ESTATE PLANNING

by

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CHAPTER 1

INTRODUCTION

1.1 DEFINITION

The following is the definition of estate planning developed by Meyerowitz:

> *"The arrangement, management and securement and disposition of a person's estate so that he, his family and other beneficiaries may enjoy and continue to enjoy the maximum from his estate and his assets during his lifetime and after his death, no matter when death may occur."*

The process can be complex and may, for example, require the drafting of a last will and testament by the planner, the creation of one or more intervivos trusts or the formation of a company or close corporation. Estate planning is therefore normally done by the planner with the assistance of his attorney and accountant, who can provide him with advice on legal and taxation matters and can arrange for the formation of any trusts or companies required by the estate plan.

There are various reasons for embarking on an estate planning exercise.

* **Fiscal Reasons**

  The planner may be concerned about the estate duty and capital gains tax that will have to be paid on his death and may wish to minimize these.

* **Personal and Family Reasons**

  The planner needs to consider how his death will affect the rest of his family.

* **Commercial Reasons**

  The planner may for example be a sole proprietor and need to provide for the continuity of his business or may want to sell his business after his death.

1.2 OBJECTIVES OF ESTATE PLANNING

1.2.1 FLEXIBILITY

It is an essential requirement in every estate plan. Building sufficient flexibility into an estate plan makes provision for changes not only in the legal environment, but also in the personal and family circumstances of the estate planner.

1.2.2 THE MINIMISATION OF ESTATE DUTY

Minimising estate duty is often seen as a major objective of an estate plan. There are other objectives listed below that are often as or more important than saving estate duty.

1.2.3 THE MINIMISATION OF INCOME TAX

A knowledge of income tax is most important in relation to the tax implications of the use of the various tools of estate planning to ensure that no income tax prejudice is suffered when doing this planning.

Although income tax savings may be difficult to achieve for the estate planner, with proper planning significant savings can often be achieved for later generations. It may be possible to achieve savings in normal tax by the transfer of assets to a trust so that the income arising from the assets is split between the beneficiaries of the trust and possibly even the trust itself. During the lifetime of the planner, the possibilities of doing this are limited by the anti-avoidance provisions of S 7 which may, in the prescribed circumstances, deem the income to have been received by the planner, but after the death of the planner the provisions of S 7 will no longer apply and savings in normal tax can be achieved by the splitting of the income.

1.2.4 THE MINIMISATION OF CAPITAL GAINS TAX

Example

If your house is in your own name and not in the trust when you decide to sell the property you are allowed a deduction of R1 000 000 if this is your primary residence.

1.2.5 THE MINIMISATION OF OTHER TAXES

It is important when drawing an estate plan that a liability for other taxes or duties is not created while arranging the planner's affairs to minimize estate duty.

1.2.6 THE PROVISION FOR LIQUIDITY

It is important to ensure on death of the planner there is no liquidity problems. Sufficient liquidity should be available after the death of the planner to ensure that liabilities can be met without having to dispose of assets at possibly the wrong time and at relatively low prices. The liabilities of the deceased which must be settled by the executor include personal debts, for example loan owing, any taxes that may be outstanding, any estate duty that must be paid on the net value of property in the estate.

It is possible to calculate the estimated estate duty liability based on projected values of the property of the planner.

If there is likely to be a shortfall in cash available one possible solution is to take out a policy of insurance on the life of the planner so that the proceeds can be used to settle the outstanding liabilities. We must remember that the proceeds will constitute property in the estate which will increase the value of the estate.

1.2.7 THE PROVISION OF CAPITAL AND INCOME FOR DEPENDANTS

It is also an essential part of the estate plan to ensure that the surviving spouse and children of the deceased have enough liquid funds available to live on during and after the period of winding up the estate, which can be many months depending on how complex the estate is.

During the planner's lifetime he may be involved in the company and drawing income from it. The problems may arise on death of the planner.

1.2.8 THE PROVISION OF RETIREMENT CAPITAL AND INCOME

Planning is an ongoing process which starts with the birth of the planners and ends on his death. Planning for one's retirement is a very important objective in this planning process and sometimes the planner does not give enough attention to this. When one is contemplating emigration, emphasis on retirement planning assumes even greater importance sometimes. The planner may want to minimize estate duty and therefore breaks the link between the planner and the growth asset. But, one must be careful that one is not cut off from the income generated by these assets which is important for a comfortable retirement. Capital generation for retirement is an ongoing process which takes place over a long period of time and links up with objectives such as the provision of liquidity.

1.2.9 CAPITAL APPRECIATION AND INCOME GENERATION

This serves as a reminder that estate planning is always subject to normal commercial considerations and decisions.

1.2.10 PROTECTION AGAINST INSOLVENCY AND INFLATION

No one plans to go insolvent. An individual who goes into business for his own account, or with others, will always run the risk that his optimism exceeds his abilities or that both his judgement and timing was wrong. Protection against insolvency includes insolvency of not only the planner but also his future beneficiaries and spouses of beneficiaries. The plan must not be vulnerable to such events. The beneficiaries must be able to weather the storm of such problems and this should in no way endanger other beneficiaries' long term benefits. The planner must also consider spendthrift ways of succeeding spouses and intervention of third parties who become involved in the family.

1.2.11 FACILITATION OF THE ADMINISTRATION OF THE ESTATE

Death of the planner is the ultimate test of an estate plan. A properly executed plan will ensure that the dependants and heirs of the planner will survive their bereavement in a condition that remains materially similar to that enjoyed prior to his death. Fear of diversion or dissipation of the assets is an important factor that needs to be taken into account when facilitating the administration of an estate. The spouse or dependants should not be in a position to take control of these assets either temporarily or permanently. The simplicity of an estate plan is a subsidiary objective. It is important for the plan to operate smoothly without the presence of the planner. Flexibility is also a very important liquidity and is a constant requirement in the planning and administration of estates. Proper administration is of utmost importance.

1.2.12 THE PROTECTION OF BUSINESS INTERESTS

These include business continuity provisions and retirement provisions for employees and directors.

a. Business Continuity Provisions

Business continuity provisions must be taken into account in estate planning. An estate may have many assets which are of material value and which the estate planner does not want to be sold after his death. A farmer may wish to bequeath his farm to one particular child because of his interest in farming, while treating all the other children equally. The estate plan should recognize this and make provision for adequate bequests to all those heirs who do not share in this farm. This can be done either by taking out insurance policies on the life of the planner to ensure that there is cash bequests for those heirs not sharing in the particular asset. Estate planning of every partner or co-shareholder will impinge upon estate planning of other partners and shareholders, thus making consultation with all partners and shareholders necessary for matters to proceed smoothly.

There is a possibility that the spouse or heirs of the partner or shareholder may want to step into the shoes of the deceased. Proper planning will also avoid unnecessary legal battles between heirs and partners or shareholders.

b. Retirement Provisions for Employees and Directors

Retirement planning is part of estate planning. Planning for retirement can be facilitated by taking advantage of beneficial tax treatment for example, retirement gratuities.

c. Liability and Loan Account Cover

To ensure that sufficient liquidity is available to meet obligations under buy and sell agreements or similar arrangements.

CHAPTER 2

AN OVERVIEW OF THE LAWS GOVERNING ESTATE PLANNING

2.1 ESTATE DUTY ACT

Estate duty is levied in terms of the estate duty act 45 of 1955 on the estates of deceased persons resident in the Republic at the time of death, no matter where it is situated. The rate of estate duty is currently 20% and is payable if the net value of the deceased estate exceeds R1 500 000, as an abatement of R1 500 000 may be deducted from the net value in determining the dutiable amount. The executor of the deceased estate is responsible for payment of the estate duty to the Commissioner for the South African Revenue Service, who has responsibility for the administration of the Estate Duty Act.

2.2 RELEVANT PROVISIONS OF THE INCOME TAX ACT 58 OF 1962

2.2.1 DONATIONS TAX PROVISIONS

The purpose of donations tax is to discourage the avoidance of income tax by the distribution of gifts where the idea is that the income derived from donated assets is spread among more taxpayers and thus taxed at a lower effective rate. Donations tax imposes a cost on, and therefore discourages, certain gifts that are made in order to reduce the donor's dutiable estate for estate duty purposes and thus reduce his potential liability for estate duty. The donations tax provisions are contained in ss 54 to 64 of the Income Tax Act 38 of 1962. Section 54 subjects donations which are made:

* by persons ordinarily resident in the Republic or
* by domestic companies

to tax at a flat rate of 20% (25% prior to October 2001). Section 58 provides that donations for this purpose include property disposed of for what, in the opinion of the Commissioner, is an inadequate consideration, to the extent of that inadequacy.

Donations tax is a tax payable on the gratuitous disposal of capital, not income by a taxpayer. It was introduced in March 1955 with the following reasons for the introduction given by the then Minister of Finance:

> *"A method also employed for avoiding taxation is by distribution of gifts – a practice which has, during recent years, been employed on a large scale: It serves a double purpose. In the first place the donor reduces the assets on which estate duty would be payable at death, and in addition whilst he is still alive, he reduces his income tax, because by means of these donations the assets, and hence also the income derived therefrom, are spread over a great number of taxpayers."*

Donation is defined as *"any gratuitous disposal of property including waiver or renunciation of a right".* *[Section 55(1)]*

The common law definition of a donation requires the following essential characteristics:

* A contract between donor and donee.
* A premise by the donor to give something to the donee, or such a gift.
* As the motive of the donor is that of pure liberality, no consideration from the donee can be involved.
* The donation impoverishes the donor's estate and enriches that of the donee.

The definition contained in Section 55 refers not to a contract, but to a disposal which would appear to have a wider meaning than the common law.

The first R30 000 of the value of property donated by a natural person in a year is exempt from donations tax. Other exemptions include:

Section	
56(1)(a)	Donations in terms of ante- or postnuptial contract
56(1)(b)	Donations to a spouse
56(1)(c)	Donations motis causa (in contemplation of death)
56(1)(d)	Donations where the donee does not benefit until the donor's death

56(1)(e)	Donation cancelled within six months
56(1)(g)	Donations of property outside the Republic
56(1)(h)	Donations by or to government or local bodies and certain institutions and funds
56(1)(k)	Voluntary wards which are subject to income tax in donee's hands
56(1)(l)	Property disposed of in terms of a trust
56(1)(m)	Property consisting of a right (other than usufructary/fiduciary) to the use or occupation of property used for farming purposes if the donee is a child of the donor.
56(1)(n)	Donations made by public companies
56(2)(c)	Maintenance payments

2.3 S 103 AND S 7 ANTI-AVOIDANCE PROVISIONS

An estate plan must take cognizance of Section 103(1) of the Act, the so called "General Anti-avoidance provision".

Section 103(1) was amended in 1978 and again in 1996. In its present form it provides as follows:

> *"Whenever the Commissioner is satisfied that any transaction, operation or scheme (whether entered into or carried out before or after the commencement of*

this act, and including a transaction, operation or scheme involving the alienation of property)-

a. *has been entered into or carried out which has the effect of avoiding or postponing liability for the payment of any tax, duty or levy imposed by the act or any previous income tax act, or of reducing the amount thereof and*

b. *having regard to the circumstances under which the transaction, operation or scheme was entered into or carried out-*

i. *was entered into or carried out-*

(aa) *in the case of a transaction, operation or scheme in the context of business, in a manner which would not normally be employed for bona fide business purposes, other than the obtaining of a tax benefit, and*

(bb) *in the case of any other transaction, operation or scheme, being a transaction, operation or scheme not falling within the provisions of item (aa), by means or in a manner which would not normally be employed in the entering into or carrying out of a transaction operation or scheme of the nature of the transaction, operation or scheme in question; or*

ii. *has created rights and obligations which would not normally be created between persons dealing at arm's length under a* *transaction, operation or scheme of the nature of the transaction, operation or scheme in question, and*

c. *was entered into or carried out solely or mainly for the purpose of obtaining a tax benefit, the Commissioner shall determine the liability for any tax, duty or levy imposed by this Act, and the amount thereof, as if the transaction, operation or scheme had not been entered into or carried out, or in such manner as in the circumstances of the case he deems appropriate for the prevention of diminution of such avoidance, postponement or reduction."*

What is meant by "tax benefit". Section 103(7) provides:

> *"For the purposes of subsection (1) 'tax benefit' includes any avoidance, postponement or reduction of liability for payment of any tax duty or levy imposed by this act or by any other law administered by the Commissioner."*

Where any resident has disposed of shares held in any company, which is a resident to a non-resident (for example a non-resident trust), such disposal unless it is proved to the Commissioner's satisfaction that the parties are independent persons dealing at arm's length with each other, is deemed to be a transaction, operation or scheme entered into or carried out by means or in a manner not normally employed in the entering into or carrying out of such a transaction, operation or scheme.

For Section 103(1) to be invoked there must be

* a transaction, operation or scheme;
* which has the effect of avoiding, reducing or postponing any tax referred to;
* which was entered into in an abnormal manner or created abnormal rights and obligations; and
* which was entered into solely or mainly for the purposes of obtaining a tax benefit.

All four requirements must be satisfied.

The position where the anti-avoidance provisions are applicable.

2.4 SECTION 7(2)(a)

Section 7(2)(a) of the Act deems any income received by or accruing to a spouse (the recipient) whether married in or out of community to be income accrued to his or her spouse (the donor). If such income was derived by the recipient:

* In consequence
  - of a donation, settlement or other disposition made by the donor on or after 20 March 1991, or
  - of a transaction, operation or scheme entered into or carried out by the donor on or after that date; and

- the sole or main purpose of such donation, settlement or other disposition or transaction, operation or scheme was the reduction, postponement or avoidance of the donor's liability for any tax, levy or duty;
- which, but for such donation, settlement or other disposition, or transaction, operation or scheme, would become payable by the donor under the Income Tax Act or any other Act administered by the Commissioner.

The object of the Section 7(2)(a) is to prevent income splitting between spouses in order to take advantage of the fact that the spouses are taxed separately.

In order for Section 7(2)(a) to operate there must be either:

* A donation, settlement or other disposition, or
* A transaction, operation or scheme.

With regard to the words "donation" and "settlement" it was held in Ovenstone v SIR that in:

> *"A donation a donor disposes of the property gratuitously out of liberality or generosity, the donee being thereby enriched and the donor correspondingly impoverished, so much so that, if the donee gives any consideration at all therefore, it is not a donation... It can therefore be regarded as a unilateral contract in the sense that the donor is the only party upon whom any obligation*

lies. In a 'settlement' the property is usually disposed of upon specific terms and conditions, set out in a deed of settlement; to or through the medium of a trustee or trustees for the benefit of some person, or for the benefit of persons in succession as in a fidei commissum... As far as the beneficiaries are concerned a settlement is also generally made gratuitously out of liberality or generosity in the sense that no consideration usually passes from them to the Settlor for the benefits conferred on them. 'Settlement' is thus usually of the same genus as 'donation'. It is probably separately mentioned in the critical phase because in form, substance, or effect it may sometimes not be regarded as a true donation. For example, where the recipients of the property are trustees who are not themselves enriched by the settlement."

2.5 SECTION 7(3)

Section 7(3) provides that income is deemed to have been received by the parent of the minor child if by reason of any donation, settlement or other disposition made by the parent of the child:

* It has been received by or accrued to, or in favour of, that child or has been expended for the maintenance, education or benefit of that child; or
* It has been accumulated for the benefit of that child.

Section 7(3) can also apply to a trust where income from an intervivos trust has been received by or has accrued to a minor child, by reason of a donation, settlement or other disposition made by the parent of the child, section 7(3) will operate so as to deem the income to accrue to the parent.

2.6 TAX CASES RELATING TO DONATIONS TO MINOR CHILDREN (SILKE)

In Kohler v CIR (1949T) the court found as a matter of law that upon a proper construction of the equivalent of S 7(3), it was only income derived in the first instance by a minor from sums donated by his parent that could be included in a parent's income. Therefore the provision did not apply.

In CIR v Widan (1955A), Centlivres C.J. interpreted the words 'by reason of' in the equivalent of S 7(3) as follows (9 + 351):

> *"When income has been received by a minor child the inquiry is whether such income has been so received by reason of any donation, settlement or other disposition" made by the parent of that child."*

There must be some casual relation between the donation and the income in question. Difficult cases may conceivably arise where, for instance, a father donates a sum of money to a minor child and the child buys a business to which he contributes his skill and labour and from which he earns an income, that income may be regarded as being attributable to two causes, viz. the donation and the skill and labour of the child. In such a case it may be impossible to say which part of his income was the result of the donation and which part was the result of his skill and labour and it may be that the Commissioner would not be able to apply (the equivalent of S 7(3)).

The expression 'donation, settlement or other disposition' employed in S 7(3) has been subjected to extensive examination by the courts.

In *Joss v SIR* (1980T) the taxpayer sold dividend-producing shares to a company, in which his minor daughter and a trust formed for the benefit of any children to be born of him owned some of the shares in return for a loan on which, for some years, no interest was paid. In the two years of assessment under review the company declared dividends to his daughter and the trust. In the first of these years the dividend would have been smaller had he charged interest on the loan. The court held that the making of the interest-free loan constituted a disposition for the purposes of S 7(3), not being a disposition for full value. The failure to charge interest effected the dividends paid to the shareholders of the company. The court effectively directed the Commissioner to amend the assessment for the two years and to include in the taxpayer's income that portion of the dividends that the company would not have been able to pay had interest been charged.

An interest-free loan advanced by a taxpayer to a private company was regarded as a continuing donation in CIR v Berold (1962A) and the resulting income was deemed to have been received by him in terms of S 7(3).

2.7 SECTION 7(4)

This section deals with the situation where the reason for income being received by or accruing to a minor is a donation, settlement or other disposition made by a third person who, or whose family, in turn, is the recipient of a donation, settlement or other disposition or other consideration from the minor's parent. The income received by or accruing to the minor child is deemed to be the parent's.

In terms of Section 90 of the Act the parent can recover from the child the tax he has had to pay, as a result of the deemed accrual.

2.8 SECTION 7(5)

Section 7(5) of the Income Tax Act provides that if any person has made a donation, settlement or other disposition which is subject to a stipulation or condition, whether made or imposed by that person or by anybody else, to the effect that the beneficiaries or some of them shall not receive the income or some portion of the income until the happening of some events, fixed or contingent, then so much of the income as would, but for the stipulation or condition, be received by or accrued to or in favour of the beneficiary in consequence of the donation, or disposition, or settlement, is deemed to be income of the maker of that donation, settlement or disposition until the happening of the event or until his death which ever takes place first.

As Meyerowitz points out, the section requires two conditions for it to be invoked:

* There must be a stipulation or condition the effect of which is that the beneficiary shall not receive the income until the happening of an event; and
* But for the stipulation the income would be received by or accrue to the beneficiary concerned.

2.9 SECTION 7(6)

The objective of Section 7(6) is to counter the tax avoidance which is achieved by being in a position to decide on an annual basis in whose hands trust income is to be taxed. A donor could set up a trust, retain the right to vary the beneficiaries of the trust income, and then proceed on an annual basis to allocate the income to the beneficiaries with the lowest marginal rate of tax. Section 7(6) seeks to prevent this by providing that when income accrues to a beneficiary in consequence of a donation, settlement or other disposition, which contains a stipulation that the right to receive the income thereby conferred, may, under powers retained by the person by whom that right is conferred, be revoked or conferred on another, such income shall be deemed to be that of the person who conferred the right.

If no income accrues to the beneficiary, Section 7(6) cannot apply but Section 7(5) may operate. Section 7(6) can only operate whilst the donor has the power referred to in the section and accordingly Section 7(6) has no application if the donor dies or renounces his power.

2.10 SECTION 7(7)

The objective of the introduction of Section 7(7) was to prevent a practice whereby money is donated to another from non-taxed income. This could be achieved, prior to the introduction of Section 7(7), by a taxpayer ceding an income generating asset to another person for a period on condition that the asset be ceded back on expiry of the period.

Section 7(7) provides that income received by or accrued to or for the benefit of some other person is deemed to have been received by or to have accrued to a taxpayer (the donor) if the following are present:

* There must be a donation, settlement or disposition made by the taxpayer.
* By reason of donation, settlement or other disposition:
    - the taxpayer's right-
        i. to receive or have paid to him or for his benefit any amount by way

of rent, dividend, interest, royalty or similar income in respect of any movable or immovable property; or

ii. in respect of the use of, or the grant of permission to use, such property, is ceded or otherwise made over to any person or to a third party (e.g. a trustee) for the benefit of

- the cession or making over is in such manner that-

  i. the taxpayer remains the owner of or retains an interest in the property; or

  ii. if the property or interest is transferred, delivered or made over to the other person or third party (e.g. trustee) for the other person's benefit, the taxpayer is or will at a fixed or determinable time be entitled to regain his ownership or interest.

* Alternatively, by reason of the donation, settlement or other disposition, the taxpayer's right to receive or have paid to him for his benefit any income that is (or may become due to him by any other person acting in a fiduciary capacity (e.g. income from a trust) is ceded or otherwise made over to any person or to a third party (e.g. a trustee) for that other person's benefit in such manner that the taxpayers is or will at affixed or determinable time be entitled to regain that right.

* But for the donation, settlement or other disposition, any such rent, dividend, interest, royalty or income received by or accruing to the other person or for his benefit (including any income which would have been exempt in his hands)

would otherwise have been received by or accrued to or for the benefit of the taxpayer.

2.11 SECTION 7(8)

Section 7(8) was inserted in the Act as an anti-avoidance measure necessitated by the move to a world-wide, residence basis system of taxation. It is aimed at the avoidance of tax where a South African resident shifts income into the hands of non-residents by disposing of income-generating assets to a non-resident.

Section 7(8) provides that:

* Where by reason of or in consequence of any donation, settlement or other disposition.
* Other than a donation, settlement or other disposition to a foreign entity, as defined in Section 9D, of a public character.
* Made by a resident.
* Income is received by or accrued to any person who is not a resident.
* Other than a controlled foreign entity as defined in Section 9D in relation to such resident.
* There shall be included in the income or such resident so much of the amount or any income as is attributable to such donation, settlement or other disposition.

*   Provided that if the income comprised foreign dividends, the amount of income to include in the resident's income must be determined in accordance with the provision of Section 9E as if the non-resident were a shareholder who is a resident.

2.12 SECTION 7(10)

Section 7(1) settles the question whether it is the Taxpayer or the Commissioner who must initiate an enquiry into the possible application of Section 7. It also authorizes the Commissioner to include in the taxpayer's returns questions relating to the possible application of Section 7 apart from the penalties applying to non-disclosure or misleading disclosure. A failure to comply with the requirement of Sec 7(10) exposes the taxpayer to unlimited application of the additional tax provision, Section 76, since the usual three-year period of prescription would be interrupted by non-disclosure. The inclusion of Section 7(10) will prevent taxpayers from reading ignorance in mitigation of the imposition of penalties in cases where they have failed to disclose Section 7 income and their non-disclosure comes to light.

2.13 CAPITAL GAINS TAX PROVISIONS

Capital gains tax (CGT) became operative on 1 October 2001. It was not introduced as a separate tax but rather as part of the Income Tax Act. In terms of Section 26A of the

Income Tax Act there shall be included in the taxable income of a person for a year of assessment the taxable capital gain of that person for the year of assessment determined in terms of the eighth schedule. The eighth schedule provides the necessary steps to be followed by which the gain is to be calculated.

2.13.1 THE STRUCTURE OF CGT

The interrelationship between the eighth schedule and Section 26A of the Income Tax Act can be set out by use of the following steps:

* Disposal of asset (deemed disposal).
* Calculation of disposal proceeds.
* Deduct base cost.
* Take account of all exclusions for capital gain as well as deferrals and capital losses.
* Calculate the sum of all capital gains and losses and then take into account annual exclusion, currently R10 000.
* From this calculation ascertain the aggregate capital gain or aggregate capital loss.
* Deduct previous assessed capital losses.
* The set of calculations undertaken above will determine whether there is a net capital gain or an assessed capital loss.
* In the event that there is an assessed loss, this can be carried forward to the next year of assessment.

* In the event that there is a net capital gain multiply by the applicable inclusion rate to obtain the amount of taxable capital gain which then is added to the taxable income as defined in terms of the Income Tax Act.

The inclusion rate is set at 25% of the net gain for natural persons and special trusts and 50% of the net capital gain for other taxpayers.

SUMMARY OF CAPITAL GAINS TAX LIABILITY CALCULATION
(INCOME TAX ACT 8TH SCHEDULE)

↓

Disposal of Deemed Disposal of An Asset

↓

Proceeds or Deemed Proceeds

↓

Deduct Base Cost of the Asset

↓

Exclusions

↓

Sum of All Capital Gains and Losses Reduced by the Annual Exclusion of R10 000

R0 or R0

Aggregate Capital Gain | Aggregate Capital Loss

Deduct Previous Assessed Capital Loss
(If Applicable)

Net Capital Gain x Inclusion Rate | Assessed Capital Loss Carried Forward

Taxable Gain Included in Taxable Income

2.13.2 CGT GAINS TAX – DEATH

A deceased person is treated as having disposed of all their assets to the deceased estate for proceeds which is equal to the market value of those assets at the time of death. In turn the deceased estate is treated as having acquired those assets at the market value. The only assets which fall out of this net are assets transferred to the surviving spouse, assets bequeathed to a public benefit organization and a long term insurance policy of the deceased if the proceeds of the policy would have been excluded if paid to that person. No capital gains tax is payable in respect of the lump-sum benefits payable from pension fund, provident funds and retirement annuities. Annuities is an event which triggers off both estate duty and capital gains tax. An annual exclusion of R50 000 is applicable to gains or losses instead of R10 000 during the lifetime of the deceased.

Where capital gains tax exceeds 50% of the net value of the estate for estate duty purposes, the lack of liquidity may obligate the executor to dispose of an asset in order to pay CGT, relief is granted to the heir of such an asset where he can pay this tax within three years after the executor has been given permission to distribute the estate assets.

2.13.3 DISPOSALS OF THE ESTATE

When assets are distributed by the estate to the heirs, legatees or trustees of a trust it is regarded as a disposal, the proceeds being equal to the base cost (the market value at date of death) of the state and resulting in no capital gains tax being payable. The base cost of the assets in the hands of the heirs, legatees and trustees are equal to the market value of the assets as at the date of death.

Should the estate sell any assets there could be a gain or loss equal to the difference of the proceeds and base cost. Such a disposal must be treated as if the deceased has disposed of the asset himself.

2.14 WILLS ACT 7 OF 1953

The Wills Act sets out the formalities involved in the making of a valid will which is very important.

Where a person dies without leaving a will, the laws of intestate succession apply. The will is a legal document and must conform to certain legal requirements. The Wills Act of 1953 has been amended with the effect that certain formalities have been relaxed. The amendment to the Act came into effect on 1 October 1992 and applies to all wills in respect of which the Testator has died on that date. Where the Testator has died before 1 October 1992, however the more stringent requirements will still apply.

2.14.1 WILLS IN RESPECT OF WHICH THE TESTATOR HAS DIED BEFORE 1 OCTOBER 1992

For a will executed after 1 January 1954, in respect of which the Testator has died prior to 1 October 1992, the more stringent requirements laid down by the will act will apply.

1. How must a will be signed?

The will must:

a. Be signed by the Testator and two competent witnesses on every page;

b. Although it is not a formal requirement, be dated on the last page; and

c. Be signed on all the pages by the Testator and two Witnesses while they are all persons at the same time.

2. Who may witness a will?

a. For a will to be valid, the witnesses must be at least fourteen years of age and able to give evidence in court.

b. Beneficiaries under the will, or their spouses, must not sign as witnesses to the signing of a will and their spouses are not able to benefit under the will.

c. A person nominated as an executor/trustee, guardian or their spouses must not sign as a witness to the will as the will render the nomination null and void.

3. Codicils and Amendments

A codicil can be described as an appendix to a will. One is normally drawn up where minor changes are required to a will which do not warrant a complete redraft of the will. Because a codicil is also a testamentary document it must comply with the same requirements as a will for validity. Any deletion, addition, alteration, or interlineations made to a will or codicil must be carefully and clearly marked or written and authenticated by the full signatures of the Testator(s) and the witnesses in the margin opposite. It is not permitted simply to initial such changes or additions.

If a section of the will is deleted, the Testators and the witnesses must sign against the deletion and, if any substituted wording has been inserted. They must also authenticate the new insertion.

Only the original document needs to be signed. It is unnecessary to either sign or initial the copy of the will although it is usual to record the date on it. If both original and copy are signed, it may be difficult to ascertain which document accurately expresses the Testator's last wishes.

2.14.2 WILLS IN RESPECT OF WHICH THE TESTATOR HAS DIED AFTER 1 OCTOBER 1992

A will executed after 1 January 1954 and in respect of which the Testator died after 1

October 1992. The amendment to the wills act will be applicable and the requirements for a valid will are as follows:

1. How must a will be signed?

a. The will must be signed at the end thereof by the Testator(s) and by two competent witnesses. If the will consists of more than one page, each page other than the page on which it ends must also be signed by the Testator(s). In this regard it is interesting to note that 'signature' is defined as including the making of initials.

b. The signing of the will by the Testator (all pages) and the Witnesses (last page) must take place while they are all present at the same time.

c. Although it is not a formal requirement, the will should be dated on the last page.

Note: It should be noted that in terms of the Wills Act, the court is empowered to accept wills that do not comply with the above requirements, provided that it is satisfied that the document before the court is intended to be the Testator's last will.

2. Who may witness a will?

a. For a will to be valid the witnesses must be at least 14 years old and must be competent to give evidence in a court.

b. Any person who signs a will as witness and the spouse of such person will be disqualified from receiving any benefit under that will. If however, a court is satisfied that such person or his spouse did not unduly influence the Testator in the execution of his will, or where the will concerned was witnessed and signed by at least two other competent witnesses who will not receive any benefit under the will, or where the witness or his spouses would be entitled to inherit from the Testator in terms of intestate succession. If the Testator died intestate, the person or his spouse will be allowed to receive the benefit under the will. In the latter case, the value of the person that said person or his spouse would receive intestate.

c. It must be noted that the nomination of a person as Executor, Trustee or Guardian will be regarded as a benefit to be received by such person from that will. In other words, if a person who witnesses a will is nominated as Executor, Trustee or Guardian under that will, such person will be disqualified from taking up such appointment except in circumstances set out in (b) above.

3. Codicils and Amendments

All the formalities required in the execution of a will apply for the execution of a codicil.

Any amendment to a will or a codicil must be carefully and clearly marked or written and authenticated by that signature of the Testator(s). the signature of the Testator must be made in the presence of two competent witnesses who must also sign next to the amendment. An amendment includes a deletion, alteration or interlineations. Note that it is no longer necessary for both the deletion and substitution of a section of the will to be authenticated separately by the signatures of the Testator and the Witnesses. The deletion and substitution need only be authenticated once with the requisite signatures. Only the original document needs to be signed. However, if the original is in the possession of someone else, it is a good idea to date a copy so the Testator knows on what date the will was drafted.

2.15 TRUST PROPERTY CONTROL ACT 57 OF 1988

2.15.1 APPLICABLE TO WRITTEN INSTRUMENTS (S 2)

The act applies to any trust being an oral agreement which is reduced to writing, whereby ownership of property is by reason of a trust instrument made over to trustees or to beneficiaries subject to the trustee's control. By reason of this definition, bewind trusts and even foundations (if such institution exists in SA) will be subject to the Act once reduced to writing.

2.15.2 REQUIREMENT OF MASTER'S REGISTRATION (S 4)

Unless the Master is already in possession of the trust deed, the trust deed must be lodged with him together with the prescribed fee. Similarly, any amendments of the deed must be so lodged.

2.15.3 TRUSTEE'S SERVICE ADDRESS (S 5)

The trustee must provide a legal service address, and notify the master by registered post within 14 days of any address change.

2.15.4 TRUSTEE'S RIGHT TO DEAL WITH THE ASSETS (S 6)

A trustee may only take up his appointment (i.e. deal with the trust assets) once the Master has officially authorized this in writing, and he will only give such authorization if the trustee has provided security for the due performance of his duties, or he has been exempted therefrom (by the Master of the court). The Master does however have the power to authorize a trustee who has not been exempted from providing security to carry out certain specific actions in deserving circumstances. The Master will dispense with "providing security" if there are sound reasons to do so. The trust deed must expressly exempt the trustee from providing security, but even if this is the case, the Master may nevertheless insist on the provision of security. The Master may also vary his decision to exempt the trustee from providing security at any time.

2.15.5 MASTER'S RIGHT TO APPOINT A TRUSTEE (S 7)

The Master may appoint a person as trustee in case of a vacancy in the office where the trust deed does not provide for successive appointments.

2.15.6 FOREIGN TRUSTEES (S 8)

If a foreign trustee administers trust property in SA, the provisions of this Act will apply, he will have to comply with Sections 4 and 6 above.

2.15.7 DUTY OF CARE (S 9)

Trustees are required to exercise care, diligence and skill which can reasonably be expected of persons managing the affairs of others. Trust provisions which exclude liability for negligence (i.e. that seek to indemnify the trustee against liability for breach of trust where he fails to show the required degree of care) have no force and effect.

2.15.8 HANDLING OF TRUST MONIES (S 10)

Trust monies must immediately be placed in a separate trust account with a bank or building society.

2.15.9 REGISTRATION AND IDENTIFICATION: TRUST PROPERTY (S 11)

Trustees must, subject to the trust deed and the financial institutions (investment of funds) Act 39 of 1984, in their bookkeeping clearly indicate what property they hold as trustees, and register such trust property so that it is identified, as far as possible, as trust property. Trustees were given 12 months from the Act's commencement to effect the necessary transfer arrangements, free of deeds office charges.

2.15.10 SEPARATE POSITION OF TRUST PROPERTY (S 12)

Trust property does not form part of the trustee's personal estate (except where as trust beneficiary, the trustee is entitled to ownership or vested rights in the trust property). Upon the trustee's personal estate being sequestrated the trust assets cannot be attached, thus effectively constituting a separate estate both in the event of the trustee's death or insolvency. This protection will only apply if the trust is duly registered with the Master in accordance with the Act, and the trustee's appointment is approved thereunder. The effect of this provision is that even though trust property is not registered in the name of the trustee, it will still be treated as such.

2.15.11 COURT'S POWER TO VARY TRUST PROVISIONS (S 13)

The court is expressly given the power to vary a trust instrument, including the right to substitute certain trust property for other property. If it is of the opinion that the founder could not have contemplated consequences which have hampered the trust in the achievement of its objectives, or which prejudice beneficiary interest or which are in conflict with public policy.

2.15.12 VARIATIONS ON BEHALF OF A WARD (S 14)

This section provides that a tutor or curator may consent to a variation of a trust deed on his ward's behalf provided the variation is in the ward's interest.

2.15.13 MATERIAL IRREGULARITIES (S 15)

A duty is placed on a person who audits a trust to report any material irregularity in the trust's administration to the trustees, and if such matter has not been rectified to the auditor's satisfaction within a month, he shall report it to the Master. It is not a requirement that a trust must be audited (unless the trust deed calls for this), but it is nevertheless customary that the trustees should ask the Master for an exemption from having to audit the trust.

2.15.14 MASTER'S RIGHT TO CALL FOR ACCOUNT (S 16)

Trustees must account for their administration in accordance with the written requests of the Master. It is not customary for the Master to call for these unless he has reason to believe that there may be irregularities in the administration/disposal of trust assets. The Master also has the right to call for trust records and documents, with powers to question the trustee and, if required, to implement an investigation by an independent person.

2.15.15 CUSTODY OF DOCUMENTS (S 17)

A trustee shall not destroy any document being proof of an investment, safe custody, control, administration, alienation or distribution of trust property before a period of 5 years from termination of a trust.

2.15.16 ACCESS TO TRUST DOCUMENTS FROM THE MASTER (S 18)

Trustees, sureties and persons who in the opinion of the Master have sufficient interest in a trust document under the Master's control may, upon payment of a prescribed fee, obtain a copy of such document.

2.15.17 COMPLIANCE BY TRUSTEES THROUGH A COURT ORDER (S 19)

If a trustee fails to comply with the Master's requests under S 16, or fails to administer the trust in accordance with the law or trust deed, the Master may apply to court for an order forcing the trustee to comply.

2.15.18 REMOVAL OF TRUSTEES (S 20)

The Master or any interested party may on application to the court, seek the removal of a trustee if it is in the interests of the trust or its beneficiaries. The Master is also entitled to remove a trustee without the court's sanction in cases where the trustee has been convicted of an offence involving dishonesty or if the trustee fails to provide adequate security after a period of 2 months from the Master's request (or such longer period as may be allowed), or if the trustee had been declared mentally incapable of running his own affairs by a court, or if he fails to comply with the law, the trust deed or any lawful request of the Master. Upon removal or resignation, a trustee must return his written authorization to act for the trust.

2.15.19 RESIGNATION OF TRUSTEE (S 21)

A trustee may resign from office upon notice to the Master and to all ascertained beneficiaries who have legal capacity and to the representatives of persons under tutorship or curatorship.

2.15.20 REMUNERATION OF TRUSTEES (S 22)

If a trust deed is silent on trustee's remuneration, the trustee is entitled to a reasonable remuneration which may be fixed by the Master in the event of a dispute.

2.15.21 MASTER'S ACTIONS REVIEWABLE BY THE COURTS (S 23)

Any person who is aggrieved by the appointment of a trustee, or by any other decision of the Master may apply to court for the appropriate relief.

2.16 ADMINISTRATION AND TAXATION OF DECEASED ESTATES

* The administration of Estates Act 66 of 1965 ("The Act") governs the administration of the estate of a deceased person who dies leaving assets situated physically in South Africa. The Act does not govern the administration of assets of a deceased person situated in a foreign country.
* The death of any person dying within or outside the country must be reported to the Master of the Supreme Court. If he leaves property or a will in the country, it must be delivered to the Master and provided it complies with legal requirements, it will be registered and accepted by the Master.
* Within fourteen days or such extended period permitted by the Master, an inventory of the deceased's property in the prescribed form must be drawn up in accordance with Section 9 of the Act. The Master may call for a further inventory at any time thereafter.
* The Master controls and supervises the liquidation and distribution of a deceased estate and it is the Master's function to ensure that the executor carries out his duties in accordance with the law and his directions.

* An executor is appointed either by nomination in the will of the deceased or if there is no will, or no nomination, by the Master. An executor has no authority to act unless letters of executorship have been granted by the Master. Executor testamentary must provide security unless he is the parent, child or surviving spouse of the deceased, or the Testator has directed that the Master dispense with security or unless the Master or the court has directed otherwise.

2.16.1 BRIEF OUTLINE OF ADMINISTRATION

* By law all institutions handling funds or investments or any nature whatsoever in the name of the deceased must be advised, preferably in writing that the relevant account must be frozen until further notice.
* The following official forms must be collected from the Magistrate's Court or nearest office of the Master of the Supreme Court:
    - Death Notice J294
    - Acceptance of Executorship J190
    - Inventory Form J243
    - Estate Duty Form J67
    - Master's Query Sheet J84
* The forms collected above must be submitted to the Master within 14 days after the deceased has passed away or as soon as possible within a reasonable period thereafter. The following additional documents must be submitted:

- Original Last Will and Testament
- Copy of the Death Certificate
- Certified Copy of Marriage Certificate
- Antenuptial Contract if married Out of Community of Property

* As soon as the letter of executorship from the master has been received the executor can proceed with the rest of the steps to wind up the estate.
* The executor must take control of the property, as well as all documents and books and if required to provide security or requested by the Master to do so, lodges an inventory thereof.
* He advertises for creditors to lodge their claims.
* He examines creditors' claims to ensure solvency of the estate.
* He attends to the income tax return in respect of the period up to the date of death, pays any tax that is payable and obtains a tax clearance from the Receiver of Revenue for lodgement with the Master.
* Opens a bank account in the name of the deceased estate.
* He attends to the sale of assets in accordance with the will.
* He calls upon debtors to settle their debts, compromise with debtors if necessary and granting extensions of time to them to discharge their debts if necessary.
* He determines the estate's liability in respect of estate duty, if any.
* He draws up a liquidation and distribution account together with supporting vouchers. This account he lodges with the Master for examination and approval.
* He advertises that the accounts are lying for inspection.

* In the absence of objections to the accounts, he pays the creditors and distributes the estate amongst the heirs and legatees and lodges their receipts and acquitances with the Master.
* He applies to the transfer for discharge from his office after the estate has been wound up.

The executor must determine the estate duty liability in terms of the Estate Duty Act and provide for its payment in the liquidation account. The executor must compute not only the estate's estate duty liability but also that of any other person and must ensure that that estate duty is paid.

If the deceased died leaving assets situated outside South Africa, the executor must take the necessary steps to have his authority to wind-up the estate recognized in the foreign country.

2.16.2 THE TAXATION OF INCOME OF DECEASED ESTATES

1. Income accruing prior to death

Income which is received by or which accrues to the deceased prior to death is taxed in the usual manner in the hands of the deceased, with the executor of the deceased estate acting as the representative taxpayer.

2. *Income accruing after death*

The taxation of income which is received by or which accrues to the deceased state is governed by Section 25 of the Act.

<u>*Section 25(1)*</u>

Provides that any income received by or accruing to the executor:

* which would have been income in the hands of the deceased
* shall, if such income has been derived for the immediate or future benefit of any ascertained heir or legatee, be deemed to be income of such heir or legatee and, if not, be deemed to be income of the deceased estate.

<u>*Section 25(2)*</u>

Provides that any deduction or allowance which relates to any income of an heir or legatee in terms of Section 25(1) shall be deemed to be a deduction or allowance of such heir or legatee. Similarly the estate is entitled to the deductions or allowances relating to the income taxed in its hands.

As the deceased and the deceased estate are separate personae for tax purposes, the assessed loss of the deceased at the date of death is not available for set off by the deceased estate.

A deceased estate is a taxable entity and is taxed in the normal way according to rates applicable to natural persons. The deceased estate is not entitled to rebates available to natural persons. The executor is the representative taxpayer of the deceased estate.

Section 25 only applies to income which is received by or which accrues to the executor and has no application to income which accrues directly to heirs or legatees.

2.17 MATRIMONIAL PROPERTY ACT

The most significant element of the Matrimonial Property Act of 1984 is the introduction of the accrual system.

The accrual system has no effect on the independent legal capacity of the spouses and is similar to the "old ante-nuptial contact".

Both parties continue to administer their own estates until dissolution of the marriage on either death or divorce, at which stage the spouse with the smaller accrual acquires a claim against the other spouse or his estate for half of the difference between the accrual of their respective estates. The accrual of the spouse's estate is the amount by which the net value of his estate at the commencement of the marriage. Each party to an intended marriage declares the commencement value of his estate in the ante-nuptial contract. The accrual of that spouse's estate will be the difference between the commencement value and the value of death or dissolution with certain exclusions (see calculation, page 49).

The commencement value is adjusted for inflation over the period of the marriage. The real growth in the estates of both spouses during the course of the marriage is divided equitably on dissolution. There is no community of property. The rights to the accrual acquired by the spouses is not transferable or attachable and nor do they form part of the insolvent estate of a spouse.

Inheritances, legacies and donations are specifically excluded from the accrual. The accrual system can be specifically excluded in the ante-nuptial contract and the "old" out of community regime is still an option from an estate planning perspective. Any individual contemplating marriage must make a choice between the three available systems:

- Community of property,
- The accrual system, or
- An ante-nuptial contract excluding accrual.

The choice is important since each of these will have its own irreversible effect on the nature, content and disposal of a person's estate, either during his lifetime or on his death.

2.17.1 THE CHOICES OF MARRIAGE

1. Community of Property

Community of property is the basic system of our law. The spouses are equal partners in a joint estate, from which only certain types of property can be excluded. Each spouse may enter into certain classes of contract without the consent of the other party, but other type of contract require the consent of both spouses either oral or written.

2. ***The Accrual System***

This can only be made applicable by entering into an ante-nuptial contract. This is a notarial contract and therefore requires the assistance of an attorney. Each spouse retains his or her pre-marriage estate, but when the marriage ends, the increase in their respective estates will be combined and in effect split equally between them or between the survivor and the estate of a deceased spouse. The parties retain an independent contractual capacity.

3. ***Ante-nuptial Contract with the Exclusion of The Accrual System***

The accrual system can be expressly excluded in the ante-nuptial contract. This means that each spouse would retain control of those assets brought into the marriage as well as those acquired during the marriage. It is probably only worth considering where one or both the spouses have considerable estates with exceptional potential for growth prior to the marriage, or where one of the spouses has extraordinary high earning potential.

Certain assets are excluded from the accrual system:

*	Assets excluded in the ante-nuptial contract.

* Amounts received by a spouse for non preliminary loss (pain, suffering, crimen injuria)
* Bequests, legacies or donations accruing to a spouse during the course of a marriage, and
* Donations between spouses.

Calculation of Accrual in terms of the Accrual System

	Mr A	**Mrs A**
Assets before the marriage (as shown in the ANC)		
Current value of each spouse's assets		
Less: Liabilities of each spouse's estate Less: Liabilities excluded from respective estates	( ) ( )	( ) ( )
Current value of respective estates Less: Original assets revalued at CPI (CPI = ------%)	R ( )	R ( )
Accrual	R =========	R =========
Greatest Accrual	R	
Less: Smallest Accrual	( )	
Divisible Accrual	R ÷ 2	
Portion that spouse with smallest accrual receives from other spouse	R ______________	

2.18 TRANSACTION TAXES

2.18.1 VALUE ADDED TAX (VAT)

VAT is a tax collected by registered businesses (vendors) on value added by them in conducting their activities. A vendor has to pay over to Revenue an amount equal to the output tax collected by the vendor on its turnover less the input tax borne by the taxpayer on its purchases of goods or services. Accordingly VAT is a transaction tax and is currently at the rate of 14% of the value of goods or services involved.

1. Where the Deceased is not a Vendor

There are no VAT consequences if the deceased was not a vendor at the time of his death.

2. Where the Deceased is a Vendor

Where a vendor dies, any enterprise previously carried out by him continues to be conducted by the executor of his estate, the deceased estate is deemed to be a vendor in respect of the enterprise. The deceased vendor and his estate are deemed to be one and the same person. The Executor is the person responsible for ensuring that the deceased estate's VAT responsibilities are fulfilled.

2.18.2 DISPOSAL OF THE ASSETS OF THE DECEASED'S ENTERPRISE

"Assets" includes both a supply of goods or a supply of services.

2.18.2.1 ASSETS WHICH FORMED PART OF THE DECEASED'S ENTERPRISE

* Where the business is sold as a going concern to another person who is also registered for VAT – sales treated as a zero-rated transaction.
* Where assets of the business are sold off piecemeal, the sales will attract VAT at the standard rate.
* Where the business is deregistered for VAT purposes then the deceased estate is obliged to account for output tax in respect of assets on hand at that date.

The above only applies to assets of the deceased's/deceased estate's enterprise.

Where the deceased's business is held via a company or close corporation and the executor disposes of the business by selling the shares or the members' interests, there are no VAT consequences.

2.18.2.2 ASSETS WHICH WERE USED PARTIALLY IN THE DECEASED'S ENTERPRISE

Assets which were partially used in the enterprise, attracts the same VAT consequences as outlined above.

Special rules apply to private residences. Where property is acquired before 30 September 1991, has been used mainly as private residence and no input tax deduction has been claimed thereof, and is subsequently disposed by the estate no VAT need be accounted for on the disposal.

2.18.2.3 DISPOSAL OF MOTOR CARS

Generally no tax needs to be accounted for by the executor on the disposal of a motor car. It is only where the enterprise in question trades in motor cars that the executor needs to concern himself.

2.18.2.4 TRANSFER OF ASSETS TO HEIRS OR LEGATEES

Where a supply is made for no consideration whilst VAT is levied at a standard rate, it is levied on a nil value and thus no tax need to be accounted for.

2.18.2.5 DISTRIBUTION OF ASSETS TO SURVIVING SPOUSE OF A MARRIAGE IN COMMUNITY OF PROPERTY

Where the joint estate of such spouses conducted an enterprise, any distribution of assets of the enterprise to the surviving spouse from the joint estate constitutes a taxable supply for VAT purposes. The executor is obliged to account for VAT on any distribution of an asset to the surviving spouse, even though the surviving spouse has an undivided share in such asset.

2.19 IMPLEMENTATION OF AN ESTATE PLAN

In the implementation of an estate plan, assets of the planner are transferred, hence VAT consequences in doing so need to be considered.

Always ensure that the recipient entity is registered for VAT before any transfer is affected.

2.20 TRANSFER DUTY

The transfer duty Act 40 of 1949 levies transfer duty on the value of any property acquired by way of a transaction or in any other manner, or on the amount by which the value of any property is enhanced by the renunciation of an interest in or restriction upon the use of disposal of that property (Section 2(1)).

Transfer duty arises where there has been an acquisition "*by way of a transaction or in any other manner*".

Rates of Transfer Duty

If property is acquired by a person who is not a natural person the rate is 10%. For individuals the rate is as follows:

2001/2002		**2002/2003**	
		INDIVIDUALS	
R0 – R70 000	1% of purchase consideration	R0 – R100 000	0%
R70 0001 – R250 000	R700 + 5% of the amount in excess of R70 000	R100 001 – R300 000	5% on the amount in excess of R100 000
R250 000 +	R9 700 + 8% on the amount in excess of R250 000	R300 000 +	R10 000 + 8% on the amount in excess of R300 000

A trust is included in the definition of "person" in the Act and accordingly property acquired by a trust attracts transfer duty at the rate of 10%.

Transfer duty must be paid within six months of the date of acquisition by the person acquiring the property or by the person in whose favour an interest in the property or restriction upon its use or disposal is renounced (Section 3(1)).

CHAPTER 3

AN OVERVIEW OF ESTATE DUTY

3.1 INTRODUCTION

When a person dies, there is a levy known as estate duty which is charged and collected in respect of that person's estate. Estate duty is payable on the estate of every person who dies and was ordinarily resident in South Africa at the date of his death. As a general rule, all assets belonging to a person who is ordinarily resident in South Africa at the date of his death will fall into his estate no matter where those assets are situated.

Estate duty is levied and collected by the Commissioner in respect of the estate of every person who died on or after 1 April 1955, irrespective of citizenship, nationality, residence, domicile or any other qualifications, including place of death.

The duty is levied at a flat rate of 20% (25% in respect of persons who died prior to 1 October 2001 and 15% in respect of persons who died prior to 14 March 1996) on the "dutiable amount" of the deceased estate.

For the purpose of the calculation of estate duty a person's estate consists of:

- All property of the deceased as at date of death and
- All property deemed to be property of a person as at the date of his death.

Estate duty is levied on the dutiable amount of a person's estate which is determined as follows:

1. Determine the value of all property of the deceased.
2. ADD the value of all deemed property of the deceased.
3. DEDUCT the allowable deductions, giving the net value of the estate.
4. DEDUCT the allowable lump-sum abatement R1,5 million (Sec 4A) therefrom, giving the required dutiable amount.
5. Calculate 20% of the dutiable amount, giving the duty payable.

3.2 PROPERTY FOR ESTATE DUTY PURPOSES

Property is defined in the Act as *"any right in or to property, movable or immovable, corporeal or incorporeal"* (Section 3(2)).

Corporeal property is property which is tangible, for example a motor car or a building, while incorporeal property is property which is intangible, for example a trademark or patent.

3.2.1 USUFRUCTARY AND OTHER LIMITED INTERESTS

Limited interests are included in property for estate duty purposes.

Limited interests are the following:

1. Fiduciary, usufructary and other like interests in property.
2. An annuity charged upon property.
3. A right to an annuity (not charged upon property) according to some other person on the death of the deceased.

3.2.2 FIDUCIARY, USUFRUCTARY AND OTHER INTEREST IN PROPERTY

A fiduciary interest arises when a fideicommissum is created. A fideicommissum is created when a person transfers ownership in property to another person, the fiduciary, on condition that the property will pass to a third person, the fideicommissory, on the happening of some event, usually the death of the fiduciary.
The fiduciary has full ownership in the property but cannot dispose of it unless the fideicommissory dies before the fiduciary.

A usufruct over property entitles the holder (the usufructary) to the use of the property and to the income therefrom for a certain period, very often for life. The owner of the property has the “bare dominium” if the bare dominium holder should die before the usufructary, the usufructary does not acquire full ownership of the property. Fiduciary, usufructary and like interests are valued in terms of the provisions of Section 5(1)(b) of the Act, while annuities charged upon property are valued in terms of Section 5(1)(c).

3.2.3 ANNUITIES NOT CHARGED UPON PROPERTY

The annuities not charges upon property must fulfill both the following conditions before being included in property:

* It must have been enjoyed by the deceased immediately prior to his death, and
* It must accrue to some other person on the death of the deceased (Section 3(2)(b)).

Annuities which do not pass to some other person on the death of the deceased do not constitute property and therefore not dutiable.

3.2.4 PROPERTY THAT BELONGS TO THE DECEASED AND ITS VALUATION

	Property	**Value for Estate Duty Purpose**
1.	Fixed assets	Market value
2.	Agricultural land	At the option of the executor either a. the fair market value, or

		b. the surface value (land plus improvements in accordance with Land Bank Act) plus the fair market value of any mineral rights.
3.	Movable assets	Market value
4.	Investments	Amount of investment
5.	Listed shares	Exchange prices
6.	Unlisted shares	As determined by auditor. If the deceased owns more than 25% but less than 50% of the shares, a rebate of 5% of the value of the shares is allowed. If less than 25% the rebate is 10%.
7.	Usufruct	Capitalise over life expectancy of the person upon whom the usufruct devolves or over term. If the term is shorter than life expectancy (or 50 years if indeterminable), but limited to the difference between the current market value and the value of the bare dominium at the time the usufruct was created, if the holder of the BD now becomes the full owner.
8.	Bare dominium	Market value less usufruct.
9.	Fideicommissum	As for usufruct.
10.	Annuity charged upon property and which devolves upon another person	Capitalise owner life expectancy of the person upon whom annuity devolves or over term if shorter than life expectancy.
11.	Annuity charged upon property and which does not devolve another person	Capitalise over life expectancy of owner or property.
12.	Annuity which is a personal liability and devolves upon	Capitalise over life expectancy of person to whom annuity accrues or over term if shorter than life

	another person.	expectancy.
13.	Annuity which is a personal liability and which does not devolve upon another person.	Nil.

3.3 ASSETS DEEMED TO BE PROPERTY

3.3.1 INTRODUCTION

The estate of the deceased, the determination of which comprises the first step in the calculation of the dutiable amount upon which estate duty will be levied, consists of property as at date of death and property deemed to be property of the deceased as at that date in accordance with the Act (Section 3(1)).

3.3.2 DEEMED PROPERTY IS DEFINED IN SECTION 3(3) OF THE ACT

Deemed property defined in Section 3(3) of the Act includes the following:

1. The proceeds of certain "domestic" policies on the life of the deceased (e.g. policy effected by the deceased, but the proceeds fall due to a cessionary, or beneficiary: policy effected by someone other than the deceased), excluding:

   * Policies effected in terms of a duly registered ante-nuptial or post-nuptial contract, if the amount due under the policy is recoverable by the

surviving spouse or child of the deceased under such a contract (Section 3(3)(a)(1)).

* Policies which the Commissioner is satisfied were taken out or acquired by a person who on the date of death of the deceased was a partner of the deceased, or held any share or like interest. In a company in which the deceased on that date held a share or like interest for the purpose of enabling that person to acquire the whole or part of:

  - the share or like interest of the deceased in the company concerned and any claim by the deceased against that company.

  This exemption operates only if the Commissioner is satisfied that no premium on the policy was paid or borne by the deceased. Member's interest in close corporation is also included in the reference made to a share or like interest. (Section 3(3)(iA)

* Policies payable to a person other than the estate of the deceased, a relative, a person who was dependent on the deceased for his maintenance or a company which was a "family company" in relation to the deceased at any time (Section 3(3)(a)(ii)), provides that:

  a. The policy was not effective at the request of the deceased.

  b. No premiums in terms of the policy were paid or borne by the deceased.

  If the policy is not exempt in terms of the above mentioned, a deduction equal to all premiums paid by the person entitled to receive the proceeds together with compound interest at 6% per year is allowed.

2. Benefits payable by funds (e.g. Pension, Provident and RA funds), excluding:

   * Total contribution paid by any person entitled to the returns together with interest compounded at 6% per year. (Section 3(3)(a)(bis)
   * Life annuities payable on or as a result of the death of a member of a pension or RA. (Section 3(3)(bis)(i))
   * Tax payable on lump sums (recoverable from the person who receives the benefit).
   * Lump sum benefit received from funds established by law or in terms of an Act.

3. Donations *"mortis causa"* (in contemplation of death) (Section 3(3)(b))

   Any property donated under a *"donatio mortis causa"* is included in the estate of the deceased person.

4. The value of the "accrual" acquired by the estate of the deceased from the surviving spouse in terms of the Matrimonial Property Act. (Section 3(3)(cA)

5. Property (including profits on property) which is otherwise not dutiable and of which the deceased immediately prior to his death was competent to dispose of for his own advantage or the advantage of his estate. (For instance, property

donated to a trust where the deceased retained the power to revoke or vary the provisions of the deed of the trust relating to the property and the deceased was a trust beneficiary.) (Section 3(3)(d))

3.4 ALLOWABLE DEDUCTIONS FROM GROSS ESTATE (SECTION 4 OF THE ESTATE DUTY ACT)

* Funeral and death-bed expenses (include tombstone). In the case of joint estates, deductible from the deceased's portion of the joint estate. (Section 4(a))

* Debts due by the deceased (including a maintenance claim awarded by a court of law to a former spouse). (Section 4(b) and 4(f))

* Costs incurred in the administration and liquidation of the estate:
    - Executor's fees in respect of deceased estates

      Above R50 000 (normally 3,5% plus 14% VAT) of gross estate and only on assets dealt with by the executor. Minimum fee R350. Executor's fees are not payable on limited rights, but are payable on the bare dominium. Only the executor's fees levied on the gross assets of the deceased portion of a massed estate are deductible.

- Master's fees
  - . Where the gross value of the estate is less than R15 000.
  - . Where the gross value is between R15 000 and R17 000.
  - . For each full R2 000 by which the gross value exceeds R17 000.
  - . Overall maximum is R600 (on R203 000 and more).
- Sworn appraisals
- Advertisement costs
- Conveyancing fees in respect of fixed property

* Property situated outside South Africa and which was acquired by the deceased before he became ordinarily resident in South Africa for the first time or after he became a R.S.A resident. If the property was acquired by a donation or inheritance from a non-R.S.A. resident.

* Bequests and donations to the state or a local authority or any charitable, educational or religious institution or fund exempt from tax.

* Premiums plus 6% compound interest in respect of a policy on the life of the deceased but which is the property of someone else who also paid the premiums.

* The value of a usufruct, or of any right to an annuity charged upon property which was included as property of the predeceased spouse, if it was not allowed as a

deduction in the estate of the predeceased spouse. (Section 4(m)

* The amount by which the value of a property increased as a result of improvements to the property at the expense of the person to whom the property accrues and which took place during the lifetime of the deceased and with his consent.

* The amount of an accrual claim by the surviving spouse acquired against the estate of the deceased.

* Accruals to the surviving spouse (Section 4(q)). These deductions are reduced by the amount which the surviving spouse must dispose of in terms of the will to another person or to a trust and are not allowed in respect of property accruing to a trust established by the deceased for the benefit of the surviving spouse and in terms of which the trustees have a discretion to allocate the property or any income from the property to any person other than the surviving spouse.

* The portion of the proceeds of any assurance policy deemed to be an asset in the estate which has already been taken into account in determining the value of any company shares already included in the estate. (Section 4(p))

* The value of books, paintings, stationery or other objects of art which have been lent to the state or any local authority or institution for the advancement of science or to a charitable, religious or educational institution provided the lending period is at least 30 years. (Section 4(o))

3.5 ASSURANCE POLICIES EFFECTED BY SPOUSE MARRIED IN COMMUNITY OF PROPERTY

Half of the surrender value of a policy on the life of the survivor is property in the estate of the predeceased. The following policies are however not the sole property of the wife and no portion thereof is dutiable in the estate of the husband:

1. A policy effected by the wife on her own life or on the life of her husband prior to or during her marriage.

2. A policy affected by the husband prior to the marriage on the life of the wife and ceded, before conclusion of the marriage to any of their children who were already born or who may be born.

3. A policy effected by the husband prior to or during the marriage on the life of the wife and ceded during the marriage to her and their child.

3.6 DEDUCTIONS FROM ESTATE DUTY PAYABLE (FIRST SCHEDULE, SECTION 16(a))

3.6.1 RAPID SUCCESSION

Where the deceased inherited the whole or a portion of an estate (in terms of which estate duty has been paid).

From a person who died less than 10 years previously, estate duty on that portion of the estate on which estate duty has already been paid by the deceased, is reduced by the following percentage:

* 100% if less than 2 years have expired since the assets were inherited.
* 80% if between 2 and 4 years expired.
* 60% if between 4 and 6 years expired.
* 40% if between 6 and 8 years expired.
* 20% if between 8 and 10 years expired.

3.6.2 TRANSFER DUTY

The deduction allowed in respect of transfer duty only arises where it has been paid by the person liable for the duty attributable to that property and not where it was paid by the deceased or by any other person. This situation will only arise where the property was acquired by donation or deemed donation in terms of the Estate Duty Act, since no transfer duty is payable on property inherited by testamentary disposition or intestate.

3.6.3 PERSONS LIABLE FOR PAYMENT OF ESTATE DUTY

Payable by the executor of the estate, but he may recover the estate duty in respect of the following:

* The proceeds of any policy on the life of the deceased which are payable to a person other than the deceased, from the person who is entitled to receive the proceeds.
* The benefit payable by a fund, from the person who receives the benefit.
* Any donation mortis causa, from the donee.
* Limited rights, from the beneficiary.

3.6.4 LIQUIDITY ANALYSIS

The following calculation sheet gives an indication of estate costs and estate duty.

Liquidity Analysis

			R
	Property and Deemed Property		
1.	Vehicles		xx
2.	Shares		xx
3.	Life Assurance Policies (except Keyman & buy & Sell)		x
4.	Lump sums (Pension, Provident, RA)		xx
5.	Current and Savings Account		xx
6.	Limited Interest (Usufruct etc.)		xx
7.	Immovable Property		xx
8.	Household Effects		xx
9.	Other		xx
		TOTAL A	xx
Less:			
	Liabilities and Administrative Expenses		
1.	Mortgage Bond		xx
2.	Overdraft		xx
3.	Instalment Sale Agreements		xx
4.	Death Bed and Funeral Expenses		xx
5.	Accrual Claim (if applicable)		xx
6.	Master's Fees		xx
7.	Executor's Remuneration (3,5%)		xx
8.	Assets which accrue to spouse (Sect 4q)		xx
9.	Other		xx
		TOTAL B	Rxx

TOTAL A minus TOTAL B = NET ESTATE

LESS: REBATE (Sec 4A) R1 500 000

DUTIABLE AMOUNT – Duty at 20%

Estate Liquidity

			R
1.	Cash at Bank		xx
2.	Life Assurance Policies		xx
3.	Lump Sums (Pension, Provident, RA)		xx
4.	Investments (Shares, Coins, etc.)		xx
5.	Bequest Prices payable by Heirs		xx
6.	Other		xx
		TOTAL C	Rxx

Liquidity Analysis

Less: Cash needed for

1.	Executor's fees		xx
2.	Master's fees		xx
3.	Liabilities		xx
4.	Funeral expenses		xx
5.	Cash bequest		xx
6.	Other		xx
7.	Estate duty at 20%		xx
		TOTAL D	Rxx

TOTAL C – TOTAL D = SURPLUS/SHORTFALL

Therefore LIQUIDITY SUPPLEMENT NEEDED

When making provision for a shortfall in liquidity it must be borne in mind that this money will also attract estate duty.

CHAPTER 4

ESTATE PLAN

The following techniques can be used to reduce estate duty liability.

4.1 USE OF R1,5M ABATEMENT (SECTION 4A)

Maximum use should be made of this abatement which is deducted from the net value of a deceased's estate to arrive at the dutiable amount.

Every estate qualifies for exemption for estate duty is payable on assets (this includes common-law spouses and same sex partners). The R1,5 million abatement is wasted if you leave everything to your spouse.

Although your estate will not pay estate duty, the payment of duty on all your assets is postponed until your spouse dies.

Example

Your estate is worth R5 million and your spouse's estate is worth R1 million. If you leave everything to our spouse, his or her estate will be worth R6 million when you die. On your spouse's death, his or her estate will make use of the R1,5 million abatement, and pay estate duty on R4,5 million. At a rate of 20 per cent, the estate duty will be R900 000. However, you can bequeath R1,5 million directly to your children or to a trust (free of estate duty because of the abatement), and the balance of R3,5 million to your spouse (also free of estate duty because it is left to a spouse).

On the death of your spouse, he or she has an estate of R4,5 million (R1 million plus the R3,5 million he or she inherited from you). Your spouse's estate can make use of the R1,5 million abatement, which will reduce the dutiable estate to R3 million. Your spouse's estate will then only have to pay estate duty on R3 million, which amounts to R600 000 which is a saving of R300 000.

4.2 USE OF DONATIONS

The following are some of the ways in which the use of donations can reduce one's estate:

* The first R30 000 of all amounts donated by a natural person in any year of assessment are exempt from tax. This exemption is applicable per person, therefore a married couple can donate up to R60 000 without incurring donations tax.

* A significant amount of estate duty savings can be achieved by donating an asset which is growing rapidly in value. You will pay less donations tax now.

* Assets may be donated to achieve outright saving of donations tax and estate duty. Donations may also have certain income tax, capital gains tax and STC consequences which must be borne in mind.

* Where a farmer donates livestock, the current market value of the livestock is included in his income. This value will generally be far much greater than the standard value of the livestock. The donor is liable for income tax on the difference between the market value of the livestock and the lower standard value of the livestock.

* A person other than a farmer donates trading stock, the current market value of the trading stock is included in his income.

* Where an asset, in respect of which the donor had previously claimed an allowance (e.g. a wear and tear allowance) is donated, the donor is deemed to have recovered or recouped an amount equal to the market value of the asset as at the date of the donation. The donor could be liable to income tax on the amount of a recoupment.

* Where an asset is distributed without any consideration to a member of a company or close corporation, there is a secondary tax on companies (STC) payable on such distribution.

* Donating a limited interest can be an effective technique especially if the donor is an elderly person.

* Donations between spouses are exempt from donations tax.

There are various reasons for one spouse donating to the other spouse:

1. To ensure the spouse with the smaller estate has greater financial resources.
2. To ensure full use is made of the R1,5m abatement in both parties estates.
3. To provide the spouse with the smaller estate an opportunity to donate R30 000 per annum to the spouse's ultimate heirs free of donations tax.
4. A limited interest over some of the property ensures that the value of the property is reduced in his estate.

* Donations and Capital Gains Tax

A donation of an asset is a disposal for capital gains tax purpose. The donor disposes the assets for proceeds equal to the market value of that asset at date of disposal. No capital gain or loss arises when any disposal of an asset is made by one spouse to another.

A donor must disregard any capital gain or loss arising as a result of a donation of an asset to an approved public benefit organization.

A donation of cash has no capital gains tax implications because capital gains tax can only arise on the disposal of an "asset" as defined excludes cash.

4.3 PEGGING THE VALUE OF AN ESTATE

4.3.1 SALE OF LOAN ACCOUNT

* Growth assets are sold by the planner to his future heirs.
* Since the heirs do not have the means to pay for the assets, the purchase price is left outstanding on loan account. Such a loan is interest free.
* The planner may reduce the amount owed on the loan by donating R30 000 per annum to the debtor to enable the debtor to reduce the indebtness. However, cash donations must be used for this purpose because they do not give rise to capital gains tax. Partial waivers of the loan will be regarded as disposals for capital gains tax purposes.

4.3.2 USE OF OPTIONS

Use of option is a way of pegging an estate for estate duty purposes. For example a farmer with a farm which is growing in value, grants an option to his son to purchase the farm at land bank value. The terms of the option are such that the option is exercisable within three months of the planner's death.

The advantages of such a scheme is as follows:

* Growth is pegged for estate duty purposes.
* It is a simple plan.
* The planner still has control of his property until death.
* The planner can grant the option to ensure that the beneficiaries of the property obtain maximum advantage from his estate.

4.3.3 SALE IN EXCHANGE FOR PREFERENCE SHARES

Where a company is integrated into the estate plan, consideration may be given to selling the planner's assets to a company in exchange for the issue of preference shares to the planner.

These shares are used "to peg" the value of the planner's estate, the right to dividends and return of capital attaching to the shares must be such as to ensure that the shares will not appreciate materially in value.

4.4 USE OF LIMITED INTERESTS

4.4.1 DONATION OF USUFRUCT BY AGED USUFRUCTARY

For donations tax purposes the usufruct or fiduciary interest is valued over the life expectancy of the donor. If the interest holder dies, the interest is valued for estate duty purposes over the life expectancy of the successor.

4.4.2 RETENTION OF USUFRUCT AND SALE OF DOMINIUM

When a planner has an asset which is rapidly increasing in value he can retain the usufruct and sell the bare dominium if he wishes to avoid estate duty.

Example

Mr A aged 50, owns a holiday home with a market value of R1m. He sells the bare dominium of the property at market value to a family trust on interest-free loan account and the usufruct is retained for 15 years. The trust now owes Mr A R182 692. Each year thereafter Mr A gratuitously reduces the credit loan account in the trust by the amount of annual donations tax exemption (currently R30 000 per person) until the amount is extinguished.

If Mr A lives for fifteen years, at the end the holiday home will attract no estate duty in his estate. Full ownership vests in the family trust. There are no donations tax liability. The full ownership of the house is transferred to the trust. Transfer duty is only paid on the value of bare dominium i.e. on R182 692.

If Mr A dies during the fifteen year period he could provide for the bequest of the usufruct to his wife in his will. This would result in the usufruct being excluded from his estate by Section 4(q) of the Estate Duty Act.

4.5 USE OF TRUSTS

An intervivos trust can be set up and certain growth assets can either be sold or donated to the trust (but donations tax will be payable on all donations over R30 000). If assets are sold to the trust, the purchase price is usually left outstanding and the trust will owe this amount to the seller. The loan is usually repayable on demand or death, whichever occurs first.

Sometimes the trust takes out a life policy on your life in order to repay the loan to your estate on your death. You can bequeath the balance of the loan account to your estate on your death. The value of the loan remains estate dutiable in your estate, but any growth on the asset takes place in the trust and is removed from your estate for estate duty purposes. The trust can repay the loan account over your lifetime providing for you to live on at retirement, and the value of the loan is then gradually reduced in your estate for estate duty purposes. If you are going to be one of the trustees of the trust you should have at least two other trustees otherwise tax legislation may regard any assets donated or sold to the trust as being yours.

4.5.1 OFFSHORE TRUSTS

You must be very careful if you use an offshore trust. As it exhibits certain characteristics which are different from that of South Africa, it is necessary to analyse it in detail.

The taxation of offshore trusts is complex and there are several provisions in tax legislation that may result in an unexpected tax liability for you.

4.5.2 TRUSTS

A usufruct is sometimes used in conjunction with a trust. Such a usufruct will have an effect on the calculation of the exemption of capital gains tax available in terms of sections 44 and 45. A usufruct can be described as the right to "the use of the fruits" of an asset over which the usufruct is registered. A bare dominium can be described as the ownership of an asset minus the usufruct. It is possible to sell the bare dominium of an asset to a trust, while someone else is the owner of the usufruct. The value of a usufruct depends on the length thereof. As a rule of thumb one can say that the value of a usufruct for a 20 year period will be approximately 90% of the value of the property. A longer period will increase the value of the usufruct and a shorter period will decrease the value. The value of the bare dominium is the difference between the value of the property as a whole and the usufruct value, that means in a 20 years scenario the value of the bare dominium will be approximately 10% of the total value of the property.

4.5.2.1 USUFRUCT AS AN ESTATE PLANNING TOOL

Let's illustrate usufruct with an example. Client A has an estate worth R15 million, in his own name. Say Client A sells the bare dominium portion of his assets to a trust and keeps the usufruct for himself for a period of 20 years, or for as long as he lives (if he should die before the 20 year period expires). Client A will have to lend approximately R1½ million (10% of R15 million) to the trust to enable the trust to buy the bare dominium right to the property. After a period of 20 years, or sooner if client A dies before the usufruct ends, the trust becomes the sole owner of the assets. After the expiry of the usufruct it cannot be included as a dutiable amount for estate duty purposes. If client A dies before the end of the 20 year period, the value of the usufruct is reduced for estate duty purposes by the fact that the remaining period of the usufruct is less than the original 20 years.

One can register a usufruct over any asset. In practice most usufructs are registered only over fixed property, because the deeds office registers a caveat that prohibits a sale of the property without the authorization of the usufruct holder. With other types of assets it will be possible to sell the assets without taking the rights of the usufruct holder and sometimes even the rights of the bare dominium holder into account. However, that does not have to deter one from using a usufruct over other assets if the parties involved can be depended on to honor the usufruct agreement.

4.6 POLICIES EXEMPT FROM ESTATE DUTY

There are three forms of assurance policies which do not attract estate duty.

4.6.1 POLICIES EFFECTED OR CEDED UNDER AN ANTE-NUPTIAL CONTRACT

Amounts recoverable under life policies which have been effected or ceded in terms of an ante-nuptial or post-nuptial contract are exempt from duty provided that the following requirements are present:

* The amount due under the policy (i.e. the proceeds must be recoverable by the surviving spouse or child and
* The ante-nuptial contract (or post-nuptial contract) must have been duly registered. *[Section 3(3)(a)]*

This exemption can be used to solve liquidity problems without attracting estate duty on the policy proceeds.

4.6.2 KEY-MAN POLICIES

The proceeds of key-man policies are exempt, provided that the Commissioner is satisfied and remains satisfied that:

* The policy was not effected by or at the instance of the deceased.
* No premium on the policy was paid or borne by the deceased.
* No amount due and recoverable under this policy has been or will be paid into the estate of the deceased, and
* No amount has been paid or utilized for the benefit of, any relative to the deceased or any person who was wholly or partially dependent for his maintenance upon the deceased or any company which was at any time a family company in relation to the deceased. *[Section 3(3)(a)(ii)]*

4.6.3 POLICIES TAKEN OUT BY PARTNERS OR CO-SHAREHOLDERS

Policies which qualify are those in respect of which the Commissioner is satisfied:

* Were taken out or acquired by a person who on the date of death of the deceased was a partner of the deceased, or held any shares or any like interest in a

company in which the deceased was a co-shareholder at the date of death.

* Were taken out or acquired by the partner or co-shareholder for the purpose of enabling him to acquire the whole or part of:

  - the deceased's interest in the partnership, or
  - the deceased's interest in the company and any claim by him against the company.
  - no premium on the policy was paid or borne by the deceased.

[Section 3(a)(a)(iA)]

It is possible to provide liquidity for an estate in terms of a buy and sell agreement. Two or more partners or co-shareholders can effect reciprocal insurance policies on the life of the others which can be used on death to fund the purchase of the deceased partner's share in the partnership, or shares and/or loans account against the company or close corporation. The executor uses the cash from the sale of the deceased's share to meet the liquidity requirements of the estate.

CHAPTER 5

INTERNATIONAL ESTATE PLANNING AND OFFSHORE TRUSTS

5.1 INTRODUCTION

More South African residents can now invest offshore because of the relaxation of exchange control regulations. Generally, property wherever situated will form part of a South African's dutiable estate. Where the deceased is not ordinarily resident in South Africa at date of death, certain assets are excluded from dutiable estate.

The reasons why sensible planning for offshore assets is important are as follows:

* To ensure any increase in value in the offshore assets is "pegged".
* To minimize foreign taxes and death duties.
* To cater for bequests to heirs who are resident outside the country.

The offshore trust therefore plays an important role in the development of such a plan.

5.2 ESTABLISHMENT OF AN OFFSHORE TRUST

The trust in an offshore context involves a quadrangle of people i.e. the Settlor, Trustees, Beneficiaries and the Protector.

1. Settlor

The Settlor establishes the trust. The Settlor is the original owner of the property being transferred to the trust. He appoints the trustees and transfers the legal ownership to them (usually by way of a trust deed) although verbal trusts are possible. He also specifies who the beneficiaries are.

Once the trust is established, the Settlor cannot force the Trustee to administer the trust in a way other than what the trustee deems appropriate, although the trustee should consider the Settlor's intentions expressed at the time the trust was created.

2. Trustees

They are the legal owners of the property and have a number of duties imposed upon them by the trust instrument and the statutory law. The Trustee can be either an individual (personal trustee) or a company (corporate trustees).

These Trustees have their limitations. The personal trustee may be someone known to the Settlor and his family. The personal trustee is subject to normal human frailties. He could become ill and even die. The safety of the trust assets is, in this case entrusted to a single individual.

A corporate trustee has advantages over an individual trustee because the corporate trustee cannot die owing to the corporate structure.

The limited liability of the corporate structure may protect the Trustees against beneficiary claims. If the individuals dealing with the trust is transferred or goes on holiday, you will then be dealing with individuals who have absolutely no knowledge of the particular Settlor or his circumstances nor of the beneficiaries. The Trustees must be chosen with caution.

In most jurisdictions, where the Settlor is able to exercise control over the trust assets and the trust is effectively an alter ego of the Settlor, this may well have adverse income tax and estate duty implications onshore. The offshore authorities may also disregard the trust and deem the assets to be those of the Settlor.

3. Beneficiaries

They are the equitable or beneficial owners of the trust property and all conduct must be for their benefit.

Beneficiaries are classified according to the types of interest they hold:

Absolute Interest

An absolute interest is the full equitable ownership that cannot be revoked. This is also referred to as a bare trust as the trustees hold the property as a nominee and have no continuing duty or power other than implementing the beneficiaries' instructions.

Life Interest

A life interest is the entitlement to income from the trust but no access to the capital thereof. The Beneficiary with a life interest is known as the life tenant, while, after their death, the property passes to other beneficiaries, known as beneficiary with a reversionary interest.

Contingent Interest

In the case of a contingent interest, the beneficiary depends on the happening of a specific event (the contingency) which may never happen.

The Beneficiaries are the only people who have the right to enforce the trust provisions. The Settlor, unless he is also a Beneficiary, does not have this right.

4. The Protector

Most offshore trust deed make provision for the appointment of a Protector. The Protector is a person with certain powers over the Trustees or the Trust Fund. The powers of the Protector may include the appointment or removal of Trustees and he may also have the power to control the Trustees' activities.

The use of a Protector is most prevalent in family trusts where the trustees are not intimately involved with the particular family. The Settlor can choose a trusted friend, colleague or family member to be appointed as Protector.

The offshore trust has certain characteristics which are different to South Africa. The Jersey Trust is very popular. The system of law that applies to a particular trust is important for a South African lawyer.

Common law applies to past and present British territories while civil law applies to continental European jurisdictions. The Trust Deed must specify title law by which the validity and interpretation of the trust is governed.

Offshore trusts are accompanied by a letter of wishes which indicates whom the Settlor wishes should benefit. The letter states the legal position, namely that the letter is not binding on the Trustees.

A major concern for the Settlor, is the control over the assets which is given to the Trustees. Therefore a Protector is sometimes employed. A Protector acts in a fiduciary capacity such that he is not entitled to benefit himself. If a Protector has the power to change Trustees then he must monitor the trust on an ongoing basis. The concept of offshore trust has become an essential part of the law of numerous offshore centres which have had historical connection with the United Kingdom.

Example of tax haven in Jersey. No tax is imposed on trust capital, income and capital gain. The trust deed empowers the Trustees to accumulate trust income during the whole of the prescribed period and empowers them at their discretion to distribute capital, income or both to beneficiaries.

5.3 LIABILITY OF TRUSTEES

In the UK, in Nestel v National Westminister Bank Plc, the plaintiff was the remainder beneficiary of a settlement established by the will of her grandfather. The Defendant Bank had been the sole trustee of the settlement since its inception.

The capital value of the Trust Fund when established in 1922 was approximately £50 000. However, by the time the plaintiff became absolutely entitled to the fund in 1986 it was worth only £269 203, whereas, by means of a calculation based upon a cost of living index, it should have been £2,6m.

The plaintiff claimed that the bank had committed various breaches of trust as a result of which she had received much less in capital value than otherwise would have been the case. Accordingly, the plaintiff alleged that the bank had been negligent in its management of the settlement and failed to maintain the real capital value of the Trust Fund in particular plaintiff argued that:

* The bank, when making investment, had not kept a fair balance between income beneficiaries and capital beneficiaries.
* The bank had improperly made investments which unduly favoured income beneficiaries over capital beneficiaries.
* The bank had improperly obtained risky stocks which had subsequently become worthless, and
* The bank had not chosen suitable investments for part of the Trust Fund.

The court found that the standard which had been imposed on the Trustee when choosing authorised investments he or she should acquire as part of the Trust Fund should include consideration as to:

* The suitability of the particular type of investment as a constituent of the Trust Fund.
* The overall level of risk inherent in the whole portfolio of investments held in trust, and
* The needs of the different beneficiary of a particular settlement.

However, the court went on to state that there was no absolute duty on a Trustee to preserve the real capital value of the Trust Fund or to achieve particular financial results in the management of the Trust Fund, nor would a breach of trust be established by showing that a Trustee had to invest in the Trust Fund and so match the rise in market indicators. The court heard that the actions of a Trustee could not be judged with the benefit of hindsight.

5.4 TAXATION OF OFFSHORE TRUSTS

The taxation of offshore trusts may arise at two levels. Firstly, when funds are actually settled upon the trust and secondly when distributions are made to the trust beneficiaries.

Until 1 March 2001, offshore trusts were governed by Section 9D of the Income Tax Act and were subject to taxability as controlled foreign entities. However, with effect from 2002 year of assessment, offshore trusts are governed by Section 25B of the Income Tax Act.

A new subsection (2A) was introduced to deal with the taxation of offshore trust distribution in the case of discretionary trusts.

In terms of the Revenue Laws Amendment Act, Section 25B(2A) provides that:

* Where during a year of assessment a resident beneficiary acquires a vested right to capital of a non-resident, and
* The capital arose from income received by or accrued to the trust in any previous year during which the resident had a contingent interest, and

* Such income had not been subject to tax in South Africa, the amount accruing to a resident is to be included in the beneficiary's income in the relevant year of assessment.

This would apply to capital distribution that arose out of income earned by the trust, which would be subject to income tax. Where capital distributions are made to South African resident beneficiaries and such distributions arose out of capital received by or accrued to the trust, this distribution would be subject to capital gains tax in terms of the relevant paragraphs of the eight schedule to the Income Tax Act.

5.5 ADVANTAGES OF AN OFFSHORE TRUST

For example, Mr and Mrs Brown both want to invest R750 000 in offshore fund. He invests these funds in ABC Trust registered in Guernsey. The trust is a discretionary trust.

The benefits of such an arrangement is as follows:

* He does not have to draw up a foreign will and appoint a foreign executor to take care of his assets after his death.
* Foreign prorate is saved and there is no freezing of assets or delays at his death.
* His letter of wishes indicates how his wishes must be followed.
* He can appoint himself and members of his family as beneficiaries.

* Confidentiality of the identity of the trust and his beneficiaries is ensured.
* The names of the Settlor and Beneficiaries is kept confidential.
* The assets transferred to the trust can also be protected against his creditors.
* *Confidentiality:* there is no public register in most tax havens.
* *Tax Planning:* a trust can often take advantage of opportunities to reduce or mitigate taxes in many jurisdictions.
* *Orderly and Efficient Estate Distribution:* allowing for the freedom to plan the future and avoid estate duties.
* *Avoidance of executorship/prorate procedures:* to avoid a procedure that is time consuming and bureaucratic.
* Avoidance of forced heirship provisions.
* *Protection of the weak:* providing financial protection for minors or those with disabilities, who may require financial support long after you are able to provide it.
* *Creditor protection:* potential protection against future unknown claims, thus safeguarding your family's wealth.
* *Flexibility:* you can change, as circumstances dictate, your plans for the future.
* *Education:* plan ahead for the education for your children and grand children.

CHAPTER 6

TRUSTS AS A MECHANISM FOR ESTATE PLANNING

6.1 INTRODUCTION

Trusts have become an important tool in estate planning. By transferring your assets to a trust, you are freezing the value, because a trust does not die and is therefore not subject to estate duty.

There is now a different slant on trusts because of capital gains tax (CGT). The South African Revenue Service (SARS) have been targeting trusts because they have been used by many as a legal vehicle to reduce income tax and estate duty liabilities.

Special care need to be taken with CGT on trusts. It is very important that you do two things:

- Look carefully at the reasons why you placed the assets in a trust in the first place and see if they are still valid.
- Proper advice on impact of CGT will be required.

Therefore, it is of vital importance to work out whether CGT will cost you more of less than estate duty would, and this will also have an impact on various other reasons for setting up a trust.

Local and foreign trusts are treated differently for CGT purposes. If less than 50 per cent of the trustees of a foreign trust are South African residents, and none of the beneficiaries are South African residents, there are no CGT consequences for assets held in a foreign trust.

There are a number of issues to be taken into account if you already have assets in a trust or are contemplating putting assets into a trust.

6.2 TYPES OF TRUSTS

The type of trusts you use is very important because of the distinctions that affect the rate of CGT you will pay.

6.2.1 INTERVIVOS TRUSTS

An intervivos trust is formed by an agreement between the founder and the trustee for the benefit of the named beneficiaries. Intervivos trusts which are also known as living or asset protection trusts are set up for various reasons from separating your personal affairs from your business affairs, to structuring your estate duty. Once an asset is placed in a trust it is no longer yours, so when you die it does not become subject to estate duty. The trust lives on. The main difference between an intervivos trust and a testamentary trust is that the intervivos trust comes into being once certain formalities prescribed by the Trust Property Control Act have been complied with and the testamentary trust only comes into being on the death of the Testator.

Advantages of an Intervivos Trust

The advantages of an intervivos trust are as follows:

* No estate duty disadvantages for your heirs.
* all growth in the value of your assets is realized in the trust and not in your estate, thereby reducing estate duty.
* If any trust assets are realized, the proceeds can be channelled to the beneficiaries.
* You will be able to draw income through loans from the trust investments which will be seen as repayment of your loan account.
* The trust deed can provide for the appropriate distribution of income and/or capital to your heirs on your death, without leaving them with an estate duty problem of their own.

Disadvantages of an Intervivos Trust

* Control of the trust assets is at the discretion of the trustees. However, the appointment of trustees is at all times at the discretion of the planner.

6.2.2 TESTAMENTARY TRUSTS

A testamentary trust is created when a Testator stipulates in his will that his estate or part thereof is to be administered in trust after his death for the benefit of his heirs or other beneficiaries. The provisions regarding the trust are contained in the will. Testamentary trusts are usually established for the purpose of ensuring that children or incapacitated dependants are properly cared for after your death. The testamentary trust is to be regarded as a will and the rule, *voluntas Testators sevanda est* (effect should be given to the Testator's wishes), the general rule is that a court has no inherent jurisdiction to consent the variation or revocation of a testamentary trust. However when circumstances unforeseen by the Testator occur, as a result of which the Testator's wishes or instructions cannot be given effect to because they are no longer practical or realistic, the courts have indicated a willingness to authorize a variation.

6.2.3 THE BEWIND TRUST

The right to the trust property vests in the beneficiary upon the founder setting the trust property on the beneficiary in terms of the trust instrument.

The control of such a trust does not vest in the beneficiary, but in the trustee who administers the trust property for the benefit of the beneficiary. The beneficiary has a personal right against the trustee that the trustee will administer the trust property to the ultimate benefit of the beneficiary.

6.2.4 SPECIAL TRUSTS

Special trusts may either be intervivos or testamentary trusts, and are established for physically or mentally incapacitated people who are unable to earn a living. Special trusts are treated as individuals, and therefore have the most favourable effective tax rate.

6.3 LEGAL STRUCTURE OF TRUSTS

Trusts in South Africa are structured in two ways, viz. as vesting trusts or as discretionary trusts.

Vesting Trusts

Give the beneficiaries of a trust the automatic right to income from the assets in the trust as well as the assets themselves.

Discretionary Trusts

Do not give beneficiaries the automatic right to income and assets. The discretion to distribute either income or assets lies in the hands of the trustees.

The difference has an impact on how CGT is levied. The vesting trust is treated as an agent. The capital gain or loss is seen as a gain or loss in the hands of the beneficiary, and the beneficiary is liable for cost. If an asset is distributed, the trust will be deemed to have made that distribution at the market value (not the original book value) of the asset, and will pay CGT on any gain. The beneficiary's base cost will be the market value with a discretionary trust. If a distribution is made by the trustees in the same year in which a capital gain or loss is made, the gain or loss is transferred to the beneficiary. If a capital gain is made in a year when there is no distribution, the trust is liable for the tax. If an asset is distributed by the trustees to a beneficiary, the disposal creates a CGT event in the hands of the trust. The asset is transferred out of the trust to the beneficiary as base cost is equal to the market value. You must take extra care with the wording of a trust deed with regard to whether the trust is a vesting or discretionary trust. Trusts do not qualify for the R10 000 annual exemption that an individual receives.

6.4 CGT EVENTS

There are differences between individuals and trusts when it comes to what constitutes a CGT event. In both cases, disposal of an asset triggers a CGT event but in the case of trusts, two additional events are considered a disposal i.e.:

- Every time you change a beneficiary in a trust it is a CGT event and subject to tax and

- Every time a property is sold, even if it is your primary residence, it is a CGT event.

6.5 CONSIDER ASSETS IN YOUR TRUST

CGT can affect different assets in different ways. The first R1 million profit you make when you sell your primary residence registered in your own name is exempt from CGT. However, this does not apply if your primary residence is held in a trust. Therefore it might be better to hold the property in your name. Note that a special dispensation has been given for individuals who hold properties in trusts and/or companies and would now like to move them out of trusts. The South African Revenue Service (SARS) has agreed that you can transfer the property into your own name without the payment of transfer duty or CGT if the transfer is completed before 1 October 2003. This dispensation does not apply if the property was registered in the name of a company, close corporation or a trust after 5 April 2001, when this legislation was first tabled in Parliament. The transfer of the property into your own name before 1 October 2003 will, however, still cost you because there are legal fees involved. You should contact a few conveyances and negotiate a fee. If there is a bond on the property, this could also affect the transfer and you will need to speak to your bank about the registration of the bond.

In deciding whether to transfer the property into your name, you should consider the reasons why you placed the property in the company or trust in the first place. You must also take two balancing factors into account:

1. You will not pay 20 per cent estate duty when you die and
2. Over the years the R1,5 million exemption will become less beneficial if it is not linked to inflation.

Note: A special trust, which is established for a person who has a mental or physical disability and is unable to earn a living, receives the first R1 million exemption, if the beneficiary of the trust (the incapacitated person) occupies the residence.

6.6 WEIGHING THE OPTIONS

The main reason for using trusts is to freeze the value of your estate at its present value for estate duty purposes. The first R1,5 million of your estate is tax free, after that an estate duty of 20 per cent is applied.

The growth in the value of the assets occurs in the trust, and not in your own estate, thus limiting the net value of your estate.

6.7 WHAT YOU HAVE TO CONSIDER BEFORE REPLACING ASSETS IN A TRUST

* The estate duty you will save at death.

* The possibility of creating CGT events, and the CGT these events will generate.

  You must take into account various reasons for a trust. These include:

  - Income tax planning - income tax advantage must be your secondary not primary motive.
  - Preservation of assets after death.
  - Continuous management of your assets.
  - Protection of assets from creditors – your personal liability is limited to the assets in your name. The assets in your trust cannot be assessed by your creditors unless these assets were shifted into a trust to avoid paying debts already incurred.

* Protection from spendthrift children who will not be able to squander your assets.
* Protection of a vulnerable spouse. Protection against someone getting married to your wife on your death.
* Protection of minor and/or mentally handicapped children.
* Income tax splitting – income from a trust can be split between a couple to reduce tax liability. It would be worthwhile making the spouse with the lower marginal rate the recipient of income from the trust.
* Impartiality – on your death, you can expect a professional trustee to be impartial, not favouring any one beneficiary.
* Assuring rapid access to income and capital after your death. Payments to beneficiaries can be delayed for up to a year when an estate is wound up.

* Multi-ownership of assets – businesses, farms or other property is sometimes difficult to divide between heirs. By placing the asset in a trust, it is held intact, with your heirs the beneficiaries of the income generated by the asset.
* Cost saving – assets in the trust are not subject to any fees or costs of winding up an estate.
* Flexibility – Trusts provide wider choices, giving you flexibility if tax, political or economic situations change significantly.

6.8 MAKE SURE THE TRUST IS VALID

Trusts play an important role in estate planning. Trusts are governed largely by the common law. A trust in the wide sense exists whenever a person is bound to hold or administer property on behalf of another or for some impersonal object and not for his own benefit. A trust in the narrow sense refers to "the legal institution where an intermediate person, trustee, holds property as owner thereof in accordance with the expressed wishes of another person, the Settlor or founder, not for his personal benefit but for the benefit of named or ascertainable beneficiaries or for an impersonal object."

A trust can be created during the creator's lifetime (intervivos trust) or by will (testamentary trust). The founder of a trust must intend to create one. He must express the intention. The property subject to the trust must be defined with reasonable certainty.

The trust object must be valid and whether the trust object is personal or impersonal. It must be defined with certainty.

A trustee may not act without authority from the Master but lack of such authority does not invalidate the trust.

It is not an essential requirement to transfer trust property to the trustee for a trust to be valued. The loss of an existing trust does not invalidate the trust.

6.9 THE TAXATION OF TRUST INCOME

* The definition of a "person" in Section 1 includes a trust.
* As a result of an amendment in Section 6(1), trusts are no longer entitled to the primary rebate.
* In terms of Section 25B of the Act:
  - Any income received by or accrued to or in favour of any person
  - in his capacity as the trustee of a trust
  - shall, subject to the provisions of Section 7,
  - to the extent that it has been derived for the immediate or future benefit,
  - of an ascertained beneficiary with a vested right
  - be deemed to be income accrued to the beneficiary
  - otherwise be deemed to be the income of the trust fund.

* In cases where the beneficiary has acquired a vested right to the trust income as a result of the trustee exercising his discretion, such income is deemed to accrue to the beneficiary. Unless S 7 intervenes, income awarded to a beneficiary at the discretion of the trustee will be treated as that beneficiary's income (S 25B(2)). Where the income accrues to the beneficiary in terms of these provisions, any deductions or allowances relating to this income are to be permitted to be claimed by the beneficiary.

* Any deductions and allowances which are not allowed to flow through to the beneficiaries can be deducted against the taxable income of the trust in the same tax year. Such deductions and allowances are limited to the taxable income in the trust before taking into consideration the deductions and allowances. If the trust is not subject to tax in the Republic the deductions and allowances can be deducted in the following year of assessment from income which the beneficiary of the trust receives in that year.

  The deductions and allowances which exceed the taxable income of the trust can be deducted in the following year of assessment from income which the beneficiary of the trust receives in that year.

* If during the year of assessment a resident acquires a vested right to capital of an offshore trust:-

- and the capital arose from income received or accrued to the trust or from any receipts or accruals of such trust which would have constituted income if such a trust had been a resident, in any previous year of assessment during which the resident had a contingent right to income, and
- the income or receipts and accruals has not been taxed in the Republic such capital amount shall be included in the income of the resident.

6.10 GENERAL PRINCIPLES

S 25B(1) ensures that, if the terms of the will or deed under which a trust is created are such that the administrator or trustee is required to pay income to a particular beneficiary, that income accrues and is deemed to accrue, to the beneficiary. He is the person to be assessed to tax on the income and not the trustee as representative taxpayer. The trustee is a mere conduit pipe by means of which the income is conveyed to the beneficiary who is legally entitled to it.

It sometimes happens that beneficiaries are not stipulated in the trust deed but the trustee is legally obliged to pay over the income to beneficiaries nominated by him in the exercise of a discretionary power conferred upon him by the deed. The income is regarded as having been received by the beneficiaries so nominated by the trustee.

Since S 25B is made subject to S 7, before applying it one would first have to ensure that the provisions of S 7(1)(2), (2A), (3), (4), (5), and (6) are inapplicable.

Where the beneficiary has a vested right in the income that beneficiary will be taxed. If there is no vested right but merely a contingent right then it cannot be said that income has accrued (ITC 76(1927((at 70)):

> *"Vesting implied the transfer of dominium and the children had clearly not in the year under review acquired dominium of the trust income or any portion thereof. A vesting right was something substantial, something which could be measured in money, something which had a present value and could be attached. A contingent interest was merely a spes – an expectation which might never be realized. From its very nature it could not have a definite present value. In the income tax sense, therefore, a vested right was an accrued right."*

With discretionary trusts, the trustee or administrator has a discretion to distribute the income or portion of it to the beneficiaries. There can be no accrual of income to the beneficiaries until the trustee exercises his discretion and makes a distribution among the beneficiaries. As soon as the trustee exercises his discretion, the contingent right of a beneficiary becomes a vested one and he is liable to tax on the income distributed to him, provided that the provisions of S 7(2), (3), (4), (5) and (6) are not applicable.

6.11 TAX RATES OF TRUSTS

Income vesting in the trust as taxpayer is taxed at a rate of 40% as from 1 March 2002 (32% on taxable income up to R100 000 and at a rate of 42% on the amount of taxable income in excess of R100 000 in the previous tax year) with the exception of a special trust and a testamentary trust created solely for the benefit of a minor.

A special trust is created solely for the benefit of a person who suffers from:

* A "mental illness" as defined in Section 1 of the Mental Health Act of 1973, or
* A serious physical disability.

Where such disability or illness incapacitates the beneficiary from earning sufficient income to maintain himself or herself.

Trusts falling into these categories will be taxed at the same rates applicable to natural persons as contained in the Income Tax Section.

PERSON TAXED		TAXATION OF TRUST INCOME	SECTION/CASE
1. Settlor : Parent		**Beneficiary: Minor Child (Own Child)**	
a.	Parent	Income received by or accrued to income that is attributable to parent's gratuitous disposition.	S 7(3); CIR v Widan; CIR v Berold; Ovenstone v SIR
b.	Minor child	Income received by or accrued to minor for full consideration, i.e. disposition for full value.	S 7(1); Joss v SIR; Ovenstone v SIR; S 25B(1) & (2)

PERSON TAXED		TAXATION OF TRUST INCOME	SECTION/CASE
2. Settlor : Parent		**Beneficiary: Major Child**	
a.	Beneficiary	i. Income actually received ii. Income due and payable i.e. accrued but not received.	S 1 "Gross Income"; S 7(1); ITC 1328; S 25B(1)
b.	Parent	Income not received by or accrued to beneficiary as a result of Settlor's stipulation or condition.	S 7(5); ITC 1328; Est. Dempers v SIR; SIR v Sidley
c.	Trustee (if Settlor is dead)	Income withheld in terms of trustee's discretion and which does not accrue to beneficiary.	S. 1 "Gross Income"; S 25B(1)
3. Settlor : Any Person		**Beneficiary: Minor Child (Not Own Child)**	
a.	Beneficiary	i. Income actually received ii. Income accrued but not received	S 1 "Gross Income"; S 7(1); ITC 1328; S 25B(1) & (2)
b.	Settlor	Income not received by or accrued to beneficiary in terms of Settlor's stipulation or condition.	S 7(5); ITC 1328; Est. Dempers v SIR; SIR v Sidley
c.	Trustee (if Settlor is dead)	Income withheld in terms of trustee's discretion and which does not accrue to beneficiary.	S 1 "Gross Income"; S 25B(1)
4. Settlor : Any Person		**Beneficiary: Person's Minor Child with Reciprocal Benefits for Settlor or his Family**	
Parents of Beneficiary		Income received by or accrued to minor child.	S 7(4)
5. Settlor : Donor Spouse		**Beneficiary: Other Spouse (Living Together)**	
Donor Spouse		Income received by or accrued to donee spouse can be taxed in the other spouse's hands if provisions of S 7(2) are met.	S 7(2)
6. Settlor: Any Person who confers a right to income but retains the power to revoke or confer the right upon another		**Beneficiary: Any Person**	
Settlor		Income received by or accrued in terms of conferred right so long as the power to revoke is retained.	S 7(6)
7. Settlor: Any Person who donates/settles a right to receive income in such a manner that he remains the owner or retains and interest therein, or is entitled to regain ownership at a specified or specifiable time.		**Beneficiary: Any Person**	

PERSON TAXED	TAXATION OF TRUST INCOME	SECTION/CASE
Settlor/Donor	Any income (e.g. rent, dividends, interest) received by the beneficiary.	S 7(7)
8. Settlor: Any Resident	**Beneficiary: Non-Resident**	
Resident	Income received by or accrued to a non-resident as is attributable to a donation, settlement, or other disposition made by the resident.	S 7(8)

6.12 TRUSTS – CASES

INCOME RETAINS ITS IDENTITY (AS PER SILKE)

In Armstrong v CIR (1938 AD) it was held that income that is the subject of a trust retains its identity until it reaches the parties in whose hands it is taxable, for example, the beneficiaries. A trust is mere conduit pipe through which the income flows, and the income retains its identity in the hands of the beneficiaries. Consequently, when the accrual of the income is to a beneficiary, any exemption from tax provided in the Act applying to the income will be available to that beneficiary.

For example, if the trust income consists of dividends, a beneficiary who is entitled to the trust income must be regarded as having received dividends and is entitled to the exemptions offered by S 10(1)(k)(i) and S 9E(7).

On the same principle, if the trust received interest on government stocks, the beneficiaries must be regarded as having received this income and if he qualifies he will enjoy the exemption from normal tax offered by S 10(1)(h).

The judgement in SIR v Rosen (1971A) is to make it clear that income flowing through a trust to its beneficiaries retains its identity, whether it is paid by way of an annuity or in some other way, provided that it accrues to the beneficiaries in the same year of assessment as it accrued to the trust. Trollip J.A., who delivered the judgement of the Appellate Division of the Supreme Court stated (at 269):

> *"It suffices to say that the trust deed may itself entitle or oblige the trustee to administer the dividends in such a way that he is not a mere conduit pipe for passing them on to the beneficiary, that in his hands their source as dividends can no longer be identified or they otherwise lose their character and identity as dividends, and that the beneficiary is thus entitled to receive mere trust income in contradistinction to the benefit of the dividend rights in terms of the above crucial phrase. Thus, a trust deed may endow the trustee with a discretion to pass on dividends to the beneficiary to retain and accumulate them. If he decides on the latter, I think (but express no firm view) that the dividends might then lose their identity and character as dividends, so that, if they are subsequently paid out to the beneficiary, they might possibly no longer be dividends in his hands, for the conduit pipe had turned itself off at the relevant time. But he decided on the former, i.e. to pass the dividends on to the beneficiary, the condition suspending the beneficiary's entitlement thereto is fulfilled, and they would constitute*

dividends in his hands in the same way as if he had been originally entitled to them unconditionally under the trust deed...."

The decision in Rosen's case, in so far as it deals with annuities, has been nullified by the introduction of S 10(2)(b). This section provides that income received by or accrued to any person in the form of an annuity will not qualify for the dividend exemption in S 10(1)(k)(i) or the exemption for interest on government stock in S 10(1)(h).

NB: Rosen's case is still of importance, in that the view was expressed (although it was not firmly decided) that trust income may change its nature if it is retained and accumulated by the trustee and paid out to the beneficiaries in a later year, having already been taxed in the hands of the trustee. Nevertheless if the income is passed to the beneficiaries in the same year in which it accrued to the trustee, it retains its nature in the hands of beneficiaries.

On the strength of Armstrong v CIR (1938 AD) it was accepted in ITC 1450 (1988) that the income or capital character of a particular profit made by a trust is retained in the hands of a beneficiary.

CHAPTER 7

WILLS AND ESTATE PLANNING

7.1 IMPORTANCE OF WILLS

Excerpt from Pace R.P. and Van der Westhuizen W.M. Wills and Trusts, 5th Service Issue, Butterworths, Page A42.

> *"Wills have been an important facet not only in law but also in the lives of people for many centuries. In a will a Testator is expressing his wishes as to how his estate is to be distributed following his death and the least he expects is that his wishes will be properly carried out and herein lies the problem. In order for his wishes to be correctly interpreted there are several basic requirements. Firstly, he must convey his intentions and desires to the draftsman of his will. Secondly, the draftsman must be able to understand what the Testator wishes to convey. This means there must be a clear and proper communication between the Testator and the draftsman. Thirdly, the draftsman must have the necessary knowledge, skill and experience in deceased estate law (this term encompasses for purpose of convenience the law of succession and the law relating to administration of deceased estates as far as these separate legal fields affects wills) to formulate stipulations and conditions that are legally binding and executable. Fourthly, the draftsman must be competent to clearly express the Testator's intention in words*

understandable not only to the world at large but more importantly to the Testator himself."

Everyday hundreds of people die without a will, leaving their families and beneficiaries in an administrative and financial mess. It is very important to make the time now to put your affairs in order to spare your family from unnecessary hardship, administrative nightmares and even the possible misallocation of legitimate assets due to them.

7.2 POINTS THAT SHOULD BE KEPT IN MIND REGARDING DEATH AND WILLS

* Upon a person's death all his or her assets are frozen. This includes bank accounts, including debit instructions and stop orders, property, credit cards and all other accounts.
* Every person has an estate after he or she dies, and every estate, no matter how large or small, is obliged to have an executor.
* An estate cannot be unfrozen or any of the deceased's requests implemented unless an executor has been formally nominated.
* Without a will, it can often take up to 12 months to sort out the details of a deceased's estate and
* Even with a will and a nominated executor, administrative formalities can delay the settlement of an estate for months.

Therefore it is in your interest to

* Draw up a will with the help of an expert who can advise you and who will make sure that your wishes will be executed properly.
* Appoint a trustworthy and capable executor, and
* Make provision for your family during the period between your death and the settlement of your estate.
* Update your will regularly, at least every two or three years.
* File documents safely and let the executor/s know where to find them.
* Do not assume the assets of marriage are yours alone if your married in community of property or with the accrual system.
* Minors can only inherit policies, not other assets.
* If you have assets offshore have a separate will to deal with how they must be disposed.
* Do not wait for something to happen to you before you consider drawing up a will. For example, a person may suddenly discover that they have a dreaded disease and have to be rushed into hospital for an emergency operation. There is no will drawn and suddenly you rush into making a will and then when you recover you do not review your will. Nine times out of ten, this will may not be suitable because it was made in a hurry and your circumstances may have changed. As one grows older circumstances change, hence the need to update your will regularly.

Many people consider these issues to be trite but yet they are critically important. These are the issues around which the future of heirs, dependants and the spouse are irrevocably shaped. Many times there are wills which only husbands have and the wife's will is ignored. When there is simultaneous death this becomes a serious problem especially when the children are minors. Make sure the trustees are somebody you know will take good care of the children when both parents are deceased.

Your will is a powerful tool in estate planning. It communicates on your behalf. It conveys your intentions.

7.3 THE SIGNING OF WILLS

A will is a legal document and must conform to certain legal requirements. These relate to the signing and witnessing of the will.

The Wills Act of 1953 lays down certain requirements which must be complied with in the execution of a will. The amendment to the Act came into effect on 1 October 1992 and applies to all wills in respect of which the Testator has died after that date. The more stringent requirements will still apply where the Testator has died before 1 October 1992.

7.4 WILLS IN RESPECT OF WHICH THE TESTATOR HAS DIED BEFORE 1 OCTOBER 1992

For a will executed after 1 January 1954, in respect of which the Testator has died prior to 1 October 1992, the more stringent requirements laid down by the will act will apply.

1. How must a will be signed?

The will must:

a. Be signed by the Testator and two competent witnesses on every page;

b. Although it is not a formal requirement, be dated on the last page; and

c. Be signed on all the pages by the Testator and two Witnesses while they are all persons at the same time.

2. Who may witness a will?

a. For a will to be valid, the witnesses must be at least fourteen years of age and able to give evidence in court.

b. Beneficiaries under the will, or their spouses, must not sign as witnesses to the signing of a will and their spouses are not able to benefit under the will.

c. A person nominated as an executor/trustee, guardian or their spouses must not sign as a witness to the will as the will render the nomination null and void.

3. Codicils and Amendments

A codicil can be described as an appendix to a will. One is normally drawn up where minor changes are required to a will which do not warrant a complete redraft of the will. Because a codicil is also a testamentary document it must comply with the same requirements as a will for validity. Any deletion, addition, alteration, or interlineations made to a will or codicil must be carefully and clearly marked or written and authenticated by the full signatures of the Testator(s) and the witnesses in the margin opposite. It is not permitted simply to initial such changes or additions.

If a section of the will is deleted, the Testators and the witnesses must sign against the deletion and, if any substituted wording has been inserted. They must also authenticate the new insertion.

Only the original document needs to be signed. It is unnecessary to either sign or initial the copy of the will although it is usual to record the date on it. If both original and copy are signed, it may be difficult to ascertain which document accurately expresses the Testator's last wishes.

7.5 WILLS IN RESPECT OF WHICH THE TESTATOR HAS DIED AFTER 1 OCTOBER 1992

A will executed after 1 January 1954 and in respect of which the Testator died after 1

October 1992. The amendment to the wills act will be applicable and the requirements for a valid will are as follows:

1. ***How must a will be signed?***

a. The will must be signed at the end thereof by the Testator(s) and by two competent witnesses. If the will consists of more than one page, each page other than the page on which it ends must also be signed by the Testator(s). In this regard it is interesting to note that 'signature' is defined as including the making of initials.

b. The signing of the will by the Testator (all pages) and the Witnesses (last page) must take place while they are all present at the same time.

c. Although it is not a formal requirement, the will should be dated on the last page.

Note: It should be noted that in terms of the Wills Act, the court is empowered to accept wills that do not comply with the above requirements, provided that it is satisfied that the document before the court is intended to be the Testator's last will.

2. ***Who may witness a will?***

a. Two or more competent witnesses (defined as persons of 14 years of age or older are competent to give evidence in court) must be present when the Testator signs, and must sign the will together in his presence on the last day.

b. Any person who signs a will as witness and the spouse of such person will be disqualified from receiving any benefit under that will. If however, a court is satisfied that such person or his spouse did not unduly influence the Testator in the execution of his will, or where the will concerned was witnessed and signed by at least two other competent witnesses who will not receive any benefit under the will, or where the witness or his spouses would be entitled to inherit from the Testator in terms of intestate succession. If the Testator died intestate, the person or his spouse will be allowed to receive the benefit under the will. In the latter case, the value of the person that said person or his spouse would receive intestate.

c. It must be noted that the nomination of a person as Executor, Trustee or Guardian will be regarded as a benefit to be received by such person from that will. In other words, if a person who witnesses a will is nominated as Executor, Trustee or Guardian under that will, such person will be disqualified from taking up such appointment except in circumstances set out in (b) above.

3. Will Amendments and Codicils

All the formalities requires in the execution of a will apply for the execution of a codicil.

Any amendment to a will or a codicil must be carefully and clearly marked or written and authenticated by that signature of the Testator(s). The signature of the Testator must be made in the presence of two competent witnesses who must also sign next to the amendment. An amendment includes a deletion, alteration or interlineations. Note that it is no longer necessary for both the deletion and substitution of a section of the will to be authenticated separately by the signatures of the Testator and the Witnesses. The deletion and substitution need only be authenticated once with the requisite signatures.

Only the original document needs to be signed. However, if the original is in the possession of someone else, it is a good idea to date a copy so the Testator knows on what date the will was drafted.

4. Who Can Make a Will?

Any mentally capable person of 16 years of age or older may make a will.

5. Acceptance of Duplicate Wills

The Master may now also accept a duplicate of the original will without a court order (i.e. a signed photocopy) by reason of an amendment to Administration of Estates Act 66 of 1965.

6. Revocation of Wills

Revocation of a will does not have to be accompanied by the destruction of the will or the writing of a new will as in the past. The revocatary document does not have to comply with the requirements of a will, provided the wishes of the Testator is absolutely clear. A will cannot be annulled orally.

7. *Disqualifying an Ex-Spouse as Heir*

A will made by a Testator after 1992, and before the Testator dissolved his marriage by annulment or divorce, the will must be carried out as if the spouse had died prior to such marriage dissolution. If the Testator died within three months after such dissolution, unless it is clear from the will that the Testator did not intend such consequence. If on the other hand the Testator died at any time after the three month period without altering his will to remove the ex-spouse as a beneficiary, it is presumed that the Testator intended to benefit the ex-spouse. Three months is considered sufficient time for the Testator to effect alternative will arrangements, if he does not want his ex-spouse to inherit from his estate.

8. *Power of court to declare a will to be revoked*

If a court is satisfied that a Testator has:

* Made a written indication on his will
* Performed any other act with regard to his will or
* Drafted another document

by which he intended to revoke his will or part thereof, the court shall declare the will or the relevant part thereof to be revoked.

This provision also applies whether the Testator before his death caused such indication to be made, such acts to be performed or documents to be drafted.

7.6 PRACTICAL ASPECTS TO BE CONSIDERED WHEN DRAFTING A WILL

1. Simplicity

* Keep the will as simple as possible to ensure effective and capable implementation.
* Avoid ambiguities without detracting from the Testator's intentions.

2. Accurate Recording of Details

* Information such as full names, relationships and physical addresses must be correctly spelt. Bequeathed assets, especially immovable property must be clearly described.

3. Policy and Fund Benefits to be reviewed

* Many people believe the proceeds of pension, provident and retirement annuity fall into their estates on death. Instead the trustees of the pension funds act use their discretion to pay these funds directly to the member's dependants and nominated beneficiaries.

7.7 BEQUESTS AND LEGACIES

* These are specific assets given to named beneficiaries.

* Bequests may change drastically in value or no longer exist at death, giving rise to unintended consequences (i.e. without the asset the bequest falls away).
* Specific bequests should be used with caution and division of smaller assets may be left to the discretion of an impartial executor.

7.8 THE RESIDUE

* This is the balance of the estate after payment of all liabilities and bequests and is divided amongst heirs in the proportion stated in the will. If an heir is deceased his share devolves upon his issue.
* Minors and Testamentary Trusts

  Where the Testator has made bequests to minor beneficiaries it is advisable to make provision for a testamentary trust, failing which a guardian or tutor may have to provide security for the minor's property, or the funds may have to be paid into the Guardian Fund.

7.9 GUARDIANSHIP

Where there are minor children, it is advisable to consider the question of guardianship.

7.10 CHARITABLE BEQUESTS

A Testator may wish to donate certain amount to a charitable, educational or religious institution. A special clause to this effect should be inserted into the will.

7.11 EXCLUSION FROM COLLATION

Descendants who are heirs are obliged to keep a record of certain kinds of gifts received during the lifetime of the deceased and their benefit from the estate will be adjusted according to the amount received. Where a Testator wishes to avoid the effects of collation a specific clause should be inserted.

7.12 LIVING WILL

Living wills are wills which contain instructions taken in advance as to the desired medical treatments in the event of terminal illness where the Testator is not capable of making decisions or giving instructions on medical matters relevant to his condition at the time due to his/her physical or mental incapacity. The whole purpose of these instructions is to prevent artificial means of sustaining life where there is no imminent or reasonable change of recovery. Another method is to give power of attorney to a third party to give specific instructions to the relevant medical practitioners in the event of the occurrence of defined medical circumstances. The living will society of South Africa (established in Natal in 1974) has in the past made recommendations to the S A Law Commission on Euthanasia and related matters, and supporters relieving the terminally ill of mental or physical pain even if such relief may expedite the occurrence of death.

7.13 THE WILL AND ESTATE DUTY

The Estate Duty Act as a whole has to be considered when drafting wills. Special care should be taken with regard to the following (the sections refer to Estate Duty Act, 45 of 1955 (as amended)):

* Check for ownership of life assurance policies. (Section 3(2))
* Check for property excluded from community of property. (Section 3(2))
* Bequests to public benefit organizations. (Section 4(h))
* Accrual claims for and against the estate. (Sections 3(3)(CA) and 4(1A))
* Provide for bequests with a value up to R1,5 million "away" from surviving spouse to a trust (testamentary or living) where the spouse is one of the discretionary beneficiaries and possibly one of the trustees. This can cause an estate duty saving of up to R300 000 after the death of the surviving spouse. (Section 4(q))
* If limited interests such as usufructs, rights similar to usufructs, uses, habitation, fiduciary or annuities where used, keep in mind the rules pertaining to valuations in terms of Section 5(1) as well as the Commissioner's discretion in Section 5(2) to fix a yield of less than 12% if he regards it reasonable to do so. This can have a

substantial effect on the value of the Section 4(q) deduction where property or shares are bequeathed subject to the usufruct of a surviving spouse.

In terms of Section 5(4) a right to the use or occupation for no consideration or inadequate consideration, which continues after the death of the deceased, must be disregarded for the purposes of the valuation of property which is subject to such a right.

* Consider consecutive usufructs in larger dutiable estates. (Section 4(q), 3(2)(a) and 5(1)(b))

* New definition of "spouse" important to keep in mind.

It means in relation to any person, a person who is his or her partner:

1. In a marriage or customary union recognized in terms of the laws of the republic,
2. In a union recognized as a marriage in accordance with the tenets of any religion, or
3. In a same sex or heterosexual union

which the Commissioner is satisfied is intended to be permanent and "married", "husband" or wife shall be construed accordingly:

Provided that a marriage or union contemplated in (b) or (c) shall, in absence of proof to the contrary, be deemed to be a marriage or union without community of property (introduced by Act 5 of 2001 which came into operation on 20 June 2001).

* Allow executor to have discretionary powers to choose whether to realize assets or distribute them to heirs because this can bring the most favourable valuation basis into play. (Section 5(1)(a))
* Also këep in mind Maintenance of Surviving Spouses Act, 27 of 1990. Where the spouse claims she has been unfairly, prejudiced by being left out in the will.

7.14 INTESTATE SUCCESSION

The Intestate Succession Act provides the following rules in the case of an individual dying wholly or partly intestate:

* where the deceased is survived only by a spouse i.e. not by a descendant or descendants, the spouse inherits the entire estate.
* Where the deceased is survived only by descendants and not by a spouse, the descendants will inherit the intestate estate per stirpes.
* Where the deceased is survived by a spouse and children, the spouse gets the greater of a child's share or R125 000. A child's share is calculated by dividing the number of children of the deceased as well as predeceased children of the deceased plus one for the surviving spouse into the value of the intestate estate. This means whether marriage is in or out of community of property the survivor is still entitled to:

  i. His/her out of community estate.

  ii. In the case of in community his/her half share of the estate.

iii. His/her accrual claim in the case of marriages with accrual.

iv. As well as his/her intestate portion on the balance of the estate.

7.14.1 NO SPOUSE AND NO DESCENDANTS

If there are no spouse or no descendants at the deceased's death, half of the estate goes to each parent. If one of the parents is predeceased, such parent's share accrues to the descendants of such deceased parent by representation (i.e. per stirpes). If the predeceased parent has no descendants, everything goes to the surviving parent. Where both parents are predeceased, the deceased estate will be split in two and thereafter accrue by representation to the descendant of each of the predeceased parents.

7.14.2 NO SPOUSE, NO DESCENDANTS AND NO PARENTS OR PARENTS' DESCENDANTS

In this case the entire estate devolves upon the closest blood relatives of the deceased in equal shares.

7.14.3 NO SPOUSE OR BLOOD RELATION

The assets may be claimed by the state as *bona vacantia* (i.e. unclaimed property) after a period of 50 years.

7.14.4 ILLEGITIMATE CHILDREN

Under the new act an illegitimate child may inherit on the basis of intestate succession both from the father and the mother, as well as from their blood relatives.

7.14.5 ADOPTED CHILDREN

Under the new law an adopted child may only inherit by intestate succession from his adoptive parents, not from his natural parents (unless the natural parent is married to the adoptive parent). The adoptive parents are deemed to be his natural parents, to the exclusion of the real parents. An adopted child may inherit by intestate succession from his adoptive parents and their blood relatives but not from the real parents or their blood relatives.

7.15 MASSING

Massing is a method of disposition that occurs

* when there is joint testamentary disposition
* by two or more persons
* in one will
* of their joint estates or part thereof
* subject to a life interest

* such as usufructary or fiduciary interest, or an annuity
* in favour of survivor or survivors.

It is irrelevant whether persons effecting massing are married or not. Whether the marriage is in or out of community of property also does not affect massing.

Advantages of Massing

* The ultimate heirs inheritance is protected.
* Massing provides an income for the survivor or survivors after the death of the first dying.

7.15.1 THE SURVIVOR'S CHOICE

Upon the death of the first dying, the survivor still has the choice to adiate (to accept the benefits conferred by the massing) or to repudiate (not to accept the benefits conferred by massing) such benefits.

If the survivor accepts the benefits under the joint will, he or she is bound by the terms of the will and cannot by way of a subsequent testamentary or intervivos disposition dispose of any part of the massed estate.

The survivor's choice will be final because in terms of Section 37 of the Administration of Estates Act 66 of 1965, the heirs acquire a real right in the survivor's share of such property as opposed to a personal right.

7.15.2 THE REAL RIGHT OF THE HEIRS

The heirs will acquire a real right to both portions of the massed estate, to the exclusion of creditors of the survivor whose debts were incurred subsequent to the death of the first dying.

Section 37 of the Administration of Estates Act states:

> *"If any two or more persons have by their mutual will massed the whole or any specific portion of their joint estate and disposed of the massed estate or any portion thereof after the death of the survivor or survivors or the happening of any other event after the death of the first dying; conferring upon the survivor or survivors any limited interest in respect of any property in the massed estate, then upon the death after the commencement of this act of the first dying, adiation by the survivor or survivors shall have the effect of conferring upon the persons in whose favour such disposition was made, such rights in respect of any property forming part of the share of the survivor or survivors of the massed estate as they would by law have possessed under the will if that property had belonged to the first dying, and the executor shall frame his distribution account accordingly."*

If the survivor repudiates the joint will, all assets that belong to the survivor will remain the survivor's, even though such assets formed part of the intended massing. However, the repudiator will have no claim to the first dying's share. Therefore, in this case the joint will remains operative only in so far as it constitutes the will of the first dying.

An example of a massing clause is:

> *"We hereby mass and consolidate our joint community estate and bequeath the whole of our massed joint estate to our children, subject to the usufruct of the survivor of us until his or her death."*

7.16 EXAMPLE OF MOST STANDARD WILLS AND TESTAMENTS IN OPERATION

<u>Example of a couple married out of or in community of property</u>

(We will have to specify which one applies, at the start of the will)

LAST WILL AND TESTATMENT

We, The Undersigned

JACK BRADY

And

JENNIFER BRADY (BORN BROWN)

Spouses married in/out of community of property and presently of Umhlanga, Natal do hereby revoke all wills, codicils and other testamentary acts heretofore made by us, whether jointly or severally, and declare the following to be our Last Will and Testament.

A.

We nominate the survivor of us to be the sole heir or heiress of the estate of the first dying of us.

B.

Should the survivor of us die without leaving a further valid will, such survivor bequeaths his or her estate to our children or their lawful issue by representation. Should any of our beneficiaries not yet have attained the age of 21 (twenty one) years, his or her inheritance shall be held in trust by our administrator to whom we grant and upon whom we impose the following powers and duties respectively:

1. To accept the assets, to control, to administer, to let, to alienate or to sell such assets or to lease or purchase any movable property or to conduct or continue any

business whenever they in their sole discretion deem it to be in the best interest of the trust.

2. To invest any cash in such manner as they in their sole discretion may deem fit without being fettered by any of the considerations which otherwise would cause them to restrict the investments to recognized trustee securities. The administrator is also empowered to call up any investments and to reinvest the proceeds in accordance with the foregoing provisions.

3. To borrow any sum of money in order to carry out any condition of this trust and to furnish any form of security for the proper repayment thereof including the power to pledge or mortgage any assets of the trust.

4. To apply so much of the income, and, in need, of the capital as they in their sole discretion may deem fit for the maintenance and education of the beneficiary or for any other purpose in his or her interest. Any income not utilized for these purposes may be capitalized.

5. To terminate the trust when the beneficiary attains the age of 21 (twenty one) years and to make over or pay the capital, as it then exists, any accrued income to him or her.

C.

Should we die in circumstances where it cannot be established who was the first dying of us, we direct that the aforementioned Section B will apply to our respective estates.

D.

It is a specific condition of this will that any benefit which may accrue to any beneficiary in terms thereof as well as any income derived therefrom, shall be excluded from the legal consequences of any existing or future marriage of such beneficiary whether contracted in community of property or out of community of property. In the case of a female beneficiary such benefit shall also be excluded from the control, power of alienation and marital power of her husband. Furthermore, the receipt of a female beneficiary given without the assistance of her husband shall be adequate discharge to our Executors.

E.

The first dying of us hereby appoints the survivor of us to be the Executor/Executrix, and Administrator/Administratrix of the estate of the first dying of us, or in the event of our joint or simultaneous death then such person or persons as may be nominated by our aforesaid children.

We hereby direct the Master of the Supreme Court to exempt our aforesaid Executor/ Executrix, Administrator/Administratrix or appointee of our children from furnishing security for the due administration of our said estate or estates.

SIGNED AT UMHLANGA THIS 10TH DAY OF OCTOBER 1994, IN THE PRESENCE OF THE UNDERSIGNED WITNESSES, ALL BEING PRESENT AT THE SAME TIME.

As Witnesses:

1.	**..................................**	**..................................** **TESTATOR**
2.	**..................................**	**..................................** **TESTATRIX**

7.17 NOTES TO BE OBSERVED WHEN FINALISING A WILL

1. You require two original, typed copies of your Last Will and Testament. Previously a photocopy of a Will could not be accepted legally. However, in terms of the latest Law of Succession Act No. 43 published on 1 October 1992, a duplicate of the original, signed correctly by all parties concerned, including witnesses, will be accepted by the Master.
2. All copies need to be signed by both spouses in the presence of two witnesses.
3. Any person or persons either directly or indirectly involved in your will or estate may not sign as witnesses, for example, heirs or beneficiaries. If they do they will be disqualified as beneficiaries. Rather select friends or acquaintances over the age of 21 (twenty one).

4. For record purposes, send photocopies to your children, heirs and beneficiaries and advise them where you keep the original.

5. Wills should always be revised as and when a person's circumstances change.

CHAPTER 8

CAPITAL GAINS TAX

8.1 INTRODUCTION

Capital Gains Tax (CGT) was implemented on 1st of October 2001, and will also be payable by a deceased estate. The introduction of CGT has made it even more important now to plan properly for what happens when you die, because now you pay both estate duty and CGT on your assets.

You have to make sure that you have the resources to pay both CGT and estate duty. Therefore it might be necessary to increase life assurance against dying.

Your estate was subject to estate duty at a rate of 25 per cent on any amount over R1 million, except for anything that was left to the spouse.

The abatement has been increased from R1 million to R1,5 million and estate duty has been reduced from 25 per cent to 20 per cent because death has become a CGT event.

8.2 ISSUES TO BE TAKEN INTO ACCOUNT WHEN PLANNING YOUR ESTATE

8.2.1 DIFFERENCE BETWEEN CGT AND ESTATE DUTY

CGT is a tax on your gross assets, while estate duty is a tax on your net assets (your assets less your liabilities).

8.2.2 EXCLUSIONS

The only exclusions from CGT at death are:

* The assets in your estate that are bequeathed to your spouse or partner are excluded on the so-called roll over basis. The assets are transferred to your spouse at their original base cost or value when the spouse or partner dies or disposes of the assets, the capital gain will be calculated from the original base cost or value.
* Bequest to charitable, religious, or educational institutions.
* Any capital gain on a life assurance policy that would not have been subject to CGT in your hands if it had matured when you were alive.
* Pension, provident and retirement annuity fund benefits.

8.2.3 EXEMPTIONS

* After your death, your assets are treated in the same way as they would have been if you disposed of them when you were alive. The R1 million exemption on your primary residence still applies. But the R10 000 annual exemption is replaced by a R50 000 exemption in the year of death. Any gain over R50 000 will be subject to CGT.
* Capital gain or loss calculations of disposal your assets will be considered to be disposed of to your estate at their market value at the time of your death. This means the capital gain or loss will be calculated by subtracting the base cost or value from the market value.

8.2.4 THE RATE AT DISPOSAL

The rate of CGT on death is the same as you would have paid while you were alive. So, after exemptions and exclusions, you will pay CGT on 25 per cent of the gain at your marginal rate in the year of your death. The top effective rate is 10 per cent.

Example

Mr X dies with the following assets which are subject to CGT. His marginal income tax rate in the year of death is 40 per cent.

	R	R
Shares		
Market value	650 000	
Base cost	- 100 000	
Capital gain		550 000
Unit Trusts		
Market value	250 000	
Base cost	- 150 000	
Capital gain		100 000
TOTAL CAPITAL GAINS		650 000
LESS: CAPITAL LOSSES		
INDUSTRIAL PROPERTY		
Base cost	1 100 000	
Market value	- 900 000	
CAPITAL LOSS	200 000	
LESS: TOTAL CAPITAL LOSS		200 000
		450 000
LESS: EXEMPTION		50 000
NET CAPITAL GAIN		400 000
25 per cent of gain		R100 000
Marginal rate		40%
CGT payable		R 40 000

8.2.5 THE CAPITAL GAIN OR LOSS IN YOUR ESTATE

Once your assets have been taken over by the executor of your estate, any capital gain or loss made on them while they are held in the estate is subject to CGT. The estate is treated in the same way as an ordinary individual.

So, 25 per cent of the capital gain is subject to CGT at the marginal rate of the estate.

If the executor disposes of an asset to an heir, this is done at market value (the value at which your estate received the asset) so no gain or loss is made in the estate.

The market value becomes the new base cost of the asset for your heir. This means executors must be careful about assets they choose to sell rather than dispose of to a beneficiary.

8.3 WHEN TAX IS PAYABLE BY AN HEIR OF A DECEASED ESTATE

A special concession applies when the CGT relating to the taxable capital gains of a deceased person exceeds 50% of the net value of the estate for estate duty purposes before the CGT itself is taken into account as a debt due by the estate.

If the executor of the estate is required to dispose of any asset for the purpose of paying the CGT, the heir who would have been entitled to the asset if there had been no liability for CGT, may choose to have the asset distributed to him, subject to a certain condition. The condition is that he undertakes to pay the amount of CGT that exceeds 50% of the net value of the estate within three years after the date on which the executor obtained permission to distribute the assets of the estate. This is to prevent the unnecessary forced sale of assets or perhaps insolvency of the estate. The amount of CGT payable by the heir will be regarded as a debt due to the state and will be treated as an amount of tax chargeable under the Income Tax Act.

8.4 DISPOSAL OF SMALL BUSINESS ASSETS

If the interest of a person in a business is deemed to be disposed of, as a result of death, and such a business qualifies as a "small business", then a gain of up to R500 000 can be excluded for CGT purposes. A "small business" means a business where the market value of all its assets does not exceed R5 million. To ascertain whether a business qualifies, the market value of all the assets, regardless of their nature and of the liabilities of the business, must be used. A "small business" can be a sole proprietorship, partnership, company or close corporation (where the deceased owned at least 10% of the equity in the company or close corporation).

For a deceased estate to qualify for relief, the following three provisos have to be met:

1. He/she had owned the business interest for a continuous period of at least 5 years prior to death, and
2. He/she must have been substantially involved in the operations of the business during that period, and
3. The disposal (change of ownership) is as a result of death.

All assets must be disposed of within 24 months from the date of the first disposal. The rule can apply to more than one business but not if the combined assets of the businesses exceed R5 million. Only active business assets qualify. Financial instruments held mainly to derive annuity income are excluded. These assets are, however taken into account in determining the value of the business. The R500 000 is per natural person and not per business.

8.5 EXAMPLE

Y, a bachelor died at the age of 41. He owned 50% of the membership interest in a close corporation and Z owned the other 50%. In terms of a buy and sell agreement, Z purchased the deceased's membership interest for R1 800 000.

Y and Z were actively involved in the close corporation for 6 years. At Y's death the close corporation had a total asset value of R3 750 000. Y originally purchased the membership interest in the close corporation for R200 000. For the purpose of the following calculation it is assumed that the original purchase occurred after the 1st of October 2001 and that it was the only asset in X's deceased estate. The maximum marginal rate of tax, 40% is used.

	R
CGT	
PROCEEDS	1 800 000
Less: Base cost	(200 000)
CAPITAL GAIN	1 600 000
Less: Small business exclusion	(500 000)
	1 100 000
Less: Annual exclusion upon death	(50 000)
	1 050 000
Taxable Gain (25%)	R262 500
Tax at 40%	R105 000
ESTATE DUTY	
GROSS ESTATE	1 800 000
Less: CGT liability	(105 000)
Other expenses	(90 000)
NET ESTATE	1 605 000
Less: Abatement	1 500 000
DUTIABLE ESTATE	105 000
ESTATE DUTY (20%)	21 000
TOTAL TAX	
CGT	R105 000
Estate Duty	R 21 000
	R126 000

8.6 BEQUESTS TO A SPOUSE

Disposal of assets to a spouse will not attract CGT in the estate of the deceased. CGT , like estate duty, will be payable at death of the surviving spouse or when the assets are disposed of, the original base cost will be used for the calculation of CGT.

8.7 EXAMPLE

Minal bequeaths his entire estate to his spouse, Meera. Minal and Meera were married out of community of property, without accrual. Minal's estate consists of the following:

	Value at Death	**Base Cost**
	R	**R**
Primary Residence (CGT exempt)	600 000	500 000
Holiday Home	700 000	500 000
Share Portfolio	500 000	400 000
Personal Effects (CGT exempt)	200 000	100 000
	2 000 000	1 500 000
	=======	=======

At Minal's death, his estate will not be liable for estate duty or CGT, since his entire estate was left to Meera.

Five years after Minal's death, Meera sells the share portfolio for R1 000 000.

Solution

The calculation of the CGT liability for the transaction will be as follows:

	R
PROCEEDS	1 000 000
Less: Original base cost	400 000
CAPITAL GAIN	600 000
Less: Annual exclusion	(10 000)
	590 000
Taxable Gain (25%)	R147 500
Tax at 40% (assumed marginal ax rate for Meera)	R 59 000

Ten years after Minal, Meera dies and her estate comprises the following assets:

	R
Primary Residence	900 000
Holiday Home	1 000 000
Cash	250 000
Personal Effects	300 000
Unit Trust (purchased after 1 October 2001 for R200 000)	300 000
	2 750 000

CGT at Meera's death:

	R	**R**
Holiday home (R1 000 000 – R500 000)		500 000
Unit trust (R300 000 – R200 000)		100 000
TOTAL GAIN		600 000
Less: Annual exemption upon death		(50 000)
Aggregate Capital Gain		550 000
Taxable Gain (25%)		137 500
Tax at 40% (assumed marginal rate at Meera's death)		R55 000

Estate Duty at Meera's death

GROSS ESTATE		2 750 000
Less: CGT	(55 000)	
Executor's fees (3,99% x R2 650 000)	(105 735)	
Assumed other expenses	(20 000)	(180 735)
NET ESTATE		R 2 569 265
Less: Abatement		1 500 000
DUTIABLE ESTATE		R1 069 265
		========
Estate Duty (20%)		R 213 853

TOTAL TAX AT MEERA'S DEATH

CGT	R 55 000
Estate Duty	R213 853
	R268 853

Although no CGT or estate duty was payable at Minal's death, these expenses were delayed until Meera's death. With proper planning these expenses could have been reduced if Minal's will was changed to bequeath some of his assets to their children, thereby effectively reducing the estate duty and CGT liability in Meera's estate. In order to limit possible taxes upon the death of the survivor, the wills of both spouses should be analysed when an estate plan is done for a client.

Although CGT is now an additional expense to be paid by death, estate planners can limit the total tax payable with proper planning. People should review their estate plans, especially the liquidity position of their estates, with a long term view while the proceeds of life assurance policies, subject to certain limited exemptions, are treated as dutiable assets for estate duty purposes, these proceeds will not attract CGT. As such, life assurance remains an affordable, tax efficient solution to provide the necessary cash liquidity in a deceased estate.

8.8 INSOLVENT ESTATES OF PERSONS

The estate of a person prior to sequestration and such person's insolvent estate is considered to be one and the same person, in terms of the Income Tax Act. An asset disposed of by an insolvent estate will be treated as if a natural person had disposed of that asset. This means that the insolvency estate will be excluded from paying CGT on personal use assets, and will qualify for primary residence exclusion. Only 25% of the capital gain will be taxable and the R10 000 annual exclusion will apply. An assessed capital loss may be carried forward to the insolvent estate but any assessed capital loss remaining in the insolvent estate, will effectively be forfeited.

8.9 CAPITAL GAINS TAX: BEQUEATHING OF A LOAN ACCOUNT

An estate planner has a loan account in his estate when he transfers property to family trusts. This loan account will have to be dealt with in the estate planner's will. Consideration needs to be given to the possible capital gains tax implications of the bequest of such a loan account.

There are two different interpretations as to capital gains tax implications where an outstanding loan account is bequeathed to the indebted trust. Firstly, paragraph 12(5) of the 8th schedule stipulated that the writing off of a loan account will form a taxable gain with a base cost of zero rand. But paragraph 40 stipulates that a deceased person must be deemed to have disposed of all his/her assets to the deceased estate for proceeds equal to the market value of the assets. Where an asset is then transferred to an heir, the deceased is deemed to have disposed of that asset at base cost. The following scenarios discuss the implications of these two interpretations, as well as other ways of bequeathing a loan account and the capital gains tax implications thereof.

Scenario 1 ***Interpretation A***

The bequest of two million rand loan account to the trust that owes the testator money, there will be capital gains tax payable, based on the interpretation that para. 12(5) will apply. The calculations are as follows:

The debtor will be liable to pay the capital gains tax.

	R
Loan account	2 000 000
Less: Base cost	(zero)
	x 50%
	R1 000 000
Tax rate of trust	x 40%
Capital Gains Tax	R 400 000

Scenario 1 *Interpretation B*

The bequest of two million rand loan account to the trust that owes the testator money, there will be no capital gains tax payable, based on the interpretation that para. 40 (and not para. 38) will apply.

	R
Loan account	2 000 000
Deemed disposal from deceased person to his/her estate	
at market value	2 000 000
Transfer to heir at base cost	2 000 000
Capital gain	R0

Scenario 2

The bequest of a two million rand loan account to a spouse. There will be no capital gains tax payable due to the roll over relief on bequests to a spouse.

Scenario 3

The bequest of a loan account to any person, legal person or trust, excluding an entity or person who is the debtor on the loan account. There will be no capital gains tax payable because the debt was not written off. These stipulations are, however, subject to the requirements of S 103 of the Income Tax Act.

Proper planning should be done in the future where loan accounts are involved and bequeathed.

8.10 USUFRUCT, CAPITAL GAINS TAX AND PRIMARY RESIDENCE

To qualify for the exemption of R1 million on capital gain in connection with a primary residence, the taxpayer must have an interest in the property in terms of Section 44 of the eight schedule of the Income Tax Act. This section defines *"interest.... (as)(a) A right to use or occupation"*. A usufruct clearly is a right to use. The usufruct can on the other hand not be described as a *"right or interest..... in a trust in terms of this section. The right to the usufruct has nothing to do with a trust, apart from being registered over property that belongs to a trust."*

It is possible to sell the bare dominium of a residence to a trust and still enjoy the benefit of the exemption of R1 million available in terms of Section 45 of the eight schedule of the Income Tax Act, provided the person who is entitled to the usufruct lives in the residence.

An example will explain this.

Mr B. Cassi wants to buy a private residence for R1 million in 2002 in a new exciting development. He foresees that he will be able to sell the property for R4 million after five years. In 2002 Mr B. Cassi will be 40 years of age on his next birthday. Mr B. Cassi can either buy the property in his own name of he can allow his trust to buy the bare dominium portion of the property while he himself buys the usufruct right over the property. In the last case and after the property was bought, the trust and the owner of the usufruct will have to sell and wave their rights simultaneously when they sell the property.

Capital Gains Tax Calculation in 2007

	In own name	Usufruct & Bare Dominium: Usufruct	Usufruct & Bare Dominium: Bare Dominium
	R	R	R
SELLING PRICE (2007)			
Property	4 000 000		
Usufruct (B. Cassi will be 45 next birthday in 2007) (R4 000 000 x 12% x 7,863 80)		3 774 624	
Value of bare dominium (R4 000 000 x R3 774 624)			225 376
Less: Base Cost (2002)			
In own name	- 1 000 000		
Usufruct (B. Cassi was 40 next birthday in 2002)		- 964 836	
Bare dominium (R1 000 000 – R964 836)			- 35 164
	3 000 000	**2 809 788**	**190 212**
Less: Exempt – Section 45	1 000 000	1 000 000	
TAXABLE AMOUNT	**2 000 000**	**1 809 788**	**190 212**
Taxed as Income (25%)	500 000	452 447	47 553
Income Tax (40%)	200 000	180 979	19 021

From the example it is clear that it is possible to qualify for the exemption of R1 million on capital gain in connection with primary residence, even though the bare dominium of the residence belongs to a trust. The total capital gains tax is the same for both scenarios.

A person will be able to benefit a little more from the R1 million exemption if the residence is registered fully in his own name and the total capital gain is less than R1 million when comparing it with the usufruct trust combination. The reason is that all the capital gain is exempt (if capital gain is below R1 million) in the case of a fully owned residence, whereas in the usufruct trust combination a portion of the capital gain is allocated to the trust and no exemption is available to the trust.

Compared with individual, the introduction of capital gains tax did not increase the tax that is payable by a trust used in combination with a usufruct, except if the capital gain is below R1 million on a private residence. Even then the extra capital gains tax is not much more. On the other hand, the saving in capital gains tax when a person dies, is really substantial if a trust is being used.

The conclusion can thus only be that the introduction of capital gains tax makes the use of trusts even more attractive than before, especially if one combines it with a usufruct. Circumstances must justify the application of a trust and a usufruct.

CHAPTER 9

CASE STUDY

SECTION A INFORMATION GATHERED FROM CLIENTS

9.1 BACKGROUND INFORMATION

Mr James and Mrs Jenny Brown are married out of community of property and with the accrual system excluded. They got married on 14 April 1976. They have two children. Their son, Darryl is 23 and daughter, Pinky is 19.

Date of Birth

Mr James Brown	20 October 1952
Mrs Jenny Brown	4 November 1957

Mr James is a designer and is employed by Spectra (Pty) Ltd, a company that designs specific garments to suit your style. Mr James and his best friend, John, started the business 10 years ago. Since then two more shareholders joined the company. Each shareholder now has 25% of the total shareholding. The total shareholding is R7 million. The value of Mr Brown's shareholding in the company is therefore R1,75 million.

9.2 INFORMATION ON MRS BROWN

Mrs Brown is a lawyer who has her own practice.

Mrs Brown has provided information regarding her assets to assist you in the planning of her husband's estate.

9.3 INFORMATION ON SPECTRA (PTY) LTD

Mr Brown's shareholding is currently 1,75 million rand. The other three shareholders indicated at a meeting that they would like to enter into a buy and sell agreement. Mr Brown does not want to enter into this agreement as he wishes to bequeath his share to Darryl Brown, his son. He would like to see his son take over his position in the company when he retires.

9.4 INFORMATION REGARDING MR BROWN'S PENSION AND RETIREMENT PROVISION

Mr Brown is a member of Spectra (Pty) Ltd Pension Fund. Retirement age in terms of the rules of the fund is age 60.

The fund is a defined contribution scheme and it is estimated that the amount available to him in the fund at retirement date will be R3 600 000 (R3,6 million). Should Mr Brown die today the death claim amount in terms of the pension fund will be R1 800 000.

9.5 INCOME FROM EMPLOYMENT

Mr Brown receives the following income and benefits from his employer:

Salary	R480 000 per annum
Travelling allowance	An allowance of R48 000 per annum of which R20 000 is taxable being the portion not used for business purposes.
Pension contributions	Mr Brown contributes 7% of his salary (7% of R480 000) to the pension fund and his employer contributes a further 7%.

Neither Mr Brown nor his wife, Mrs Brown is currently a member of a medical aid scheme.

9.6 INFORMATION REGARDING HIS ASSETS

His assets consist of the following:

	R
Family Home	750 000
Holiday Cottage	300 000
Shareholding Spectra (Pty) Ltd	1 750 000
Private Motor Vehicle	120 000
Furniture and Personal Effects	60 000
Listed Shares (JSE)	130 000
Unit Trust Fund	120 000
Life Assurance	
i. on his own life payable to his estate	1 200 000
ii. on his wife's life – surrender value	45 000

There are no disability or trauma benefits attached to any of his policies.

Mr Brown will inherit R1 000 000 from the assets of his late father within a month.

9.7 MR BROWN'S LIABILITIES

His liabilities are as follows:

		R
*	Bond on House	250 000
*	Bank Overdraft	50 000
*	Outstanding Balance on Car Loan	32 000

9.8 HIS WILL (TESTAMENTARY DISPOSITION)

Mr Brown would like to leave his shares in Spectra (Pty) Ltd, to his son, Darryl, and would like to leave a cash legacy of equal value to his daughter. The legacy to his daughter should be equal to the current value of these shares. Mr Brown will review his will from time to time and adjust the amount of the legacy to his daughter. The residue of his estate he wants to leave to his spouse.

9.9 MRS BROWN'S ASSETS

Mrs Brown owns the following assets:

		R
*	Cash Investments and Savings	120 000
*	Motor Vehicle	100 000
*	Personal Effects and Jewellery	50 000
*	Life Assurance payable to her estate	250 000

9.10 MONTHLY CASH FLOW POSITION

Their income expenditure and liabilities are as follows:

INCOME	R
Cash Salary per month	40 000
Travelling Allowance (car)	4 000
Interest on Unit Trusts (1% of R120 000 ÷ 12)	100
Dividends on Unit Trusts (2% x R120 000 ÷ 12)	200
Interest earned on Dividends ((R100 000 at 9%) ÷ 12)	-
Dividends (3% x R130 000)	350
	44 650

Their monthly expenditure and other payments are as follows:

MONTHLY EXPENDITURE AND LIABILITIES	R
Pension Fund Contributions	2 800
Retirement Annuity Contribution	146
Municipal Taxes	500
Water and Electricity	450
Telephone Bills	600
Clothing	1 600
Short Term Insurance	1 600
Fuel and Other Car Expenses	1 000
Recreation for Family	2 000
Life Insurance	1 000
Care Instalment	3 600
Interest on Overdraft	650
Household Expenses	3 500
Bond Repayable	4 900
School and University Fees	2 500
Income Tax (as calculated R158 320 ÷ 12)	13 193
	R40 039

9.11 HIS POSITION AT RETIREMENT

He wants to retire in 10 years time in 2012 when he turns 60.

Income Tax

He is paying too much tax and wants advice.

His Will

He is not sure if his wife will have sufficient income on his death because he has decided to bequeath his shares in Spectra (Pty) Ltd to his son and an equivalent amount to his daughter.

Estate Duty and Capital Gains Tax

Mr Brown is concerned about these two taxes and the effect this will have on his estate.

Medical Treatment

He is also worried about the cost of medical treatment should he be hospitalized.

Investments

Mr Brown is conservative. He does not want to invest in a high-risk investment but he prefers medium-risk investments.

SECTION B CALCULATION DONE IN ANALYSING AND EVALUATING MR BROWN'S FINANCIAL STATUS

Tax Calculation – Mr Brown	R	R
Salary		480 000
Travelling Allowance		20 000
Interest – Unit Trusts		1 200
Dividends – Shares JSE		3 900
Gross Income		505 100
Less: Exemptions		
Dividends (3 900 + 2 400)	6 300	
Interest	1 200	7 500
		497 600
Less: Deductions		
Pension Fund Contributions	33 600	
R.A. Contribution	1 750	35 350
		462 250
		======
Tax on R462 250 (2003 rate) (73 800 + 88 900)		162 700
Less: Rebate		4 860
Tax Payable		R157 840

Capital Gains Tax Liability on Death

Asset	Market value on 1.10.2001	Market value at date of death	Gain	Exempt	
House (Family Home)	740 000	750 000	10 000	10 000	Nil
Holiday Cottage	285 000	300 000	15 000	Nil	15 000
Shares in Spectra (Pty) Ltd	1 750 000	1 750 000	Nil	Nil	Nil
Unit Trust Fund	108 000	120 000	120 000	Nil	12 000
Listed Shares	127 000	130 000	3 000	Nil	3 000
					30 000

The R30 000 capital gain on his death will, however not attract capital gains tax due to the exclusion of R50 000 on death.

Estate Duty Calculation – Mr Brown

	R
Inheritance from Late Father	1 000 000
House	750 000
Holiday Cottage	300 000
Shares in Spectra (Pty) Ltd	1 750 000
Motor Vehicle	120 000
Furniture and Personal Effects	60 000
Listed Shares (J.S.E.)	130 000
Unit Trust Funds	120 000
Life Assurance – On his wife's life (surrender value)	45 000
- On own life, payable to estate	1 200 000
Pension Fund Lump Sum (R1 800 000 ÷ 3)	600 000
	6 075 000

	R	R
Balance brought forward		6 075 000
Less: Deductions		
Funeral Expenses (Assumed)	15 000	
Liabilities Bond	250 000	
Overdraft	50 000	
Balance Car Loan	32 000	
Capital Gains Tax	Nil	
Executor's Fee (3,5% x R6 075 000) x 1,14	212 625	
Masters Fee	600	
Section 4(q) – Bequest (Residue) to Spouse	2 015 375	
- Pension Fund Lump Sum	600 000	3 175 600
Net Estate		2 899 400
Less: Section 4A Abatement		1 500 000
Taxable Estate		1 399 400
		=======
Tax Payable (20% x R1 399 400)		279 880

Calculation of Amount Inherited by Mrs Brown

	R
Total Value of Estate	6 075 000
Less: Legacies - Spectra (Pty) Shares	(1 750 000)
- Cash (to daughter)	(1 750 000)
	2 575 000
Less: Liabilities and Estate Admin Expenses	559 625
Residue before Estate Duty is paid	2 015 375
Less: Estate Duty	279 880
Value of Residue Inhered by Wife	1 735 495

Cash Position of Estate on Death

	R
ASSETS THAT WILL BE CONVERTED TO CASH	
Cash Inherited from Father	1 000 000
Listed Shares	130 000
Unit Trust Funds	120 000
Life Assurance on Own Life	1 200 000
	2 450 000
	=======
CASH PAYMENTS TO BE MADE ON DEATH	
Legacy	1 750 000
Estate Duty	279 880
Liabilities and Administration Expenses	559 625
	2 589 505
	=======

His estate will thus have a cash shortfall of R139 505 (R2 450 000 – R2 589 5050)

His Wife's Inheritance will consist of:

House	750 000
Holiday Cottage	300 000
Motor Vehicle	120 000
Furniture and Personal Effects	60 000
Surrender Value Policy	45 000
	1 275 000
	=======

Mrs Brown will, only inherit the above assets (unrealized) if she pays the cash shortfall of R139 505,00 that will exist in Mr Brown's Estate.

(R1 275 000 – R139 505) = R1 135 495.

CHAPTER 10

CONCLUSION

10.1 THE IMPORTANCE OF ESTATE PLANNING

1. It is the process through which the juridicial, financial, economical, social, psychological and other needs of a person (the estate owner) with regard to his estate and in relation to himself, his family and beneficiaries during his lifetime and in contemplation of death is determined and planned, which involves deciding in advance by the estate owner of what to do with his assets and liabilities (determining the intervivos and *mortis causa* needs referred to above and setting the goals). How to do it (namely, which estate planning tools are to be used) when to do it (for example upon marriage when selecting a matrimonial property system) and who to do it (namely which member/s of the estate planning team is to render assistance.)

2. It is an ongoing process. It starts at the birth of the estate owner and end on his death. The distinction between "estate owner" and "estate planner" is that the latter refers to the service of estate planning to an estate owner.

3. The estate planner must have more than an average creative mind. He must be

someone who is knowledgeable in all aspects relating to the estate owner. It is important for experts such as an attorney, accountant, broker, bank, trust official, investment adviser to form an estate planning team.

4. Estate planning is often described as a multidisciplinary science. It is important to master the skills and techniques in order to practice estate planning as a profession.

5. The estate planner must be up-to-date with all changes in law, he must have a thorough knowledge of tax laws, law of succession, family law, corporate law, trust law, short and long term insurance and various forms of investments. It is also important for the planner to have sufficient information regarding the estate owner's culture, religion, personal particulars, fears, wishes and financial position.

6. The process of estate planning commences by determining the factual personal environment of the estate owner, his family and estate, his psychological and social environment. The social environment includes the cultural, political and religious environments as also the legal environment and economical/financial environment. Once these environments have been properly determined, special objectives can be set to which the estate planning should comply.

7. Sometimes people only start thinking of estate planning when they realize that they are sick and need to be hospitalised or when they are going on a long trip or when a recent death in the family or a recent experience for example hijacking or armed robbery. All these circumstances can affect an estate owner's mind and this is when he realizes the importance of estate planning.

8. The estate owner may have fears or is concerned about the following, namely he realizes the importance of putting his affairs in order. He realizes that death can come at any time. His dependants are his main concern. Should the estate owner die will his dependants be well provided for. The estate owner realizes lots of family feuds can be solved by proper planning. He also realizes that his possessions will have to be distributed amongst heirs favourably to avoid conflict on his/her untimely death. Any projects that he may have started will have to be completed after his death and he hopes that others will be able to do so. He is also aware of the various taxes, such as income tax, estate duty, capital gains tax as well as possible future taxes. The estate owner is also concerned that his estate may fall into hands of people who should not have anything to do with his estate.

9. The views and remarks of politicians, the budget speeches all form part of the political environment which may have a bearing on the objectives set by the estate owner. The political environment together with economic/financial environments in most cases also determine the framework for international and

offshore estate planning.

10. The estate owner's family and personal surroundings and the cultural environment in which the estate owner finds himself may have an important bearing on the estate plan. In estate planning, the planner will also plan his estate according to cultural custom and religion as to what he may or may not do with his assets.

11. All relevant legislative enactments and provisions of the common law may have an effect on the estate of the specific estate owner. These may include common law principles of things, persons, family, succession and trusts as well as the relevant provisions of the Estate Duty Act, 45 of 1955, the Income Tax Act, 58 of 1962, the Companies Act 61 of 1973, the Close Corporations Act, 69 of 1984, the Matrimonial Property Act, 88 of 1984, the Wills Act, 7 of 1953, the Intestate Successions Act, 81 of 1987, the Trust Property Control Act, 57 of 1988, the Transfer Duty Act, 40 of 1949, the Value Added Tax (VAT) Act, 89 of 1991, the Administration of Estates Act, 66 of 1956 to mention only the more important statutes.

12. The economic climate always has an important bearing on estate planning. Stock markets crashing may have a bad effect on asset values but it also creates opportunities for removing those assets from the estate owner's estate and pegging the growth at the low recession values. Drought or other factors can

cause property values to either increase or decrease. All these factors need to be considered during this stage of estate planning.

13. The economic and financial environment also includes the analysis of the financial position of the estate owner and his family.

14. The estate owner arrives at a set of objectives which may include one or more of the following, the providing of income to heirs and family, the protection of himself against any unpleasantness or dissatisfaction in the family group, savings in capital gains tax and estate duty, facilitating continuity in farming or business operation.

15. The estate planning tools are important in the implementation of an estate plan for example, the selecting of a matrimonial property system, an antenuptial contract with or without a trust, certain donations, companies, close corporations, trusts, limited interests, the will, long term assurance, investments to mention only a few.

16. For any successful estate plan to be implemented, it must be cost effective. Often the cost is one of the reasons why an estate plan is not implemented.

17. Estate planning is an ongoing process which takes each day into account. Plan now and avoid unnecessary hardship and bitterness in the future.

CHAPTER 11

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