



# TRUSTS AND ESTATES ALERT

## DOES IT FALL IN MY ESTATE? – PART 2

In this alert we continue our focus on assets that may or may not fall into your estate. To determine whether an asset falls into your estate, you need to determine the following:

- Are you are the outright owner of the asset?
- Can you determine in your Will who the asset must go to on your death and whether the asset will be dealt with by your executor?
- Does the asset attract estate duty irrespective of whether you are the owner and whether it is dealt with in your Will and by your executor?

### Trusts

If you have created an inter-vivos trust, as a general rule you cannot deal with those assets in your Will. An inter-vivos trust is created either by donation or as a loan account in the books of the trust.

In the case of a donation, the asset belongs to the trust, not to you. With a loan account, the asset no longer belongs to you, but your estate may have a claim against the trust to the value of the loan account or the amount outstanding at your date of death. This becomes an asset in your estate that must be allocated. The introduction of capital gains tax (s12(5) of the 8th Schedule of the Income Tax Act) has complicated the method of relinquishing the loan as a legacy to the trust.

Certain trust deeds intend to reserve testamentary powers for the benefit of the founder over the trust's assets. You would be well advised to consider the terms of your deed as to whether you have such powers and intend to exercise these powers in your Will. Since creating a trust and handing over its assets is legally irrevocable, we do not recommend applying these provisions and prefer the route of using Letters of Wishes.

It may also be that, as a beneficiary of a testamentary or inter-vivos trust, you have vested rights as opposed to a discretionary hope. These rights usually terminate on your death and any undistributed income that is vested would be an asset in your estate, but the capital will remain as part of that trust. These amounts are usually not substantial.

### Limited Interest

Certain assets may have been bequeathed to you on a limited interest basis. This means that you have the right to enjoy these assets or the fruits of the assets, but you generally cannot sell the assets during your lifetime. More importantly, you cannot sell determine who will be the beneficiaries of these assets after your death.

Classic forms of limited interest are *usufructs* and *fideicommissums*. In the case of a *usufruct*, the ownership vests in someone else, while you are entitled to enjoy the benefits of the assets. With a *fideicommissum*, the ownership vests in you and you can enjoy the benefit (and in limited circumstances, sell the asset) of the asset, but again, you cannot determine to whom the assets should go after you die.

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A complex form of a limited right, known as massing, may have been created through a joint mutual Will, usually created by married couples. The assets of both parties are pooled and the first dying spouse determines who will own the assets, subject to a limited interest or use of some or all of the assets by the surviving spouse. In this case, the surviving spouse cannot deal with the assets in their estate if they have "adiated" or accepted the benefits of the estate as part of their inheritance. Consequently, the second spouse to die can only deal with any additional assets acquired as their own as the first dying spouse's Will determines what happens to pooled assets.

With all forms of limited interest, you do not own the asset and you cannot determine who inherits the asset. However, the asset forms part of your estate for estate duty purposes, in that the term "property" is expanded in the Act to include limited rights (see s3(2)(a) and (b)). The formula to calculate a ceasing limited interest is set out in the Act. It is largely dependent on the full ownership value of the assets, the life expectancy of the person who will receive full ownership and the yield the asset is expected to generate over the period.

### Life rights

You may have a life right to an asset. A common form of this is the life right that can be acquired in retirement villages that are subject to the Housing Development Schemes for Retired Persons Act, No 65 of 1988. In terms of the agreement entered into between the occupants and the retirement village's, management company or developer, your right to enjoy the property terminates on your death. Whether another party is entitled to enjoy the property after you die, or whether the property must be sold and the proceeds dealt with, are determined by the terms of the contract.

### Corporate entities

If you have structured your affairs so that certain assets are held in a close corporation or company, you need to realise that even if you were the sole funder of the acquisition, the property is owned by the relevant corporate entity and managed by the member(s) of the close corporation or the director(s) of the company.

Your interest in these entities is limited to the value of the membership interest or value of the shares that you own. You cannot, in your Will, direct how the underlying assets of the corporate entity must be used or distributed. You may direct to whom any of your loans can be ceded or to whom the membership interest or shares must

be transferred. Such distribution is subject to any contractual terms concluded as embodied in any association agreement or memorandum of incorporation.

Often in business ventures, such document will provide for a right of pre-emption for fellow members or shareholders to buy out your interest, so restricting unfettered distribution to your own beneficiaries. In the case of an unlisted company, the value of the shares is determined by the company auditor and subject to the revenue Inspectors endorsement, to determine the value for estate duty purposes.

### Offshore/Foreign Assets

Given the most recent amnesty and extensive relaxation of exporting foreign funds, it is not uncommon to have interest and assets in foreign countries. These assets, in any form, are part and parcel of your estate. Generally, a local executor will be unable to deal with these foreign assets unless he is given authority to do so by the proper officials in that foreign jurisdictions. It is better to provide a separate Will for different jurisdictions, but care should be taken that these Wills don't inadvertently revoke any others and that your overall scheme of testation is still achieved.

As far as executor's commission is concerned, the general principle is that the executor is entitled to commission on those assets that come under his control and that he deals with them in his liquidation and distribution account.

The Estate Duty Act is clear that for purposes of calculation of your estate duty, your entire worldwide estate must be taken into account. However, s4(e) of the Act provides some relief in that the value of any overseas assets that were acquired before you became ordinarily resident of South Africa for the first time as well as any assets that you acquired offshore by donation or inheritance from a person who was not a resident in South Africa at the time, is deducted from the value of your assets. Therefore, such qualifying assets are not effectively dutiable.

### Some unusual assets

You may be the co-owner of an asset that you have all but forgotten about. Typically this takes the form of an inheritance of a minority interest in an asset with other joint beneficiaries or owners. In general, the issue of co-ownership should not be expanded so it is often best to grant other owners the right to acquire the asset as a right of first refusal.

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It may appear that you are the owner of certain assets but on closer scrutiny you may hold them as a nominee or in Trust for another person (for example as an estate agent) and these would be excluded from your estate for all purposes.

You may hold property of another given as a pledge or held as a lien as security for a debt due to you. In this instance, the property does not form an asset in your estate but the obligation quantified will be an asset.

You may have an interest in property without being the owner, for instance, you may have rights that entitle you to royalties based on copyright or a licence agreement over a patent. You may even hold an interest in the physical property of another person in the form of mineral rights. These rights have values and their valuations are often complex to determine but generally approximated based on future income flow based on specialist calculations.

## Conclusion

If you fail to recognise an asset as belonging to you or being included for the purpose of estate duty, the entire scheme of your devolution plan could be upset. Similarly, to deal with an asset that in fact does not belong to you may, depending on the wording in limited cases, create an obligation for your executor to acquire the asset.

Clearly, preparing a Will requires thorough preparation, which includes a detailed analysis of assets that are under your control or that you are entitled to enjoy. For the exercise to be most effective, you might need to refer to earlier Wills and other legal documents, such as marriage contracts, association agreements, memorandum of incorporation and trust deeds and other contractual and financial documents.

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