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Page: 4

YOUR LETTERS

ON LIFE POLICIES, TRUSTS AND ESTATE DUTY

The questions I would appreciate answers to from a planning perspective are as follows:

1. A six-percent compounded deduction of the premiums for life cover as an estate-duty deduction on a deceased estate applies to natural persons. Does it apply where a policy is trust owned after the proceeds of the life cover are added back to the value of the estate?

2. A trust resolution dealing with an advance to the executor to settle estate duty and tax of the beneficiaries was passed soon after the trust was formed many years ago. What is the best way of dealing with this when required? Should it take the form of a loan to the estate? The view of the trust accountants was that this, in fact, reduces the value of the estate.

Name withheld

Phia van der Spuy, Fiduciary Practitioner of South Africa and director of Trusteeze, replies: If the life premiums were paid by the person who is entitled to the proceeds (a third-party beneficiary such as a trust), then a deduction of the aggregate of any premiums paid plus six percent compounded interest a year calculated from the date of inception of the policy until the date of death, is permitted against the proceeds, which are included as deemed property in the deceased's estate. This benefit is available only if a person other than the deceased (such as your trust) is the owner of the policy; that this person or entity pays the premiums on the policy; and is the person entitled to the proceeds of the policy – in other words, the beneficiary. If you have paid the premiums and the policy is paid out into your estate, or into a trust, you will lose this benefit.

Regarding your second question, due to the fact that a life policy held in a trust is dutiable in a deceased estate (after the deductions as discussed above), while the policy proceeds will pay out to the trust, often funds are not available in the deceased estate to pay estate duty on such life policies. In the event that the estate is insolvent and cannot pay the estate duty on the policy, the executor or SARS would be able to recover the duty from the beneficiary – for example, the trust. It will therefore be a cost to the trust.

The executor will only allow a loan from a trust to a deceased estate if the estate has sufficient liquidity to repay such a loan before its finalisation. This will not reduce the value of the estate – another asset will merely have to be liquidated to repay such a loan, and the net effect on the estate will be zero.

INHERITANCE TO MINORS

I am considering rewriting my will so that half of my estate will go to an unmarried adult son and remaining half will be shared between the two children of a married son when they reach 18. The children are eight years of age. What are the pros and cons?

Name withheld

Louis van Vuren, chief executive of Fiduciary Institute of Southern Africa, replies: Not having all the facts at my disposal, the following should be seen as general remarks and not as specific advice.

Depending on the value and nature of the assets that the minors will inherit, it may be best to leave such assets in a testamentary trust for their benefit. This is created in the will by including trust clauses in the will. After your death, the executor of your estate will then be obliged to set up and register the trust with the Master of the High Court, and the trustee(s) that you appoint in your will must then administer the trust in accordance with the trust clauses in the will. Such a testamentary trust for family members receives favourable income tax and capital gains tax treatment compared to other trusts, as long as the youngest beneficiary of such a trust is under the age of 18 years.

It is extremely important to ensure that the trust clauses in the will facilitate flexibility, proper administration and effective investment powers for the trustees. Professional help to set this up will be essential.

Unless a testamentary trust is created, any inheritance of substantial value that a minor becomes entitled to must be transferred to the Guardian's Fund under the control of the Master of the High Court. The Guardian's Fund is not equipped to hold fixed property or assets other than cash. A cumulative maximum of R250 000 can be released for the maintenance, education and general welfare of each minor beneficiary during the whole term the benefit is held for the beneficiary. Therefore, a trust is a better and more flexible option in general, specifically if the trust capital is needed to pay for things such as the minor's education.

Administration of a testamentary trust by professional trustees incurs costs, but these could very likely be offset by effective administration, flexibility and sound investment of the trust property.

If the inheritance is relatively small (for example, only a few hundred thousand rands) a trust will most probably not be effective due to the costs involved.

Leaving the inheritance to the parent of the minor does not safeguard the inheritance, nor does it ensure that the inheritance will be used for the benefit of the minor.