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June 2018

Trusts and Estates: Tax and Other Issues
Bennie Groenewald LLM Tax Law, B.Proc, HDip Tax, PED (IMD Switzerland)

After having qualified and practiced as a Commercial lawyer Bennie worked in the Banking and Financial services industry for 25 years across multiple market segments in South Africa, Sub-Saharan Africa and the UK, the last 14 years of which in senior and executive leadership positions.

During this time, he dealt extensively with cross-border banking and finance including project finance, asset finance, debt capital markets and derivatives, including the legal aspects thereof. In recent years, Bennie has played an active leading role in investment, credit and risk management as well as sound corporate governance.

The Tax Shop Franchise is a professional services organisation providing comprehensive services in the knowledge intensive accounting and taxation domain. The experienced practitioners in the Tax Shop group are well positioned to provide advisory and compliance related services in all areas of accounting, payroll, taxation including consulting on strategy, cash flow forecasts/management, business performance measurement and much more…..
Contents

1. Trusts in context
2. Advantages of a trust
3. Disadvantages of a trust
4. What is a trust? Nature of trustees
5. Problems with trusts
6. The parties to a trust
7. When are trust assets at risk?
8. Death of a taxpayer and deceased estates
9. Estate duty
10. Estate planning
REFERENCES AND ACKNOWLEDGEMENTS

Books:
2. Trust Law in South Africa by WD Geach, published in 2017 by Juta and Co.

Notes:
These SAIPA notes have been prepared by Professor Walter Geach CA(SA), BA LLB (Cape Town), MCOM (UDW), Professor and Head of the Department of Accounting at the University of the Western Cape
TRUSTS (OTHER THAN PBOs) IN CONTEXT: TAX

- Ring-fencing of trusts in the future, where trusts are taxed and **not** the beneficiaries
- 45% flat rate of income tax
- Inclusion rate for CGT: effective rate is 36% of a net gain (R100 x 80% x 45%)
## TAX RATES: INDIVIDUALS
### 2018/19

<table>
<thead>
<tr>
<th>Income Range</th>
<th>Taxation Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 – 195 850</td>
<td>18% of taxable income</td>
</tr>
<tr>
<td>195 851 – 305 850</td>
<td>35 253 + 26% of taxable income above 195 850</td>
</tr>
<tr>
<td>305 851 - 423 300</td>
<td>63 853 + 31% of taxable income above 305 850</td>
</tr>
<tr>
<td>423 301 - 555 600</td>
<td>100 263 + 36% of taxable income above 423 300</td>
</tr>
<tr>
<td>555 601 - 708 310</td>
<td>147 891 + 39% of taxable income above 555 600</td>
</tr>
<tr>
<td>708 311 - 1 500 000</td>
<td>207 448 + 41% of taxable income above 708 310</td>
</tr>
<tr>
<td>1 500 001 and above</td>
<td>532 041 + 45% of taxable income above 1 500 000</td>
</tr>
</tbody>
</table>
TAX RATE: COMPANIES

- 28% normal tax rate
- Dividends received by individuals from South African companies are exempt from income tax (section 10(1)(k)(i)), but **dividends tax at a rate of 20% is withheld** by the company paying the dividends to the individuals (section 64E).
## TAX RATES: TRUSTS (OTHER THAN SPECIAL TRUSTS)

<table>
<thead>
<tr>
<th>Year of assessment</th>
<th>Rate of Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 March 2018 - 28 February 2019</td>
<td>45%</td>
</tr>
<tr>
<td>1 March 2017 - 28 February 2018</td>
<td>45%</td>
</tr>
<tr>
<td>1 March 2016 - 28 February 2017</td>
<td>41%</td>
</tr>
<tr>
<td>1 March 2015 - 29 February 2016</td>
<td>41%</td>
</tr>
<tr>
<td>1 March 2014 - 28 February 2015</td>
<td>40%</td>
</tr>
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</table>
### TRUSTS IN CONTEXT: CAPITAL GAINS TAX

Increase in inclusion rate %...effective rate increase

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Individuals</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>And disability</td>
<td>18%</td>
<td>16.4%</td>
<td>13.65%</td>
<td>13.32%</td>
<td>13.32%</td>
</tr>
<tr>
<td>special trusts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Companies</td>
<td>22.4%</td>
<td>22.4%</td>
<td>18.65%</td>
<td>18.65%</td>
<td>18.65%</td>
</tr>
<tr>
<td>Trusts (other</td>
<td>36%</td>
<td>32.8%</td>
<td>27.31%</td>
<td>26.64%</td>
<td>26.64%</td>
</tr>
<tr>
<td>than special trusts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
EXAMPLES OF TRUST TAX DISADVANTAGES

- High tax rates (flat rate, no progressive tax rates, CGT)
- No rebates (s6)
- No s10(i) interest exemption
- No primary residence exclusion for CGT
TRUSTS: Pros & Cons

Advantages
- Vehicle for protection against creditors
- Establish continuity - efficient succession
- Reduce certain taxes, such as estate duty – “Estate freezing”
- Effective planning mechanism for future generations
- Trust can be used to achieve the same benefits as a *usufruct*

Disadvantages
- Loss of ownership and control over the assets
- Costs involved in setting up and running a trust
- Income tax is payable at a flat rate of 45%
- Capital Gains Tax (CGT) is payable at an effective rate of 36% and Section 7C
SPECIAL TRUSTS AND TAXATION

- Rate of income tax not fixed at 45%, sliding scale applicable to natural persons applies.
- The CGT inclusion rates applicable to a natural person apply.
- Therefore, for CGT a special trust is subject to the same CGT inclusion rate of 40% and it is also entitled to the annual CGT exclusion of R40 000.
- A special trust is entitled to primary residence and personal-use asset exclusions from aggregate capital gains.
Although a special trust is taxable at the rates of normal tax applicable to a natural person, it is not a natural person and accordingly does not qualify for any rebate or exemption that applies only to natural persons.

For example, a special trust does not get:

- the primary, secondary and tertiary rebates under section 6
- the medical tax credits under sections 6A and 6B, or
- the interest exemption under section 10(1)(i).
There are two types of “special trust” for income tax purposes:

- a trust that is created solely for the benefit of a person with a **disability**, and
- a testamentary trust created solely for the deceased’s relatives and the youngest beneficiary must be **under 18** on the last day of the tax year

There is one type of “special trust” for CGT purposes: **disability trust**
SPECIAL TRUSTS AND TAXATION: **DISABILITY**

- Trust that has been created solely for the benefit of one or more persons who is or are persons with a disability as defined in section 18(3) of the Income Tax Act where such disability incapacitates such person or persons from earning sufficient income for their maintenance, or from managing their own financial affairs.

- Special trust treatment terminates in respect of years of assessment ending on or after the date on which all such persons are deceased.

- Where such trust is created for the benefit of more than one person, all persons for whose benefit the trust is created must be relatives in relation to each other.
SPECIAL TRUSTS AND TAXATION: AGE

- Trust created by or in terms of the will of a deceased person
- Solely for the benefit of beneficiaries who are relatives of deceased person and
- Who is alive on the date of death of that deceased person (including any beneficiary who has been conceived but not yet born on that date),
- The youngest of those beneficiaries is on the last day of the year of assessment of that trust under the age of 18 years
- If the youngest beneficiary turns 18 in December 2017, the trust will be an ordinary trust for the entire 2018 year of assessment
The definition of a special trust for the purposes of CGT is narrower than that for income tax purposes.

A so-called “under 18 years of age” trust is not recognised as a special trust for the purposes of CGT.
TRUSTS IN CONTEXT: TAX

- A “person” as defined in Income Tax Act, includes a trust

- A trust is treated differently from a company or close corporation

- This is because income or capital gains which are received by trustees might not be taxed in the trust at all but be taxed in the hands of the beneficiaries of the trust

- The **conduit principle** applies to the source of income flows and retains its nature as it passes through to a beneficiary

- Read the trust deed to establish if a beneficiary is entitled to a certain type of income (for example, dividends).
Section 25B - any income allocated or paid to a beneficiary who has a vested right in the year that the income is received by, or accrues to a trust, then income will be deemed to have accrued to the beneficiary for tax purposes.

Beneficiary will also be deemed to have incurred the expenditure relating thereto.

Section 25B is subject to the provisions of section 7 of the Income Tax Act.
Section 25B (4), (5) and (6) provides,

- The **deductions claimed by a beneficiary** may not exceed the income that accrues to a beneficiary i.e. **tax losses cannot be distributed** to a beneficiary

- **Trust** can use the deductions not used by the beneficiaries in the year that the expenditure is incurred

- If the trust cannot use all the deductions then surplus deductions **may be used by beneficiaries in subsequent tax years**
Section 25B read with section 7 means, A trust is in essence a taxpayer of “last resort”.

…If there is no,

- Donor/lender, or
- Beneficiary to tax,

Then the trust is taxed.
If a person has a vested right to income, it means that the person is entitled to the income, even though enjoyment/payment may be postponed to a future date.

- Gross income = amounts received and accrued
- A contingent right = a hope
- Offshore trusts are only liable for tax in SA on SA-sourced income.

- **SA trusts**: income in a year is taxed in the hands of (1) donor (2) beneficiary or (3) trust. Accumulated income distributed to a beneficiary is tax-free (it has already been taxed).

- **Offshore trusts**: a resident who *obtains a vested right* to (a) an accumulated capital gain or (b) accumulated income of an offshore trust, must include that capital gain/income in the year of vesting.
Requirements for these rules to apply:

1. A SA-resident acquires a vested right to the accumulated capital gain or accumulated income of an offshore trust.

2. The accumulated capital gain/accumulated income arose through amounts that would have been taxed in SA if the trust was a SA-resident.

3. The amount has not already been subject to tax in SA.
Section 7C applies in respect of any loan, advance or credit advanced (directly or indirectly) to a trust by

(a) a natural person who is a connected person to the trust; or

(b) a company, at the instance of that natural person who is a connected person in relation to that company

Section 7C also applies to loans from the lender to a company, in which the trust or a beneficiary of that trust holds at least 20% of the equity shares or voting rights

Section 7C applies in respect of all loans made on, after, or before 1 March 2017, or pre-existing loans on which no interest /low interest is charged.
SECTION 7C

- If interest on a loan is less than the official rate a donation will arise.
- If the loan is granted by a company at the instance of a natural person, the natural person is deemed to have made the loan and liable for any donation arising therefrom.
- The annual donations tax exemption of R 100 000 can be used against any donation that arises in terms of section 7C.

Official rate = Repo + 1%

<table>
<thead>
<tr>
<th>DATE FROM</th>
<th>DATE TO</th>
<th>RATE</th>
</tr>
</thead>
<tbody>
<tr>
<td>01.02.2016</td>
<td>31.03.2016</td>
<td>7.75%</td>
</tr>
<tr>
<td>01.04.2016</td>
<td>31.07.2017</td>
<td>8.00%</td>
</tr>
<tr>
<td>01.08.2017</td>
<td>31.03.2018</td>
<td>7.75%</td>
</tr>
<tr>
<td>01.04.2018</td>
<td>Until change in Repo rate</td>
<td>7.50%</td>
</tr>
</tbody>
</table>
If a trust incurs—
(a) no interest in respect of a loan, advance or credit
or
(b) interest at a rate lower than the official rate of interest

Interest @ official rate, say 7,5% = R x
Interest on the loan to the trust = (R y)

Difference between R x and R y = a donation

Donations tax @ 20% (but will be at 25% on the portion above R30m – per 2018 budget proposal)
Where a loan advanced to a trust does not exceed an amount of **R1 333 345**

7,5% thereof amounts to **R 100 000**

the taxpayer would be entitled to rely on the exemption of donations tax, which exempts the first R100 000 from donations tax.
Example:
If a natural person lends R10 000 000 to a trust and does not charge interest from 1 March 2017, that will constitute a **donation of R 750 000** for the 2018 tax year of which R100 000 is exempt from donations tax.

\[
R 650 000 \text{ (donation)} \times 20\% \text{ (donations tax)} = R 130 000 \\
\text{payable by 31 March 2018}
\]

Effective maximum rate of donations tax if NO interest is charged:
\[
R100 \text{ (loan)} \times 7,5\% \text{ (official rate)} \times 20\% \text{ (donations tax)} = 1,5\% \text{ of the loan every year}
\]
SECTION 7C EXCLUSIONS:

PUBLIC BENEFIT ORGANISATION

No deemed donation in respect of any amount owing by a trust if that trust is a PBO (s30(3)) or a small business funding entity (s 30C)

TRADING/BUSINESS TRUSTS

- Loan to trust and in return the lender obtained a vested right to the trust in proportion to the loan (business trusts), and
- none of the vested interests held by the beneficiaries of that trust is subject to a discretionary power conferred on any person in terms of which that interest can be varied or revoked
No deemed donation if the trust used the loan wholly or partly for purposes of funding a property and:

1. the lender or the spouse of that person used that asset as a primary residence throughout the year, and

2. the amount owed relates to the part of that loan, advance or credit that funded the acquisition of that asset;

NB: Use agreement or resolution
SECTION 7C EXCLUSIONS: TRANSFER PRICING RULES

No deemed donation if that loan, advance or credit constitutes an affected transaction as defined in section 31(1) that is subject to the provisions of that section; (transfer pricing rules in respect of loans to an offshore trust)

SHARIA COMPLIANT LOANS

No deemed donation if that loan, advance or credit was provided to that trust in terms of a sharia compliant financing arrangement as contemplated in section 24JA
No deemed donation if that loan, advance or credit is subject to the provisions of section 64E(4)….i.e. it is a deemed dividend
SECTION 7C EXCLUSIONS: DIVIDEND

64E. Levy of dividends tax
A trust which owes an amount to a company,........
that company **is deemed to have paid a dividend** if that debt arises
by virtue of **any share held in that company** by that trust

The amount of the dividend that is deemed to be equal to the greater of:
- the **market-related interest** in respect of that debt, less the amount of interest that is payable to that company in respect of that debt for that year of assessment; or
- nil
SECTION 7C EXCLUSIONS: CERTAIN EMPLOYEE SHARE SCHEMES

Employee share schemes

- Due to negative impact on some employee shares schemes that make use of trusts to hold shares in the employer company.
- These types of trusts are established to facilitate incentive programmes for employees.
- Requirements ensure that owners of businesses do not abuse the exclusion to transfer wealth to family members that are in the employ of the business.
Requirements for exclusion from section 7C by employee share plans:

- Trust **solely created for employee share incentive scheme** and
- Loan was provided for share acquisition
- Shares may only be offered by that trust to someone by virtue of that person being in the **full-time employment/director** of a company
- Connected persons may not participate in scheme (20% or more interest)
Since the introduction of section 7C schemes to avoid the deemed annual donation:

1. Interest-free loans/advances/credit/low interest loans could be made to companies owned by trusts; or

2. There could be a transfer of loans to current or future beneficiaries of trusts
TRUSTS IN CONTEXT:
TAX AMENDMENTS TO SECTION 7C
Low or no interest loans to trusts

- Loans advanced to a company owned by a trust
- Transfer of loan claims to beneficiaries
The trust holds the ordinary shares
Interest-free or low-interest loans to companies owned by trusts:

- **Loan to the company** rather than the trust, section 7C *(before it was amended)* would not apply because it *originally* only applied to loans advanced to trusts

- Benefit from this low or no interest funding and tax can only be collected at a much later stage when the company makes distributions to the trust.

- **Amendment**: interest free or low interest loans, by a natural person or a company (at the instance of a natural person) to a company that is a connected to a trust now also fall under the anti-avoidance measures.
Section 7C will apply to loans made to

(ii) a company if at least 20 per cent of—
(aa) the equity shares in that company are held, directly or indirectly; or
(bb) the voting rights in that company can be exercised, by the trust referred to in subparagraph (i) or by a beneficiary of that trust.”

Effective date: 19 July 2017
TRUSTS IN CONTEXT: TAX AMENDMENTS TO SECTION 7C

Transfer of loan claims to other connected persons:

- Person acquires a loan owing by a trust or company as envisaged by s 7C, the person who acquires that loan is deemed to have made the loan to the trust or company.
- The person who acquires the loan at face value, thereby avoiding donations tax.
- Person acquiring such a claim must be a connected person to (a) the trust or (b) to the original lender.
- The deemed loan will be for the amount acquired.
- Prior to this amendment, it was argued that, by transferring the loan, this breaks the link between the person who advanced the loan and the loan itself.
“(1A) If a person acquires a claim to an amount owing by a trust or a company in respect of a loan, advance or credit referred to in subsection (1), that person must for purposes of this section be treated as having provided a loan, advance or credit to that trust or company—

(a) on the date on which that person acquired that claim; or

(b) if that person was not a connected person on that date in relation to—

(i) that trust; or

(ii) the person who provided that loan, advance or credit to that trust or company,

on the date on which that person became a connected person in relation to that trust or person,

that is equal to the amount of the claim so acquired.”;
CURRENT TAX ADVANTAGES OF TRUSTS
TAXES UP TO DEATH OF A PERSON

1. Income tax up to date of death
2. CGT (deemed disposal)
3. Estate duty

SA NORMAL TAX: In the last tax return of the deceased

ESTATE DUTY TAX: paid by the executor on behalf of the deceased estate
USE OF TRUSTS TO AVOID ESTATE DUTY

[SOURCE: SAIPA TAX UPDATE 2018]

Sells growth asset to trust at market value on loan account bearing no/low interest

Loan reduced as trust uses annual R100k donated to repay

Growth occurs in trust
No estate duty or CGT on death
ADVANTAGES OF A TRUST

- Protection from taxes that arise on death
- No wealth tax on trusts if assets are retained in the trust

DISADVANTAGES OF A TRUST

- Hostile tax environment
- Planner loses control of the assets in trust
- Identification of proper trustees
- Rights of beneficiaries
- Amendment of trusts
- Problems with trusts
DEFINITION OF TRUST (part (a) of the definition): TRUST PROPERTY CONTROL ACT

A trust is not a legal person but is an arrangement brought about by a contract or last will and testament:

- Trustees
- For the benefit of beneficiaries
SWANEPOEL N.O. [as Trustee of the HARNE TRUST] vs STANDARD BANK OF SOUTH AFRICA LIMITED

- Loan agreement was entered into between “The Harne Trust (the borrower) and the Standard Bank Ltd (the lender)”

- The trustee, in his personal capacity, signed a suretyship agreement
DEFINITION OF TRUST
(part (a) of the definition):

TRUST PROPERTY CONTROL ACT

- A trust instrument
SECTION 2: CERTAIN DOCUMENTS DEEMED TO BE TRUST INSTRUMENTS

If a document represents:

(1) the reduction to writing of

(2) an oral agreement

(3) by which a trust was (a) created or (b) varied

(4) such document shall for the purposes of this Act be deemed to be a trust instrument.
Chief Master’s directive 2 of 2017

- The Master must consider appointing an INDEPENDENT TRUSTEE where the trust is a family business trust
- This is a trust where the trustees are the beneficiaries and the beneficiaries are related to each other
INDEPENDENT TRUSTEES

- Must have knowledge of trust matters
- Must not be a beneficiary
- Must not be related to:
  (a) the founder
  (b) other trustees
  (c) any beneficiary
- Must be able to check the conduct of other trustees
- Must be aware of a trustee’s duties

If no independent trustee:
- May be required to provide security; or
- May require the trust to be audited
A TRUST IS SEPARATE FROM THE FOUNDER, BENEFICIARIES AND TRUSTEES


The thrust of the appellant’s case is that any loss that may have been suffered was not suffered by the respondent personally.
SECTION 12 TRUST PROPERTY CONTROL ACT:

Trust property shall not form part of the personal estate of the trustee except in so far as he as trust beneficiary is entitled to the trust property.
PROBLEMS WITH TRUSTS

1. Thinking that trusts are not regulated at all

2. The way trusts are formed and the way assets are put into a trust

3. The way trusts are administered

4. The way trusts are amended

5. Taxation of trusts in the future?
PROBLEMS

1. Thinking that trusts are not regulated at all

2. The way trusts are formed and the way assets are put into a trust

1. The way trusts are administered

2. The way trusts are amended

3. Taxation of trusts in the future?
PROBLEMS

Thinking that trusts are not regulated at all

1. The Trust Property Control Act applies
2. The common law applies
3. The trust deed is the constitution of the trust and applies
4. Trustees hold an office: powers and statutory duties
5. All beneficiaries get rights: both actual and potential
   Certain laws apply depending where the trust is formed (b) administered (c) managed
6. The Master has powers
There is a separation of ownership/control vs. benefit

*Thorpe v Trittenwein* 2007 (2) SA 172 (T):

- a valid trust will not have been created where the trustees are exactly the same persons as the beneficiaries

- Consider “business” or “trading” trusts: trustees, beneficiaries? Partners?
THE WAY ASSETS ARE TRANSFERRED INTO A TRUST

- **Sale** on loan account (section 7C)
- **Repayment** terms?
- **Interest**-free or interest-bearing?
- Assets put in trust in settlement of **an obligation**
SECTION 17 TRUST PROPERTY CONTROL ACT

A trustee must not without the written consent of the Master destroy any document which serves as proof of the

1. Investment
2. Safe custody
3. Control
4. Administration
5. Alienation or
6. Distribution of trust property

before the expiry of a period of 5 years from the termination of a trust
Potgieter v Potgieter NO and Others
2012 (1) SA 637 (SCA) (30 September 2011)

- The trust deed: the trustees could amend the trust deed
The importance of acceptance by the beneficiary is that it creates a right for the beneficiary, while no such right existed before. Acceptance of benefits need not be formal acceptance, but acceptance by conduct.
and it is not without relevance that the respondent alleged that she conducted part-time farming operations on the farm, and paid certain farming expenses at a time after the trust had been created.

These facts are consistent with her having accepted the benefits of the trust.
“It is established law that beneficiaries of discretionary trusts who have received conditional benefits, … have vested rights, and the trust deeds cannot be changed without their consent”
PARTIES TO A TRUST

- Founder
- Trustees
- Beneficiaries
- Protector (consider section 9 Trust Property Control Act)
- Master
TRUSTS’ ASSETS: WHEN ARE THEY AT RISK?

1. No need to lift the veil
2. Sham trusts
3. Lifting the veil
4. Universal partnerships
1. No need to lift the veil: *Jordaan, Badenhorst and Britz cases*
TRUSTS’ ASSETS: WHEN ARE THEY AT RISK?

1. No need to lift the veil
2. Sham trusts
3. Lifting the veil
4. Universal partnerships
Khabola NO v Ralitabo NO  
Case No: 5512/2010

• **A trust** was formed for the purpose of acquiring agricultural land on which farming activities were to be conducted.

• **No beneficiaries** were appointed in the trust instrument

• **No trustee meetings** were held

• The trust was registered and had a reference number
(1) establishing that a trust is a sham and

(2) ‘going behind the trust form’

teal fundamentally different undertakings
TRUST ASSETS: WHEN ARE THEY AT RISK?

1. No need to lift the veil
2. Sham trusts
3. Lifting the veil
4. Universal partnerships
Lifting the trust veil

It is a remedy that will generally be given when the trust form is used in a dishonest or unconscionable manner to

- evade an existing liability,

or

- avoid an obligation
A trust that is aimed at frustrating either the founder’s creditors (Ex Parte Executor Testamentary Estate Boulton 1958 2 PH G24 (C)) or the beneficiary’s creditors (Ruskin NO v Sapire NO [1966] 2 All SA 11 (W)) where an enforceable right to the trust property has already vested will not be upheld.
1. Deceased
2. Deceased estate
3. Executor
4. Last will and testament
5. Intestate succession
6. The Master
7. Heirs and legatees
8. Surviving spouse
PROCEDURE WINDING UP THE ESTATE OF A DECEASED TAXPAYER

1. Appointment of Executor
2. Information Gathering
3. Collection of claims & realisation of assets (if applicable)
4. Lodgement of liquidation & distribution account (L&D Account)
5. Distribution of surplus to heirs and legatees

Payment of outstanding debt in accordance with approved L&D account

SARS VAT 413 Guide on Estates
DEATH OF A TAXPAYER: TAX CONSEQUENCES

1. **Existing taxpayer**: last tax return up to date of death (income tax AND CGT): then no longer a taxpayer

2. **New taxpayer**: the deceased estate

3. **Surviving spouse**: base cost of inherited assets (same as deceased)

4. **Other heirs and legatees** (other than the surviving spouse): base cost of inherited assets (MV)
TAXES ON DEATH

1. **Income** tax up to date of death

2. **CGT** (deemed disposal)

3. **Estate duty**

   ESTATE DUTY TAX: paid by the executor on behalf of the deceased estate

SA NORMAL TAX: In the last tax Return of the deceased
1. **Income Tax**: will be a debt due by deceased (liability of the estate; claim against the assets of the estate)

2. **CGT**: deemed disposal of assets on day before death. CGT taxes growth, ignores liabilities

3. **Estate Duty**: taxes net assets (i.e. assets less liabilities)
DEATH OF A PERSON

Income Tax

a) Deceased: **income** up to date of death
(received, + accrued, + deemed receipts)

b) Deceased estate: **income** received and accrued
that would have been income in the hands of the
deceased which does not fall into (a) above
• Income received by or accrued to the deceased **before**
date of death

  - Included as part of the last tax return

• Income receipt or accrual **after** date of death: there are
certain **deemed accruals**, included as part of the last
tax return

  - (a) sections 8A, B, C,
  - (b) gross income paragraph (d)(iii)(bb)
  - (c) 2\textsuperscript{nd} schedule

**All other receipts and accruals after death:**
**taxed in the hands of the deceased estate**
DEEMED INCOME: SECTION 8A

Income receipt or accrual after date of death

- Section 8A: **exercise** of options into Employee Share Incentive Schemes operational before 26 October 2004)
  - **Exercise** of share options (s8A): accrual of income on *date of exercise*. BUT if there are restrictions: deferral of tax i.e. the taxpayer was not entitled to sell until a date after death

- If there has been a **deferral**, there is a deemed income of the gain on date before death
DEEMED INCOME: SECTION 8A

Income receipt or accrual after date of death

➢ **Restricted equity instruments** only taxed on **vesting date** – s8C: there is a deferral of income tax liability until restrictions no longer apply

➢ If there was a deferral and if the taxpayer **dies** before vesting date: deemed income

➢ Instruments vests immediately before death but only if the restrictions may be lifted on or after death
DEEMED INCOME: SECTION 8B

Income receipt or accrual after date of death

- Gain on s8B (Broad-Based Employee Share Plans) instruments: income if sold within 5 years

- But if the taxpayer **dies within 5 years** of receiving s8B shares

- There will **only be CGT implications for the deceased** – Disposal at MV
DEEMED INCOME 8B - EXAMPLE

Income receipt or accrual after date of death

- Mr A was granted 25 000 shares on 7 March 2014 in terms of a broad-based employee share plan.
- The market value of the share on grant date was R1 per share and no consideration was paid by Mr A.
- Mr A tragically died on 1 May 2016.
- The market value of the shares on the date of Mr A’s death was R2.
DECEASED PERSON - EXAMPLE

Result:

- No s8B income tax implications although the taxpayer died within 5 years

- Shares will be actually disposed of by the deceased estate but not accounted for in the deceased estate – no section 25

- Deemed disposal in the hands of the taxpayer

Therefore there is a **capital gain** of R2 x 25 000 = R50 000. **On date before death**
DECEASED PERSON : OTHER
DEEMED INCOME

Income receipt or accrual after date of death

1. Lump sum received from a fund on the death of a member (2\textsuperscript{nd} Schedule)

2. Lump sum as compensation for loss of office (gross income)

3. Severance benefit from employer (gross income)

Amounts deemed to have been received by or accrued to the deceased immediately before death
DECEASED PERSON

Income Tax and CGT implications – death on or after 1 March 2016
Dealt with under s 9HA(1) and s25

- Deceased is DEEMED to have disposed of all his/her assets (with some exceptions: see exceptions below) @ Market Value on day before death: capital assets AND trading stock AND depreciable assets (Recoupment provisions apply)

- No deemed disposal for the following:
  1. Assets transferred to surviving spouse
  2. Qualifying long-term insurance policies
  3. Benefits from retirement funds
DEATH OF A TAXPAYER: LAST TAX RETURN

- X had a motorbike - used in his business
- He claimed 11 (e) wear and tear on the bike
- Cost of bike was R 100 000
- Tax value at time of death was R 70 000
- Market value at time of death was R 90 000
- He dies and there is a deemed disposal of the bike
- There is a recoupment of R 20 000
- This must be included in X’s final tax return
EXCEPTIONS TO DEEMED DISPOSAL RULE

Section 9HA(1) deeming provision does not apply in the following 3 circumstances:

- where assets are **awarded to a surviving resident spouse** (then the provisions of section 9HA(2) will apply);
- in respect of any **long-term insurance policy** of the deceased if the capital gain or loss on the disposal of the policy would have been disregarded in terms of paragraph 55 (of the 8th schedule); and
- in respect of any interest of the deceased in **any pension, pension preservation, provident, provident preservation or retirement annuity fund** in the Republic (or any similar fund or instrument outside the Republic) if the capital gain or loss on the disposal of the interest would have been disregarded in terms of paragraph 54 (of the 8th schedule).
SURVIVING SPOUSE

Section 9HA(2)

Rules that apply if surviving resident spouse gets assets of the deceased in any of the following ways:

- **Inheritance** in terms of the will of deceased
- Acquired by **intestate succession**
- Acquired as part of an **accrual claim** (Matrimonial Property Act)
AMOUNTS INHERITED BY THE SURVIVING SPOUSE

- Deemed disposal of capital assets at base cost to the deceased as at date of death

- Deemed disposal of Revenue assets (trading stock) at the amount allowed as a deduction (s 11 (a) or opening stock) for the tax year ending on the date of death

- CGT = R0 and Recoupment = R0

In other words, assets inherited by a surviving spouse ~ spouse steps into the shoes of the deceased
CGT AND DEATH

- The deceased person will be entitled to a CGT exclusion of R300 000 in the year of death (an increase from the annual R40 000 exclusion)

- Moreover all the other CGT exclusions will also apply, such as the personal-use asset exclusion, the partial primary residence exclusion, and any previously unused portion of the partial small business asset exclusion up to R1,8 million.
**DEATH OF A TAXPAYER**

- Last tax return: rebates are **apportioned** up to date of death
- **Ages** of children are determined for tax purposes at date of death (additional medical credits)

**Example**
- X died on 1 August 2017 at age of 55 years
- Income from sole proprietorship to date of death for the year was R 131 500
- Interest received and accrued was R 24 300

What are the taxes payable for the year ended February 2018?

[silke]
DEATH OF A TAXPAYER: LAST TAX RETURN

- Gross income (131 500 + interest of R 24 300)
- Less interest exemption (R 23 800)
- Taxable income: R 132 000
- Period of assessment: 1 March 2017 to 1 August 2017 = 154 days
- Tax R 132 000 (@18%): R 23 760
- Primary rebate: R 13 635 x 154/365: (R 5 752)
- SA normal tax: R 18 008

NOTE:
1. The interest exemption IS NOT apportioned
2. The Primary rebate IS apportioned
DECEASED ESTATE

- Separate person i.t.o section 1 definition of a person

- Executor/Administrator is the representative taxpayer

- Estate to register for VAT, where applicable

- Amounts treated as income of deceased estate
  - Income received by or accrued to the executor; and
  - Amount received or accrued which would have been income in the hands of the deceased person if that person would have been alive

Any assessed loss after his/her last tax return, this is NOT transferred to the deceased estate - The assessed loss falls away
DECEASED ESTATE

Assets disposed to an heir or legatee by the executor

- **Disposed of** at an amount equal to the Market Value at time of death of deceased

- Heir or legatee **acquired asset for base cost purposes** at MV at the time of death of deceased

- No income or capital gain or loss on transfer of assets

- Deceased estate treated as a **natural person**
DECEASED ESTATE AS A NATURAL PERSON

This means that the deceased estate is entitled to the same exclusions and relief provisions below as a natural person:

- annual exclusion of R40 000
- inclusion rate of 40%
- primary residence exclusion
- personal-use asset exclusion
- small business asset relief (paragraph 57 of the Eight Schedule) – this is the R1.8 million lifetime exclusion (the remainder of the exclusion amount not utilised by the deceased person)
THE ESTATE AND CAPITAL GAINS TAX

- Any asset in the deceased estate **retains the same nature in the deceased estate** as it had in the hands of the deceased.
- This means that if the estate sells the asset the same **exemptions and exclusions** are available as would have been available to the deceased.
- Example, estate sells an asset which was the primary residence of the deceased, **an exemption of up to R2 million will be available** if the property is sold for more than R2 million.
- **Base cost** of the asset, as far as the estate is concerned, is the **market value of the asset at the date of death** of the deceased.
- The **inclusion rate percentage applicable to individuals** to apply...
The return caters for the insertion of the **primary residence** exclusion. If a primary residence was disposed and the difference between **the proceeds** and **the base cost** is less than the primary residence exclusion, the gain must be indicated as a ‘0’.

**Example:**
Proceeds on the disposal of a primary residence:  R 3 800 000  
Base cost:  R 2 500 000  
Gain prior to primary residence exclusion:  R 1 300 000  

Primary residence exclusion R2 000 000 (this will be limited to the R1 300 000):  
Gain  
R 0
DECEASED ESTATE TREATED AS A NATURAL PERSON

However the following will not apply to deceased estates:

- primary, secondary or tertiary rebates
- medical tax credits
- additional medical tax credits
DECEASED ESTATE: INTEREST INCOME

Section 10(1)(i) provides only for an exemption of interest received from a source in the Republic.

- SARS practice: the exemption applicable for a deceased estate is R23 800.
DECEASED ESTATE AND HEIRS/LEGATEES

Once an executor has handed over an asset/use of an asset to an heir/legatee, and the heir/legatee has an enforceable right to claim any income from the asset, that income will then accrue to that heir or legatee.
EXECUTOR AND MARRIAGE IN COMMUNITY

- An executor administers the assets of the joint estate
- Executor pays the liabilities of the joint estate
- Executor collects the income of the joint estate, but half is taxed in the hands of the survivor
- Half of the joint estate accrues to the surviving spouse, other half accrues to heirs/legatees
Heir or legatee can elect to receive an asset that *must be disposed of* to settle the deceased estate’s CGT, if that heir or legatee pays the tax:

- If the CGT on the deemed disposal on death is > than 50% of Net Asset Value of the deceased's estate

- If the Executor would be required to dispose of that asset to settle the CGT
Deceased Estate can be VAT vendor (section 1 of the VAT Act includes a deceased estate as a person)

Deceased Estate liable for VAT on distribution of assets if the assets formed part of the enterprise of the deceased
Apply tax fraction for Output VAT based on MV of the asset

The consideration will be nil where assets are bequeathed to a non-connected person (for example a business partner) for no bequest price: see notes @ page 25 (example)

If an asset is transferred to a connected person, there will be VAT based on the market value of the asset
20% rate of estate duty

But Estate Duty rate increases from 20% to 25% on dutiable amount of estates of more than R30 million (but it is only the portion of the dutiable estate that exceeds 30 million that is subject to 25%)

Estate duty is a wealth tax payable on the transfer of wealth from a deceased estate to the heirs/legatees

The tax is payable only if the net value of an estate is greater than R 3,5m
ESTATE DUTY

- Estate Duty is payable on the following assets:
  - SA Residents > World-wide assets
  - Non Residents > South African assets
- Levied on the estate of the deceased person
NON-RESIDENTS

- **Donations tax** …….exempt even if donation of SA assets
- **Estate duty** ……..liable for estate duty on SA assets
- **CGT**: liable for gains on immovable property in SA
ESTATE DUTY

- Inform SARS of deceased estate regardless of whether Estate Duty is payable
- 20% of dutiable amount
- Executor or administrator pays Estate Duty
- Due within 1 year of date of death or 30 days from date of assessment
## ESTATE DUTY FORMULA

### Framework – Dutiable Amount

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property in Estate - s3(2)</td>
<td>Rxxx</td>
</tr>
<tr>
<td>Deemed property in the estate - s3(3)</td>
<td>xxx</td>
</tr>
<tr>
<td>Gross value of the estate</td>
<td>xxx</td>
</tr>
<tr>
<td>Less: Allowable deduction - s4</td>
<td>(xxx)</td>
</tr>
<tr>
<td>Net Value of Estate - s4</td>
<td>xxx</td>
</tr>
<tr>
<td>Less: Abatement - s4A</td>
<td>(3 500 000)</td>
</tr>
<tr>
<td>Dutiable amount - s4</td>
<td>xxx</td>
</tr>
<tr>
<td>Estate Duty calculated @ 20% of dutiable amount</td>
<td>xxx</td>
</tr>
<tr>
<td>Less: Applicable tax rebates (s16 and 1st Schedule)</td>
<td>(xxx)</td>
</tr>
<tr>
<td>Less: Amount of estate duty to be recovered from beneficiaries</td>
<td>(xxx)</td>
</tr>
<tr>
<td>Estate Duty payable by the estate</td>
<td>xxx</td>
</tr>
</tbody>
</table>
ESTATE DUTY

- Property and deemed property?
- Value?
- Deductions?
- Abatement?
PROPERTY AND DEEMED PROPERTY

- Movable
- Immovable
- Tangible
- Intangible
- No matter where the property is located
- Includes any right (limited interest) in property that passes to another
PROPERTY OF THE DECEASED
SECTION 3(2)

- Shares
- Houses
- Land
- Cars
- Patents
- Trade marks
- Farms
- Furniture
- Gold coins
- Debts
- Rights (usufructs, fiduciary rights, bare dominium rights)
- Income earned by deceased prior to death (income earned after death is not property)
Any contributions made by the deceased to any pension, provident or retirement annuity fund as was not allowed as a deduction for tax purposes

This applies to any person who dies after 1 January 2016 in respect of contributions made after 1 March 2015

Prior to this amendment, duty was avoided by making retirement contributions which were not deductible and not subject to retirement lump sum tax tables

It is specifically provided that no retirement benefits (lump sum or annuity) received as a result of the death of the taxpayer will be included in property for estate duty purposes
ESTATE DUTY: PROPERTY IN TERMS OF SECTION 3(2)

Fiduciary, Usufructuary or other like (limited) interest in property (Including the right to an annuity charged upon any property and including the right to other annuities)
X bequeaths a house to Z on condition that Y has a lifelong usufruct in the house.

Usufruct

• Right to use the asset
• Right to income from the asset
FIDUCIARY INTEREST: EXAMPLE

- X bequeaths his house to his sister on condition that she must leave the house (on her death) to X’s son

- A “fiduciary interest has been bequeathed by X to his sister
FIDUCIARY INTEREST

- Fiduciary cannot dispose of the property
- Property must go to Fideicommissary
- Fiduciary can use the property
- Fiduciary can get income from the property
- If Fideicommissary dies before the Fiduciary, the Fiduciary gets full ownership (unlike a usufructuary)
VALUE: ESTATE DUTY

Underlying principle: estate duty

- To what extent **has someone benefitted** from the deceased? (very different from donations tax)

- What is *the value that someone gets* as a result of the death of the deceased?

- If limited right: look at life expectancy of beneficiary
Charged upon property means that there is some particular property or fund out of which the annuity is payable.

*Example,* Annuity is payable to the deceased estate by an executor from rentals from a block of flats.

Requirements must be met for it to be the property in the estate of a deceased:

1. The annuity must have been charged upon property and
2. The annuity must have been held by the deceased immediately prior to his death.
ANNUITY CHARGED UPON PROPERTY

Valuation of annuities charged upon property (section 5(1)(c)):

• where the right to the annuity (enjoyed by the deceased) accrues to some other person, the limited right will be **based on the age of the beneficiary** on his next birthday, after the death of the deceased; and

• where the annuity does not accrue to some other person, but full ownership over the property becomes vested in the owner of the property on which the annuity was charged, the limited right will be **based on the age of the owner of the property** (on his next birthday, after the death of the deceased).


ANNUITY NOT CHARGED UPON PROPERTY

- Annuity not charged upon property (any other annuity) means any right to an annuity which was enjoyed by the deceased immediately prior to his death and which accrues to some other person on the death of the deceased (annuitant).
- This type of annuity is not based on a specific property or capital fund but is the right to receive an annuity such as those which can be purchased from a life assurance company or which is paid out in terms of a pension fund.
- If the annuity does not accrue to another annuitant, the annuity enjoyed by the deceased will not be property in terms of s 3(2)(b).
1. Proceeds from *life insurance policies* on life of deceased (but 3 exceptions)

2. Donations made *in contemplation of death*

3. *Claims* in terms of the Matrimonial Property Act in favour of the deceased’s estate

4. Property that the deceased was *competent to dispose of* for his own benefit immediately prior to death (property that was under the control of the deceased)
DEEMED PROPERTY

Domestic insurance policies – section 3(3)(a)

- Proceeds from domestic insurance policy on deceased’s life
- Reduce by premiums paid by beneficiary plus 6% p.a. interest
- Premiums paid by the deceased cannot be deducted
PROPERTY AND DEEMED PROPERTY

Domestic life insurance policies BUT there are 3 exclusions

1. **Buy and sell** policies provided the deceased paid no premiums (to buy shares, partnership interest etc of the deceased)

2. Proceeds payable to **spouse or child** under an antenuptial or postnuptial contract

3. Life policies where proceeds do not fall into (a) estate or (b) to a relative or (c) to a family company and provided the deceased paid no premiums (for example, “keyman policies”)
1. **If sold** in winding up estate: selling price (except sale of shares in a pty ltd or cc or unlisted public shares: market value)

2. **If not sold**: MV (except farms where value is 70% of MV)
- **Fiduciary, Usufructuary interest**: basic principle (extent to which someone benefits)

- **Annuities**: an annuity charged upon property and annuity not charged upon property (basic principle again)
VALUE OF USUFRUCTUARY /FIDUCIARY INTEREST IN DECEASED’S ESTATE?

1. Annual value? ...........................................

2. 12% x market value of full property

3. Who will benefit?

4. Age next birthday of beneficiary

5. Capital over that period (or lesser period if right of enjoyment is less)
BENEFICIARY OF LIMITED RIGHT 
NOT CERTAIN

- Use 50 years
- MV x 12% x 50 years
ALLOWABLE DEDUCTIONS

- Funeral & Death-bed expenses
- Debts due within the Republic
- Costs of administration & Liquidation
- Master or Commissioner requirement costs
- Foreign property
- Debts due to creditors outside SA
- Limited interest reverting to donor
X gives his uncle the free use of two flats: *this is the donation of a usufruct. X retains the bare dominium*

- **Donations tax:** 20% of the value of the usufruct

- The uncle dies: **estate duty**: *include in the estate of the uncle (as property) the value of the usufruct. Value is calculated by Age Next Birthday of X*

- *Take a full estate duty deduction of this value because the donor (X) gets full ownership*
ALLOWABLE DEDUCTIONS (CONT...)

- Bequests to PBO’s or exempt persons
- Improvements to property made by heir or legatee
- Improvements to limited interest made by heir or legatee
- Claims by spouses
- Limited interest created by predeceased spouse
- Books, pictures, statutory & other works of art
- Deemed property taken into account to value shares
- Amounts accruing to surviving spouse
- R3 500 000 from net value of estate
- **Surviving spouse** qualifies for predeceased spouse abatement *less* abatement used by predeceased spouse
- Multiple spouses
  - Apportion equally among surviving spouses
  - Surviving spouse can only enjoy 1 predeceased spouse abatement
Mr X is married to Mrs X
He dies
Net estate is R 500 000
He bequeaths this to his child
Dutiable estate = R 500 000 less abatement = nil

Mrs X dies with a net estate of R 10 000 000
Dutiable estate = R 10m less R 6,5m = R 3,5m
(R 7m less R 500 000)
Where X was the spouse at the time of death of one or more previously deceased persons:

(1) R 3 500 000
(a) multiplied by two (i.e. R 7m) ; and
(b) reduced by the amount deducted from the net value of the estate of any one of the previously deceased persons in accordance with this section.
Foreign death duties – s16(c)

- Estate Duty payable on foreign property and death duties payable in other foreign country

- Rebate of foreign death duties limited to SA Estate Duty

- Where there’s a DTA, relief sought under DTA and NOT s16(c) rebate
PERSONS LIABLE FOR ESTATE DUTY

- Fiduciary, usufructuary or like interest
  - *Person to whom the advantage accrues on the deceased’s death*
- Right to an annuity (including an annuity charged upon property)
  - *Succeeding annuitant*
- Domestic policy of insurance on life of deceased
  - *Person entitled to proceeds*
- Donatio mortis causa
  - *Donee*
- Any other property
  - *The executor*
MARRIED IN COMMUNITY OF PROPERTY

- Assets and liabilities of both spouses constitute their joint estate

- At death of one of the spouses, surviving spouse and deceased estate entitled to a half-share of joint estate

- Estate of the deceased includes:
  - Half share of net joint estate
  - Property excluded from joint estate
MARRIED IN COMMUNITY OF PROPERTY

- Fiduciary or usufructuary of deceased spouse **excluded** from joint estate. Added to the net value of deceased estate

- Liabilities arising only after death excluded from joint estate. Deducted in full in the estate duty of deceased spouse
Questions?

EMAIL YOUR QUESTIONS & COMMENTS/SUGGESTIONS TO ENQUIRIES@TAXSHOP.CO.ZA

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