



THE FIDUCIARY INSTITUTE OF SOUTHERN AFRICA



**UNIVERSITY OF THE FREE STATE**

**CENTRUM FOR FINANCIAL PLANNING  
LAW**

**TRUST ADMINISTRATION**

**EXAMINATION REPORT: FPSA BOARD  
EXAMS**

**NOVEMBER 2014**

**General comments:**

**PLEASE NOTE THAT THIS IS NOT A MEMORANDUM. THIS IS SUGGESTED ANSWERS. MARKERS MARKED WITH MISTAKES.**

**THE EFFECT OF RELEVANT ASSUMPTIONS WAS TAKEN INTO CONSIDERATION.**

It seems that the majority of the candidates have a good grasp of the technical and practical aspects relating to trust administration and is well versed in the current case law and the practical implications of a well vs a bad managed trust.

Overall there seemed to be little consistency where marks were lost on a single question, however it seemed that some candidates could have misinterpreted some one or two questions, however where this was apparent they were not penalised if their motivation was correct.

**QUESTION 1**

Question 1.1 – 1.6 is theoretical and questions to determine whether the candidates are *au fait* with the Trust Property Control Act and theoretical matters relating to trusts in general.

Question 1.4 required candidates to provide case law as a motivator, however when marking the question I realised that there is no specific notable case law to this question and gave all the candidates 1 credit for this question.

Most candidates did well in this section which is evident that these candidates were well versed in theoretical matters relating to trust Law and Administration.

- 1.1 Although the courts have consistently held that a trust is not a legal person, describe two instances where a trust is, per current statutes, given separate and independent status as a person. (2)

Income tax Act, value added tax Act and Transfer duty Act. The National Credit Act also makes reference to a trust, but classes it as a “juristic person” (Du Toit p10 1<sup>st</sup> edition and Du Toit 2<sup>nd</sup> Edition p 23)

- 1.2 The trustees of XYZ Family Trust utilised the personal bank account of the founder of the trust to deposit trust funds while they were waiting for the trust’s bank account to be opened. Discuss whether this action was valid and motivate your answer by referring to applicable legislation. (2)

No, s. 10 of the TPCA – must open a bank account – s 10 is absolute and no co-mingling of funds may occur – Du Toit 2<sup>nd</sup> ed page 90

- 1.3 Briefly discuss whether a testator may, in his will, stipulate that the trustees of a testamentary trust are empowered to create further trusts where at least one of the beneficiaries of the new trust is also a beneficiary of the testamentary trust. Motivate your answer, discuss the potential consequences of such a stipulation and refer to any relevant case law. (2)

No, it will amount to delegation of the powers of testation and render the provision null and void – *Braun v Blann & Botha* Trust Law and Practice page 6-26

- 1.4 Section 9 of the *Trust Property Control Act, 57 of 1988*, stipulates that a trustee must “act with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another”. However, a trust deed could contain certain provisions indemnifying the trustees from any liability in terms of this provision. Discuss whether such a provision would protect the trustee from any such liability and motivate your answer by referring to the relevant legislation. (2)

No it would not protect from any liability and at best only against any liability that would have arisen from such actions where the trustees could show that their actions complied with the standards that could have been expected of a trustee who acted with care, diligence and skill. A clause indemnifying a trustee against dishonest, gross negligence and negligence would therefore fall foul of section 9(2) and will as a consequence be invalid.

- 1.5 Apart from the founder and the trustees of a trust, name 4 (four) other possibilities of who may nominate trustees to a trust. (4 x ½ = 2)

Beneficiaries, if empowered by the trust deed

The Master

Other persons such as a person empowered by the founder/trust deed

Legislation

The Courts

Trust Law and Practice p 3-3

- 1.6 The trustees of a South African discretionary trust have passed a resolution, having been empowered by the trust deed, to distribute (in cash) all the capital gains realised during the trust’s financial year to the two capital beneficiaries of the trust. One of the capital beneficiaries is a natural person, but not resident in South Africa for tax purposes, while the other is a South African discretionary trust and resident in South Africa for tax purposes. The distributions are to be made in equal proportions. Assume that the attribution rules/deeming provisions (section 7(5) and paragraph 70 of the *Eight Schedule of the Income Tax Act, 58 of 1962*) do not apply.

- 1.6.1 Briefly explain the South African income tax consequences for the trust and/or beneficiaries as a result of the distributions being made and refer to the applicable legislation. (4)

Paragraph 80 (1) and (2) regulates the taxability of capital gains vesting in a discretionary beneficiary(½). This paragraph effectively reserves the application of the conduit principle(½), when distributing Capital Gains to a beneficiary who is a tax resident(½) of South Africa. If the beneficiary is a non-resident(½), the capital gains tax liability remains with the trust and cannot be ignored and applied in determining the net capital gain of the beneficiary in whom it vests(½). It is therefore important that a discretionary trust which distributes capital gains to non-resident beneficiaries accounts for the gains (for tax purposes) in the trust’s income tax return as it remains taxable(½) in the trust. For resident beneficiaries the gain will be ignored(½) in the trust and accounted

for in the hands of the recipient beneficiary in whom it vests(½). The legislation furthermore provides that if the recipient beneficiary is another discretionary trust, that trust will remain liable for taxation even though it distributes that gain in the same financial year to a its beneficiary i.e. a natural person.

- 1.6.2 Explain whether your answer would have been different had the distribution been made from trust income. (2)

Where income is distributed to a non-resident beneficiary(½), section 25B determines that the income would nevertheless be ignored in the hands of the trust and taxable in the hands of the beneficiary(½), subject to certain deductions (section 25B(4),(5) and (6)) being disallowed(½) in terms of section 25B(7), but by in large the tax liability of income distributed to non-resident beneficiaries is taxable in their hands(½) and not in the trust's. If the non-resident beneficiary is not a resident, certain income such as interest may escape SA taxation, Du Toit 2<sup>nd</sup> Ed page 166 and 146

[16]

## QUESTION 2

Questions 2.1 – 2.8 are true and false questions, but with the caveat that the candidates must motivate their answers to eliminate “guesswork”.

The questions were a combination of theoretical issues and case Law, but also practical issues arising in trust administration and some questions had a few “curveballs” thrown in to identify the top scorers.

It appears as if one or two of the questions were misunderstood, and this could have given rise to an incorrect “true or false” and the motivations could have led to a full mark even if the “true or false” answer was incorrect. Most candidates fared well in this section especially the high scorers.

Answer the following questions by stating whether they are true or false. Motivate your answer. If no motivation is given, no marks will be awarded.

- 2.1 Section 15 of the *Trust Property Control Act, 57 of 1988*, refers to “a person who audits the accounts of a trust”, and as a consequence a trust’s financial statements must be audited accounts, even if the trust deed does not specify that the accounts must be audited. (1)

False – although a trustee is required to keep proper records of trust affairs, the TPCA, nor any other statute requires these records/accounts to be audited. Where the deed does stipulate such a requirements, then it must be audited – *Deedat v The Master 1995(2) SA 377 Du Toit 2<sup>nd</sup> ed p93*

- 2.2 A company may not be appointed as a trustee given that the Master, when issuing a Letter of Authority, insists that a natural person must be noted on that Letter of Authority. (1)

False – section 6(4) of the TPCA facilitates the appointment of a corporation as a trustee, but stipulates that in such an instance a natural person must be nominated as the nominee of the corporation. Du Toit 2<sup>nd</sup> Ed p 74

- 2.3 A person who acted as a witness to a will is always disqualified from accepting the appointment as trustee of a testamentary trust created in that will. (1)

False, where the Courts are convinced that the testator was not defrauded or unduly influenced in executing his Will or where the Will was executed by at least two other witnesses who will not receive any benefits under the Will. S 4A(1),(2) and (3) of the Wills Act

- 2.4 A founder has provided the trustees of a South African discretionary inter vivos trust with a letter of wishes, which clearly states that this letter is merely a wish and has no binding effect on the trustees what so ever. According to recent case law, such a letter of wishes may, under no circumstances be used as evidence to call into question the independence of the trustees. (1)

False – Jordaan v Jordaan – where trustees “slavishly” follow the wishes in the LOW the courts have taken the LOW in consideration and held that the trustees in this instance were acting merely as nominal trustees and the Courts treated the trust as the founder’s alter ego. Du Toit 2<sup>nd</sup> Ed p 61

- 2.5 A discretionary trust is not freely accessible by the general public either for inspection or to obtain copies, whereas a testamentary trust is indeed open for inspection and to obtain a copy by the general public at the prescribed fee. (1)

True, Section 18 of the TPCA provides that only upon payment of the prescribed fee, the master *may*, subject to the provisions of section 5(2) of the Administration of Estates Act furnish a certified copy to a trustee, his representative *or any other person* if the Master is of the opinion that the person is satisfied that the person requesting the copy has sufficient interest in the document. In contrast a testamentary trust, which forms part of the Will, is therefore subject to section 5(2) of the Administration of Estates Act, which provides that any person is allowed to inspect and copy any Will lodged with the Master. Du Toit 2<sup>nd</sup> ed p 84/85

- 2.6 Section 21 of the *Companies Act, 71 of 2008*, makes provision for pre-incorporation agreements and as such a contract may be concluded on behalf of a company yet to be incorporated. Although no similar provisions are contained in the *Trust Property Control Act, 57 of 1988*, the application of common law provides that a contract concluded on behalf of a trust to be formed will also be valid. (1)

False, Common Law provides that such a contract will be invalid on the basis that a person cannot act on behalf of a principle if the principle is not yet in existence. Trust and Practice page 3-14

- 2.7 A trustee must keep documents that serve as proof of investments, safe custody, control, administration, alienation or distribution of trust property for a minimum period of 7 years. (1)

False, both sections 17 of the TPCA and the section 23 of the FIC Act 38 of 2001 prescribe a period of 5 years from the termination of the trust.

- 2.8 The concept of a “sham” trust has, on many occasions, been recognised and given effect to in our courts and where applied, the courts have consistently held that the trustees merely acted as “puppets” and consequently the trust was not validly constituted. (2)

False, the concept of a sham trust has to be distinguished from the alter ego principle and the sham principle has never been formally applied in our courts. The concept of a sham trust is often used liberally by trust commentators as an alternative for an alter ego trust. If a trust is held to be a sham, the trust de facto never came in existence whereas with the alter ego principle, the courts have merely followed a “look through” approach rather invalidating the trust in its entirety. Trust Law and Practice, p 2-18 and A legal-comparative study of the interpretation and application of the doctrines of the sham and the alter-ego in the context of South African trust law: the dangers of translocating company law principles into trust law, by ROWAN BELL STAFFORD New Van Zyl v Kaye case

[9]

### QUESTION 3

This question consisted of 3 subsections which were aimed at testing candidate's practical (day to day) knowledge about current issues regarding trusts administration. It was also clear that the low scoring candidates did not fare well in this section.

Most candidates indicated that they are well equipped to deal with these practical administration matters.

- 3.1 You are the professional advisor of a South African discretionary trust and during a trustee meeting (to which you were invited), the trustees raised the issue that they have had correspondence from a UK solicitor representing the deceased estate of an uncle of the founder (who is also a beneficiary of the trust). The legitimacy of the UK solicitor and the existence of the uncle and his estate have already been independently verified by the trustees and their local lawyers, especially given the many fraudulent schemes of this nature doing the rounds.

This correspondence notifies the trustees that the trust is nominated as the sole heir of all the late uncle's assets (all situated offshore). The solicitor is also requesting the trustees for further particulars of the trust in order for him to register the assets in the name of the trust. Discuss what you would advise during the trustee meeting, especially considering any SA exchange control provisions.

(3)

South African trusts as a rule may not own any foreign assets and where they do acquire assets by way of a foreign inheritance; explicit prior exchange control approval must be obtained in order to retain any assets abroad. In the absence of obtaining any such approval or where such approval is declined, the foreign assets must be liquidated and the proceeds repatriated back to SA.

- 3.2 You have been requested to review a trust deed to ensure that it complies with the latest legislation and case law and whilst perusing the deed, you note that there are indeed certain provisions that may need amendment. You also note that the trust deed contains the following amendment clause: *"The trust deed may be amended by agreement between the founder and the trustees"*. Explain the factors that you would need to take into consideration in order to amend the trust deed.

(4)

The variation clause is the most important factor to consider and that will govern whether the trust may be varied or not and if there are any limitations i.e. the variation of beneficiaries etc. The clause appears to be wide and therefore any provision including the beneficiaries may be amended by virtue of the power provided by the Deed. The next step would be to determine whether the donor is still alive as the amendment must be agreed to between the founder and the current trustees. If the founder is no longer alive, the only option to facilitate the

amendment of the trust deed would be to approach the courts to sanction such amendments. If the founder is alive, then any beneficiaries who have already benefitted or accepted from the trust previously must also be, together with the founder and the trustees, parties to the amendment (Jordaan v Jordaan case), given that a trust is considered a *stipulation alteri* and once a beneficiary has benefitted or accepted benefits from the trust, they have become parties to the deed. (Extra Mark) Finally it is paramount that the minimum requirement of number of trustees is in office in order to pass a valid resolution to enable the amendment. Du Toit 2<sup>nd</sup> edition page 50

- 3.3 You are approached by the trustees of ABC Trust (a discretionary *inter vivos* trust) to advise and assist with formalizing the appointment of a replacement trustee and obtaining a new Letter of Authority from the Master of the High Court. This is necessary following the demise of one of the existing trustees. The remaining trustees have also indicated that they want to ensure that the trust affairs are continued to be managed on an extremely prudent basis. You, however, note that the trustees reflected on the latest Letter of Authority are the founder, Mr X, his wife Mrs X and Mr X's father (the latter now deceased). The trust deed provides for the current trustees to appoint new or successor trustees. The current trustees are considering appointing Mrs X's father as the new trustee.

Explain, whether in your opinion, this will be a prudent choice and motivate your answer especially with reference to relevant case law.

(4)

Land and Agricultural Bank of South Africa v Parker, – It could be problematic especially in view of the Parker case where the Courts emphasized the importance of at least one independent trustee. In this case given that the newly appointed trustee would not qualify as an independent trustee. It would be advisable, if the trustees would want to ensure that the trust is managed by the trustees as a unit and on an absolute independent basis that at least one independent trustee is appointed instead of the wife's father, who will fall outside the scope of the requirement of an independent trustee. The Courts in the Parker case concluded that an independent trustee is a person who is not related/a family member or a beneficiary and should actively participate in trust decisions and cannot fulfill the role as a "passive" trustee" – In Nedbank v Thorpe the courts held that notwithstanding the appointment of an independent trustee, the trust was still managed on an "alter ego" basis. Even though the appointment of an independent trustee may create independence at first glance, it remains crucially important the trustees act as a unit and the independent trustee, notwithstanding his independence must play a very active role in the administration of the trust to ensure the effectiveness of the trust and to not fall foul of potential attack from creditors etc. Trust Law and Practice page 3-40

[11]

#### QUESTION 4

This question focused on factual case Law relevant to many existing trusts where the “efficiency” of the trust can be challenged in certain instances.

Most candidates fares well in this question, however some of the candidates did not do so well in this question.

It was evident that the candidates were very well versed in the relevant case Law although many of the other case Law are equally relevant to the circumstances.

It would seem that this important aspect of trust administration is well understood and candidates will be able to apply this in practice.

The alter ego principle, as applied by our Courts, has on numerous occasions resulted in the “veil” of discretionary trusts successfully being pierced. Briefly discuss whether the alter ego principle would, in your opinion, also be available to SARS for income tax and/or estate duty purposes, and if so refer to existing legislation that may assist SARS once the alter ego principle has been successfully applied to assess the trust’s assets, income or gains for income tax and/or estate duty purposes on an individual rather than the trust basis.

[4]

Yes, most definitely. The principle of “substance over form” is well established in our Income Tax legislation and if it is clear that the alter ego principle applies, SARS will be able to assess, given that there was no clear separation of control, the trust as merely an arrangement in form and therefore had no substance. Furthermore, the general anti avoidance rules (“GAAR”) contained in section 80 of the Income Tax Act may then be successfully applied for Income and Capital gains Tax purposes, resulting in the trust being ignored in its entirety for Income Tax purposes. As far as estate duty is concerned GAAR would not (yet) apply, however section 3(3)(d) of the Estate Duty Act may be applicable if the Courts found that in terms of the alter ego principle the founder was indeed in a position i.e. competent to dispose of the trust assets for his own or for the benefit of his estate and as a result, SARS may therefore also take the trust assets into consideration when assessing the founder for estate duty purposes. Also new Morrel case – “all purposes”

## QUESTION 5

This question had two sections. The 1<sup>st</sup> section tested the candidate's practical ability to perform day to day function relating to trust administration such as preparing and drafting trust minutes and resolutions.

Most candidates who completed this question indicated that they are capable of drafting these documents and identifying the pertinent matters relating to the preparation, finalisation and execution of such documentation.

The 2<sup>nd</sup> section was purely theoretical and given that it was the last question it would seem that those candidates who had time left answered this well.

5.1 You are provided with the following extracts from annual financial statements (for the year ending 29 February 2012) of the Leapfrog Family Trust, IT number 2011/3250, a discretionary inter vivos trust. The trustees had a trustee meeting that took place on 20 February 2012 during which the relevant decisions for the financial year ending 29 February 2012 were taken and unanimously agreed to.

From these extracts of the financial statements, prepare the necessary trust resolutions that would reflect the trustee's actions and decisions regarding any loans and distributions made during the trust's financial year, and stipulate the time frame within which the resolutions must be signed (if any). Assume that the trustees were empowered by the trust deed and that they complied with all other formalities to give legal effect to all the transactions. The settlor is Jumping Leapfrog and the beneficiaries are Jumping Leapfrog, his wife Pebbles Leapfrog and their major daughter, Mini Leapfrog.

(8)

**THE LEAPFROG FAMILY TRUST (“THE TRUST”)**

**REFERENCE IT 2011/3250**

**RESOLUTION OF TRUSTEES**

Passed on ..... 20.....

Resolved unanimously that:

The Trust will distribute the total rental income and the total capital gains made in the tax year ending 29 February 2012 to the Trust beneficiary **PEBBLES LEAPFROG** in terms of the Trust Deed.

The above amounts payable to **PEBBLES LEAPFROG** will vest in her on 20 February 2012. The amount will be owed by the Trust as a loan to **PEBBLES LEAPFROG**.

**JUMPING LEAPFROG** in her capacity as Trustee is authorised to sign all documentation to give effect to the above transaction.

**SIGNED AT ..... ON THIS ..... DAY OF .....20....**

\_\_\_\_\_  
**TRUSTEE:**  
**JUMPING LEAPFROG**

\_\_\_\_\_  
**TRUSTEE:**  
**PEBBLES LEAPFROG**

\_\_\_\_\_  
**TRUSTEE:**  
**POND HOLDINGS (PTY) LTD represented by JOE BLOGGS**

**THE LEAPFROG FAMILY TRUST (“THE TRUST”)**

**REFERENCE IT 2011/3250**

**RESOLUTION OF TRUSTEES**

Passed on \_\_\_\_\_ 20.....

Resolved unanimously that:

An amount of R123 000 (ONE HUNDRED AND TWENTY THREE THOUSAND RAND) will be paid from the Trust to **MINI LEAPFROG** as part of a repayment of the loan account owed to her by the Trust.

SIGNED AT \_\_\_\_\_ ON THE \_\_\_\_ DAY OF \_\_\_\_\_ 20...

\_\_\_\_\_  
**TRUSTEE:**  
**JUMPING LEAPFROG**

\_\_\_\_\_  
**TRUSTEE:**  
**PEBBLES LEAPFROG**

\_\_\_\_\_  
**TRUSTEE:**  
**POND HOLDINGS (PTY) LTD represented by JOE BLOGGS**

**THE LEAPFROG FAMILY TRUST ("THE TRUST")**

**REFERENCE IT 2011/3250**

**RESOLUTION OF TRUSTEES**

Passed on \_\_\_\_\_ 20.....

Resolved unanimously that:

An amount of R123 000 (ONE HUNDRED AND TWENTY THREE THOUSAND RAND) will be paid from the Trust to **JUMPING LEAPFROG** as part of a repayment of the loan account owed to him by the Trust.

SIGNED AT \_\_\_\_\_ ON THE \_\_\_\_ DAY OF \_\_\_\_\_ 20...

\_\_\_\_\_  
**TRUSTEE:**  
**JUMPING LEAPFROG**

\_\_\_\_\_  
**TRUSTEE:**  
**PEBBLES LEAPFROG**

\_\_\_\_\_  
**TRUSTEE:**  
**POND HOLDINGS (PTY) LTD represented by JOE BLOGGS**

- 5.2 Name four (4) changes to a trust that will require an amended Founding Statement of a Closed Corporation ("CC"), to be lodged with the Master of the High Court if the trustee is a member of the CC, and briefly explain why this is a requirement even though no CC may be registered after 1 May 2011. (4 x ½ = 2)

Any changes to the following will require an Amended Founding Statement to be lodged:

The Trustees of the Trust,

A change to the representative of the Trustee,

A change to the representative of the trustee, if that representative is a juristic person,

## The beneficiaries

This is a requirement to ensure that the beneficiaries of the trust, together with the members of the CC do not exceed 10 in number. If this does occur, i.e. where the beneficiaries and the members of the CC exceed 10 in number, it can become problematic as the provisions of section 29.(1A)(d) of the Close Corporation Act will render the membership void and even if the number of beneficiaries and members are brought below 10, this section will continue to apply once triggered. It is also important to note that although CC's can no longer be registered, there are still many CC's in operation and trustee must therefore be extremely vigilant when they are members of a CC or are acquiring a member's interest in a CC. Trust Law and Practice, page 8-36

**[10]**

**[TOTAL 50]**