

INTERPRETATION NOTE 99 (Issue 2)

DATE: 11 October 2019

ACT : INCOME TAX ACT 58 OF 1962
SECTION : PARAGRAPH 4(1) OF THE SECOND SCHEDULE
SUBJECT : UNCLAIMED BENEFITS

Preamble

In this Note unless the context indicates otherwise –

- “**fund**” means a “pension fund”, “provident fund”, “pension preservation fund”, “provident preservation fund” and “retirement annuity fund” as defined in section 1(1) of the Income Tax Act;¹
- “**Income Tax Act**” means the Income Tax Act 58 of 1962;
- “**paragraph**” means a paragraph of the Second Schedule to the Income Tax Act;
- “**Pension Funds Act**” means the Pension Funds Act 24 of 1956;
- “**Schedule**” means a Schedule to the Income Tax Act;
- “**section**” means a section of the Income Tax Act; and
- any other word or expression bears the meaning ascribed to it in the Income Tax Act.

1. Purpose

This Note explains the treatment of lump sum benefits classified as unclaimed benefits that accrued to members (both before and from 1 March 2009) for income tax purposes.

2. Background

Historically some members of a fund did not, after exiting the fund, claim the lump sum benefit² to which they became entitled under the rules of the fund. These lump sum benefits were classified as an “unclaimed benefit” if they were not claimed after a reasonable period (see **4.1**). The legislation did not regulate when and how a lump sum benefit should be classified as an “unclaimed benefit”. Fund administrators, as a result, applied different rules to determine when a lump sum benefit was classified as an “unclaimed benefit”.

¹ The definitions of “pension preservation fund” and “provident preservation fund” were introduced into the Income Tax Act with effect from 1 January 2009.

² As defined in section 1(1) read with the Second Schedule.

In many instances, fund administrators applied for a tax directive for an unclaimed benefit only when the member or the member's beneficiaries claimed the unclaimed benefit, as opposed to when the lump sum benefit accrued.

3. The law

The relevant provisions of the law are quoted in the **Annexure**.

4. Application of the law

4.1 What is an unclaimed benefit?

An unclaimed benefit is a lump sum benefit³ that the member of a fund failed to claim within a reasonable period after the lump sum benefit accrued. A reasonable period was six months from the date of accrual of the benefit (that is, up to six months from the day after resignation or termination of employment or retirement, or up to six months from the day before death). The insertion of the definition of "unclaimed benefit" into the Pension Funds Act⁴ introduced a period of 24 months before a lump sum benefit is classified as an unclaimed benefit.

The above amendment to the Pension Funds Act does not have an impact on the date of accrual of the unclaimed benefit. It merely extends the period for a benefit to be classified as an "unclaimed benefit".

4.2 Position before 1 March 2009

A lump sum benefit was deemed to have accrued to a member on the date that he or she became entitled to claim a lump sum benefit under the registered rules of the fund. The rules of most funds confirmed that a member became unconditionally entitled to claim a lump sum benefit on the day of his or her resignation, dismissal, retrenchment or retirement from employment or on death.⁵ The accrual of the amount was determined by the fact that the member became unconditionally entitled to the lump sum benefit and not whether the lump sum benefit was claimed.⁶

The fact that a member did not complete administrative requirements for his or her claim, or the fact that the administrator was unable to trace the member, or unable to determine whether or not the member would need to exercise some option for the payment of the lump sum benefit did not affect that member's unconditional right to claim the benefit.

Similarly, the fact that a member had a right to transfer the lump sum benefit to another fund on resignation, or to choose to commute a portion of the lump sum benefit on retirement and failed to exercise that right, does not affect the fact that the full amount of the lump sum benefit accrued on the member's resignation date or retirement date for income tax purposes.

³ "Lump sum benefit" as defined in section 1(1) excludes any portion of the benefit, payable as a result of the member's retirement from the fund, used to purchase an annuity.

⁴ Effective from 1 September 2008.

⁵ Paragraph 4(1) before amendment by the Taxation Laws Amendment Act 7 of 2010.

⁶ *Lategan v CIR* 1926 CPD 203, 2 SATC 16.

In the case of a death benefit, the lump sum benefit was deemed for income tax purposes to accrue to the deceased member the day before his or her death.⁷ The payment of these benefits is regulated by the provisions of section 37C of the Pension Funds Act. The definition of “unclaimed benefit” in the Pension Funds Act, inserted with effect from 1 September 2008, excludes any lump sum benefit payable, as a result of death, and not paid to beneficiaries within 24 months of the fund becoming aware of the death of the member. The fact that the lump sum benefit cannot be classified as an “unclaimed benefit” under the Pension Funds Act does not affect the accrual of the lump sum benefit for tax purposes. Any subsequent tracing of or payment to the deceased member’s beneficiaries does not create a further accrual event.

In 2003, SARS requested all funds to submit a list of all lump sum benefits not claimed within the reasonable period in order to determine the tax payable on these unclaimed benefits. In most instances the information submitted to SARS did not stipulate the exit event that gave rise to the accrual of the benefit (for example resignation or retirement). These unclaimed benefits were taxed as withdrawal benefits at a rate of between 18% and 30%. The fund was required to issue a corresponding IRP5 tax certificate for the member of the fund.

Any interest that accrued on the value of the unclaimed benefit, after the date of accrual, should have been treated as interest for income tax purposes. The fund or fund administrator was supposed to issue an IT3(b) tax certificate in respect of the interest amount that accrued in each year of assessment.

Example 1 – Unclaimed benefit taxed during the 2003-project

Facts:

On 1 December 2001 a lump sum benefit of R103 500 accrued to X under the rules of ABC Retirement Fund. The benefit was not claimed by the member and was taxed at a rate of 21% during the 2003-project. The value of the unclaimed benefit after tax was R81 765. The fund was required to issue an IRP5 tax certificate for the member reflecting the original lump sum benefit of R103 500 and employees’ tax of R21 735 deducted. In addition, IT3(b) tax certificates were issued for the member for each year of assessment that interest accrued.

X approached the fund on 1 April 2015 to claim the benefit. Interest to the value of R68 000 accrued on the benefit from 1 December 2001 until 1 April 2015. The average tax rate⁸ for X was 21%.

⁷ Paragraph 4(1) before amendment by the Taxation Laws Amendment Act 7 of 2010.

⁸ Section 5(10). The special tax rate table applicable to retirement fund lump sum benefits was introduced in 2007 and was applicable to those benefits that accrued on or after 1 October 2007. The special tax rate table in respect of retirement fund lump sum withdrawal benefits was introduced only in 2009 and was applicable only to retirement fund lump sum withdrawal benefits that accrued on and after 1 March 2009.

Result:

The following steps must be followed by the administrator of the ABC Retirement Fund in order to determine the tax payable on the benefit claimed by X on 1 April 2015 and to correctly reflect that benefit and any interest received:

Step 1: Apply for a tax directive

A tax directive must be applied for on the total value of the unclaimed benefit (R103 500). The reason on the tax directive application must reflect the reason for exit from the employer's employment as "resignation".⁹ The reason for submitting the directive with the correct reason and original amount (R103 500) is to allow the system to take the Second Schedule deduction into account to ensure the assessment is correct.

The interest accrued to or payable to the member does not form part of the unclaimed benefit and only the original value of R103 500 must be reflected as the "gross lump sum amount" on the tax directive application.

| | |
|----------------------------------------------------------|----------|
| Lump sum benefit as at 1 December 2001 (date of accrual) | R103 500 |
| Tax at average rate per the tax directive (21%) | R21 735 |

Step 2: Issue an IT3(a) tax certificate

An IT3(a) tax certificate must be issued to the member reflecting the original value of the unclaimed benefit (R103 500). An IT3(a) tax certificate has to be issued (as opposed to an IRP5 tax certificate) as no additional employees' tax is payable.

The information on the IT3(a) tax certificate relating to the tax directive application must include the tax directive number as well as the following:

| <u>Source code</u> | <u>Amount</u> |
|--------------------|---------------|
| 3902 | R103 500 |

Code 04 must be inserted in the "Reason for Non-Deduction of Employees' Tax" field (4150).

The transaction year must be reflected as 2016 and the year of assessment as 2002.

Step 3: Issue IT3(b) tax certificates

IT3(b) tax certificates must be issued for the interest that accrued on the lump sum for each year of assessment since the accrual of the lump sum. These certificates must be provided to SARS via an IT3(b) submission on an annual basis.

The following documents must be provided to the member:

- IRP5 tax certificate issued during the 2003-project
- IT3(a) tax certificate issued in 2016
- IT3(b) tax certificates reflecting the interest that accrued for each year of assessment

⁹ Paragraph 9(3) of the Fourth Schedule.

If the tax payable reflected on the tax directive is more than the tax deducted during the 2003-project, the difference has to be paid to SARS. An IRP5 tax certificate reflecting the original unclaimed benefit amount and any additional employees' tax paid must be provided to SARS.

A benefit that is classified as an "unclaimed benefit" is subject to tax. This places an obligation on the fund to apply for a tax directive using the reason "unclaimed benefit".¹⁰ A retirement fund lump sum withdrawal benefit¹¹ that accrued before 1 March 2009 was taxed at the member's average rate. However, if the member's tax affairs were not in order, the benefit was taxed at a rate of 40%. Retirement fund lump sum benefits are taxed in accordance with the special tax rate table with effect from 1 October 2007.¹²

Example 2 – Unclaimed benefit that accrued after the 2003-project and complied with the legislative requirements

Facts:

On 1 January 2006 a lump sum benefit of R208 400 accrued to X as a result of resignation under the rules of ABC Retirement Fund. The benefit was not claimed by the member on resignation. The lump sum benefit was classified as an "unclaimed benefit" on 1 August 2006. The fund applied for a tax directive with the reason indicated as "unclaimed benefit". The average tax rate for X was 21%. Employees' tax of R43 764 was deducted from the unclaimed benefit. An IRP5 tax certificate was issued as well as the IT3(b) tax certificates for each year of assessment that interest accrued.

X approached the fund on 1 June 2015 to claim the benefit. The unclaimed benefit accrued interest of R80 000 from 1 January 2006 until 1 June 2015. The average tax rate for X was in fact 23% and not 21%, based on additional information available on the SARS system.

¹⁰ Paragraph 9(3) of the Fourth Schedule.

¹¹ Definition of "retirement fund lump sum withdrawal benefit" inserted by the Taxation Laws Amendment Act 3 of 2008 with effect from 1 March 2009. Previously referred to as a "withdrawal benefit".

¹² Section 5(10). The special tax rate table applicable to retirement fund lump sum benefits was introduced in 2007 and was applicable to those benefits that accrued on or after 1 October 2007. The special tax rate table in respect of retirement fund lump sum withdrawal benefits was introduced only in 2009 and was applicable only to retirement fund lump sum withdrawal benefits that accrued on and after 1 March 2009.

Result:

The following steps must be followed by the administrator of the ABC Retirement Fund when the benefit is claimed:

Step 1: Apply for a tax directive

A tax directive must be applied for on the total value of the unclaimed benefit (R208 400). The reason on the tax directive application must reflect the reason for exit from the employer's employment as "resignation". The reason for submitting the directive with the correct reason and original amount (R208 400) is to allow the system to take the Second Schedule deduction into account to ensure the assessment is correct.

The interest accrued to or payable to the member does not form part of the unclaimed benefit and only the original value of R208 400 must be reflected as the "gross lump sum amount" on the tax directive application.

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|------------------------------------------------------------------|----------|
| Lump sum benefit as at 1 January 2006 (date of accrual) | R208 400 |
| Tax at average rate ¹² as per the tax directive (23%) | R47 932 |

| | |
|----------------------------------------------------------------|-----------------|
| <i>Step 2: Determine whether any additional tax is payable</i> | R |
| Tax as per tax directive (step 1) | 47 932 |
| Less: Tax already paid on unclaimed benefit | <u>(43 764)</u> |
| Tax payable | <u>4 168</u> |

The information on the IRP5 tax certificate relating to the directive application must include the tax directive number as well as the following:

| <u>Source code</u> | <u>Amount</u> |
|--------------------|---------------|
| 3902 | R208 400 |
| 4102 | R4 168 |

The transaction year must be reflected as 2016 and the year of assessment as 2006.

Step 3: Issue IRP5 and IT3(b) tax certificates

IT3(b) tax certificates must be issued for the interest that accrued on the lump sum for each year of assessment since the accrual of the lump sum benefit. These certificates must be provided to SARS via an IT3(b) submission on an annual basis.

The following documents must be provided to the member:

- IRP5 tax certificate issued in June 2006
- IRP5 tax certificate issued in 2016
- IT3(b) tax certificates reflecting the interest that accrued for each year of assessment

Not all funds complied with their obligation to apply for a tax directive when the benefit was classified as an "unclaimed benefit". **Example 3** explains the process to be followed when this obligation was not complied with.

Example 3 – Unclaimed benefit that accrued after the 2003-project and the legislative requirements were not complied with

Facts:

On 1 December 2006 a lump sum benefit of R182 600 accrued to Y as a result of a dismissal under the rules of ABC Retirement Fund. The benefit was not claimed by the member on dismissal. The fund did not classify the lump sum benefit as an “unclaimed benefit” nor did the fund apply for a tax directive on accrual.¹³

The unclaimed benefit accrued interest of R35 200 from 1 December 2006 until 1 September 2015. Y did not claim the benefit until 1 September 2015. The average tax rate for Y was 22%.

Result:

The following steps must be followed by the administrator of the ABC Retirement Fund:

Step 1: Apply for a tax directive

A tax directive must be applied for on the total value of the unclaimed benefit (R182 600). The reason on the tax directive application must reflect the reason for the exit from the employer’s employment as “withdrawal” (dismissal). “Unclaimed benefit” should not be reflected as the reason for the tax directive application.

The interest accrued to or payable to the member does not form part of the unclaimed benefit and only the original value of R182 600 must be reflected as the “gross lump sum amount” on the tax directive application.

| | |
|------------------------------------------------------------|----------|
| Lump sum benefit as at 1 December 2006 (date of accrual) | R182 600 |
| Tax at average rate ¹⁴ as per the tax directive | R40 172 |

The information on the IRP5 tax certificate relating to the tax directive application must include the tax directive number as well as the following:

| <u>Source code</u> | <u>Amount</u> |
|--------------------|---------------|
| 3902 | R182 600 |
| 4102 | R40 172 |

The transaction year must be reflected as 2016 and the year of assessment as 2007.

Only one tax directive should be applied for reflecting the reason for the exit from the employer’s employment as “withdrawal” and not as an “unclaimed benefit”.

¹³ Paragraph 4(1) before amendment by the Taxation Laws Amendment Act 7 of 2010.

¹⁴ Section 5(10). The special tax rate table applicable to retirement fund lump sum benefits was introduced in 2007 and was applicable to those benefits that accrued on or after 1 October 2007. The special tax rate table in respect of retirement fund lump sum withdrawal benefits was introduced only in 2009 and was applicable only to retirement fund lump sum withdrawal benefits that accrued on and after 1 March 2009.

Step 2: Issue IT3(b) tax certificates

IT3(b) tax certificates must be issued for the interest that accrued on the lump sum benefit for each year of assessment since the accrual of the lump sum. These certificates must be provided to SARS via an IT3(b) submission on an annual basis. The relevant reconciliations must be resubmitted to SARS in order for the interest to be taken into account in the correct year of assessment.

The following documents must be provided to the member:

- IRP5 tax certificate issued in 2016
- IT3(b) tax certificates reflecting the interest that accrued for each year of assessment

4.3 Position on and after 1 March 2009

The legislation was amended with effect from 1 March 2009 to provide that lump sum benefits that become payable under the rules of the fund as a result of a member's resignation, dismissal or retrenchment from employment will accrue to the member for tax purposes only on the date that he or she elects to receive the lump sum benefit as a cash amount, or to transfer the lump sum benefit to another approved fund. These benefits can, as a result, be classified as an "unclaimed benefit" under the provisions of the Pension Funds Act, but the lump sum benefit accrues to the member for tax purposes only once he or she makes an election regarding the benefit. The classification and tax treatment of lump sum benefits due to a member's resignation, dismissal or retrenchment from employment, which accrued before 1 March 2009, remains unchanged.

A lump sum benefit that accrued to a member as a result of his or her retirement before 1 March 2015 accrued to a member on his or her retirement date.¹⁵ The legislation provided no flexibility for a member to determine when he or she would like to receive his or her benefits. The provision was amended with effect from 1 March 2015 to provide that retirement benefits accrue only when an election is made by the member to receive the benefit. This means that no benefit payable after 1 March 2015, as a result of a member's retirement, can be classified as an "unclaimed benefit" for income tax purposes.

The benefit payable by the fund as a result of the member's death accrues to the deceased member on his or her date of death. The fund has an obligation to apply for a tax directive on the death of the member,¹⁶ the reason must be indicated as "death before retirement" and an IRP5 tax certificate must be issued. The payment of these benefits is regulated by the provisions of section 37C of the Pension Funds Act but there are some instances where the beneficiaries of the deceased cannot be traced within 24 months after the date of the member's death. These benefits should be classified as "unclaimed benefits" if the death benefit was not claimed by the beneficiaries. The death benefit, classified as an "unclaimed benefit", will not be subject to tax in the hands of the deceased member's beneficiaries.

¹⁵ Definition of "retirement date" before amendment by the Taxation Laws Amendment Act 3 of 2008.

¹⁶ Paragraph 9(3) of the Fourth Schedule.

4.4 Transfers of unclaimed benefits

4.4.1 Benefits that accrued before 1 March 2009

Historically, unclaimed benefits remained in the fund until claimed by the members or the member's beneficiaries. This practise prohibited funds from being liquidated under section 28 of the Pension Funds Act, as a fund could only be liquidated once all the members, assets and liabilities have been paid or transferred out of the fund.

The definitions of "pension preservation fund" and "provident preservation fund" were inserted into the Income Tax Act with effect from 1 January 2009.¹⁷ These definitions specifically made provision for a pension preservation fund or provident preservation fund to be established solely for the purpose of housing unclaimed benefits. This gave a fund the option to transfer all the unclaimed benefits in a fund to an approved unclaimed benefit preservation fund¹⁸ rather than keeping these benefits in the fund.

Only lump sum benefits that were classified by the fund as "unclaimed benefits" and have been taxed as such can be transferred to an unclaimed benefit preservation fund. The transfer of the unclaimed benefits in the fund to an unclaimed benefit preservation fund is an accrual event for income tax purposes.¹⁹ The fund transferring the unclaimed benefits has an obligation to apply for tax directives before transferring the unclaimed benefits. An amount equal to the value of the unclaimed benefit to be transferred to the unclaimed benefit preservation fund will be allowed as a deduction against the lump sum benefit, provided that the unclaimed benefit has been taxed before the transfer took place and the information relating thereto was provided to the unclaimed benefit preservation fund on transfer.²⁰ The benefit payable to the member by the unclaimed benefit preservation fund is subject to the provisions in the registered rules of the unclaimed benefit preservation fund. The unclaimed benefit preservation fund has an obligation to apply for a tax directive when the benefit is claimed by the member. The onus is therefore on the unclaimed benefit preservation fund (transferee fund) to ensure that the information on the composition of the amounts transferred is obtained from the transferor fund, especially if those unclaimed benefits were taxed before the transfer. The member might be taxed on the benefit for a second time when he or she claims the benefit if an IRP5 tax certificate and the information on the composition of amount transferred are not provided to the unclaimed benefit preservation fund.

The transferring fund did not have to apply for a tax directive if the transfer was done under section 14(1) of the Pension Funds Act.²¹ In the event that the unclaimed benefits were not taxed before the transfer to an unclaimed benefit preservation fund, the full unclaimed benefits will be subject to tax when the member claims the benefit from the unclaimed benefit preservation fund.

¹⁷ Taxation Laws Amendment Act 3 of 2008.

¹⁸ The term "unclaimed benefit preservation fund" means a "pension preservation fund" or "provident preservation fund", as defined in section 1(1) of the Income Tax Act, established solely for housing unclaimed benefits.

¹⁹ Paragraph 4(1)(c).

²⁰ Paragraph 6(1)(b)(iv).

²¹ Paragraph 9(3)(b) of the Fourth Schedule.

A pension fund can transfer unclaimed benefits only to an unclaimed benefit pension preservation fund, and a provident fund can transfer unclaimed benefits only to an unclaimed benefit provident preservation fund. Unclaimed benefits in a retirement annuity fund may not be transferred to any unclaimed benefit preservation fund.

A member who claims a benefit, classified as an “unclaimed benefit”, which accrued before 1 March 2009, cannot elect to transfer the benefit to another fund. The Second Schedule provides a deduction in respect of a transfer to another qualifying fund.²² This deduction is, however, only available for the year of assessment in which the benefit accrues (that is, in the year of resignation). The effect of this is that where a beneficiary failed to elect to transfer to another fund in the year of assessment during which the benefit accrued, the deduction falls away.

Example 4 – Transfer of benefits that accrued after 2003-project to an unclaimed benefit preservation fund – information provided by the transferring fund

Facts:

On 1 November 2008 a lump sum benefit of R650 000 accrued to X as a result of resignation under the rules of EFG Retirement Fund. The benefit was not claimed by the member on resignation. The lump sum benefit was classified as an “unclaimed benefit” on 1 May 2009.

The fund applied for a tax directive with the reason indicated as “unclaimed benefit”. The average tax rate for X was 22%. The employees’ tax of R143 000 was deducted from the unclaimed benefit and an IRP5 tax certificate was issued for the member. IT3(b) tax certificates were issued for the member for each year of assessment that interest accrued.

The trustees of the fund decided to transfer all the unclaimed benefits in EFG Retirement Fund to XYZ Unclaimed Benefit Pension Preservation Fund on 30 June 2013. Interest accrued to the value of R100 000 from 1 November 2008 to 30 June 2013. The EFG Retirement Fund applied for a tax directive on the total value of the benefit of R607 000 transferred to the unclaimed benefit preservation fund (R570 000 + R100 000). The amount transferred of R607 000 was reflected as the “gross lump sum amount” on the tax directive application.

The IRP5 tax certificate that reflects the amount of tax deducted of R143 000 from the original benefit and the IT3(b) tax certificates that reflect the total R100 000 interest that accrued to the member for the period of 1 November 2008 to 30 June 2013 were provided by the EFG Retirement Fund to the XYZ Unclaimed Benefit Pension Preservation Fund.

X approached the unclaimed benefit preservation fund on 2 July 2019 to claim the benefit. The value of the unclaimed benefit claimed by X is R960 000.

²² Paragraphs 6(1)(a)(ii)(aa) and 6(1)(a)(ii)(cc).

Result:

The following steps must be followed by the administrator of the XYZ Unclaimed Benefit Pension Preservation Fund:

Step 1: Determine taxable portion of lump sum benefit

The taxable portion of the lump sum benefit may be reduced by the amount transferred to the unclaimed benefit preservation fund only if the amount transferred was subject to tax before the transfer and that information was provided to the unclaimed benefit preservation fund.

| | |
|------------------------------------------------------|------------------|
| | R |
| Lump sum benefit as at 2 July 2019 (date of accrual) | 960 000 |
| Less: Amount transferred ²³ | <u>(607 000)</u> |
| Taxable portion of the lump sum benefit | <u>353 000</u> |

Step 2: Apply for a tax directive

A tax directive must be applied for on the taxable portion of the lump sum benefit claimed by the member (R353 000). The reason on the tax directive application must reflect the reason for the termination of membership as per the rules of the unclaimed benefit preservation fund.

| | |
|-----------------------------------------|----------|
| Taxable portion of the lump sum benefit | R353 000 |
| Tax as per the tax directive | R63 540 |

The information on the IRP5 tax certificate relating to the directive application must include the tax directive number as well as the following:

| <u>Source code</u> | <u>Amount</u> |
|--------------------|---------------|
| 3920 | R353 000 |
| 4115 | R63 540 |

The transaction year must be reflected as 2020 and the year of assessment as 2020.

Step 3: Issue IRP5 tax certificate

An IRP5 tax certificate issued for the 2020 reconciliation year must be provided to the member.

Step 4: Provide historical information

The documents received from the EFG Retirement Fund must be provided to the member:

- IRP5 tax certificate issued in 2009
- IT3(a) tax certificate issued on transfer
- IT3(b) tax certificates reflecting the interest that accrued for each year of assessment before transfer

²³ Paragraph 6(1)(b)(iv)

Example 5 – Transfer of benefits that accrued after 2003-project to an unclaimed benefit preservation fund – no information provided by the transferring fund

Facts:

On 30 June 2013 an amount of R750 000 was transferred from the EFG Retirement Fund to the XYZ Unclaimed Benefit Pension Preservation Fund in respect of X. The EFG Retirement Fund provided no information on the composition of the amount (that is, whether or not the transferred amount was already taxed or includes interest).

X approached the unclaimed benefit preservation fund on 2 July 2019 to claim the benefit. The lump sum benefit to the value of R960 000 is payable to X in accordance with the rules of the XYZ Unclaimed Benefit Pension Preservation Fund.

Result:

The following steps must be followed by the administrator of the XYZ Unclaimed Benefit Pension Preservation Fund:

Step 1: Apply for a tax directive

A tax directive must be applied for on the total value of the unclaimed benefit (R960 000). The reason on the tax directive application reflects the reason as per the rules of the XYZ Unclaimed Benefit Pension Preservation Fund as “resignation”.

| | |
|------------------------------------------------------|----------|
| Lump sum benefit as at 2 July 2019 (date of accrual) | R960 000 |
| Tax as per the tax directive | R195 300 |

The information on the IRP5 tax certificate relating to the directive application must include the tax directive number as well as the following:

| <u>Source code</u> | <u>Amount</u> |
|--------------------|---------------|
| 3920 | R960 000 |
| 4115 | R195 300 |

The transaction year must be reflected as 2020 and the year of assessment as 2020.

Step 2: Issue an IRP5 tax certificate

An IRP5 tax certificate issued for the 2020 reconciliation year must be provided to the member.

4.4.2 Benefits that accrued on and after 1 March 2009

All lump sum benefits that become payable from 1 March 2009 under the rules of the pension fund, pension preservation fund, provident fund and provident preservation fund as a result of a member's resignation, dismissal, retirement²⁴ or death, that are classified as "unclaimed benefits" under the Pension Funds Act, can be transferred to an unclaimed benefit pension preservation fund or an unclaimed benefit provident preservation fund.²⁵

Death benefits fall within the definition of "unclaimed benefit" in the Pension Funds Act and as such could be transferred from a retirement fund to the relevant preservation fund for unclaimed benefits. These death benefits may be subject to tax again when the preservation fund for unclaimed benefits pays the death benefit to the deceased's beneficiaries or dependants as a lump sum under the rules of that fund. This is because death benefits paid are deemed to accrue to the deceased on the date immediately before his or her death and should have already been subjected to tax as a death benefit.

Unclaimed benefits in a retirement annuity fund may not be transferred to any unclaimed benefit preservation fund.

The transfer of the unclaimed benefits in the fund to the unclaimed benefit preservation fund is an accrual event for income tax purposes.²⁶ The transferring pension fund, pension preservation fund, provident fund and provident preservation fund has an obligation to apply for a tax directive on the transfer of these unclaimed benefits to the unclaimed benefit pension preservation fund or unclaimed benefit provident preservation fund.²⁷ An amount equal to the value of an unclaimed benefit to be transferred to the unclaimed benefit preservation fund will be allowed as a deduction against the lump sum benefit.²⁸ The transferring pension fund, pension preservation fund, provident fund and provident preservation fund did not have to apply for a tax directive for any transfer done under section 14(1) of the Pension Funds Act²⁹ before 1 March 2017. After 1 March 2017 the transferring pension fund, pension preservation fund, provident fund and provident preservation fund must apply for a tax directive in respect of all transfers, irrespective of whether the transfer was done under section 14 of the Pension Funds Act.

The unclaimed benefit preservation fund then has an obligation to apply for a tax directive for any lump sum benefit which accrues to the member, indicating the reason for exit on the tax directive application as per the rules of the unclaimed benefit preservation fund.

²⁴ With effect from 1 March 2015.

²⁵ Paragraph (b)(i) of the definitions of "pension preservation fund" and "provident preservation fund".

²⁶ Paragraph 4(1)(c).

²⁷ Paragraph 9(3) of the Fourth Schedule.

²⁸ Paragraph 6(1)(b)(iv).

²⁹ Paragraph 9(3)(b) of the Fourth Schedule

A member who comes forward after a benefit was classified as an “unclaimed benefit” and transferred to an unclaimed benefit preservation fund, after 1 March 2009, can choose to transfer that benefit to another fund. An amount equal to the value of the benefit transferred is allowed as a deduction against the lump sum benefit³⁰ for the following transfers:

- Unclaimed benefit pension preservation fund to a pension fund, pension preservation fund or retirement annuity fund
- Unclaimed benefit provident preservation fund to a pension fund, pension preservation fund, provident preservation fund or retirement annuity fund

The definition of “provident preservation fund” in section 1(1) of the Income Tax Act³¹ provides only for unclaimed benefits relating to a former member of a provident fund or nominees or dependants of that former member to be transferred to a provident preservation fund. This means that a transfer from an unclaimed benefit pension preservation fund to a provident preservation fund is not allowed and no deduction will be allowed for such a transfer.

5. Conclusion

The tax treatment of a lump sum benefit, classified as an “unclaimed benefit”, depends on the date on which the benefit accrued to the member.

Legal Counsel
SOUTH AFRICAN REVENUE SERVICE
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³⁰ Paragraph 6(1)(a)(ii)(aa) and 6(1)(a)(ii)(cc).

³¹ Paragraph (a)(iii).

Annexure – The law

Income Tax Act 58 of 1962 – before 1 March 2009

Definition of “lump sum benefit” in paragraph 1 of the Second Schedule applicable after 1 March 1998

“lump sum benefit” includes any amount determined by the commutation of an annuity or portion of an annuity and any fixed or ascertainable amount (other than an annuity) payable by or provided in consequence of membership or past membership of any fund referred to in paragraph (e) of the definition of "gross income" in section one of this Act whether in one amount or in instalments;

Paragraph 4(1) of the Second Schedule

(1) If in terms of the rules of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund any lump sum benefit arising out of a member's withdrawal or resignation is payable at a fixed or ascertainable future date, such benefit shall be deemed to have accrued to such member on that date or on the date of his or her death, whichever is earlier, and shall be assessed to tax in respect of the year of assessment during which such benefit is deemed to accrue as though it were a lump sum benefit derived by him or her upon his or her withdrawal or resignation from the fund or upon his or her retirement or immediately prior to his or her death, as the case may be,

Income Tax Act 58 of 1962 – after 1 March 2009

Definition of “lump sum benefit” in paragraph 1 of Second Schedule

“lump sum benefit” includes—

- (a) any amount determined in respect of the commutation of an annuity or portion of an annuity—
 - (i) payable by; or
 - (ii) provided in consequence of membership or past membership of, a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund; and
- (b) any fixed or ascertainable amount (other than an annuity)—
 - (i) payable by; or
 - (ii) provided in consequence of membership or past membership of, a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund,

whether in one amount or in instalments, but does not include any amount deemed to be income accrued to a person in terms of section 7(11);

Paragraph 4(1) of the Second Schedule with effect from 1 March 2009³²

(1) Notwithstanding the rules of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund, any lump sum benefit arising out of a member's withdrawal or resignation shall, subject to paragraph 3, be deemed to have accrued to such member on the date he or she elects to have the benefit paid to him or her or the date on which the benefit is transferred to another pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund or on the date of his or her death, whichever is earlier, and shall be assessed to tax in respect of the year of assessment during which such benefit is deemed to accrue as though it were a lump sum benefit derived by him or her upon his or her withdrawal or resignation from the fund or upon his or her retirement or immediately prior to his or her death, as the case may be.

Paragraph 4(1) of the Second Schedule with effect from 1 March 2010³³

(1) Notwithstanding the rules of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund, any lump sum benefit shall be deemed to have accrued to such member on the earliest of the date—

- (a) on which an election is made in respect of which the benefit becomes recoverable;
- (b) on which any amount is deducted from the benefit in terms of section 37D(1)(a), (b) or (c) of the Pension Funds Act, 1956 (Act No. 24 of 1956);
- (c) on which the benefit is transferred to another pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund;
- (d) of his or her retirement; or
- (e) of his or her death,

and shall be assessed to tax in respect of the year of assessment during which such lump sum benefit is deemed to accrue.

Paragraph 4(1) of the Second Schedule with effect from 10 January 2012³⁴

(1) Notwithstanding the rules of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund, and subject to paragraphs 3 and 3A, any lump sum benefit shall be deemed to have accrued to a member of such fund on the earliest of the date—

- (a) on which an election is made in respect of which the benefit becomes recoverable;
- (b) on which any amount is deducted from the benefit in terms of section 37D(1)(a), (b) or (c) of the Pension Funds Act, 1956 (Act No. 24 of 1956);
- (c) on which the benefit is transferred to another pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund;
- (d) of his or her retirement; or
- (e) of his or her death,

and shall be assessed to tax in respect of the year of assessment during which such lump sum benefit is deemed to accrue.

³² Revenue Laws Amendment Act 60 of 2008 (promulgated 8 January 2009).

³³ Taxation Laws Amendment Act 7 of 2010 (promulgated 2 November 2010).

³⁴ Taxation Laws Amendment Act 24 of 2011 (promulgated 10 January 2012).

Paragraph 4(1) of the Second Schedule with effect from 1 March 2012³⁵

(1) Notwithstanding the rules of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund, and subject to paragraphs 3 and 3A, any lump sum benefit shall be deemed to have accrued to a person who is a member of such fund on the earliest of the date—

- (a) on which an election is made in respect of which the benefit becomes recoverable;
- (b) on which any amount is deducted from the benefit in terms of section 37D (1)(a), (b) or (c) of the Pension Funds Act, 1956 (Act No. 24 of 1956);
- (c) on which the benefit is transferred to another pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund;
- (d) of his or her retirement; or
- (e) of his or her death,

and shall be assessed to tax in respect of the year of assessment during which such lump sum benefit is deemed to accrue;

Pension Funds Act 24 of 1956**Definition of “unclaimed benefit” in section 1 with effect from 1 September 2008**

“unclaimed benefit” means—

- (a) any benefit, other than a benefit referred to in paragraphs (b), (c) and (d), not paid by a fund to a member, former member or beneficiary within 24 months of the date on which it in terms of the rules of the fund, became legally due and payable: or
- (b) in relation to a benefit payable as a pension or annuity, any benefit which has not been paid by a fund to a member, former member or beneficiary within 24 months of—
 - (i) the expiry date of any guarantee period for pension payments provided for in the rules of the fund; or
 - (ii) the date on which any pension payment or annuity legally due and payable in terms of the rules of the fund became unpaid; or
- (c) in relation to a benefit payable to a former member who cannot be traced in accordance with section 15B(5)(e) of this Act, any benefit that has become legally due and payable to a former member in terms of a surplus apportionment scheme approved in terms of this Act not paid to that former member within 24 months of the date on which it became legally due and payable; or
- (d) any benefit that remained unclaimed or unpaid to a member, former member or beneficiary when a fund applies for cancellation of registration in terms of section 27 or where the liquidator is satisfied that benefits remain unclaimed or unpaid,
 - excluding—
 - (aa) a benefit due to be transferred as part of a transfer of business in terms of section 14, where an annuity is purchased in respect of a pensioner or otherwise in terms of this Act; or
 - (bb) a death benefit payable to a beneficiary in terms of section 37C of this Act not paid within 24 months from the date of the death of the member or such longer period as reasonably justifiable by the board of the fund;.

³⁵ Taxation Laws Amendment Act 22 of 2012 (promulgated 1 February 2013).

Definition of “unclaimed benefit” in section 1 with effect from 16 January 2014

“unclaimed benefit” means—

- (a) any benefit, other than a benefit referred to in paragraphs (aA), (b), (c) and (d), not paid by a fund to a member, former member or beneficiary within 24 months of the date on which it in terms of the rules of the fund, became legally due and payable;
- (aA) a death benefit payable to a beneficiary under section 37C not paid within 24 months from the date on which the fund became aware of the death of the member, or such longer period as may be reasonably justified by the board of the fund in writing;
- (b) in relation to a benefit payable as a pension or annuity, any benefit which has not been paid by a fund to a member, former member or beneficiary within 24 months of—
 - (i) the expiry date of any guarantee period for pension payments provided for in the rules of the fund; or
 - (ii) the date on which any pension payment or annuity legally due and payable in terms of the rules of the fund became unpaid;
- (c) in relation to a benefit payable to a former member who cannot be traced in accordance with section 15B(5)(e), any benefit that has become legally due and payable to a former member in terms of a surplus apportionment scheme approved in terms of this Act not paid to that former member within 24 months of the date on which it became legally due and payable;
- (d) any benefit that remained unclaimed or unpaid to a member, former member or beneficiary when a fund applies for cancellation of registration in terms of section 27 or where the liquidator is satisfied that benefits remain unclaimed or unpaid; or
- (e) any amount that remained unclaimed or unpaid to a non-member spouse within 24 months from the date of the deduction contemplated in section 37D(4)(a)(ii),

but does not include a benefit due to be transferred as part of a transfer of business in terms of section 14, where an annuity is purchased in respect of a pensioner or otherwise in terms of this Act;