

# Money Matters

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## Different types of trusts and when to use them

### Trusts

Last month we explained the various benefits of trusts.

This month we deal with the different types of trusts and when to use them.

Understanding the different types of trusts created in South Africa, as well as when and how they should be used, can save a client, his family members and the financial planner numerous frustrations during the lifetime of the client, as well as after his death.

South African trust law is regulated by the Trust Property Control Act 57 of 1988.

We can distinguish between two types of trusts, namely *mortis causa* trusts (testamentary trusts) and *inter vivos* trusts (trusts created during the lifetime of the founder). The main difference between the two types of trusts is that a testamentary trust is created by way of a Last Will and Testament of the founder whereas an *inter vivos* trust is created by way of

an agreement between the founder and trustees during the lifetime of the founder (the death of the founder is the reason for the creation of the trust). Both kinds of trusts can either be vesting (beneficiaries have a vested right to benefits) or discretionary (trustees have a discretion to decide when to vest benefits in or distribute benefits to beneficiaries). The main differences between the testamentary trust and the *inter vivos* trust are as follows:

- **Flexibility.** An *inter vivos* trust deed can be amended and trustees may be varied, compared to a testamentary trust where the trustees are bound by the Last Will and Testament of the founder.
- **Control over assets.** The donor, who in most instances is also the founder, will lose control over his assets during his lifetime with an *inter vivos* trust, compared to a testamentary trust where the donor

will only lose control at death.

- **Taxes and fees payable on death.** Assets owned in your personal name, which are bequeathed to a trust in your Last Will and Testament, will attract far more taxes and fees on death, compared to assets owned by an *inter vivos* trust before the date of your death (assuming there are no outstanding loan accounts payable to your estate by the trust).

Considering the above, it is of utmost importance that the correct trust structure is put into place for a client in accordance with his current and future needs. The main reasons for creating a testamentary or an *inter vivos* trust are as follows:

#### Testamentary trust:

- **Minor children.** When children are under the age of 18 years, they cannot receive an inheritance in their personal capacity and therefore, should no provision be made for a trust, the inheritance will be paid to the Guardians Fund (a state entity which is governed by the Master of the High Court).
- **Protection.** A trust is a separate legal entity and trust assets do not form part of the beneficiary's personal estate. Furthermore, beneficiaries cannot dispose of trust

assets as and when they please (the "spendthrift" beneficiary).

- **Special needs of an heir,** for example a mentally disabled child who will receive an inheritance.

#### Inter vivos trust:

- **Pegging of estate value.** Once assets are transferred to an *inter vivos* Trust, any future growth in the value of the assets will take place in the name of the trust. This ensures a lower value in the donor's estate at date of his death, which will result in a tax and administration fee saving on death.
- **Tax benefits** during the client's lifetime (conduit principle [Section 25(B) and Paragraph 80 of the 8<sup>th</sup> Schedule of the Income Tax Act 58 of 1962]) and after his death (no estate duty and capital gains tax payable on death, as well as a saving on executors fees).

- **Protection.** Trust assets are protected against the claims of creditors and spouses.
- **Minor children.** Assets can be bequeathed to an *inter vivos* trust which was created for minor children. There will then be no need for the creation of a testamentary trust.
- **Succession.** No estate administration after the client's death.

People also often refer to business, property, investment and even family trusts. Note that these trusts are still either testamentary or *inter vivos* trusts. The only difference is that they are administered for a different purpose and most likely in accordance with a different risk profile. For example, a client may want to create a property or

business trust for high-risk investments (short term) and an investment or family trust for low-risk investments (long term). Other trusts created for a specific purpose include BEE, charitable- and Sharia trusts.

Trusts are therefore extremely effective estate planning vehicles, particularly when dealing with clients who would like to invest in growth assets, but also for other reasons as stated above.

An expert should however be consulted before advising a client on a suitable trust structure for his needs.

Contributions to this column came from FISA member Diederick Bisschoff, Fiduciary

Specialist at RMB Private Bank. A list of FISA-registered practitioners available from [secretariat@fidsa.org.za](mailto:secretariat@fidsa.org.za) Visit our website at [www.fidsa.org.za](http://www.fidsa.org.za) FISA is a non-profit organisation that represents practitioners in the fiduciary industry and sets high minimum standards to protect the public's interests. Activities of FISA members include but are not restricted to the drafting of wills, administration of trusts and estates, tax and financial advice and the management of client funds. FISA has 21 member companies and more 600 individual members who collectively manage in excess of R200 billion. Membership is open to any professional who meets the membership criteria.

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