The capping of the deductibility of retirement contributions for tax: A comparison between South Africa and developed countries

CJ du Plessis
22093052

Dissertation submitted in partial fulfillment of the requirements for the degree Master of Commerce in South African and International Taxation at the Potchefstroom Campus of the North-West University

Supervisor: Prof Dr K Coetzee

November 2015
ABSTRACT

In the Taxation Laws Amendment Act of 2013 the deductibility of retirement contributions for taxation purposes in South Africa was changed. This changed the way in which pension fund contributions, provident fund contributions and retirement annuity fund contributions are treated for tax purposes. These adjustments include the capping of the amount of retirement contributions that will be deductible for income tax purposes. The cap amounts to R350 000 annually.

In this study the amended South African tax consequences, specifically the capping of retirement contributions, are compared to the tax legislation of developed countries, which include Australia, Denmark and Ireland. These countries are selected from the Melbourne Mercer Global Pension Index (MMGPI) as this index lists the best countries in terms of three sub-indices. The countries selected have the highest index amounts for the adequacy sub-index. This sub-index takes into consideration the tax consequences of retirement savings. As such, the South African tax consequences are compared to the best pension systems in the world according to the MMGPI to determine whether the South African tax legislation is in line with those of developed countries.

Quantitative analyses are performed to determine the income tax consequences in all selected countries for individuals in different income categories. Based on the findings in this study, it can be reasonably concluded that, for each of the selected countries some adverse tax implications will result from contributions above the imposed limits. With the introduction of the cap of contributions to the South African tax legislation, South African taxpayers will now be subject to similar limits as in the selected developed countries. Therefore the legislation is now more in line with the legislation of the aforementioned countries.

KEYWORDS: Developed countries, undeveloped countries, pension fund contributions, provident fund contributions, retirement annuity fund contributions, retirement savings, capped amount.
UITTREKSEL

In die Wysigingswet op Belastingwette van 2013 is die aftrekbaarheid van bydraes tot aftreefondse vir belastingdoeleindes gewysig. Hierdie verandering het die belastinggevolge ten opsigte van die aftrekbaarheid van pensioenfondsbydraes, voorsorgfondsbydraes sowel as uittredingsannuiteteitsfondsbydraes, gewysig. Hierdie wysigings sluit die beperking van die bydraes vir belastingdoeleindes afgetrek kan word, in. Die beperking is ’n jaarlikse bedrag van R350 000.

In hierdie studie word die gewysigde belastinggevolge in Suid-Afrika met die belastinggevolge in ontwikkelde lande vergelyk. Daar word spesifiek gefokus op die beperking (R350 000) wat ingestel is. Die ontwikkelde lande wat in die studie gebruik is, is Australië, Denemarke en Ierland. Hierdie lande is geselekteer van die “Melbourne Mercer Global Pension Index” (MMGPI), ’n indeks wat lande lys op grond van drie sub-indekse. Die geselekteerde lande het die hoogste indekse gebaseer op die toereikendheid van hul pensioenstelsels. Hierdie sub-indeks neem die belastinggevolge in ag. Die Suid-Afrikaanse belastinggevolge word dus vergelyk met die beste pensioenstelsels in die wêreld volgens die MMGPI. Hierdie vergelyking bepaal of die Suid-Afrikaanse belastinggevolge in lyn is met die gevolge in ontwikkelde lande.

Kwantitatiewe analises is gebruik om die belastinggevolge te bepaal vir individue in verskillende inkomstegroepe. Gebaseer op die bevindinge in die studie kan daar geredelik die gevolgtrekking gemaak word dat al die lande nadelige belastinggevolge instel wanneer die aftreebydrae ’n sekere limiet, soos vasgestel deur die onderskeie lande, oorskry. Die instelling van ’n beperking op hul bydraes beteken dat Suid-Afrikaanse belastingbetalers onderwerp sal word aan soortgelyke limiete as in die geselekteerde ontwikkelde lande. Dus is die Suid-Afrikaanse belastingwetgewing nou meer in lyn met dié van bogenoemde ontwikkelde lande.

SLEUTELWOORDE: Ontwikkelde lande, ontwikkelende lande, pensioenfondsbydraes, uittredingsannuiteteitsfondsbydraes, voorsorgfondsbydraes, aftreebydrae, bydraebeperkings.
ACKNOWLEDGEMENTS

This study would not have been possible without the technical assistance and guidance provided by my study leader, Professor Karina Coetzee. Also thanks to my colleagues, family and friends for the sincere interest and motivation the past two years.

Without my mother, who is my pillar, I would not have been where I am today. Thank you for all the motivation, encouragement and patience.

A big thank you to Gary who had to listen to me every time I hit a brick wall and he was always ready to assist, helpful, kind and also supportive.

Last, but not least, I am thankful to God for all the opportunities that I am granted and for the talents that he has provided me with to be able to complete this study.
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KEYWORDS: Developed countries, undeveloped countries, pension fund contributions,
provident fund contributions, retirement annuity fund contributions, retirement savings, capped
amount.
CHAPTER 1 - INTRODUCTION

1.1 Introduction

In recent years, National Treasury has proposed many changes and restructuring of retirement savings to promote savings by South Africans. This includes the abolition of retirement fund tax and changes to the deductibility of contributions to retirement funds as from 1 March 2007 (SARS, 2007:9). In 2012 National Treasury once again considered reforming the tax treatment of contributions made to pension, provident and retirement annuity funds (collectively referred to as “retirement funds” hereafter) to a uniform retirement contribution model (National Treasury, 2012:3). These changes were proposed to promote household savings.

In the Tax Law Amendment Act of 2013 the deductions for retirement funds were amended in section 11(k) of the Income Tax Act No 58 of 1962 (hereafter referred to as “The Act”). These amendments would have become effective on 1 March 2015, on all contributions made on or after this date. National Treasury announced on 16 October 2014, through a media statement, that the implementation will be postponed to 1 March 2016, and possibly even 1 March 2017, due to ongoing consultation with NEDLAC (National Economic Development and Labour Council) (KPMG: 2014).

The savings behaviour of South Africans is also topical. As indicated in a study performed by Prinsloo, the gross savings of households as a percentage of the gross domestic product was 9.1 per cent for the period between 1960 and 1972 (Prinsloo, 2000:13). This decreased to 4.2 percent for the period between 1990 and 1999. As per the South African Savings Institute (SASI, 2006) this rate was just more than 1.5 percent in the first quarter of 2006. In 2014 the Ministry of Finance reported that the savings rate in 2013 was -2.2 percent (South Africa, 2013:2). It is therefore clear that the savings rate, as a percentage of the gross domestic product, is decreasing. The household savings include the contributions made to retirement funds and therefore an understanding of the household savings is relevant as all changes made to the tax legislation relating to retirement savings will be to stimulate household savings (National Treasury, 2014:1).

This study looks at the comparison between the income tax implications of retirement savings by an individual in a developing country (South Africa) and a developed country and specifically looks at the capping of retirement savings for tax purposes. Tanzi and Zee (2000:300) state that high tax levels cannot be reached in developing countries and therefore the differences between
developed countries and developing countries will also have to be considered. The study is thus to compare the income tax implications of retirement savings in South Africa to that of developed countries. The study specifically looks at the capped amount introduced when the changes were made to section 11(k) where there previously was no fixed capped amount for the deduction of contributions made to funds. This cap states that the maximum amount of contributions (to retirement funds) that a South African taxpayer may deduct for income tax purposes is capped at an amount of R350 000 (in total per annum).

The reason for comparing the income tax implications of South Africa with developed countries is that South Africa has a dual economy (Biepke, 2007:4). This means that the South African economy shows characteristics of both developed countries as well as developing countries. The study determines how the income tax implications for retirement savings in South Africa compare to that of developed countries (as the country has a dual economy), thus determining whether the income tax implications for retirement savings are in line with those of developed countries. The cap will have an influence on the developed portion of the South African population as it will only influence highly paid individuals in the marginal tax bracket. The income tax implications for the employers are not included in the study as these will not influence the cap amount. Performing a comparison between the cap amount in South Africa to those of developed countries is therefore viable.

1.2 Literature review of the topic/research area.

savings behaviour of South Africans, the current tax implications regarding retirement savings, why changes to the Income Tax Act are necessary as well as papers on the changes to the Income Tax Act announced in the 2012 budget speech and the implications thereof to individuals.

The current income tax implications in terms of the Income Tax Act No 58 of 1962 are the following:

- Employer contributions to pension and provident funds are not fringe benefits while contributions made to a retirement annuity fund will be a fringe benefit\(^1\);
- For the contributions made by the employer on behalf of the employee, an amount equal to 20\% of the total employee remuneration will be deductible for the employer, in terms of SARS practice. In terms of section 11(l) of the Income Tax Act the deduction is available at the discretion of SARS and the Commissioner must allow a deduction of at least 10\% of employee remuneration ;
- Employee contributions made to provident funds are not tax deductible while up to 7.5\% of the retirement funding income will be deductible in terms of employee contributions made to a pension fund;
- Up to 15\% of the non-retirement funding income will be deductible in terms of contributions made to a retirement annuity fund; and
- 100\% of provident fund income may be paid out while at least two thirds of a pension fund or retirement annuity fund must be taken as an annuity.

The Taxation Laws Amendment Act of 2013 (South Africa, 2013a), as validated by Foster (2014:7), states that the new tax implications in terms of section 11(k) will be the following:

- The limitations will now be calculated based on the “remuneration” and not the “retirement funding income” as before;
- A maximum of 27.5\% of the greater of the remuneration and the taxable income will be deductible per annum. The percentage will be multiplied by the aggregate of contributions made by the individual and the employer. This will also include provident fund contributions and employer contributions to approved life insurance; and

\(^1\) In terms of paragraph 13 of the Seventh Schedule to the Income Tax Act the taxable fringe benefit will be the cash equivalent of the cash value of the release of an amount owing by the employee. The employer’s contribution to a pension fund or provident fund is due based on the fund rules and is therefore not an amount due by the employee. As such, this will not be a fringe benefit in terms of this paragraph.
- There will be a cap of R350 000 per year on the amount deductible as discussed above; and
- All employer paid contributions made to a pension -, provident - or retirement annuity fund will now be taxed as a fringe benefit in terms of paragraph 2(l) of the Seventh Schedule to the Income Tax Act; and
- For pension -, provident- and retirement annuity funds two thirds of the benefit must be taken as an annuity while one third may be paid out as a lump sum.

### 1.3 Motivation of topic actuality

No information could be found on comparisons of the tax implications of retirement savings between different countries except for comparisons between OECD countries (Yoo and De Serres, 2005). South Africa is only an observer to the OECD and has therefore not been included in these studies. Since the capped amount is fairly new, no comparison could be found where the cap of contributions was compared between countries and South Africa was included in those studies. The impact of the cap is only researched by Australia as indicated above. This clearly indicates that there is a gap and therefore this research attempts to fill this gap.

Since changes are regularly made to the taxation of retirement savings, this research area is relevant. A whole pension fund reform process is also currently in process as announced by The Minister of Finance (South Africa, 2014:4). Amendments were made to section 11(k) of the Income Tax Act No 58 of 1962 where the cap amount of R350 000 per year was introduced. These changes should have been implemented from 1 March 2015. National Treasury announced on 16 October 2014, through a media statement, that the implementation will be postponed to 1 March 2016, and possibly even 1 March 2017, due to ongoing consultation with NEDLAC (National Economic Development and Labour Council) (KPMG: 2014). The topic is therefore relevant as the changes made to the section are fairly new. The changes were made to stimulate household retirement savings due to the fact that South Africa’s savings rate is very low, as indicated in a press release by National Treasury (South Africa, 2012:1). In this press release it is stated that households can retire comfortably and they can reduce excessive reliance on debt when the household savings are increased. This is also corroborated in 1.1 above where statistics regarding household savings were obtained. Based on the fact that much is written on the topic as included under “Literature review” above, it portrays the actuality of the topic.
Based on the above it would be relevant to determine whether the changes made to the Income Tax Act will be in line with that of developed countries, specifically referring to the fact that the amount of contribution deductions is capped for income tax purposes.

1.4 Problem statement

The household retirement savings of South Africans are declining. Changes to the income tax implications to stimulate savings when contributions are made to retirement funds are regularly discussed, as indicated in 1.1 above. For this study it is important to look at how the income tax implications for these contributions differ between developed countries and South Africa. This study specifically looks at whether the amounts of contributions are capped in developed countries and how this compares to the South African cap.

The following problem statement is addressed in this dissertation: A comparison on how the income tax implications for retirement savings differ between developed countries and South Africa relating to the cap of retirement saving deductions.

1.5 Objectives

1.5.1 Main Objective.

The main objective of the study is to determine how the income tax implications of retirement savings regarding the capping of contributions compare between developed countries and South Africa.

Developed countries are selected and these countries’ legislation relating to retirement savings are then compared to South Africa’s legislation on the same matter. The objective is to determine which changes need to be made to the Act to be more in line with the income tax implications of retirement savings in a developed country.

1.5.2 Secondary Objectives.

The secondary objectives of the dissertation are the following:

- To determine what the income tax implications for retirement savings in South Africa will be in terms of the new provisions of the Taxation Laws Amendment Bill, 2013 (chapter 2);
- To differentiate between developed and developing countries (chapter 3);
- To gain an understanding of the Mercer Melbourne Pension Fund Index as the developed countries from this index are used in the study (chapter 3);
- To determine the income tax implications for retirement savings in developed countries relating to the capping of contributions made (chapter 3);
- To determine the differences between the income tax implications for retirement savings in South Africa and developed countries (chapter 4); and
- To recommend changes that can be made to South African tax legislation regarding retirement savings (specifically referring to the capped amount) to be more in line with developed countries as analysed in this chapter and to summarise and conclude (chapter 4).

1.6 Research design/method
Paradigmatic assumptions and perspectives

1.6.1 Ontological assumptions.

Ontology is how the researcher views the world (McKerchar, 2008:1). Ahmed (2008:2) states that ontology is “the study of being”. The question to answer when looking at the ontological assumption would be to discuss what the nature of reality is.

In this study a realist view is adopted. The reality is external and it exists independently. The information for the countries and the tax consequences of retirement savings can be gained independently. This can be performed by research on the income tax implications of retirement savings in South Africa as well as in developed countries by gaining knowledge of the relevant income tax regulations.

1.6.2 Epistemological assumptions.

The epistemological assumptions look at the theory of knowledge. This describes the relationship between the knower and what can be known.

An interpretivist paradigm is followed in the study as knowledge can be derived from evidence gathered through the research phase. A conclusion could be made on what changes should be made to South African tax law regarding the cap on retirement savings to be more in line with that of developed countries after the tax law of South Africa as well as developed countries have been researched. Research will be qualitative in nature. Inductive reasoning is followed as deductions are made after the different tax laws have been researched.
1.6.3 Methodological assumptions.

The methodological assumption looks at how the enquirer can perform research to determine whether what he/she believes to be correct, is correct. Qualitative methods are followed as the relationship between data is considered. Legal research is also performed as tax laws are researched. This is a doctrinal approach as research in law is performed as the technical aspects of tax law are considered in the study.

Descriptive research is performed. This is the chosen methodology as the main objective of this methodology is to describe the state of affairs as it is in the present. This method allows the researcher to report on what is currently happening. Descriptive research is performed as the objective of the study is to compare the income tax implications of retirement savings in a developing country (South Africa) to that of developed countries (for example Denmark, Australia and Ireland).

The descriptive research is in the form of applied research. The aim of applied research is to find a solution for an immediate problem. In this case all the information is available. It should just be analysed and a conclusion should be reached.

The research is qualitative as the research areas are not based on the measurement of amounts. No quantitative research was performed as no quantitative data was collected from which conclusions were made. The qualitative research includes references to quantitative information when looking at the income tax implications as these include amounts.

Since there is a comparison between the tax implications in South Africa and those of developed countries, comparative research was also performed.

1.6.4 Literature review performed during the research phase

The purpose and the objective of the literature review are to answer the research question. A literature review was performed to gain an understanding of the income tax implications of retirement savings, specifically the cap amount, in South Africa as well as in developed countries; for example Denmark, Australia and Ireland. This was necessary to be able to perform a comparison between South Africa and developed countries. A literature review was also performed to define the difference between a developed country and a developing country.
The following sources of information were used during the research phase:

- Journals;
- Articles;
- Legislation;
- Books;
- Reports;
- Websites (scholarly websites as well as databases on the North-West University library website); and
- Theses.

1.7 Overview of chapters

Chapter one gives an introduction as well as the background to the study. The research question and the objective of the study are included. The research methodology is explained as well as the motivation for the specific research methodology.

The objective of chapter two is to understand what the income tax implications of retirement savings are in South Africa. This includes an understanding of the amended section 11(k) included in the Income Tax Act No 58 of 1962. This chapter specifically looks at the cap amount that was introduced in the Taxation Laws Amendment Bill 2013. An understanding of this is important to be able to compare the South African income tax implications to those of developed countries.

As the study looks at the different tax implications for developed and developing countries, assigning definitions to the terms “developed countries” and “developing countries” are addressed in chapter three. The developing country used in this study is South Africa.

In chapter three the rationale for the selection of the developed countries is discussed. The objective of this chapter is to substantiate the use of these countries in the study. An understanding of the Melbourne Mercer Global Pension Index (regarding pension funds) is also discussed as these countries take up top positions on this index.

Further, the objective of this chapter is to understand what the income tax implications in the developed countries are when contributions are made to retirement funds, specifically focussing
on the capping of contributions. This understanding is necessary to be able to compare the income tax implications with that of South Africa.

Chapter four compares the income tax implications of the developed countries with the income tax implications in South Africa. The objective of the chapter is to determine the similarities as well as the differences between the legislations of the developed countries and South Africa regarding retirement savings.

In this last chapter a conclusion is reached on the differences between the income tax implications of retirement savings regarding the cap in South Africa and of those in developed countries. The research problems are answered. The chapter also includes recommendations on how the Income Tax Act of South Africa can be adapted to be more in line with the income tax implications of those in developed countries. A summary is provided.
CHAPTER 2 – CURRENT SOUTH AFRICAN TAX CONSEQUENCES

2.1 Introduction

The objective of this chapter is to understand what the income tax implications of retirement savings will be in South Africa. An understanding of the current section 11(k) and section 11(n) of the Income Tax Act (No 58 of 1962) is discussed. The chapter specifically looks at the cap amount of retirement savings for income tax purposes, which was introduced in the Taxation Laws Amendment Act of 2013. An understanding of the South African income tax implications is important in order to compare these implications to those of developed countries.

2.2 Currently implemented section 11(k) and section 11(n) of the Income Tax Act No 58 of 1962

Currently the requirements for the deductibility of pension fund contributions are prescribed in section 11(k). The requirements for the deductibility of contributions made to retirement annuity funds are prescribed in section 11(n). The contributions made to a provident fund are not deductible in the hands of the employee. In terms of section 11(l) the contributions made by an employer to a pension fund, provident fund or benefit fund on behalf of its employees are deductible. This excludes a fund defined in paragraph a) of the definition of a benefit fund, which is any friendly society registered under the Friendly Societies Act. Three different deductions are currently available in the tax legislation; two of these deductions are for the taxpayer (the employee) and one for the employer (Income Tax Act No 58 of 1962).

2.2.1 Definitions

It is important to define the different types of funds to which contributions are made before the tax implications of the different funds can be discussed.

These funds are defined in section 1 of the Income Tax Act No 58 of 1962 (South Africa):

2.2.1.1 Pension fund

A “pension fund” includes any “pension, provident or dependents’ fund or any pension scheme established by law”. This also includes the above-mentioned funds established for any municipal employees or employees of any local authority. In subparagraph (c) in proviso (ii)(dd) it is also stated that not more than a third of the total value may be paid out as a single payment and the remainder must be paid out as an annuity, except where two-thirds of the total value does not
exceed R50 000 or where the employee is deceased. In such cases, the full benefit may be paid out as a lump sum. In the Taxation Laws Amendment Bill of 2013, this amount was increased to R100 000 (section 4(1)(zE)).

In terms of section 1 of the Pension Fund Act (No. 24 of 1956) a pension fund is an “association of persons” that is established to provide annuities or lump sum payments to the members or former members of the association when they reach retirement age. The pension fund will also provide these benefits to “dependents of the members or former members” when the members die.

2.2.1.2 Retirement annuity fund
A “retirement annuity fund” means “any fund (other than a pension fund, provident fund or benefit fund) which is approved by the Commissioner”. The fund should be permanent and “bona fide established for the sole purpose of providing life annuities” or annuities to the dependents or nominees of deceased members. Not more than a third of the total benefit may be paid out as a lump sum, “except where the two-thirds of the total value does not exceed R50 000 or where the member is deceased”. In the Taxation Laws Amendment Bill of 2013, this amount was increased to R100 000 (section 4(1)(zZb)).

2.2.1.3 Provident fund
A “provident fund” includes any fund which is not a pension fund, pension preservation fund, provident preservation fund, benefit fund or retirement annuity fund which is approved by the Commissioner. The fund should be permanent and bona fide be established to provide annuities to the members or the dependents or the nominees in the case where the member is deceased. The purpose of the fund may also be to provide benefits other than annuities.
2.2.2 Current Tax Legislation

The impact of the different sections as in the Income Tax Act are briefly summarised.

**Table 1: Current income tax implications of retirement savings**

<table>
<thead>
<tr>
<th>Section</th>
<th>Section 11(k)</th>
<th>Section 11(l)</th>
<th>Section 11(n)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deduction available for</td>
<td>Employee</td>
<td>Employer</td>
<td>Employee</td>
</tr>
<tr>
<td>Deduction relating to</td>
<td>Pension fund contributions</td>
<td>Any sum contributed to pension, provident or benefit fund (excluding friendly societies but including medical aid funds)</td>
<td>Retirement annuity fund contributions</td>
</tr>
</tbody>
</table>
| Deduction (current contributions) | The greater of:  
- R1 750;  
or  
- 7.5% of the remuneration derived during the year in respect of the ‘retirement-funding employment’.  
Limited to the actual contribution made. | Deduction of 10% of the approved remuneration.  
Approved remuneration is the fair and reasonable amount of remuneration that accrued to the employee in respect of the services rendered during the year of assessment.  
In practice a deduction of up to 20% is allowed by SARS. (Stiglingh et al, 2014:168) | The greater of:  
- 15% of the amount of income other than ‘retirement-funding employment’; or  
- R3 500 less any amount deducted in terms of section 11(k); or  
- R1 750.  
The deduction is limited to the income of the taxpayer. The deduction cannot create or increase an assessed loss.  
The amount not deducted may be carried forward. |

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2 The term is defined in section 1 of the Income Tax Act. This will include remuneration in terms of the Fourth Schedule to the Income Tax Act. This includes remuneration, emolument, salary as well as fees that form the pensionable salary – thus the amount on which the pension or provident contributions are based. This definition will not be included in the Act after the amendments.
Table 1: Current income tax implications of retirement savings (continued)

<table>
<thead>
<tr>
<th>Section</th>
<th>Section 11(k)</th>
<th>Section 11(l)</th>
<th>Section 11(n)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deduction (arrear contributions)</td>
<td>- Excess amount can be carried forward to the next period.</td>
<td></td>
<td>- The amount is also limited to the deduction that the member would have received in terms of section 11(n) in the previous year of assessment (as it applied in that year).</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>- The excess amount can be carried forward to the next period.</td>
</tr>
<tr>
<td>Fringe Benefit</td>
<td>Where an employer pays an amount to the pension fund on behalf of the employee, it is not a fringe benefit as it does not qualify as the payment of debt on behalf of the employee. (Par 2(h) of the Seventh Schedule – Income Tax Act No 58 of 1962)</td>
<td>Not applicable.</td>
<td>Where the employer made a contribution on behalf of the employee and it has been included in the income of the employee, it is deemed to be made by the employee for this section.</td>
</tr>
</tbody>
</table>

Income Tax Act No 58 of 1962 (own compilation)

2.3 Reason for changes to the current legislation

In the Explanatory Memorandum on the Taxation Laws Amendment Bill of 2013 the reasoning behind the revised contribution incentives for retirement savings is discussed (South Africa, 2013b). It is stated that the government has been encouraging South Africans to contribute to retirement by giving them a tax incentive. The tax treatment is also fragmented and it differs between funds. A more consistent treatment is preferred where the result will be the same irrespective of the source of the funding. The current treatment of the contributions made by
employers and individuals does not always produce an equitable result (South Africa, 2013b).

As indicated in a press release by National Treasury (South Africa, 2014), the proposed retirement reforms are aimed at ensuring that pension fund members are better protected and that they will have enough savings to retire comfortably. The government wants to encourage workers to keep their savings until they retire. It is also stated that only six percent of South Africans will be able to maintain their lifestyle and be able to replace their income when they retire (South Africa, 2014).

The press release also indicates that workers cash in their retirement savings when they resign instead of preserving these funds. The consequence of this is that the savings do not have enough time to grow and individuals end up not having sufficient savings for retirement.

In current legislation, the members of a provident fund can get their full benefit as a lump sum. This leaves people that retire vulnerable and in later years they cannot afford their retirement (South Africa, 2014). The Government therefore wants to encourage retirees to reduce the lump sums that they take from their provident fund when retiring and encourages them to take the biggest part of the benefit as an annuity. The accumulated funds up until the effective date of the new legislation can still be taken as a lump sum (South Africa, 2014). For members over 55 the funds can still be taken as a lump sum. The conversion will thus only be for new contributions made by members younger than 55 years of age.

2.4 Amended section 11(k) of the Income Tax Act No 58 of 1962

As indicated above, National Treasury proposed changes to the current legislation to encourage workers to save more. The changes were included in the Taxation Laws Amendment Bill of 2013 (South Africa, 2013). These amendments would have become effective on 1 March 2015 on all contributions made on or after this date. A recent proposal was made by National Treasury to Parliament to postpone this implementation until March 2017. The amended section 11(k) would have the following to effect as indicated in the Taxation Laws Amendment Bill of 2013 (South Africa, 2013):
### Table 2: Amended section 11(k) implications

<table>
<thead>
<tr>
<th>Section</th>
<th>Section 11(k)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(South Africa, 2013)</td>
</tr>
<tr>
<td><strong>Deduction available for</strong></td>
<td>Employees</td>
</tr>
<tr>
<td><strong>Deduction of contributions</strong></td>
<td>Any amount contributed to any pension fund, provident fund or retirement annuity fund.</td>
</tr>
<tr>
<td><strong>Deduction</strong></td>
<td>Total deduction per year may not exceed the lesser of:</td>
</tr>
<tr>
<td></td>
<td>- R350 000</td>
</tr>
<tr>
<td></td>
<td>- 27.5% of the higher of:</td>
</tr>
<tr>
<td></td>
<td>• Remuneration as defined in the Fourth Schedule</td>
</tr>
<tr>
<td></td>
<td>• Taxable income as determined before taking any deduction in terms of this section into account.</td>
</tr>
<tr>
<td></td>
<td>If contributions could not be deducted in a prior year due to the fact that it exceeds the deduction allowable, it will be deemed to be an amount contributed in the current year of assessment.</td>
</tr>
<tr>
<td><strong>Fringe benefit</strong></td>
<td>Any amount contributed to a fund on behalf of an employee will be a fringe benefit and will be deemed to be a contribution made by the employee for purposes of section 11(k) (Par 2(l) of the Seventh Schedule to the Income Tax Act No 58 of 1962).</td>
</tr>
</tbody>
</table>

**Taxation Laws Amendment Bill 2013 (own compilation)**

In terms of the amended section 11(l), the employer will be able to deduct any contributions made on behalf of the employee to any pension fund, provident fund and retirement annuity fund and it will not be capped to 10% (20% in practice) (Stiglingh et al, 2014:168) of the approved remuneration as the current legislation reads. When contributions are made to a defined contribution fund the fringe benefit will be the actual cash contribution. In the case of a defined benefit fund a special formula will be used to determine the fringe benefit (South Africa, 2013). Section 11(n) will also be deleted as section 11(k) now provides for contributions made to pension funds, provident funds and retirement annuity funds and therefore section 11(n) is not necessary anymore.
It should also be considered that the benefit that is being paid out by the pension fund, provident fund and the retirement annuity fund may be taxed in terms of the Second Schedule to the Income Tax Act. No amendment regarding the taxation of lump sum benefits has been made when the amendments were made to section 11(k).

As indicated above, a cap amount of R350 000 was introduced in the Taxation Laws Amendment Bill. This caps the amount of the deduction available for all contributions made to pension funds, provident funds and retirement annuity funds.

2.5 Understanding the cap amount

The cap amount as introduced in the new section 11(k) will be the main focus in the comparison following in the next chapter. The cap was introduced to support the fiscus and to ensure that high earners do not shield their income from the tax collector (Nathan, 2012). The cap will have an influence on taxpayers where the taxable income exceeds R1 272 730 (R350 000 ÷ 27.5%) per annum (Foster, 2014). Ndlovu (2013) states that the Minister should increase the cap amount to be more in line with other countries to encourage savings.

2.5.1 Disadvantages of the cap

Nathan (2012) states the following disadvantages of the cap:

- It disincentivises savings in countries with low savings rates;
- it may lead to offshore savings; and
- by disallowing higher contributions now, Treasury forfeits higher tax revenues in future (when the benefit is paid out).

He also states that if the cap is not adjusted annually, it may also start to limit middle income households. The impact of the cap may be that members of retirement funds cannot deduct all their contributions and therefore they may consider investing offshore as there is no tax incentive to contribute to South African funds. Benefits paid by retirement funds are taxed when a payment is made to a member in terms of the Second Schedule to the Income Tax Act No 58 of 1962. If the contributions made by members are capped when contributing, this means that the pension fund benefit will be smaller and therefore Treasury will lose tax when the benefit is being paid out. This will not be the case as there will be tax on a benefit when contributions are made and when a contribution is not deductible the taxable income of the person will be more and therefore
SARS will not lose any tax. In the Explanatory Memorandum to the Taxation Laws Amendment Bill 2013 (South Africa, 2013:9) it is stated that the cap is introduced to ensure that wealthy individuals do not get excessive deductions for contributions made to funds.

2.5.2 Impact of the cap amount

The capping of the amount will work as follows (example taken from Momentum, 2014:2) for example:

The cost to company (remuneration) of a person is R1 750 000 per annum. The basic salary is R1 500 000 per annum. His employer contributes 15% (of his basic salary) to the defined contribution pension fund while he contributes 7.5% of his basic salary. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

- Employer contribution to pension fund: R225 000
- Member contribution to pension fund: R112 500
- Member contribution to retirement annuity fund: R75 000

He also receives R120 000 from his business and incurs business expenses of R250 000. His taxable income will be determined as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>R1 500 000</td>
</tr>
<tr>
<td>Employer contribution (fringe benefit)</td>
<td>R225 000</td>
</tr>
<tr>
<td>Business income</td>
<td>R120 000</td>
</tr>
<tr>
<td>Business expenses</td>
<td>(R250 000)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>R1 595 000</td>
</tr>
</tbody>
</table>

As his remuneration of R1 750 000 is higher than the taxable income as determined, the contribution deductible will be calculated based on the remuneration,

The total contributions made equals R412 500. The deduction will be calculated as the lesser of:

- 27.5% of the higher of the taxable income or the remuneration; and
- R350 000.
Therefore:

- 27.5% of R1 750 000 is R481 250.

As this is more than R350 000, only R350 000 will be deductible in the current year of assessment and the balance will be deductible in the following year of assessment. If his contributions stay the same year on year, the amount will keep rolling forward. If it cannot be deducted, it will be taken into account when the lump sum is paid on retirement and the amount can then be deducted from the lump sum before the tax implications of the lump sum are determined.

It is clear from the above that the new section will cap the amount of deductible contributions at R350 000.

The current income tax implication would be that there will be a deduction for the pension fund contribution as well as the retirement annuity fund contribution. The retirement annuity fund contribution to be deducted will be limited to the greatest of 15% of the income other than “retirement-funding employment”, R3 500 minus any pension fund contributions deducted for income tax purposes or R1 750. The income other than the retirement-funding employment will thus be the R120 000, which is income received from the business, minus the business expenses to the amount of R250 000. The deduction that the taxpayer would receive would thus be R131 250 (R1 750 000 x 7.5%). The deduction for the retirement annuity contributions will be R1 750 as the amount of pension contributions deducted will be more than R3 500 and the income other than the “retirement-funding employment” is negative. This means that he taxpayer will get a deduction amounting to R133 000.

In terms of the old legislation the taxpayer would therefore receive a deduction of R133 000, while he will receive a deduction of R350 000 under the new tax legislation, thus indicating that the taxpayer will be in a better tax position in terms of the new legislation.

2.6 Conclusion

In this chapter the current income tax implications as well as the amended section 11(k) have been discussed. The reasons for the amendments have also been discussed. The chapter refers specifically to the cap imposed on the deductions of retirement savings for income tax purposes. An understanding of the South African income tax implications has therefore been discussed, as the next chapter looks at the income tax implications in other developed countries and
specifically at whether they cap the amount of contributions that is deductible for income tax purposes.
CHAPTER 3 – THE CAPPING OF RETIREMENT CONTRIBUTIONS IN DEVELOPED COUNTRIES

3.1 Introduction

In chapter 2 the South African tax consequences of retirement contributions were discussed. This chapter defines developed and developing countries. As the developed countries used in the study are selected from the Melbourne Mercer Global Pension Index, an understanding of this index will also be gained. The rationale for the selection of the countries is explained, after which the income tax implications and the cap of retirement contributions for taxation purposes are discussed for the selected countries. The tax implications of the developed countries, and specifically whether there is a cap on the amount of retirement contributions that can be deducted for income tax purposes, are then compared to the income tax implications in South Africa as discussed in the previous chapter.

3.2 Reason for comparing South Africa to developed countries

The cap will have an influence on taxpayers whose taxable income exceeds R1 272 730 per annum (Foster, 2014). This means that the cap amount will only have an influence on taxpayers who fall within the highest marginal tax bracket as included in the Income Tax Act. These taxpayers represent the developed sector of our country. As this is the case, South Africa will be compared to developed countries. The reason is thus to determine how the South African tax law should be changed to be more in line with those of developed countries, and also to see where South Africa can learn from other developed countries.

3.3 Defining developed and developing countries

In the comparison which will be performed, South Africa will be the developing country in the study, while countries from the Melbourne Mercer Global Pension Index will be used as developed countries. It is therefore important to define developed and developing countries before the comparison is performed.
3.3.1 Developed countries

The Oxford Dictionary defines developed as being “of a country or region advanced economically and socially” (Oxford, 2015). A developed country is a country that shows a modern infrastructure (both physical and institutional) (Parker & Veldsman, 2010:1). These countries move away from low-value-added sectors like agriculture and resource extraction. The focus of these countries is more intellectual and they are involved in capital based economic activities. The standard of living is high and countries have economic systems based on continuous, self-sustaining economic growth. According to Investopedia there is a relatively high level of economic growth and security. The evaluation of the degree of development of a country can be determined by means of the following criteria: the gross domestic product (GDP) or the income per capita, the level of industrialization, general standards of living and the amount of widespread infrastructure. Other non-economic factors are also included in evaluating the development of a country. This will include the degree of education, literacy and health (Investopedia, s.a.).

3.3.2 Developing countries

Developing countries have relatively low standards of living, undeveloped industrial bases and moderate to low human development indices (HDI). These countries have low per capita income, widespread poverty and low capital information. A significant degree of industrialisation relative to the populations has not been achieved. There is also a strong correlation between low income and high population growth (Parker & Veldsman, 2010:1). Investopedia indicates that the term “developing countries” refers to countries that do not have the same level of economic security, industrialization and growth as developed countries. The United Nations Conference on Trade and Development (UNCTAD) states that developing countries are highly disadvantaged in the development process, many of them based in their geographical place. There is also a higher risk for developing countries that they will not be able to come out of poverty when the country is poverty-stricken. According to The International Statistical Institute, South Africa is ranked on the list of developing countries (The International Statistical Institute). This is based on the fact that the Gross National Income (GNI) is less than US$11 905 per capita per year.
3.4 Melbourne Mercer Global Pension Index

The Melbourne Mercer Global Pension Index (MMGPI) was introduced in 2009 (Melbourne Mercer Global Pension Index). The Index is a partnership between the Australian Centre for Financial Studies (ACFS) and Mercer. Mercer is a global leader in pension fund management and consulting while ACFS is an independent non-profit research institute. The funding is provided by the Victorian Government (Melbourne Mercer Global Pension Index).

The Index includes a wide range of countries; ranging from developed to developing countries. Since 2009 the Index has been providing a report regarding pension funds on a yearly basis. The number of countries used in the study increased to 25 in 2014 while 11 countries were used in the study in 2009. The pension systems around the world are under pressure due to longer life expectancies, increased government debt in many countries, uncertain economic conditions and the global shift to defined contribution plans. South Africa has been included in the Index for the first time in 2014 (Melbourne Mercer Global Pension Index).

3.4.1 Objective of the MMGPI

The objective of the MMGPI is to use more than 50 questions to benchmark each country’s retirement income system. The Index will also indicate any shortcomings and from these the Index may also suggest possible areas of reform (Melbourne Mercer Global Pension Index, 2014: 3). An index is calculated per country out of 100. The Index takes into account the adequacy, sustainability and the integrity of pension fund systems. The Index value per country will represent a weighted average of three sub-indices. The adequacy is weighted at 40%, sustainability at 35% and integrity at 25% (Melbourne Mercer Global Pension Index, 2014:6).

The same weighting system has been used since the 2009 report.

The adequacy looks at the benefits that are currently being provided and also looks at the benefit design features. Sustainability looks at whether the system will be able to provide the same benefits in future. The confidence that the citizens have in the pension fund system will impact the integrity sub-index. The 25 countries are then ranked based on the index calculated (Melbourne Mercer Global Pension Index, 2014:6).

The index looks at the following indicators:
Table 3: MMGPI sub-indices and the indicators

<table>
<thead>
<tr>
<th>Sub-index</th>
<th>Indicators</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adequacy</td>
<td>• Benefits&lt;br&gt;• Savings&lt;br&gt;• Tax support&lt;br&gt;• Benefit design&lt;br&gt;• Growth of assets</td>
</tr>
<tr>
<td>Sustainability</td>
<td>• Coverage&lt;br&gt;• Total assets&lt;br&gt;• Contributions&lt;br&gt;• Demography&lt;br&gt;• Government debt</td>
</tr>
<tr>
<td>Integrity</td>
<td>• Regulation&lt;br&gt;• Governance&lt;br&gt;• Protection&lt;br&gt;• Communication&lt;br&gt;• Costs</td>
</tr>
</tbody>
</table>

(Melbourne Mercer Global Pension Index, 2014: 6) (own compilation)

The Index focuses on the provision of financial security in retirement. It is not a comprehensive measurement of living standards when people have retired (Melbourne Mercer Global Pension Index, 2014:15). The Index has also started focusing on transparency and trust in pensions (Melbourne Mercer Global Pension Index, 2014:3). With the recent reform from defined benefit to confined contribution systems, it is essential that members have greater clarity and understanding so that they can make better decisions. Members are starting to make more decisions regarding the contribution levels, investment selection as well as the form of their retirement benefit (Melbourne Mercer Global Pension Index, 2014:19). In a defined benefit plan, the employee bears the risk of the investment return being higher or lower than expected. In a defined contribution plan this risk is transferred to the members of the fund (South Africa, 2004:6). The change from defined benefit to defined contribution funds was made as the defined benefit fund is designed so that the employee will be in the service of the employer for a long time. When a benefit is paid out before resignation, but when the member retires or dies, the benefit will be less than it would have been if the member invested the money himself (South Africa, 2004:10).

As indicated above, the Index also looks at the tax support that is provided by the pension system as part of the adequacy sub-index. As such, the tax also influences how the countries are ranked and this substantiates why the countries selected are from the MMGPI. Even though the ranking
of the countries is not entirely based on their taxation systems, this will have an influence on the rankings. The adequacy sub-index will now be discussed further.

3.4.2. Adequacy sub-index

As per the 2014 report (Melbourne Mercer Global Pension Index, 2014:13) the adequacy sub-index is the most obvious way to compare different pension systems as the primary objective of any pension system is to provide adequate retirement income. The following six factors are taken into consideration when determining the adequacy (Melbourne Mercer Global Pension Index, 2014:13):

- Are voluntary contributions made by the member of the fund treated more favourably by the tax system than having the money in the bank? Will the pension fund be taxed on the investment income received? If the investment income is taxed this means that the compounding effect of interest will be lost and the adequacy of future benefits will therefore be reduced.
- Is the retirement age determined or can the retirement income leak before the member retires?
- If a member retires, will he receive his full benefit? Will the member be able to move the pension benefit to another fund? This therefore determines what happens when a person changes employment.
- Which part of the retirement benefit should be taken up as an income stream? Are there any tax incentives for taking the benefit as an income stream rather than a lump sum?
- When there is divorce or separation, are the individual’s pension benefits taken into account in the division of the assets? This may have a major influence on the financial security of one or both of the partners.
- Should contributions be paid to the pension fund in the period that a person is temporarily out of the workforce and receives income support? The individual’s retirement income can be affected if there is no requirement that the benefits should continue to accrue (Melbourne Mercer Global Pension Index, 2014:13).

This sub-index takes into account the tax treatment in terms of retirement funds and therefore the countries selected for the comparison are the developed countries with the highest rankings in terms of the adequacy sub-index. The sub-index considers whether there are any tax incentives to take the pension benefit as an income stream and not a lump sum benefit. It also considers whether the tax treatment of voluntary contribution to a pension fund is better than investing money in a bank account.
The higher the index in a certain category, the better the country performs in that specific category. Assigning marks when certain criteria are met and determining an index out of 100 per country, a comparison can be made between the countries on the MMGPI and the countries with better pension fund systems in accordance with the index can be identified.
The following represents the overall index per country as disclosed in the 2014 report:

**Table 4: Overall index per country: 2014**

<table>
<thead>
<tr>
<th>Country</th>
<th>Overall Index Value</th>
<th>Sub-Index Values</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Adequacy</td>
</tr>
<tr>
<td>Australia</td>
<td>79.9</td>
<td>81.2</td>
</tr>
<tr>
<td>Austria</td>
<td>52.8</td>
<td>67.5</td>
</tr>
<tr>
<td>Brazil</td>
<td>52.4</td>
<td>61.8</td>
</tr>
<tr>
<td>Canada</td>
<td>69.1</td>
<td>75.0</td>
</tr>
<tr>
<td>Chile</td>
<td>68.2</td>
<td>57.3</td>
</tr>
<tr>
<td>China</td>
<td>49.0</td>
<td>62.5</td>
</tr>
<tr>
<td>Denmark</td>
<td>82.4</td>
<td>77.5</td>
</tr>
<tr>
<td>Finland</td>
<td>74.3</td>
<td>72.2</td>
</tr>
<tr>
<td>France</td>
<td>57.5</td>
<td>76.4</td>
</tr>
<tr>
<td>Germany</td>
<td>62.2</td>
<td>75.8</td>
</tr>
<tr>
<td>India</td>
<td>43.5</td>
<td>37.1</td>
</tr>
<tr>
<td>Indonesia</td>
<td>45.3</td>
<td>37.5</td>
</tr>
<tr>
<td>Ireland</td>
<td>62.2</td>
<td>77.6</td>
</tr>
<tr>
<td>Italy</td>
<td>49.6</td>
<td>68.1</td>
</tr>
<tr>
<td>Japan</td>
<td>44.4</td>
<td>48.0</td>
</tr>
<tr>
<td>Korea (South)</td>
<td>43.6</td>
<td>42.6</td>
</tr>
<tr>
<td>Mexico</td>
<td>49.4</td>
<td>49.9</td>
</tr>
<tr>
<td>Netherlands</td>
<td>79.2</td>
<td>75.3</td>
</tr>
<tr>
<td>Poland</td>
<td>56.4</td>
<td>61.7</td>
</tr>
<tr>
<td>Singapore</td>
<td>65.9</td>
<td>56.4</td>
</tr>
<tr>
<td>South Africa</td>
<td>54.0</td>
<td>48.3</td>
</tr>
<tr>
<td>Sweden</td>
<td>73.4</td>
<td>67.2</td>
</tr>
<tr>
<td>Switzerland</td>
<td>73.9</td>
<td>71.9</td>
</tr>
<tr>
<td>UK</td>
<td>67.6</td>
<td>69.8</td>
</tr>
<tr>
<td>USA</td>
<td>57.9</td>
<td>55.2</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td><strong>60.6</strong></td>
<td><strong>63.0</strong></td>
</tr>
</tbody>
</table>

*Source: (Melbourne Mercer Global Pension Index, 2014: 8)*

As can be seen in the table above, the three sub-index values are used to determine an overall index value per country. It can be seen that Australia has the highest overall index value with an overall score of 79.9, indicating that Australia has the best pension system of all the countries included in the MMGPI. South Africa is much lower on the list with an overall index of 54.

### 3.4.3 Relevance of the MMGPI

The MMGPI is used to select the developed countries in the comparison between South Africa and developed countries. The reason for this is that the Index indicates the countries with the
best pension systems in the world. As the tax system is presented as part of the adequacy sub-index, the countries with the highest rankings in this sub-index were used in the comparison. Comparing South Africa to developed countries from the Index, ensures that the South African pension system is compared to the best pension systems world-wide. As all countries would strive to good pension systems, it will be appropriate to select countries from this Index.

3.5 Countries selected for comparison

The countries selected for the study is from the MMGPI. The countries selected are the top developed countries as per the adequacy sub-index for 2014. The 2014 report is used as this represents the most recent report. Comparing South Africa to the top developed countries on the list will give a clear indication of the differences between the South African income tax implications and the income tax implications of developed countries. The countries selected for the comparison are the following: Australia (81.2%), Ireland (77.6%) and Denmark (77.5%). The tax consequences for the 2015 year of assessment have been used in the study as it is the most recent information available. For all countries the 2015 year of assessment has been used to make the information more comparable. The tax consequences regarding retirement savings will now be discussed, including whether the contributions deductible for tax purposes will be capped.

3.5.1 Australia

3.5.1.1 Tax Authority

Australia has the highest value as per the adequacy sub-index per the MMGPI, being 81.2 (Melbourne Mercer Global Pension Index, 2014:8). The Australian Taxation Office is responsible for revenue collection of the Australian government on behalf of the Commissioner of Taxation (Australian Government, 2015a). As with the tax legislation in all countries, the legislation makes provision for different types of funds. This will now be discussed.
3.5.1.2. Types of funds included in tax legislation

In Australia there are five basic types of funds:

- Industry funds: These funds are available to all members of the public. It may also be the case that the employee works for a specific industry and the employer signs the employee up with the fund.
- Retail funds: These funds are run by financial institutions and are available to the public.
- Public sector funds: These funds offer defined benefit plans and constitutionally protected funds to the members. These funds are open for the Commonwealth, state and government employees.
- Corporate funds: These are funds that are available for the people working for a specific institution or employer. These funds may be defined benefit funds.
- Self-managed super funds: These funds work like all the other super funds but all investment decisions and legal responsibilities lie with the trustee, which will be the member of the fund. The member is also responsible to manage the fund which means that the member makes the investment decisions (Australian Government, 2015d).

3.5.1.3. Capping of contributions for tax purposes

In Australia the pension funds are referred to as “superannuation” (in short referred to as “super”). The tax that you pay on your super will depend on the following:

- Whether the contribution was made before or after income tax was paid on the amount;
- Whether the super contributions cap has been exceeded; and
- Whether the taxpayer is a high-income earner (Australian Government, 2015b).

In Australia it has to be considered whether the contributions made are concessional or non-concessional (see below). There will be different tax implications and therefore these contributions have to be considered separately. There may also be excess contributions tax or Division 293 tax as discussed below (Australian Government, 2015b). A deduction of the contributions will be available unless more than 10% of your assessable income is obtained from an employer (Australian Government, 2014). The assessable income is the income that tax will be payable on and therefore includes all income received from the employer. For an employee there will thus not normally be a deduction for the contributions made to a retirement fund.
Before-tax super contributions (Concessional)

Before-tax contributions are from amounts that have not been taxed yet. The before-tax super contributions will include the following (Australian Government, 2015b):

- Contributions made to super funds by the employer. This may be compulsory payments made by the employer or salary sacrifice payments made to the super funds;
- Where contributions will be deductible from income as in the case where the contributions are made by someone who is self-employed; and
- Notional taxed contributions made by a member of a defined benefit plan.

These contributions are taxed at a rate of 15% in the fund. These contributions (being concessional contributions) are not taxed yet and they will not be included in the income to be taxed as the contributions made are taxed separately at the rate of 15%. There is, however, a cap on the amount of contributions that should not be taxed at the marginal tax rate but at a rate of 15%. For the concessional contributions the yearly cap for the 2015 – 2016 tax year for taxpayers under 50 years old will be $30 000 for the year. When the taxpayer contributes more than this limit, the amount over $30 000 will be added to the taxpayer’s income and be taxed at the marginal income tax rate. When the taxpayer is 50 or over 50, the cap will be $35 000 (Australian Government, 2015c).

After-tax super contributions (Non-concessional)

After-tax super contributions will be made from amounts that have been taxed already. The after-tax super contributions can include the following:

- Contributions made by an employee or an employer from after-tax income;
- If your spouse makes contributions to your super fund;
- Where personal contributions are made to super funds that cannot be deducted from income tax (Australian Government, 2015b).

These contributions are not subject to tax. There is, however, a cap of $180 000 for the 2015-2016 tax year of the amount of non-concessional contributions that can be made. The contributions over the $180 000 will be taxed at a rate of 49%. There is also a bring forward provision for people under 65. These taxpayers are allowed to go over the non-concessional cap by up to two years’ worth of contributions without any penalty. This means that $540 000 can be contributed in a year (Australian Government, 2015c).
Excess contributions tax

Depending on your age, there is a limit on the before-tax and the after-tax contributions that can be made to your super. In the case of before-tax super contributions, if the cap is exceeded the excess will be included in the income tax return and taxed at the marginal rate. Some of the excess contributions can then be withdrawn to pay the additional tax (Australian Government, 2015b).

In the case where the after-tax super contributions cap is reached, the taxpayer can decide to withdraw the excess contributions and also any earnings on these contributions. The earnings will be included in the income tax return of the taxpayer and taxed at the marginal rate. If the excess cash is not withdrawn, tax will be payable on the excess (Australian Government, 2015b). The excess contributions tax is discussed under the “Before tax contributions” and the “After-tax contributions” above as the excess contributions tax will differ based on the type of contribution made.

Division 293 tax for very high income earners

When a taxpayer’s income, combined with contributions to super, exceeds $300 000 per year, additional tax, known as Division 293 tax, will be payable. Division 293 tax will be calculated as 15% of the taxable concessional (before-tax) contributions above the $300 000 threshold (Australian Government, 2015e). This will amount to R2 625 000 ($300 000 x R8.75) as at 27 February 2015. If the taxpayer is a member of a defined benefit fund, the tax may be calculated on the notional contributions which are not taxed. This means that the amount is based on the annual increase in a defined benefit superannuation account based on what the individual expects when he/she leaves the fund (Australian Government, 2015e).

3.5.1.4. Tax on benefits

The objective of this study is to compare the cap of contributions in South Africa to those of developed countries. The contributions cannot be seen in isolation as it may be that the contributions are not capped, as there will be adverse tax consequences when benefits are paid out. Therefore the tax on benefits will be considered.

In Australia the tax consequences on benefits paid out will differ based on a number of factors, such as the age of the member and whether the benefits come from a taxed or untaxed source. The tax consequences will also differ based on whether the benefit is being paid out as a lump sum (once-off payment) or as an income stream (Australian Government, 2015f). The tax will
depend on which part of the benefit is tax-free, taxable or untaxable. This will depend on the type of contribution that was made and whether tax was paid on the contributions (Australian Government, 2015g). Non-concessional (after-tax) contributions made will be tax-free as tax has already been paid on the amount. Other after-tax contributions will also be tax-free unless the taxpayer has received a deduction for the contributions made to a super fund. Where the member has made concessional contributions, the benefit will be taxable when paid by the super fund. The tax payable on the withdrawals will depend on the age of the member and also whether the super fund has paid tax on the contributions (Australian Government, 2015g).

Where the super fund has paid tax at a rate of 15% on the concessional contributions, these benefits will be the taxed element of the taxable super benefits. If no tax has been paid on the concessional benefits, the money is the untaxed element of the super benefit that will be taxed (Australian Government, 2015g).

Therefore a benefit will normally include a tax-free, as well as a taxable component, which will consist of a taxed element as well as an untaxed element. When a member gets a benefit, the super fund will calculate which part of the benefit will be tax-free and which part taxable. This will be based on the same proportion as the contributions that were paid to the fund (Australian Government, 2015g).

**Tax on tax-free element**

No tax will be payable on the tax-free element. This will be for concessional contributions. This will be regardless of the age of the members (Australian Government, 2015g).

**If the member is younger than the preservation age**

The preservation age is 60 if a member was born after 1 July 1964. This is the age at which members may access their super if they are retired. The following table will show the tax implications when a member receives a benefit before the preservation age:
Table 5: Income tax implications of benefits when member is younger than preservation age

<table>
<thead>
<tr>
<th>Type of super</th>
<th>Type of withdrawal</th>
<th>Effective tax rate (including Medicare levy)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxable component – taxed element</td>
<td>Income stream</td>
<td>Your marginal tax rate</td>
</tr>
<tr>
<td>Taxable component – taxed element</td>
<td>Lump sum</td>
<td>Your marginal tax rate or 22%, whichever is lower</td>
</tr>
<tr>
<td>Taxable component – untaxed element</td>
<td>Income stream</td>
<td>Your marginal tax rate</td>
</tr>
<tr>
<td>Taxable component – untaxed element</td>
<td>Lump sum</td>
<td>Your marginal tax rate or 32%, whichever is lower</td>
</tr>
</tbody>
</table>

(Australian Government, 2015g)

If a member is older than 60 years

If a member is older than 60 years and has therefore also passed the preservation age, the tax consequences of the benefits will be different. The following table will summarise the tax implications:

Table 6: Income tax implications of benefits when member is 60 years or older

<table>
<thead>
<tr>
<th>Type of super</th>
<th>Type of withdrawal</th>
<th>Effective tax rate (including Medicare levy)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxable component – taxed element</td>
<td>Income stream</td>
<td>No tax</td>
</tr>
<tr>
<td>Taxable component – taxed element</td>
<td>Lump sum</td>
<td>No tax</td>
</tr>
<tr>
<td>Taxable component – untaxed element</td>
<td>Income stream</td>
<td>Your marginal tax rate less tax offset of 10%</td>
</tr>
<tr>
<td>Taxable component – untaxed element</td>
<td>Lump sum</td>
<td>Your marginal tax rate or 17%, whichever is lower</td>
</tr>
</tbody>
</table>

(Australian Government, 2015g)

As the benefits are taxed at the marginal rate, the income tax rates will be the following for the 2015 – 2016 year of assessment (Australian Government, 2015h):
Table 7: Income tax rates for 2015 -2016

<table>
<thead>
<tr>
<th>Taxable income</th>
<th>Tax on this income</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 – $18 200</td>
<td>Nil</td>
</tr>
<tr>
<td>$18 201 - $37 000</td>
<td>19c for each $1 over $18 200</td>
</tr>
<tr>
<td>$37 001 - $80 000</td>
<td>$3 572 plus 32.5c for each $1 over $37 000</td>
</tr>
<tr>
<td>$80 001 - $180 000</td>
<td>$17 547 plus 37c for each $1 over $80 000</td>
</tr>
<tr>
<td>$180 001 and over</td>
<td>$54 547 plus 45c for each $1 over $180 000</td>
</tr>
</tbody>
</table>

(Australian Government, 2015h)

3.5.1.5. Summary

From the above it is clear that the tax deductions for contributions made are capped and additional tax may be raised on amounts contributed above these caps. The following table will summarise the capping of contributions made to retirement funds for income tax purposes.

Table 8: Australian caps, tax payable and actions

<table>
<thead>
<tr>
<th>Type of contribution</th>
<th>Cap</th>
<th>Tax effect</th>
<th>Actions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concessional</td>
<td>$30 000 per annum (if under 50 years in 2015-2016)</td>
<td>Amount over cap will be included in taxable income and taxed at marginal income tax rate</td>
<td>Taxpayer can elect to release up to 85% of the excess contributions. Only 85% can be released as the super fund already paid 15% contributions tax. A 15% tax offset will be received for this on the tax return.</td>
</tr>
<tr>
<td>Concessional</td>
<td>$35 000 per annum (if 50 or over 50 in 2015 – 2016)</td>
<td>Amount over cap will be included in taxable income and taxed at marginal income tax rate</td>
<td>Taxpayer can elect to release up to 85% of the excess contributions. Only 85% can be released as the super fund already paid 15% contributions tax. A 15% tax offset will be received for this on the tax return.</td>
</tr>
</tbody>
</table>
Table 8: Australian caps, tax payable and actions (continued)

<table>
<thead>
<tr>
<th>Type of contribution</th>
<th>Cap</th>
<th>Tax affect</th>
<th>Actions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-concessional</td>
<td>$180 000</td>
<td>49% for amounts over $180 000.</td>
<td>An excess non-concessional determination is available. The taxpayer can withdraw all the excess non-concessional contributions and 85% of the earnings. The return will be taxed at the marginal rate. The super fund would have paid 15% tax on the earnings and therefore a 15% tax offset will be available.</td>
</tr>
</tbody>
</table>

(Australian Government, 2015c) (own compilation)

3.5.2. Ireland

3.5.2.1 Tax Authority

Ireland is the country with the second highest index in terms of the adequacy sub-index with 77.6 out of 100. The Office of the Revenue Commissioners is responsible to collect tax, duties and also to implement Customs Control (Revenue, 2015a).

3.5.2.2. Types of funds included in tax legislation

Occupational Pension Schemes: The members of these funds will be employed by a specific employer. This will also include former employees of the employer. The fund does not need to be open for all employees (Revenue, 2015b:Chapter 2). In this section all references made to chapters refer to different links in the same webpage.

Retirement annuities and approved pension funds: A retirement annuity is a contract between a member and an insurance company. This is also referred to as personal pension. (Revenue, 2015b:Chapter 21). An approved fund will be a fund where a member can invest after retirement and the benefit is not taken as pension or an annuity. The benefit stays the property of the owner and it may be withdrawn at any stage (Revenue, 2015b:Chapter 23).
Personal Retirements Savings Account: This is a long term savings account. These accounts assist people to save for their retirement (Revenue, 2015b:Chapter 24).

### 3.5.2.3. Capping of contributions for tax purposes

All contributions made to an exempt approved scheme will be deductible for the taxpayer. (Revenue: 2015b:Chapter 3). An exempt approved scheme will be any scheme that is approved by the Revenue Commissioners. (Revenue, 2015b:Appendix I). For a fund to be an approved scheme the employer must contribute to the scheme (Revenue, 2015b:Chapter 4). It is stated that these contributions need to be “meaningful” in the context of the establishment. A minimum level is not stated.

When the employer pays contributions to the fund, the employer will be able to deduct the expenses for income tax purposes. In the case where the employer pays over special contributions to the fund (not an ordinary contribution), it may be required that the amount be deducted over a few years. The contributions need not be spread over a few years in the case where the special contribution does not exceed the ordinary annual contribution made by the employer or €6,350. The period is determined by dividing the special contribution by the annual ordinary contribution. The minimum period will be five years. (Revenue, 2015b:Chapter 4).

There are two controls in place which determine what amount may be deducted for income tax purposes (Revenue, 2015b:Chapter 3): This includes the age-related control as well as the upper level of earnings that may be taken into account when the contributions to be deducted are determined (Revenue, 2015b:Chapter 3).

#### Age-related control

This control shows the maximum amount of contributions that a taxpayer may deduct for tax purposes. This means that a taxpayer may only deduct a specific percentage of the individual earnings for tax purposes (Revenue, 2015b:Chapter 3).

### Table 9: Age-related percentage limits

<table>
<thead>
<tr>
<th>Age</th>
<th>Limit (% individual earnings)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under 30</td>
<td>15%</td>
</tr>
<tr>
<td>30 – 39</td>
<td>20%</td>
</tr>
<tr>
<td>40 – 49</td>
<td>25%</td>
</tr>
<tr>
<td>50 – 54</td>
<td>30%</td>
</tr>
<tr>
<td>55 – 59</td>
<td>35%</td>
</tr>
<tr>
<td>60 or over</td>
<td>40%</td>
</tr>
</tbody>
</table>

(Revenue, 2015b:Chapter 3)
Upper limit

As the limit above is based on the individual earnings, there is also a cap on the maximum amount that may be taken into account as earnings when the deduction for contributions is determined. For the 2011 year and all subsequent years, this limit is set at €115 000. This amount equals an amount of R1 473 932 (€115 000 x R12.8168) as at 27 February 2015 (Standard Bank, 2015). This will be the limit whether the person is contributing to more than one pension product or only a single pension product (Revenue, 2015b:Chapter 3).

Both the age related and the upper limit should be taken into account when determining the contributions that will be deductible for income tax purposes. Therefore the individual earnings used to determine the deductible contributions will be the lesser of the actual earnings and the upper limit of the earnings (€115 000). When an individual has more than one stream of income, the income streams will be aggregated to determine whether the upper limit should apply.

3.5.2.4. Tax on benefits

There is a threshold on the amount that a taxpayer can receive as a benefit from tax relieved pension products. This is a lifetime limit and is called the standard fund threshold (SFT). This limit is currently €2 million. (Revenue, 2015b:Chapter 25). In certain instances a higher limit, the personal fund threshold (PFT), may apply. PFT is available to individuals where the capital value of the pension exceeds €2 million as at 1 January 2014. The PFT is € 2.3 million. A notification has to be provided electronically to Revenue for PFT to apply (Revenue, 2015b:Chapter 25). The deadline for this notification was 31 July 2015.

When the benefit exceeds the fund threshold tax is payable at 40% for the 2015 year of assessment. The fund threshold will therefore first be deducted from the benefit before the excess tax is determined (Revenue, 2015b:Chapter 25).

From 1 January 2011 there is a maximum amount of a pension lump sum benefit that will not be taxable. This amount is €200 000. This amount is a lifetime limit. The benefit will then be taxed in two stages. The difference between 25% of the SFT and the €200 000 will be taxed at a rate of 20%. The second portion of the excess will be taxed at the individual’s marginal tax rate as it is regarded as being received from employment.

3.5.2.5. Summary

It is clear that Ireland has caps on the contributions that may be deducted for tax purposes. The following table summarises the caps in place in the 2015 year of assessment:
Table 10: Annual cap of deductibility of contributions for income tax purposes

<table>
<thead>
<tr>
<th>Control</th>
<th>Tax implication</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age-related control</td>
<td>The deduction for contributions is limited to a certain percentage of the individual’s earnings annually, based on age.</td>
</tr>
<tr>
<td></td>
<td><strong>Age</strong></td>
</tr>
<tr>
<td>Under 30</td>
<td>15%</td>
</tr>
<tr>
<td>30 – 39</td>
<td>20%</td>
</tr>
<tr>
<td>40 – 49</td>
<td>25%</td>
</tr>
<tr>
<td>50 – 54</td>
<td>30%</td>
</tr>
<tr>
<td>55 – 59</td>
<td>35%</td>
</tr>
<tr>
<td>60 or over</td>
<td>40%</td>
</tr>
</tbody>
</table>

Upper limit: The individual’s earnings used in the age-related control above is set at €115,000.

(Revenue, 2015b:Chapter 3) (own compilation)

3.5.3 Denmark

3.5.3.1 Tax Authority

Skat is Denmark’s tax authority. They are responsible for enforcing and administrating the tax laws (Skat, 2014). In Denmark, the tax effect of the retirement savings differ based on the type of fund that the taxpayer is a member of. The types of funds will now be discussed to determine which funds will be in line with the type of funds that South Africa has.

3.5.3.2. Types of funds included in tax legislation

According to Deloitte there are three pillars to the Danish pension system:

- National public pension;
- Labour market pension and company paid pension; and
- Individual pension plan (Deloitte Touche Tohmatsu Limited, 2015:9).

National public pension - State pension:

Every person who is 65 years or older is entitled to a state pension. This is paid on a pay-as-you go basis from the tax funds. The amount consists of a basic benefit and also a pension supplement. The basic amount is a fixed amount that is paid to the pensioner. This amount will decrease when the annual income exceeds a certain limit. The benefit will not be reduced if income is received from another pension fund. There is also a pension supplement, which is lower than the basic benefit. This amount will be decreased when the annual income of the pensioner exceeds a certain limit. Other pension fund payments may decrease the pension supplement amount (Winther-Sørensen, 1). According to the Deloitte report a person will earn
the right to national pension between the ages of 15 and 65 and a person will have the right to the full amount of national public pension after 40 years of residence. The amount of the national public pension will be reduced where a person was not a resident for 40 years (Deloitte Touche Tohmatsu Limited, 2015:9).

**Labour market supplementary pension and company pension:**

The labour market supplementary pension fund (ATP = Arbejdsmarkedets Tillægs Pension) is a pension scheme to which employees contribute from the age of 16 until the person retires. A person also has to contribute to this fund in instances where he/she has received unemployment benefits, benefits for sickness or maternity leave, social benefit assistance or other social pensions. The employer has to pay 2/3rds of the amount that the employee pays to this fund. The benefits will be paid out at retirement together with any ordinary state pension (Winther-Sørensen, 3).

**Individual private pension schemes:**

This will be where a person is not covered by an occupational pension scheme or where a person wants to enhance the pension from the occupational pension scheme (Winther-Sørensen, 3). There is no tax deduction available for contributions made to the scheme. An amount of DKK28 600 can be contributed. Any contribution above this will be taxed at a rate of 20%. This percentage can be reduced to 4% where the contributions are transferred to a pension fund that provides regular income or a pension annuity (Skat, 2015a).

**Annuity pension or temporary old-age pension**

The tax law also makes provision for a retirement annuity or temporary old-age pension (Skat, 2015a). According to the Merriam-Webster Dictionary an annuity is “a sum of money payable yearly or at other regular intervals” (Merriam-Webster Dictionary).

**3.5.3.3. Capping of contributions for tax purposes**

It will be considered whether there is any cap on the contributions made to the above-mentioned funds which will be deductible for income tax purposes. The caps as in the 2015 year of assessment will be discussed.
National public pension - State pension

As no contributions are made to these funds by the member, no deduction for the contributions will be available. Therefore a cap is also not applicable (Skat, 2015a).

Individual pension plan

The tax treatment of retirement savings changed in 2013. From 2013 no tax deduction is available for contributions made to old-age pension savings, old-age pension insurance and supplementary lump sum pension (Skat, 2015a). When the pension is paid out, there will be no tax on the disbursement made. For the 2015 year of assessment an amount of DKK28 600 (Danish Krone) can be contributed to these schemes (which will not be deductible for income tax purposes). This amounts to a Rand value of R46 480 (DKK28 600 x R1.66) as at 27 February 2015 (Standard Bank, 2015). When an amount of more than the DKK28 600 is paid into the pension scheme in the current year, the amount exceeding this will be taxed at a rate of 20%. Tax relief is available for contributions above the maximum amount and the amount charged will be reduced to 4% where the amount is transferred to a pension fund that provides regular income or annuity pension (Skat, 2015a).

Labour market supplementary pension (ATP)

Tax rules are also available for pension where a regular income is provided in retirement. This will include the following: labour market supplementary pension, lifelong old-age pension (living annuity), surviving spouse or cohabiting partner pension, children’s pension and disability pension. When the employer pays the contributions, the contributions will be deductible in full for tax purposes. When the taxpayer pays his own contributions to a pension fund for more than 10 years, the contributions will be deductible in full in the hands of the employee. When the time period that the taxpayer contributed to the fund is less than ten years or a once-off payment is made, the tax relief (the deductibility of contributions) will be spread over ten years. This means that one tenth of the amount will be deductible per year. If the relief is less than DKK47 600 in the 2015 year of assessment, the deductible amount can be increased to the amount of DKK47 600 yearly until all contributions have been deducted (Skat, 2015a).

Annuity pension and temporary old-age pension (life annuity)

With these products monthly pay-outs will be available for a period of 10 to 25 years. In the 2015 year of assessment tax relief of DKK51 700 is available for contributions made to these two types of funds. The tax relief will automatically apply. The deductible amount can increase
and all amounts can be deducted if the contributions are transferred to a pension scheme that will provide lifelong benefit payments. When the benefit is paid out, income tax will be payable but there will be no labour market contributions. An equalisation tax is also payable. Equalisation tax is a tax that is levied based on the fact that the socio-economic circumstances of the population differ. Therefore this tax will be payable by the part of the population who lives in better socio-economic circumstances. In the 2015 year of assessment this is 5% of pension contributions exceeding DKK374 800 (Skat, 2015a).

3.5.3.4. Tax on benefits
The tax on the benefits of the above-mentioned funds will now be discussed due to the fact that the contributions cannot be studied in isolation. The whole pension system has to be considered and this includes the benefit payments.

National public pension - State pension
When the benefit is paid out there will be income tax on the benefit but no labour market contributions will be payable (Skat, 2015a). The Danish labour market contributions (Arbejdsmarketsbidrag) is an amount of 8% of the gross salary (KPMG, 2011).

Individual pension plan
When the scheme pays out the benefits there will be no tax or charges on the benefit (Skat, 2015a). No labour market contributions will be payable on the benefits (Skat, 2015a). The Danish labour market contributions (Arbejdsmarketsbidrag) is an amount of 8% of the gross salary (KPMG, 2011).

Labour market supplementary pension (ATP)
When a benefit is paid out, there will be income tax on the benefit paid out but there will be no labour market contributions. The Danish labour market contributions (Arbejdsmarketsbidrag) is an amount of 8% of the gross salary (KPMG, 2011). The 8% is also withheld on contributions made to employer-managed pension funds. This amount is withheld by the pension fund (KPMG, 2011).

Annuity pension and temporary old-age pension (life annuity)
In the instances where pension payments are more than DKK374 800 per year, an equalisation tax of 5% will be payable on the amount in excess of DKK374 800 in the 2015 year of assessment. Income tax will also be payable on the annuities received but there will be no labour
market contributions (Skat, 2015a). The tax ceiling for personal income tax is 51.9% for the 2015 year of assessment where the lower limit is DKK459 200 (Skat, 2015b).

3.5.3.5. Summary

The above can be summarised as follows:

Table 11: Danish tax consequences

<table>
<thead>
<tr>
<th>Type of fund</th>
<th>Tax consequences (2015)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual pension plan</td>
<td>- No deduction for contributions made.</td>
</tr>
<tr>
<td></td>
<td>- Amount of DKK28 600 per annum can be contributed. Amount above this will be taxed at 20%. This can reduce to 4% where money is transferred to a pension fund providing regular income or a pension annuity.</td>
</tr>
<tr>
<td>Labour market supplementary pension</td>
<td>- Contributions deductible in full when made for a period longer than ten years by the employee.</td>
</tr>
<tr>
<td></td>
<td>- When the period that a contribution is made is less than ten years or a once-off payment is made – deduction available over ten years.</td>
</tr>
<tr>
<td></td>
<td>- If relief is less than DKK47 600 then the deduction can be increased to a maximum of DKK47 600 until all contributions have been deducted.</td>
</tr>
<tr>
<td>State pension</td>
<td>- No contributions are made by the member and therefore no deduction is available for tax purposes.</td>
</tr>
<tr>
<td></td>
<td>- Income tax, but not labour market contributions, will be payable on the benefits received from state pension.</td>
</tr>
<tr>
<td>Annuity pension and temporary old-age pension</td>
<td>- Deduction available of DKK51 700.</td>
</tr>
<tr>
<td>(life annuity)</td>
<td>(Skat, 2015a) (own compilation)</td>
</tr>
</tbody>
</table>

3.6 Conclusion

From the above it is clear that the different developed countries (Australia, Ireland and Denmark) all have different tax implications regarding capping of retirement contributions for income tax.

In Australia the contributions will be taxed at a rate of 15% in the fund when concessional contributions (before tax amounts) are made. Where the amount of the contributions exceeds
$30 000 when the taxpayer is below the age of fifty, the additional contributions above this amount will be included in the income of the taxpayer and taxed at the marginal income tax rate. Where the taxpayer is 50 years or older, this limit will increase to $35 000. Where the contributions are non-concessional (after tax amounts) the amount will not be taxed in the fund as the income from which the contributions are made has already been taxed. If these contributions, however, exceed $180 000, the contributions will be taxed at a rate of 49%. There are special rules for taxpayers above 65 years.

In Ireland the contributions made to retirement funds are deductible. The deduction is limited based on the age of the taxpayer. This age-related control is based on the percentage of the individual’s earnings. The percentage of the contributions that are deductible for the taxpayer will increase based on the age of the taxpayer (the older the taxpayer, the higher the percentage of the individual earnings that may be deducted). There is also a cap on the individual earnings that should be used to determine the contributions that may be deductible. The maximum individual earnings used when determining the deductible contributions, are €115 000.

In Denmark an amount of DKK28 600 per annum can be contributed to an individual pension plan. There is no deduction available for contributions made. Any contributions made above this amount will be taxed at a rate of 20%. For an annuity pension an amount of DKK51 700 may be deducted for income tax purposes. In a market labour supplementary pension fund the contributions will be deducted for income tax purposes when the contributions have been made for a period of more than ten years. Where the contributions have been made over a shorter period or where a lump sum payment is made, the contributions will be deductible over a period of ten years.

In the next chapter the income tax consequences of the three developed countries are compared to that of South Africa. The differences, as well as the similarities, are discovered. It is also considered in which country the taxpayer will have the greatest tax advantage in terms of income tax. A conclusion is reached regarding the different tax treatments.
CHAPTER 4 – COMPARISON AND CONCLUSION

4.1 Introduction

In the previous chapter the income tax implications of retirement savings have been discussed for Australia, Ireland and Denmark. In this chapter the income tax implications as in the previous chapter are compared to the South African income tax implications for retirement savings. A comparison is performed by use of a case study to determine how a person will be impacted in each of these countries when contributing to a retirement fund. A conclusion is reached regarding how the South African Income Tax Act and the new amendments compare to the income tax implications in developed countries and specifically the capping of retirement contributions for tax purposes in line with the objective stated in chapter 1.

4.2 Limitations of the study

As the tax legislations of the different countries are compared in this chapter, it is important to note the limitations of this study. In this chapter the tax implications are compared between high income individuals, middle income individuals as well as low income individuals. These amounts would not necessarily fall into these categories in all of the countries used in this study as it is subjective. The high income individuals’ contributions will be capped in the countries where these amounts are capped but the income will not necessarily fall within the marginal tax brackets of the countries used in this study.

The impact that the cap of contributions has on the individuals is considered. The economic circumstances of the countries differ and this is not included in the study. This will include the general economy, the cost of living, government subsidies, medical services as well as tertiary education. The exchange rates also have an influence on the conclusions reached in this study and the reason for the exchange rates fluctuation are not studied.

This study also only looks at the tax implications for an individual for one year of assessment. The pension will differ when a person saves for a few years and the tax consequences may differ when this is taken into account.

For the low income individuals, the maximum amount of contributions are not necessarily deducted for income tax purposes as the contributions made do not exceed the cap amount. For
example, in South Africa (see 4.3.1. below) the taxpayer will be able to deduct 27.5% of the remuneration. As the taxpayer only contributes 25% of the remuneration, the contributions are not capped. The study will therefore not look at all possible scenarios to determine what the income tax implications will be for an individual.

4.3 Comparison and summary of differences between South Africa and developed countries

In order to compare the countries, a case study is used. The comparison will be performed to be able to see the impact of the cap amount in the different countries as the study is performed to look at the impact of the cap of the deductibility of retirement contributions. In order to compare the countries with one another to get to the taxable income based on to the deductibility of retirement contributions, the currencies will be converted using the exchange rates as at 28 February 2015. This exchange rate will be used as the 2015 year of assessment is used in this study and the year of assessment in South Africa (for a natural person) ended on 28 February 2015. The average exchange rate is not used as the volatility of the currencies should not be taken into account when comparing South Africa to the other developed countries. As the rand weakened in the 2015 year (Bishop, 2015) it is deemed appropriate to use the exchange rate as at 28 February 2015 as this will represent the current situation. As the exchange rates at a point in time is used, the volatility of the exchange rates will not have an influence on the comparison.

The amounts for the 2015 year of assessment will be used for the other countries as the tax implications for the 2015 year of assessment are considered for each country in chapter 3. The proposed legislation for South Africa is compared therewith. Any contributions made by the employers are not included in the comparison as the tax legislation differs between countries and the impact of the cap alone will be assessed. The tax legislation will be applied to a highly paid individual (determined at an amount above the cap influence), a middle income individual as well as to a low income individual to be able to assess the impact of the cap. The comparisons will also include where the age of the taxpayer exceeds 55 years to determine whether age has any influence on the capping of contributions for income tax purposes. All calculations performed will be included in Appendix A. In all instances it is assumed that the individual has no other income or expenditure which would have a tax impact and also to be able to compare the impact that the cap has in the different countries as used in the study. The following information will be used in performing the comparison for the highly paid individual:
Highly paid individual

The cost to company (remuneration) of a person is R2 000 000 per annum. This person is 35 years old. The basic salary is R1 500 000 per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund (as defined in South African law). He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

<table>
<thead>
<tr>
<th>Contribution Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund</td>
<td>R 300 000 (R1 500 000 x 20%)</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund</td>
<td>R 75 000 (R1 500 000 x 5%)</td>
</tr>
</tbody>
</table>

R 375 000

For the person over the age of 55, the same information will be used as for the high income earner. This will show whether older individuals will be affected by the capping of contributions for income tax purposes.

For the middle income individual the scenario will be such that the individual earns 50% of the income of the highly paid individual and therefore the scenario will be as follows:

The cost to company (remuneration) of a person is R1 000 000 per annum. This person is 35 years old. The basic salary is R750 000 per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

<table>
<thead>
<tr>
<th>Contribution Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund</td>
<td>R 150 000 (R750 000 x 20%)</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund</td>
<td>R 37 500 (R750 000 x 5%)</td>
</tr>
</tbody>
</table>

R 187 500

For the low income individual, the scenario will change and the individual will earn 10% of the income of the highly paid individual:
The cost to company (remuneration) of a person is R200 000 per annum. This person is 35 years old. The basic salary is R150 000 per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

<table>
<thead>
<tr>
<th>Contribution Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund</td>
<td>R 30 000 (R150 000 x 20%)</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund</td>
<td>R 7 500 (R150 000 x 5%)</td>
</tr>
</tbody>
</table>

\[ \text{Total Contributions} = R 37,500 \]

### 4.3.1 South Africa

**Highly paid individual**

The tax treatment for a taxpayer in South Africa is summarised in table 2 in chapter 2. The income tax implications will be the following in South Africa:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>R1 500 000</td>
</tr>
<tr>
<td>Deduction for contributions made (see Appendix A - 1a)</td>
<td>(R350 000)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>R1 150 000</td>
</tr>
</tbody>
</table>

The taxable income as a percentage of the basic salary is thus 77%.

**High income individual – over 55 years**

The income tax implications will be the following in South Africa:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>R1 500 000</td>
</tr>
<tr>
<td>Deduction for contributions made (see Appendix A - 1b)</td>
<td>(R350 000)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>R1 150 000</td>
</tr>
</tbody>
</table>

The income tax implications will not differ in South Africa based on the age of the taxpayer. Therefore the tax implications will be the same as for the highly paid individual. The taxable income as a percentage of the basic salary will still be 77%.
Middle income individual

For the middle income individual the income tax implications will be the following:

<table>
<thead>
<tr>
<th>Basic salary</th>
<th>R750 000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deduction for contributions made (see Appendix A – 1c)</td>
<td>(R187 500)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>R562 500</td>
</tr>
</tbody>
</table>

The taxable income as a percentage of the basic salary is 75%. This will be used to compare South Africa to the other developed countries.

Low income individual

The income tax implications for the low income individual will be as follows:

<table>
<thead>
<tr>
<th>Basic salary</th>
<th>R150 000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deduction for contributions made (see Appendix A – 1d)</td>
<td>(R37 500)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>R112 500</td>
</tr>
</tbody>
</table>

Due to the fact the full deduction is available for the retirement contributions, the taxable income is 75% of the basic salary as included in the tax calculation. The full amount of contributions will be deductible based on the fact that 27.5% of the remuneration will be deductible and currently 25% will be deductible as only 25% is contributed.

Benefit

When the benefit is being paid out there will be tax payable in terms of the Second Schedule to the Income Tax Act. All contribution amounts not previously deducted for income tax purposes will be deducted from the benefit before the tax on the benefit is determined.

4.3.2 Australia

The exchange rate as at 27 February 2015 was R8.75 per Australian Dollar (Standard Bank, 2015). The contributions will be concessional as they are made by the employer before the amounts are taxed. In the Australian tax law there is no distinction made between the different types of funds and therefore the tax implications as discussed in chapter 3.5.1.3. will be used when determining the tax consequences as in the scenario. The income tax consequences in Australia, based on the above scenario, will be the following:
Highly paid individual

The cost to company (remuneration) of a person is $228 571 (R2 000 000 ÷ R8.75) per annum. The basic salary is $171 429 (R1 500 000 ÷ R8.75) per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

- Member contribution to pension fund: $34 286 ($171 429 x 20%)
- Member contribution to retirement annuity fund: $8 571 ($171 429 x 5%)
- Total contributions: $42 857

The income tax implications will be the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>$171 429</td>
</tr>
<tr>
<td>Deduction for contributions made taxed separately</td>
<td>($42 857)</td>
</tr>
<tr>
<td>Inclusion of contributions above $30 000 (see Appendix A – 2a)</td>
<td>$12 857</td>
</tr>
<tr>
<td>Taxable income</td>
<td>$141 429</td>
</tr>
</tbody>
</table>

There will also be tax payable on the contributions as it is concessional contributions. This tax will be an amount of $6 360 (please see Appendix A – 2a). Division 293 tax will not be payable in this instance as the income of the taxpayer together with the super contribution does not exceed $300 000. If this tax was applicable, the taxpayer would have been taxed at a rate of 15% on the amount above the $300 000 (see chapter 3.5.1.3.).

The taxable income as a percentage of the basic salary is 83%. The employee cannot get a deduction for the contributions made (the contributions are deducted from the basic salary as they are taxed separately) and the contributions over the cap is taxed at the marginal rate.

Highly paid individual – over 55 years

The income tax implications of the individual will be the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>$171 429</td>
</tr>
<tr>
<td>Deduction for contributions made taxed separately</td>
<td>($42 857)</td>
</tr>
<tr>
<td>Inclusion of contributions above $35 000 (see Appendix A - 2b)</td>
<td>$7 857</td>
</tr>
<tr>
<td>Taxable income</td>
<td>$136 429</td>
</tr>
</tbody>
</table>
The taxable income as a percentage of the basic salary is now 80%. There will also be tax payable on the contributions as it is concessional contributions. This tax will be an amount of $6 429 (please see Appendix A – 2b).

**Middle income individual**

The scenario for the middle income individual will be as follows:

<table>
<thead>
<tr>
<th>The cost to company (remuneration) of a person is $114 286 (R1 000 000 ÷ R8.75) per annum. The basic salary is $85 714 (R750 000 ÷ R8.75) per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund: $ 17 143 ($85 714 x 20%)</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund: $ 4 286 ($85 714 x 5%)</td>
</tr>
<tr>
<td>$ 21 429</td>
</tr>
</tbody>
</table>

Based on the scenario the income tax implications will be the following:

| Basic salary | $85 714 |
| Deduction for contributions made taxed separately | ($21 429) |
| Inclusion of contributions above $ 30 000 (see Appendix A – 2c) | $ 0 |
| Taxable income | $64 285 |

The taxable income as percentage of the basic salary will thus be 75% for the middle income earner. The concessional contributions will be taxed at a rate of 15%. This means that tax of $3 214 ($21 429 x 15%) will be payable on the contributions.
Low income individual

The cost to company (remuneration) of a person is $22 857 (R200 000 ÷ R8.75) per annum. The basic salary is $17 172 (R150 000 ÷ R8.75) per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

<table>
<thead>
<tr>
<th></th>
<th>$</th>
<th>($17 172 x %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund:</td>
<td>3 434</td>
<td>20%</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund:</td>
<td>859</td>
<td>5%</td>
</tr>
<tr>
<td></td>
<td>4 293</td>
<td></td>
</tr>
</tbody>
</table>

The tax consequences for the low income individual will be as follows:

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>$17 172</td>
</tr>
<tr>
<td>Deduction for contributions made taxed separately</td>
<td>($4 293)</td>
</tr>
<tr>
<td>Deduction of contributions (see Appendix A - 2d)</td>
<td>$ 0</td>
</tr>
<tr>
<td>Taxable income</td>
<td>$12 879</td>
</tr>
</tbody>
</table>

The taxable income is therefore 75% of the basic salary.

4.3.3 Ireland

As per Standard Bank the exchange rate was R12.8168 to the Euro on 27 February 2015 (Standard Bank, 2015). This is therefore the rate that will be used to convert the information in the scenario to determine what the income tax implications will be in Ireland. The tax consequences in Ireland is discussed in chapter 3.5.2.3. Therefore the information used is as follows:

Highly paid individual

The cost to company (remuneration) of a person is €156 045 (R2 000 000 ÷ R12.8168) per annum. The basic salary is €117 034 (R1 500 000 ÷ R12.8168) per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

<table>
<thead>
<tr>
<th></th>
<th>€</th>
<th>($117 034 x %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund:</td>
<td>23 407</td>
<td>20%</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund:</td>
<td>5 852</td>
<td>5%</td>
</tr>
<tr>
<td></td>
<td>29 259</td>
<td></td>
</tr>
</tbody>
</table>
The following will be the income tax implications:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>€117 034</td>
</tr>
<tr>
<td>Retirement contributions deductible (see Appendix A – 3a)</td>
<td>(€23 000)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>€94 034</td>
</tr>
</tbody>
</table>

The taxable income as a percentage of the basic salary is 80%.

**Highly paid individual – over 55 years**

The same scenario as for the highly paid individual will be used. The taxpayer, however, is not 35 anymore but over the age of 55. It is assumed that the taxpayer will fall within the 55 – 59 year age bracket. The income tax implications will thus be the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>€117 034</td>
</tr>
<tr>
<td>Retirement contributions deductible (see Appendix A – 3b)</td>
<td>(€40 250)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>€76 784</td>
</tr>
</tbody>
</table>

The taxable income as a percentage of the basic salary is thus 66%. This indicates that the taxpayer over 55 years will be taxed on a lower amount than the same taxpayer who is 35 years old.

**Middle income individual**

The scenario will be the following for a middle income individual:

The cost to company (remuneration) of a person is €78 023 (R1 000 000 ÷ R12.8168) per annum. The basic salary is €58 517 (R750 000 ÷ R12.8168) per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund:</td>
<td>€ 11 703 (€58 517 x 20%)</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund:</td>
<td>€ 2 926  (€58 517 x 5%)</td>
</tr>
<tr>
<td></td>
<td>€ 14 629</td>
</tr>
</tbody>
</table>

Based on the above scenario the income tax implications for the individual will be the following:
Based on the scenario above the taxable income as a percentage of the basic salary is 75%.

**Low income individual**

The scenario for the low income individual will be the following:

<table>
<thead>
<tr>
<th>Cost to company (remuneration) of a person</th>
<th>€15 605 (R200 000 ÷ R12.8168) per annum.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>€11 703 (R150 000 ÷ R12.8168) per annum.</td>
</tr>
<tr>
<td>He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:</td>
<td></td>
</tr>
<tr>
<td>Member contribution to pension fund:</td>
<td>€ 2 341 (€11 703 x 20%)</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund:</td>
<td>€ 585 (€11 703 x 5%)</td>
</tr>
<tr>
<td></td>
<td>€ 2 926</td>
</tr>
</tbody>
</table>

The income tax implications for the individual will be the following:

<table>
<thead>
<tr>
<th>Basic salary</th>
<th>€11 703</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retirement contributions deductible (see Appendix A – 3d)</td>
<td>(€2 926)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>€8 777</td>
</tr>
</tbody>
</table>

The taxable income as a percentage of the basic salary is 75%. The percentage is lower than for the highly paid individual as fewer of the contributions are capped as all the contributions are deductible.

**4.3.4 Denmark**

The exchange rate as per Standard Bank was R1.66 per Danish Kroner as at 27 February 2015 (Standard Bank, 2015). This is the exchange rate that will be used to determine what the tax implications would be in Denmark. Denmark’s tax consequences are discussed in chapter 3.5.3.3. Therefore the scenario will be the following:
Highly paid individual

The cost to company (remuneration) of a person is DKK1 204 819 per annum (R2 000 000 ÷ R1.66). This person is 35 years old. The basic salary is DKK903 614 (R1 500 000 ÷ R1.66) per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

| Member contribution to pension fund: | DKK 180 723 (DKK903 614 x 20%) |
| Member contribution to retirement annuity fund: | DKK 45 181 (DKK903 614 x 5%) |
| **Total Contributions** | DKK 225 904 |

In order to consider the tax consequences and to be able to compare the Danish tax consequences with those of South Africa, the types of funds need to be considered as this will have an impact on the tax consequences in Denmark. In this case the pension fund is considered to be an individual pension plan as in chapter 3. This is used as any individual may belong to these schemes. For the labour market pension scheme and the company schemes, the employer has to contribute two thirds of the contributions and this is not in line with the South African law. The retirement annuity will be an annuity pension. Therefore the tax consequences will be the following for the individual:

| Basic salary | DKK903 614 |
| Retirement contributions deductible (see Appendix A – 4a) | (DKK45 181) |
| Taxable income | DKK858 433 |

Due to the fact that there is no deduction available for the contributions made to the pension fund and only a deduction available for the contributions made to the retirement annuity, the taxable income is 95% of the basic salary. There will also be additional tax payable on the contributions made to the pension fund when the contributions exceed DKK28 600. This will amount to 20% of the amount that exceeds this limit, therefore the additional tax will amount to DKK30 425 (please refer to Appendix A – 4a).
Highly paid individual – over 55 years

The following will take into account the same information as for the highly paid individual except for the fact that the individual is 55 years old. The following will be the income tax implications for the individual:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>DKK903 614</td>
</tr>
<tr>
<td>Retirement contributions deductible (see Appendix A – 4b)</td>
<td>(DKK45 181)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>DKK858 433</td>
</tr>
</tbody>
</table>

In terms of the above tax calculation the taxable income as a percentage of the basic salary will also be 95% as in the case of the highly paid individual. There will be no deduction available for the contributions made to the pension fund. There will also be additional tax payable on the contributions made to the pension fund when the contributions exceed DKK28 600. This will amount to 20% of the amount that exceeds this limit, therefore the additional tax will amount to DKK30 425 (please refer to Appendix A – 4b).

Middle income individual

The above scenario will now be adjusted for the middle income earner. The scenario will be the following:

The cost to company (remuneration) of a person is DKK602 410 per annum (R1 000 000 ÷ R1.66). This person is 35 years old. The basic salary is DKK451 807 (R750 000 ÷ R1.66) per annum. He contributes 20% (of his basic salary) to the defined contribution pension fund. He will also contribute 5% towards a retirement annuity fund. The contributions will thus be the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member contribution to pension fund:</td>
<td>DKK 90 361</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund:</td>
<td>DKK 22 590</td>
</tr>
<tr>
<td></td>
<td>DKK112 951</td>
</tr>
</tbody>
</table>
The income tax implications for this individual will be the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>DKK451 807</td>
</tr>
<tr>
<td>Retirement contributions deductible (see Appendix A – 4c)</td>
<td>(DKK22 590)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>DKK429 217</td>
</tr>
</tbody>
</table>

The taxable income as a percentage of the basic salary is 95%. This agrees to the high income individual as the full retirement annuity fund contribution is deductible.

**Low income individual**

The scenario will be changed for the low income individual. The scenario will then be as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>The cost to company (remuneration) of a person</td>
<td>DKK120 482</td>
</tr>
<tr>
<td>This person is 35 years old. The basic salary</td>
<td>DKK90 361</td>
</tr>
<tr>
<td>He contributes 20% (of his basic salary) to the defined</td>
<td></td>
</tr>
<tr>
<td>contribution pension fund. He will also contribute 5%</td>
<td></td>
</tr>
<tr>
<td>towards a retirement annuity fund. The contributions will</td>
<td></td>
</tr>
<tr>
<td>thus be the following:</td>
<td></td>
</tr>
<tr>
<td>Member contribution to pension fund:</td>
<td>DKK 18 072</td>
</tr>
<tr>
<td>Member contribution to retirement annuity fund:</td>
<td>DKK 4 518</td>
</tr>
<tr>
<td></td>
<td>(DKK90 361 x 20%)</td>
</tr>
<tr>
<td></td>
<td>(DKK90 361 x 5%)</td>
</tr>
<tr>
<td></td>
<td>DKK 22 590</td>
</tr>
</tbody>
</table>

The income tax consequences for this individual will be the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic salary</td>
<td>DKK90 361</td>
</tr>
<tr>
<td>Retirement contributions deductible (see Appendix A – 4d)</td>
<td>(DKK4 518)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>DKK85 843</td>
</tr>
</tbody>
</table>

The taxable income as a percentage of the basic salary is 95%. This is the same as for the high as well as middle income individuals as the full contributions made to the retirement annuity funds are deductible.
Table 12: Comparison between South Africa and developed countries

<table>
<thead>
<tr>
<th>Criteria</th>
<th>South Africa</th>
<th>Australia</th>
<th>Ireland</th>
<th>Denmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cap for contributions deductible for income tax purposes</td>
<td>R350 000</td>
<td>No deduction available for employee. Contributions excluded from remuneration as taxed separately.</td>
<td>€23 000</td>
<td>DKK51 700 (Retirement annuity fund)</td>
</tr>
<tr>
<td>Cap for contributions converted (Rand)</td>
<td>R350 000</td>
<td>No deduction available for employee.</td>
<td>R294 786 ($23 000 x R12.8168)</td>
<td>R85 822 (DKK51 700 x R1.66)</td>
</tr>
<tr>
<td>Taxable income as percentage of basic salary (highly paid individual)</td>
<td>77%</td>
<td>83%</td>
<td>80%</td>
<td>95%</td>
</tr>
<tr>
<td>Taxable income as a percentage of the basic salary (highly paid individual over 55 years)</td>
<td>77%</td>
<td>80%</td>
<td>66%</td>
<td>95%</td>
</tr>
<tr>
<td>Taxable income as a percentage of the basic salary (middle income individual)</td>
<td>75%</td>
<td>75%</td>
<td>75%</td>
<td>95%</td>
</tr>
<tr>
<td>Taxable income as percentage of basic salary (low income individual)</td>
<td>75%</td>
<td>73%</td>
<td>75%</td>
<td>95%</td>
</tr>
<tr>
<td>Additional tax payable (highly paid individual)</td>
<td>No additional tax payable.</td>
<td>Contributions are taxed at a rate of 15%. Additional tax at marginal rate for contributions exceeding R262 500 ($30 000 x R8.75), R306 250 ($35 000 x R8.75) when over 50.</td>
<td>No additional tax payable.</td>
<td>Contributions made over R47 476 (DKK28 600 x R1.66) are taxed at a rate of 20%.</td>
</tr>
<tr>
<td>Additional tax payable (low income individual)</td>
<td>No additional tax payable.</td>
<td>Contributions made are taxed at a rate of 15%</td>
<td>No additional tax payable.</td>
<td>No additional tax payable.</td>
</tr>
<tr>
<td>Taxing of benefits</td>
<td>Benefit is taxed when it is paid out. Contributions not deducted will be deductible from the benefit taxed.</td>
<td>No tax when benefit paid out after age of 60 as the contributions were taxed when made.</td>
<td>The benefit amount above R2 563 360 (€200 000 x R12.8168) will be taxed.</td>
<td>No tax payable on pension fund but tax will be payable on the retirement annuity.</td>
</tr>
</tbody>
</table>

(Own compilation)
4.4 Conclusion based on the comparison

In order to compare South Africa to the developed countries, it is necessary to make use of different scenarios to identify the differences as well as the similarities between the different tax legislations. Therefore the study looks at different income categories such as high income, middle income as well as low income individuals. As the tax consequences will also differ based on the age of the taxpayer, a scenario has been sketched for a 35 year old taxpayer as well as for a 55 year old taxpayer. The conclusions reached from the comparison will now be discussed.

In all the countries the taxpayers in the highly paid category will be affected most by the respective tax legislations due to the fact that amounts to be deducted for income tax purposes may be capped. This can be seen from the fact that the taxable income as a percentage of the basic salary is the highest percentage in all the countries for the highly paid individuals. This indicates that the capping of contributions for taxation purposes will influence the taxpayers in the marginal tax brackets of the respective countries. In Australia a highly paid individual will also pay additional tax as all concessional (before tax) contributions made will be taxed at a rate of 15% and tax will be payable at the marginal rate for all contributions made over R262 500 ($30 000 x R8.75), thus also imposing a limit on the contributions that can be made without any further adverse tax consequences. This amount will increase to R306 250 ($35 000 x R8.75) when the taxpayer is above 50 years. The concessional contributions are taxed at a rate of 15% as these are before tax contributions and as such the taxpayer pays a lower percentage of tax on the contributions than the tax that would have been payable at the marginal income tax rate.

Australia is the only country included in the study where there is no deduction available for the contributions made to a pension fund unless the person is not in employment. In both Denmark and in Australia the contributions may be taxed when certain limits are exceeded. As the contributions in Australia will not be deductible for income tax purposes, the benefits will not be taxed when they are paid out after the member turns 60. In Denmark there will also not be any tax on the benefits paid out by a pension fund but the benefits from a retirement annuity fund will be taxed at the marginal rate.
When we compare the cap amount in terms of Rand between the countries it can be seen that the amount at which the deduction for contributions is capped, is the highest in South Africa, followed by Ireland and then by Denmark. In Australia there is no deduction available but the contributions made above R262 500 will be taxed. The determination of the cap will be based on the economic inequalities.

When the age of the taxpayer is considered, it can be seen that the most beneficial tax consequences are in Ireland as the taxable income as a percentage of the basic salary is the lowest at 66% when the taxpayer is over 55. This is due to the fact that there is an age-related control in place which influences the amount of contributions that the taxpayer may deduct for income tax purposes. This clearly indicates that Ireland promotes savings as a person becomes older, which may ensure that he/she has the financial means to retire. In South Africa there is no additional benefit in terms of the deductibility of retirement contributions when the age of the taxpayer is considered. As such, the taxpayer’s taxable income as a percentage of the basic salary will not differ based on whether the taxpayer is 55 or whether he is 35. When a benefit is being paid and the taxpayer is over 55, the tax rate on the benefit will be lower. In Australia the taxpayer will also benefit when he is over 50 as the amount to be included in the taxable income will be lower, as the limits differ depending on the age of the taxpayer. The limit for a person younger than 50 is R262 500 while this amount increases to R306 250 when the taxpayer is over 50 years.

In terms of the middle income individual, the taxable income as a percentage of the basic salary will be the same in South Africa, Australia and Ireland. This shows that the countries are all in line and that the capping of the retirement contributions for income tax purposes will not influence the middle income individuals as the countries will allow deductions for the contributions made and there will be no additional tax payable on the contributions made.

In Denmark the taxable income as a percentage of the basic salary is consistently 95% for a highly paid individual aged 35, a highly paid individual aged 55, a middle income individual as well as a low income individual. This is due to the fact that the pension fund contributions will not be deductible for income tax purposes and in all situations the full contributions made to a retirement annuity fund are deductible for income tax purposes as the contributions are below the cap for retirement annuity fund contributions. The contributions made over an amount of R47 476 will be taxed at a rate of 20%.
For the low income individual the taxable income as a percentage of the basic salary is more or less the same in South Africa, Australia and Ireland. This means that the cap amounts do not have an influence on the low income individuals and that the deductibility of the retirement contributions are more or less the same in these different countries as the net effect on the taxpayer is almost the same.

In terms of additional tax on the contributions there is no additional tax on contributions made above a certain amount in South Africa. In Australia the contributions made are taxed at a rate of 15%. This is due to the fact that the amounts received from the salary is not included in the taxable income but it is taxed separately at a rate of 15%. In both Ireland and Denmark there is no additional tax payable on the contributions made.

It is also important to consider the tax on the benefits as the taxpayer will either deduct the contributions or pay tax on the benefits or the contributions will not be deductible and the benefits will not be taxed. In South Africa the contributions are deducted but the benefits are taxed. If a contribution amount could not be deducted for income tax purposes previously, the contributions amount will be deductible from the benefit before the tax on the benefit is determined. In Australia the benefit paid out is not taxed if the taxpayer is over the age of 60. This is due to the fact that the contributions are taxed at a rate of 15% when they are made. In Denmark, as the contributions made to the pension fund are not deductible for income tax purposes, the benefits paid out will be taxed. The retirement annuity fund contributions are deductible up to the limit and therefore the benefits will be taxed when they are paid out. In Ireland the contributions made are deductible and therefore the benefits will be paid when the limit of R2 563 360 is exceeded.

In Denmark the cap amount for the deductibility of the contributions is much lower than in Ireland and South Africa, therefore demotivating the taxpayers to contribute to a pension scheme. As the cap in Denmark is very low the percentage of the taxable income of the basic salary is very high.

In all the countries there is a cap on the contributions that can be deducted for income tax purposes or a way of limiting the contributions that a taxpayer would want to make by imposing income tax on the contributions exceeding a certain limit. As the contributions are treated differently by the different countries, the way that the benefits are taxed are also different.

In terms of the comparison, all the countries have a monetary cap for contributions after which there will be adverse tax effects for the taxpayer. Therefore, when the legislation changed in
terms of the Taxations Laws Amendment Bill 2013, the tax treatment of contributions became more in line with those of other developed countries. The South African legislation is in line with those of the developed countries used in this study.

4.5 Other research possibilities from the study

In this study different countries are used from the Melbourne Mercer Global Pension Index. These countries are not necessarily representative of all developed countries. These countries are selected as they have the highest index amounts for the adequacy index. As such a study can be performed to include other developed countries which may be more representative of population for developed countries.

In order to perform this study the currencies had to be converted to be able to compare the caps of the different countries. The different economies were not researched. This may have an influence on the exchange rates and therefore the conversion of the currencies may have an influence on the conclusions reached. The general economy of a country can also influence the tax consequences. The use of the high, middle and low income individuals may also not be correct and reasonable to reach the conclusion. A study can be performed which takes into account these considerations and a more accurate conclusion can be reached.

The study looks at the income tax implications for one year of assessment. The results may differ if the time frame is longer. This can thus also be included in a study and the impact of time can be taken into account.

Further research can also be performed on the cap amount of R350 000 included in the South African tax legislation to determine whether this cap is sufficient and the impact on high income individuals as well as low income households as no information is available on how the cap amount was determined. The impact of this specific amount can be further researched.

4.6 Conclusion and summary

The South African legislation is changed to cap the contributions made to retirement funds to R350 000 per year. When compared to developed countries, the capping of contributions before there will be other adverse tax consequences is evident when looking at the tax legislations of Australia, Denmark and Ireland. Thus, when the tax legislation in South Africa was proposed,
the South African tax legislation became more in line with those of developed countries as these countries all have a cap amount and the contributions are not capped based only on a percentage of the earnings of the individual. This is the case as all the developed countries used in the study have monetary limits for the contributions. Before the changes were made to the South African legislation we had monetary limits (which differed based on the type of fund the contribution was made to) as well as percentage-based limits which is not used in any of the developed countries in this study.

The objective of this study was to determine how the South African income tax implications differ from those of developed countries and specifically if the cap amount is in line with the income tax implications in developed countries. The objective was also to determine whether the South African tax legislation should be changed to be more in line with the tax legislation of developed countries. As can be seen from the research performed, the developed countries all have a fixed amount above which there will be adverse tax consequences when the amount of contributions made to retirement funds are more. The amount of the cap in South Africa is higher than the caps in the developed countries included in this study. This does not indicate that the tax legislation should be changed, as other factors should be considered before determining what the cap amount should be, such as the general economy, the household savings rates, other pension subsidies paid by the government and other legislation. As the changes made to the South African tax legislation in terms of the Taxation Laws Amendment Bill 2013 introduced the cap amount, the South African tax legislation is now more in line with the tax consequences in other developed countries. In conclusion, the South African tax legislation is now more in line with the legislation of developed countries and therefore no changes to the South African tax legislation are necessary.
APPENDIX A: CALCULATION OF RELEVANT TAX DEDUCTIONS
The following appendix will show the calculations performed in chapter 4. This will set out how the amounts used in the different tax calculations were determined.

1. South Africa
   a. Highly paid individual – 35 years old

   For the highly paid individual the deduction cap will be the lesser of 27.5% of remuneration or R350 000.

   27.5% of the remuneration is: R2 000 000 x 27.5% = R550 000

   Therefore the deductible contributions will be capped at R350 000. The full amount of the contributions will not be deductible for income tax purposes. The amount that will not be deductible in the current year of assessment is R25 000 and this will be carried forward to the 2016 year of assessment.

   b. Highly paid individual – over 55 years old

   The highly paid individual will still be able to deduct the lesser of 27.5% of the remuneration or R350 000, thus the lesser of:

   - R350 000 and
   - 27.5% x R2 000 000 = R550 000.

   The deduction will thus still be R350 000.

   c. Middle income individual

   For the middle income individual the contributions deductible for income tax purposes will also be determined as the lesser of R350 000 and 27.5% of the remuneration, thus the lesser of:

   - R350 000 and
   - 27.5% x R1 000 000 = R275 000.

   The lesser of the two amounts is R275 000. The amount that may be deducted will be limited to the actual contributions made and therefore the actual contributions of R187 500 will be deductible for income tax purposes.
d. **Low income individual**

The deduction will be the lesser of 27.5% of the remuneration or R350 000.

27.5% of the remuneration (R200 000) is R55 000. The actual amount of R37 500 is lesser and therefore the individual will get a deduction of R37 500.

The full contributions will thus be deductible and no amount will be carried forward to the next year of assessment.

2. **Australia**

a. **Highly paid individual**

The concessional contributions made will be taxed at a rate of 15%. Therefore tax of $6 429 ($42 857 x 15%) will be payable on the contributions made. Where the contributions made are in excess of $30 000 (as the taxpayer is younger than 50 years), the amount above will be added to the income tax calculation of the individual and taxed at the marginal income tax rate. There will be no deduction available for the contributions made as more than 10% of the assessable income is received as an employee (Australian Government: 2014).

An amount of $42 857 has been deducted from the basic salary as the contributions are concessional, which means that it is not taxed yet. This means that the taxpayer is taxed at a reduced rate of 15% on the contributions made to a retirement fund up to an amount of $30 000. The amount above this will be taxed at the marginal tax rate and therefore included in the tax calculation.

b. **Highly paid individual – over 55 years**

The concessional contributions made will be taxed at a rate of 15%. Therefore tax of $6 429 ($42 857 x 15%) will be payable on the contributions made. Where the contributions made are in excess of $35 000 (as the taxpayer is above 50 years), the amount above this will be added to the income tax calculation of the individual and taxed at the marginal income tax rate. There will be no deduction available for the contributions made as more than 10% of the assessable income is received as an employee (Australian Government: 2014).
An amount of $42,857 has been deducted from the basic salary as the contributions are concessional, which means that they are not taxed yet. This means that the taxpayer is taxed at a reduced rate of 15% on the contributions made to a retirement fund up to an amount of $35,000. The amount above this will not be deductible for income tax purposes and taxed at the marginal income tax rate.

c. **Middle income individual**

For the middle income earner the total contributions made are $21,429. The concessional contributions will be taxed at a rate of 15%. This means that tax of $3,214 ($21,429 x 15%) will be payable on the contributions. The contributions will be deductible from the basic salary that will be taxed as the contributions are taxed separately. As the contributions made are less than $30,000 there will be no additional amount that has to be included in the income tax calculation to be taxed at the marginal income tax rate.

d. **Low income individual**

There is no deduction available as the person earns more than 10% of the assessed income as an employee. The contributions made also do not exceed the cap of $30,000 and therefore there is no inclusion in the income tax liability. The total contributions made in the current year is $4,293 ($3,434 + $859). There will also be additional tax payable on the concessional contributions at a rate of 15% and therefore tax of $644 ($4,293 x 15%). As the contributions are before tax contributions, they will not be taxed twice and therefore the contributions made will be deductible for income tax purposes but taxed at a rate of 15%.

3. **Ireland**

a. **Highly paid individual**

As the taxpayer is 35 years old, the limit of the retirement contributions will be 20% of the earnings of the individual. The individual earnings of the taxpayer is €156,045, which is higher than the upper limit as imposed by the Irish tax law. The upper limit is €115,000 and therefore the cap will be 20% of this amount. The cap of the retirement contributions that will be deductible for tax purposes will thus be €23,000 (€115,000 x 20%).
b. **Highly paid individual – over 55 years**

The taxpayer is over the age of 55 and therefore the limit on the retirement contributions will be 35% of the earnings of the individual. The individual earnings of the individual is €156,045 and as this exceeds the upper limit of €115,000, the cap will be determined as 35% of this limit. The amount deductible will therefore be €115,000 x 35% = €40,250.

c. **Middle income individual**

The taxpayer is 35 and therefore the limit of the contributions to be deductible will be 20% of the earnings of the individual. As the earnings of the individual equals €78,023 and this does not exceed the limit of €115,000, the deduction will be limited to:

€78,023 x 20% = €15,605

The actual contributions made are €14,629 (€11,703 + €2,926), which is less that the cap and therefore the full amount of the contributions will be deductible for income tax purposes.

d. **Low income individual**

As the taxpayer is 35 years old, the limit of the retirement contributions will be 20% of the earnings of the individual. The individual earnings of the taxpayer are €15,605. This amount is lower than the upper limit, which is €115,000, and therefore the cap will be determined as 20% of the earnings. The deduction will therefore be €3,121 (€15,605 x 20%). The total contributions made is an amount of €2,926 (€2,341 + €585). As the actual contributions are less than the deductible contributions only the actual contributions will be deductible for income tax purposes.

4. **Denmark**

a. **Highly paid individual**

In the 2015 year of assessment the deductions for retirement contributions made to pension funds are capped at DKK28,600. Any amount exceeding this will be taxed at a rate of 20%. This means that tax amounting to DKK30,425 (DKK152,123 [DKK180,723 – DKK28,600] x 20%) will be payable on the contributions made. This additional tax will only be on the pension fund contributions. There will be no deduction available for the contributions made to the pension fund. For the retirement annuity an amount of DKK51,700 will be available as a deduction for the 2015 year of assessment but limited to the actual amount and therefore the full amount of DKK45,181 will be deductible for income tax purposes.
b. **Highly paid individual – over 55 years**

In Denmark the tax legislation for the deductibility of retirement contributions does not differ based on the age of the taxpayer. As this is the case the deduction of retirement contributions will be limited to the retirement annuity fund contributions as in a. above. The tax amount payable will also be DKK30 425

c. **Middle income individuals**

In the 2015 year of assessment the deductions for retirement contributions made to pension funds are capped at DKK28 600. Any amount exceeding this will be taxed at a rate of 20%. This means that tax amounting to DKK12 352 (DKK61 761 [DKK90 361 – DKK28 600] x 20%) will be payable on the contributions made. There will be no deduction available for the contributions made to the pension fund. For the retirement annuity an amount of DKK51 700 will be available as a deduction for the 2015 year of assessment but limited to the actual amount and therefore the full amount of DKK22 590 will be deductible for income tax purposes.

d. **Low income individual**

In the 2015 year of assessment the deductions for retirement contributions made to pension funds are capped at DKK28 600. As the contributions made are DKK18 072, it will not exceed this limit and no additional tax is payable on contributions made. There will be no deduction available for the contributions made to the pension fund. For the retirement annuity fund an amount of DKK51 700 will be available as a deduction for the 2015 year of assessment but limited to the actual amount and therefore the full amount of DKK4 518 will be deductible for income tax purposes.
LIST OF REFERENCES

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South Africa. 1956. Pension Funds Act No. 24 of 1956


