ASAP

Legal and Technical Update

Retirement funds and the *de minimis* rule

When a member of a retirement fund faces retirement, it is mainly legislation contained in the Income Tax Act (ITA) and the Pension Funds Act that will prescribe what portion of the retirement interest a member is entitled to upon retirement.

It is commonly known that the member is restricted to one third as a lump sum when dealing with a pension/pension preservation/retirement annuity fund. At the moment a member of a provident/provident preservation fund will have unlimited access to the retirement interest on retirement. This is legislated to change on 1 March 2021, when all benefits accruing after that date will also become subject to the one third limitation.

There is one instance when a retiring member can access the full retirement interest in a pension, pension preservation, retirement annuity fund (and provident and provident preservation funds post 1 March 2021), and that is if the two thirds of the retirement interest does not exceed R165 000 – which implies a total retirement interest of R247 500 or less. This amount is referred to as the *de minimis* and in this case the member can withdraw the full value as a lump sum.

As with all retirements, any taxable lump sum will be subject to income tax, using the retirement tax table.

There is often confusion when dealing with retirement annuity funds and preservation funds as a client may have more than one policy in the same retirement annuity/preservation fund and/or more than one fund with a specific administrator, which can restrict that member's access due to the wording of the Income Tax Act (read with the Pension Funds Act).

All or nothing rule

This rule is best explained using an example. Let's assume the client has the following retirement funds:

Registered retirement fund	***Member/Policy number***	***Retirement interest***
Momentum Retirement Annuity Fund (Wealth product)	*PP00001100*	*R233 500*
Momentum Retirement Annuity Fund (Investo product)	*UL00001101*	*R 16 500*
Momentum Pension Preservation Fund	*UP123456*	*R246 000*
Company A pension preservation fund	*AB45698*	*R158 000*
Company A pension preservation fund	*CD12568*	*R680 000*
Company C retirement annuity fund	*CDX12E*	*R177 000*
Company C retirement annuity fund	*CDS15E*	*R245 000*

The member would like to retire from all the funds and wants to withdraw the maximum cash lump sums possible. To determine how the *de minimis* rule must be applied, one has to consult the wording in the ITA. Each retirement fund's definition, being pension, provident (post 1 March 2021), retirement annuity and preservation funds, must be considered. It generally states something like this:

> *"not more than one-third of the total value of the retirement interest may be commuted for a single payment, and that the remainder must be paid in the form of an annuity (including a living annuity) except where two-thirds of the total value does not exceed R165 000 or where the member is deceased…"*

The next relevant definition is that of retirement interest – what is a retirement interest in terms of the ITA:

> *"means a member's share of the value of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund as determined in terms of the rules of the fund on the date on which he or she elects to retire or transfer to a pension preservation fund, provident preservation fund or retirement annuity fund"*

The next step will be to determine what the ITA defines each one of the funds to be. There is general wording that is present in each of the definitions. The retirement annuity fund definition is as follows:

> ***"****means any fund (other than a pension fund, provident fund or benefit fund) which is approved by the Commissioner in respect of the year of assessment in question and, in the case of any such fund established on or after 1 July 1986, is registered under the provisions of the Pension Funds Act"*

When interpreting the wording, it has the outcome that the *de minimis* rule is applied per registered retirement fund and not per underlying policy/retirement interest in that fund.

If a member wishes to retire and that member has more than one retirement interest with one fund administrator, the first step would be to determine if each retirement interest is in the same registered fund or not. Applying the definitions to the example, the member in our example has the following funds in the same registered funds – each highlighted by a different colour:

Registered retirement fund	**Member/Pol number**	**Retirement interest**	**Maximum lump sum**
Momentum Retirement Annuity Fund (Wealth product)	PP00001100	R223 500	R223 500
Momentum Retirement Annuity Fund (Investo product)	UL00001101	R 16 500	R 16 500
Momentum Pension Preservation Fund	UP123456	R246 000	R246 000
Co A pension preservation fund	AB45698	R158 000	R 52 667
Co A pension preservation fund	CD12568	R680 000	R226 667
Co C retirement annuity fund	CDX12E	R177 000	R59 000
Co C retirement annuity fund	CDS15E	R245 000	R81 667

The result is that the member will be entitled to withdraw the total lump sums under both the policies in the Momentum Retirement Annuity Funds as the COMBINED retirement interest in that registered fund is R240 000, which is below the R247 500.

The total retirement interest in the Momentum Pension Preservation Fund is also below the minimum amount in that registered fund, and therefore it is totally accessible.

The COMBINED retirement interest in the Co A pension preservation fund (the registered fund) is in excess of the R247 500 amount and as it is a pension fund, the member is limited to one third of the value in each.

Co C retirement annuity fund also has a COMBINED value in excess of the R247 500. So even though the individual values are below this amount, it will not be accessible and the member will be limited to one third from each retirement annuity policy.

Important factors to note:

- When a member of one registered retirement fund wants to access a retirement interest in that fund, all previous retirement interests that the member received from the fund will also be aggregated to determine the COMBINED value in that fund.

- In addition, if one considers the definition of a retirement interest, the following must be highlighted:

  > *"means a member's share of the value of a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund as determined in terms of the rules of the fund on the date on which he or she elects to retire or transfer to a pension preservation fund, provident preservation fund or retirement annuity fund"*

  As a result, if a member elects to transfer the retirement interest in a fund, the transfer will also have to happen on registered fund level. The result is that the entire retirement interest in that registered fund will be subject to the transfer and not just one underlying part. If a member has more than one policy in a fund, he would therefore not be entitled to transfer only one of those policies to another fund.

  In the example, if one assumes the member wishes to transfer his Retirement Annuity with Co C to Momentum, both policies CDX12E and CDS15E will have to be transferred. It will not be possible to transfer only one of the policies to Momentum – it is all or nothing. It is also not possible to transfer one policy to Momentum and the other to Co A.

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