to investigate and come up with a solution that will not have as much of a negative impact on unit trust holders and the industry.

As always, we urge investors to stay informed about the changing tax proposals and chat to their financial planners where clarity is required. In turn, we will continue to communicate important information. ■



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