Dear Sir/ Madam,

The South African Revenue Service’s Draft Guide on the taxation of special trusts refers. We hereby present the SAICA National Tax Committee’s response to your request for comments.

General comment:

We found the guide to be useful and believe it would assist those involved with special trusts to gain an understanding of the provisions of the Income Tax Act relating to such special trusts.

Comments with regard to the Glossary:

‘CGT’

The statement that it ‘means capital gains tax’ is wrong and should be removed. We don’t have a ‘capital gains tax’. The rest of the description is correct.
Comments with regard to paragraph 2 – background

The definition of “special trust”, upon its initial introduction into section 1(1), with effect from the 2002 year of assessment, only referred to a trust created solely for the benefit of “a person” who suffers from a defined mental illness or a serious physical disability.

We are not sure that it is correct to say that the special trust was initially introduced in 2002. It was previously catered for in the Appendix to the Taxation Amendment Acts and its meaning was much the same.

Tax rate comments

The guide states that “a single rate of tax of 40% for trusts was introduced with effect from the 2003 year of assessment to combat the practice of income splitting through the use of multiple trust structures. This higher rate of tax does not, however, apply to special trusts which are taxed under the same rate structure as natural persons.”

This statement is hardly relevant to a special trust and should be deleted. The relevant part is that the flat rate (40%) does not apply to a special trust. The introduction of the flat rate had no impact on a special trust.

The special trust was previously defined for purposes of the tax – the Explanatory Memorandum stated ‘such a special trust is effectively, for purposes of income tax and capital gains tax, regarded to be a natural person.’

Comments with regard to paragraph 4.3.3 - The sole benefit requirement

The guide states that “the trust should be created solely for the benefit of one or more persons who is or are persons with a disability. In essence, this means that the trust deed must not provide for the possibility of any beneficiary who does not have a “disability” as defined in section 6B(1).”

We agree that this is correct in terms of the law. There is a practical problem that it is potentially possible that the trust deed would have to deal with the cessation of the trust for
instance after the death of the beneficiary (the person with a disability). In essence the remaining assets or capital of the trust must be dealt with after the death of the beneficiary.

We submit that as long as the beneficiary was (the person with a disability) was the only beneficiary while he or she was alive, the fact that another beneficiary benefits from the trust after his or her death should not disqualify the trust from being a special trust.

We propose that the guide deals with this issue.

Example 2 hints at this when it states in the solution that “The fact that the children of C may be added as beneficiaries as long as B is alive disqualifies the trust from being classified as a type-A trust.” This implies that where beneficiaries are added after death of the person with the disability, the trust would still qualify as a special trust.

Comments with regard to paragraph 4.3.4 - The incapacity and financial management requirements

The guides states the following: “A trust will not qualify as a type-A trust if a beneficiary of the trust is a person with a disability but is still able to earn sufficient income for that person’s maintenance and is able to manage that person’s own financial affairs.”

It is clear from the legislation that it is only one of the two requirements that have to apply. The reason is that they are separated by an “or” (earning sufficient income for their maintenance, or from managing their own financial affairs). The ‘and’ in the paragraph should therefore be replaced by an “or”.

It would be useful if the guide gives some indication of examples of when a “disability incapacitates such person or persons from earning sufficient income for their maintenance”.

Comments with regard to paragraph 4.4.3 - The “living beneficiaries on the date of death of the deceased” requirement

The guides states that “it follows that a trust will not qualify as a type-B trust if it allows for the unborn and not conceived descendants of the testator to benefit under the trust formed after the testator’s death.”
We agree that a beneficiary that has not been conceived before the date of death of the deceased will disqualify the trust from being a type-B trust. The emphasis is therefore not on “unborn and not conceived descendants of the testator” as is stated, but rather on the fact that the beneficiary was not yet conceived at the date of death.

It would be clearer to simply say that if the last will and testament also includes as beneficiaries persons conceived after death it would not be a type-B trust.

*Death of a beneficiary and example 7*

The guides states that “a trust will not qualify as a type-B trust if one of the qualifying beneficiaries of the trust dies before the date of death of the testator and the estate of that beneficiary benefits from the trust.”

We are not sure that the statement (in the facts in example 7) that “The MN Trust was created on 15 October 2013” is correct. The first point is that the trust is created in terms of the last will and testament. We are not sure in what context the word ‘created’ is used here. The date of death was 16 August 2013 and this implies that the estate in the period between date of death and ‘creation’ was not a special trust.

Example 7 then states that “the MN Trust will qualify as a type-B trust for the benefit of M if N’s estate will not benefit from the trust. Should N’s estate benefit from the trust, the trust would not be solely for the benefit of living beneficiaries of the trust and it would be disqualified as a special trust.”

It does not provide detail of whether or not the beneficiaries may be relatives of the deceased. It is possible that the beneficiaries of N’s trust may well be beneficiaries of the deceased and then indirectly meet the requirement.

*Comments with regard to paragraph 4.5 - Resident status of a special trust (type-A and type-B) and of the beneficiaries of a special trust*

The guide states that “the tax residency of a special trust, that is not a resident of the RSA, is of course only of any relevance if such special trust derives gross income or capital gains and is accordingly subject to South African tax.”
That statement is not quite right – if the trust is a resident of the RSA it will be a taxpayer. If not, it will only have tax consequences if the source of the income is in the RSA. See the notice dealing with the submission of returns of income. It states that the following persons must furnish an income tax return:

(a) every company, trust or other juristic person, which is a resident;

(b) every company, trust or other juristic person, which is not a resident-

(i) which carried on a trade through a permanent establishment in the Republic;

(ii) which derived any capital gain from a source in the Republic; or

(iii) which derived service income from a source in the Republic.

Comments with regard to paragraph 5.1 Provisions of the Act applicable to a special trust (sections 7 and 25B)

The guide states that “the provisions of the Act relating to a special trust will only apply if income is taxable in the trust.”

What is the intention with this sentence? The fact that the trust doesn’t have taxable income can’t mean that it is no longer a special trust.

Comments with regard to paragraph 5 - Income tax provisions relating to a trust constituting a special trust (type-A and type-B trusts)

General

The 2015 implications and figures in the examples should also be included as we are currently in this year of assessment and taxpayers need to be aware of the tax implications of transactions or arrangements been made or to be made.
Deductions

The guide doesn’t deal with deductions that may be made against the income of the trust. It also doesn’t deal with the apportionment of expenses (deductions or allowances) in a trust. It is suggested that the guide be amended to include a brief discussion on deductions in general and on apportionment specifically.

Comments with regard to paragraph 6 - CGT provisions relating to a special trust

Example 15

The word taxable should be removed after the words “The capital gain of R1, 4 million is”. The gain is to be disregarded because the exclusion applies.

Comments with regard to paragraph 7 - Procedures to register as a special trust for income tax and CGT purposes

We suggest that it is appropriate to include reference to the registration process of a trust with the Master of the high Court for completeness.

Comments with regard to paragraph 8.8 - Transfer duty

We suggest that this guide should refer the reader to SARS’s guide on Transfer duty.

Comments with regard to Annexure A - Whether a trust is regarded as a special trust for income tax and CGT purposes (Definition of “special trust” in section 1(1))

The decision tree in Annexure A is quite useful.
Our comment relates to the question “Was at least one such person still alive on the last day of the year of assessment of the trust?”

We submit that the “one such person” in the question should be replaced with beneficiary or beneficiaries. This would be more in line with the wording used in the rest of the Annexure.

Please do not hesitate to contact us if you have any questions in this regard.

Yours faithfully

Piet Nel CA(SA)
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The South African Institute of Chartered Accountants