Recent developments regarding tax free savings accounts

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Johannesburg, South Africa- Oct. 8, 2014 – A proposed section 12T to be inserted into the Income Tax Act will allow individuals to save up to R30 000 per annum, tax free. It appears that this concession will also apply to minor children.

In order to encourage savings, in the 2013 Budget speech the Minister of Finance proposed the introduction of tax free savings accounts. The idea was that individuals could invest up to R30 000 per annum into such accounts, with an overall lifetime ceiling of R500 000. Returns generated in the account would be tax free, whether by way of income or capital gains. The individual could withdraw the amount invested at any stage on a tax free basis.

This proposal has eventually found concrete form by way of a proposed section 12T to be inserted into the Income Tax Act. The proposal is contained in the Draft Taxation Laws Amendment Bill of 2014.

The proposed section 12T contains a definition of ‘tax free investment’ which must be issued by a bank, long-term insurer, collective investment scheme in property or securities or the National Government.

According to National Treasury, regulations (presumably in draft form) are expected to be issued by mid-October which will detail which type of investment products will qualify for inclusion.

Indications from National Treasury, at a feedback meeting on the Draft Bill, are that the intention is to engage with issuers of such investments so as to limit exit charges that will apply upon withdrawal.

If an individual invests R30 000 in a given year and withdraws say R10 000, he or she will still be regarded as having invested the full R30 000 for that year i.e. may not re-invest the R10 000 as part of the R30 000 limit for that year. This is part of the intention of National Treasury in enacting the concession – to encourage individuals not to withdraw amounts invested.

The intention appears to be not to include reinvested income within the fund as part of the annual or overall contribution limits.

It would appear that Treasury may consider the determination of the limits on a rolling basis rather than a strict application of the R30 000 limit per annum.

As currently drafted, extremely stiff penalties apply if an individual exceeds the R30 000 per annum or R500 000 lifetime contributions limits. A penalty by way of additional tax payable in the amount of 40 per cent of the excess applies.

An interesting angle is that as currently drafted, individuals may take out such savings accounts regardless of their age. Therefore it is possible for minor children to contribute in their own names. So a family of four, including two minor children, may contribute a total of R120 000 per annum up to a lifetime limit of R2 million. Care would however have to be taken to ensure that each contributor did not exceed his or her limit, which is calculated on an individual basis. As currently drafted it may be argued that income or a capital gain received by a child as a result of a donation by the parent would be tax free despite the attribution of the income or capital gain to the parent who donated the investment funds to the child.

It will be interesting to see whether or not the current proposals survive through to the final version of the Bill.

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