OVERSEAS TRUST & PENSION

Why International Pensions represent the future of trust structures for effective wealth preservation.

Executive Summary

In this article we consider and compare discretionary trusts and international pensions. The conclusion reached is that international pensions provide many of the sought-after features associated with trusts but without the drawbacks.

The future for Discretionary Trusts is becoming increasingly uncertain. World-wide, Governments are imposing high rates of tax and International reporting requirements on Trust structures. The common misconception that Trust structures are used by the wealthy to minimise or mitigate tax means that Trusts have become politically sensitive in these times of austerity.

SARS Proposals

We only need to look at the changes proposed by Pravin Gordhan in his 2013 budget speech whereby discretionary trusts would no longer be taxed according to the flow through/conduit principle, i.e. according to the conduit principle all income and gains distributed by the trust to a beneficiary are taxed in the beneficiary's hands (between 18% - 40% income tax or up to maximum 13.3% CGT).

This would represent a dramatic change with Trusts paying income tax at a flat rate of 40% and CGT at an effective rate of 26.6% (trusts don't qualify for the rebates available to individual tax payers). Using trusts as a way to mitigate paying taxes will simply no longer work.

Government Perspective

Against a background of increasing longevity Governments actively encourage individuals to save for their retirement and favour retirement structures and pensions. What's more the legislation that supports retirement provision is specifically developed to minimise tax and protect the individual's assets.

A Modernisation Opportunity

This landscape presents a threat to all clients holding trusts but also an opportunity for people to modernise their affairs through the use of international retirement plans. The end result is a structure that avoids the pending pitfalls of trusts but retains many of the advantages. International retirement plans provide a modern, acceptable and robust environment which in many cases will also prove significantly more cost effective to run.

The Retirement Annuity Trust

OPES International Retirement Plan is a Retirement Annuity Trust based in Guernsey, with its trust deed tailored specifically for South African tax residents:

	OPES International	Discretionary Trusts	SA Retirement Annuity
Set up	• Contributions to OPES are not subject to donations tax as they are a contribution and not a gift • Uncapped contributions	• Settlement is subject to 20% donations tax • Or trusts set up by way of loan avoid donations tax but the loan remains an asset of the settlor's estate and is subject to estate duty of 20% • Loans have to be disclosed to SARS and are taxed at a commercial rate of interest	• Current tax deductible contributions of 15% of NRFI • Proposed changes from 2015 will increase the deduction to all approved retirement funds to 27.5% - but this will now be capped at R350K p.a.
Growth	Tax exempt growth in the accumulation stage (much like local RA's)	Income and gains withheld in the trust are taxed at 40% and 26.6% respectively	Tax exempt growth
Income	• The initial contribution can be returned with no tax payable. Growth distributed will only incur CGT at max rate of 13.3% • Full access to capital from age 50	• If income/gains are distributed – currently taxed in beneficiary's hands according to conduit principle* (18-40% income tax and up to max 13.3% CGT) • *The conduit principle is under scrutiny and proposed changes would tax income and gains at trust level making the trust tax inefficient	• Conventional annuities and living annuities taxed as income between 18% - 40% • Max 1/3 in cash – with up to R500K tax free depending on previous withdrawals, resignations etc. from all retirement funds

	OPES International	Discretionary Trusts	SA Retirement Annuity
Estate Planning & Succession	• Assets owned by OPES so no longer form part of the deceased's estate saving 20% in estate duty • Can nominate anyone as a beneficiary so that, on death, assets pass seamlessly to family/ loved ones • Process can take days compared to the winding up of an estate which takes months, sometimes years	• If assets settled by way of a loan – the loan remains the property of the deceased's estate and therefore subject to estate duty • Danger that settlor is seen to retain control of the trust assets – which will result in the assets being deemed as property of the estate and subject to estate duty of 20%	• Fall outside estate and not subject to 20% estate duty • Subject to Section 37C – the trustees are legally obliged to distribute benefits to legal and factual dependants first
Probate	No need for an executor saving on their fees (up to 3.99%)	Loan account part of estate and subject to executor fees of up to 3.99%	No need for executor
Asset Allocation	Open architecture with no prescribed limits	N/A	Subject to Reg. 28 with Max 75% in Equities (includes up to a max of approx. 25% offshore)

The above table serves as a synopsis and is based on our current understanding of the generic features and tax treatment of the products listed. The table and its content do not constitute advice of any type and should not be interpreted as such. The exact treatment of these structures may differ from client to client and we recommend that individuals seek independent tax advice before investing in any product.

Conclusion

OPES provides an opportunity for individuals to increase their retirement capital in a tax-efficient and flexible manner, but it also provides all the benefits of a typical trust structure and more. In summary, it is clear that the OPES International Retirement Plan, represents the future in terms of efficient wealth structuring for creating, preserving, and eventually passing on one's wealth.