Money Matters

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Estate planning - trusts

Trusts

Trusts are very useful estate- and financial planning tools that combine fiscal benefits with the non-tax benefits of custodianship and asset protection. The main reasons for setting up a trust can be summarised as follows:

Estate "pegging" or freezing of asset values

This is one of the cornerstone benefits of inter vivos trusts. Once an asset has been transferred to a trust, either by way of a loan account or by means of a donation, any future growth will take place in the trust.

Minor children

Trusts can be used to hold or protect assets for minor children until they are old enough to handle their own financial affairs. If such a trust is set up in your will, it will qualify as a special trust and will be liable for income tax at the same rates as a natural person.

Disabled beneficiary

A trust that is set up for the benefit of a disabled beneficiary who cannot earn sufficient income for self-maintenance or who cannot manage his/her own affairs will qualify as a special trust and will be liable for income tax and CGT at the same rates as a natural person.

Continuity/perpetual succession

A trust is a separate vehicle and will not be affected by the death of the founder or a trustee. The beneficiaries will continue to receive income and do not have to wait until the deceased's estate is wound up.

Protection of assets against creditors

A discretionary trust enjoys protection against creditors in the event of insolvency. This is subject to the normal insolvency rules in respect of impeachable transactions. If the transfer of the assets to the trust took place at a time when the founder was solvent, it will be difficult for the creditors to set aside the trust transaction.

Tax planning

- **Income tax**
  The general method of taxation of a trust is that any trust income earned, which is not paid over to a trust beneficiary, is taxed in the hands of the trust (without the benefit of any rebates). If trust income is distributed to a trust beneficiary, it retains its original identity and is taxed in the beneficiary's hands and not in the hands of the trust. Income previously taxed in the trust, and which is subsequently paid to a trust beneficiary in another year, is not again subject to taxation.
- **Estate duty**
  Estate duty can be saved by divesting yourself of ownership of growth assets in favour of a trust. In doing so, the growth in the assets accrues to the trust and at most only the value of the assets at date of transfer (usually in the form of a loan account) is retained in your own estate. No estate duty will be payable on the assets in the trust.
- **Transfer duty**
  As of 23 February 2011 the same transfer duty rates applicable to natural persons also apply to trusts However, when a property is distributed from a trust to a beneficiary who is a relative of the founder, no transfer duty will be payable.
- **Donations tax**
  Settlement of assets to trust can take place either by way of donation or by way of selling the assets to the trust. If an asset is donated to the trust, any amount over R100,000 will be subject to donations tax at 20%. The asset will, however, then be completely out of the donor's estate.
  Where assets are sold to a trust on an interest-free loan basis, such a transaction does not constitute a donation for purposes of donations tax. Reduction of this loan can take place by means of annual donations of R100,000 by both the seller and his/her spouse to the trust.
- **Capital gains tax**
  On transferring assets to a trust, you will incur a CGT liability. All the necessary calculations should be done in order to determine whether it will be practical to transfer assets to a trust. If it is clear that a transfer will not be worthwhile, you could still make use of the other benefits of a trust and consider acquiring any future growth assets directly in the trust. As death is a disposal for CGT purposes, your estate will be liable for CGT at your death. Assets held by a trust will, however, not be subject to CGT at your death.
  CGT will be payable by the trust on any gains made as a result of the disposal of any of its assets. As a capital gain is included in a trust's taxable income at a rate of 50%, the effective CGT rate of a trust is 20%. Any gains can, however, be distributed to the beneficiaries, who will be taxed in their own hands at their effective rate (maximum 10%) and subject to the relevant rebates for individuals.

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