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WEALTH MANAGEMENT

Developments in Offshore Structuring

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Introduction

- Why is Offshore Structuring so Important?
  - Most SA Investors invest offshore – Often the bulk of their investments
  - As Fiduciary Advisors we should advise on the most appropriate structure
- Whether you plan or administer estates you need at least a working knowledge of
  - SA Tax implications of foreign structures and investments
  - Exchange Control,
  - Foreign Estate Taxes (E.g. Situs Tax)
- Offshore Structuring does not necessarily equal trusts
  - The most appropriate vehicle for an individual or family's financial needs may not be a trust structure

Controlled Foreign Companies (CFC) & CGT

- What is the highest effective CGT rate that may apply to individuals?
  - 18%?
  - 36%?
- A CFC is a foreign company where more than 50% of the participation rights (or voting rights) are held by SA Resident
  - Participation Rights: Benefits of the Rights attaching to a share
  - Sec 9D: Net income of CFC, proportionate to Participation Rights, imputed to SA Shareholder.
  - Taxable income includes taxable Capital Gains
  - Section 9D
- SARS CGT Guide (Issue 9): "If the CFC's gain is being taxed in the hands of an individual, it is appropriate that it should be taxed at the inclusion rate applicable to individuals of 40%." (My underlining)
  - "Appropriate"….Apparently not
  - Issue 9 – 5 November 2020

Controlled Foreign Companies (CFC) & CGT

- Sec 9D(2A)(f) Amended
  - Words “Natural Person” and “Special Trust” were deleted and therefore the 40% inclusion rate of capital gains does not apply for natural persons anymore.
  - By implication 80% of Capital Gains will be included in net income of CFC and imputed to SA Resident shareholder.
  - Therefore possible max effective CGT rate of 36% (80%x45%)
- Example
  - Family owns all the shares in a US company
  - US company holds substantial assets
  - Family decides to liquidate. (Following the father’s death)
  - Shareholders has 100% of Participation Rights, therefore CGT at max. 36%!
  - Section 9D
  - Explanatory Memorandum

Foreign Estate Taxes (Situs)

- Most Advisors know: When an SA estate holds foreign situs assets, Estate Taxes in that jurisdiction may apply – often at a much higher rate than SA
  - Situs Assets E.g. Listed Shares
  - US & UK – up to 40%
  - SA Credit only up to 20%(or 25%)
  - (Using the US for all examples)
- Is there really a risk if the if the Situs Assets are not reported to the IRS (or equivalent)?
- We can't say that the IRS will find out about estates that are not reported but consider the following:
  - The executor is and remains personally liable for payment of FET to the IRS
  - When assets are transferred to heirs, they become personally liable.
  - Do not underestimate authorities ability to mine third party data.

Foreign Estate Taxes: Practical Guidance

- Returns for Federal Estate Taxes (FET) should be filed and taxes paid within 9 months from date of death
  - IF not: Penalties and Interest
  - Different from SA Process: In US filings need to be made regardless whether estate is probated or not.
  - Do not fall foul of these time limits – IRS is a lot less efficient than what you are used to dealing with SARS!
- Returns are complex – ensure that you use a suitably qualified professional in the jurisdiction
  - Their services are expensive – often between $10k-&20k
- As a planner, rather steer clear of situs assets – there are other options that do not attract situs tax. (Unit Trusts, ETF's, Offshore Endowments)
- Trust structures work, but are expensive and should be considered carefully
- Final thought: As an advisor we can never advise a client to willfully evade tax – regardless of the jurisdiction!

Exchange Control Developments

- Quite a number of important Circulars issued by Fin Serv
- 7-2022:
  - Residents may retain donations received from non-resident without having to declare
  - This applies to distributions from foreign trusts as well!
  - Residents may also retain Inheritance from South African estates abroad – executor/heir therefore does not need to apply for exemption of Regs 6&7 anymore
  - SA Residents may also lend and dispose authorized foreign assets to other SA Residents
  - Only applies after 23-02-2022.
- 8-2022: Special Application for amounts above R10m may be invested in foreign trusts

Exchange Control Developments

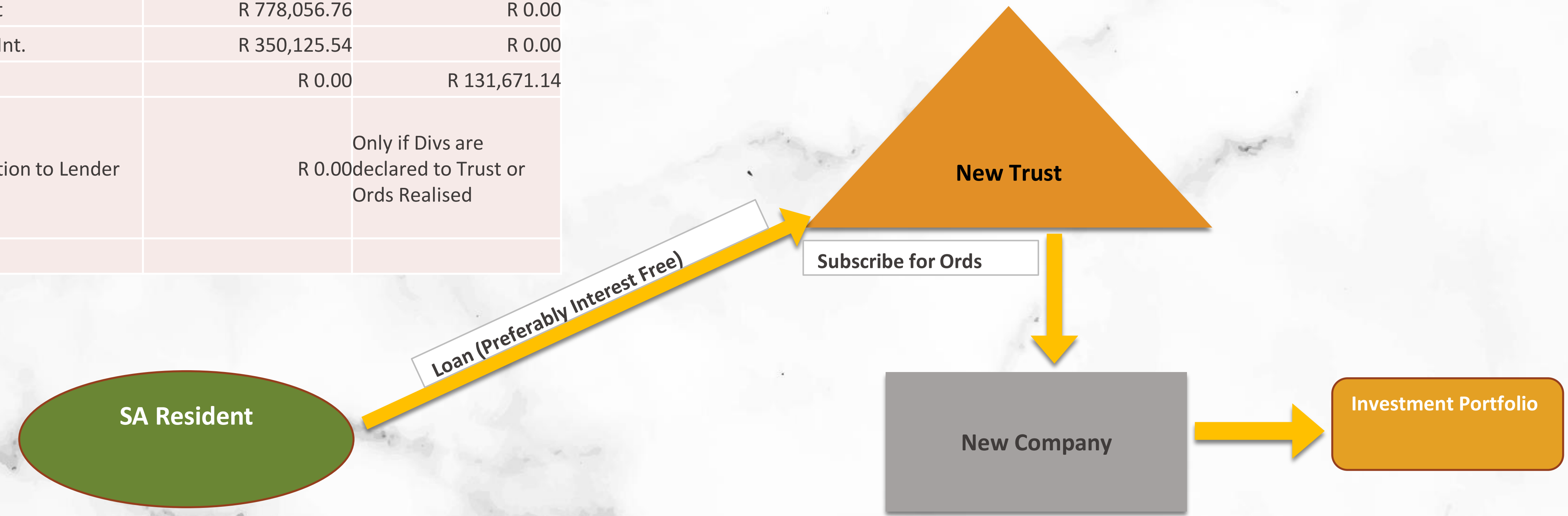
- Note: No indication that SA trusts may own foreign assets. (To the contrary)
- Loop Structures (1-2021)
  - The circular lift the loop structure restrictions
  - Loop Structure Example: SA resident settles an offshore structure with authorized foreign assets. The structure then invests in an SA Asset – e.g. company shares
  - In terms of the Circular, a loop structure should merely be reported to Fin Serv once completed
  - BUT: It seems that Fin Serv has made an about turn on Loops
  - Apparently applications are not being approved or share certificates endorsed – Let's Wait and See…
- **Concerning Development**: SARB informed Authorised Dealers that they will no longer permit Testamentary trusts to inherit foreign assets!
  - (Then the very next week they approved an application!)

Considerations: Offshore Structures

- Your Objectives with the structure
  - Estate Planning: Capping the Estate, Succession Planning etc.
  - Retirement Planning
- Tax Implications
  - Funding (loans, equity, contributions)
  - Ongoing Tax Implications. (Attribution, Controlled Foreign Company etc.)
  - Implications of withdrawals from the structure
- Residence Status of beneficiaries
  - There are exceptionally negative tax implications for beneficiaries of foreign trusts in some jurisdictions.
  - E.g. USA, Australia – In some cases the tax implications may exceed the amount of distribution
- NB: Cost of the Structure
  - Always consider the cost of maintaining the structure in relation to the quantum of the investments.
  - Trust structures: £5000+ per annum
  - Offshore Retirement Funds: £2500 per annum

Offshore Structure Funding: Interest Free Loan

	Interest	Interest Free
Loan	$1,496,263.00	$1,496,263.00
Interest	R 778,056.76	R 0.00
Tax on Int.	R 350,125.54	R 0.00
Sec 7C	R 0.00	R 131,671.14
Attribution to Lender	R 0.00	Only if Divs are declared to Trust or Ords Realised



Implications of Some Offshore Financial Products

- Dollar Life Plan
  - This is a foreign life policy (pure life) on the life of a South African Resident
  - If the policy pays to the estate = "Property" for purposes of sec 3(2)
  - But if it pays to a beneficiary, it cannot be "deemed property" for purposes of sec 3(3) as it is not a "domestic policy"
- Foreign Endowments
  - Use as investment platform
  - Beneficial tax rates under 5-Fund approach (If held my individual of trust)
  - Effective Situs-blocker
  - Asset in the Estate
- Foreign Pensions
  - Many benefits including contributions off-balance sheet and not Estate Dutiable, only taxed on benefits,
  - **BUT: Must be structured and intended for provision of retirement funding not some quasi-estate planning structure**

Thank You