Legal and Technical Update

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Note from the editor

Sharon Teubes, Senior Legal Adviser: Advice and Wealth Management

The National Budget has come and gone, and for some it was less eventful than anticipated. More tax increases were expected and we can simply breathe a sigh of relief. In my opinion it was a well balanced budget thought out by a new finance minister who wanted to please the nation whilst meeting his key performance areas.

As we know, income tax was increased by 1% which will impact those who earn in excess of approximately R180 000 per annum. We will also feel the extent of the increase in the fuel and electricity levies. However, this was well planned and well-timed as inflation was lower than expected over the last few months.

We are eagerly awaiting the draft legislation to see what other changes will in fact become a reality and to what extent. One change that we are surely looking out for is the inclusion of non-deducted contributions made to retirement funds into the dutiable estate of
the deceased. This will surely have estate planning implications and also pose a challenge when doing financial planning for clients – since many clients will not have the figures readily available.

Thus, this will again be an interesting year in the world of financial planning, and we will certainly keep you up to date as it happens.

In this month’s edition we introduce one of our very capable and knowledgeable fiduciary specialists. Tanya Cohen takes a look at the impact minor beneficiaries have on succession planning. We also include the ‘Fiduciary Corner’ – something that will become a regular addition to Leverage in the future. This section will provide you with short, concise information, to assist you in building up a wide knowledge base to ensure the best possible advice for clients on estate and succession planning.

Happy reading!
Who will look after a minor’s inheritance?

By Tanya Cohen, TEP, Senior Fiduciary Specialist at Momentum Trust Limited

When advising clients on their succession planning, it is very important that bequests to minor children are discussed and the appropriate provisions made. In general, this entails setting up a testamentary trust that will receive the assets on behalf of that minor.

Something that is often overlooked is what happens to benefits payable to a minor child (as a result of one’s death) by a retirement fund or a life insurance policy. Clients need to be properly advised in relation to the differing rules and practices of life companies, and pension or provident fund trustees in this regard.

Retirement funds

The trustees of a retirement fund must distribute a deceased member’s death benefit to members’ dependants (as defined in the Pension Funds Act) and/or nominated beneficiaries according to what they believe is fair and equitable. This is not necessarily in accordance with members’ wishes set out in their wills and/or beneficiary nomination forms.

Where a dependant or beneficiary is under the age of 18,
the trustees must decide whether to pay the money:

a) to the minor child’s legal guardian (if any). A potential disadvantage to this is that money intended to be set aside for children may easily be consolidated with the legal guardian’s own funds and not invested and/or expended as the testator originally intended; or

b) to a trust already established or provided for in their will. The trustees will generally be willing to make payment to such a trust, provided that the minor child or children are the only beneficiaries of the trust. Therefore, a separate testamentary trust created for the benefit of each child is a safe option to follow. Most trustees will also accept an inter vivos trust, where that trust is created during the lifetime of members and where the minor children are the beneficiaries of that trust. It is important to note that the board of trustees of the fund have a fiduciary duty towards the beneficiaries and this duty can be exercised differently by different boards. Therefore, it is important to consult with the fund when appointing the beneficiaries to determine if the nomination will be acceptable to them.

c) If there is no legal guardian or appropriate trust
then the benefit will be paid into a beneficiary fund. A beneficiary fund is a fund established to administer and invest benefits, referred to in Section 37C of the Pension Funds Act, on behalf of beneficiaries, payable on the death of members of pension funds. The disadvantage of this option is that the funds are paid out of the beneficiary fund when the minor child turns 18, regardless of whether that is appropriate in the circumstances of the child or children. The advantage is that the administration costs tend to be lower than the costs charged by trustees of a testamentary trust.

Life insurance policy proceeds

Clients often appoint their minor children as beneficiaries. This in itself can have practical implications that clients might not be aware of. Alternatively, no beneficiary is nominated with the idea that the benefit goes to the minor via the will. If there is no named beneficiary, the proceeds will be paid into the estate of the policyholder. If the will is correctly drafted, the proceeds will be dealt with by the executor and paid into the testamentary trust set up for the minor children in terms of the will. The disadvantage, as compared to nominating the children as beneficiaries on a life policy, will be that executor’s fees will be payable on the value
of the proceeds of the policy. Where a minor child is nominated as a beneficiary, executor’s fees will not be payable.

Note: You may create a liquidity problem if the minor(s) are the beneficiaries of the total proceeds of the life insurance policies. It is recommended that the liquidity needs of the estate are always considered when appointing beneficiaries to ensure all costs and taxes can be settled.

If a minor is appointed as a beneficiary, the life company will generally pay as follows:

a) To the minor’s guardian if there is one, or upon the instruction of the guardian, into the minor’s bank account. If this option is chosen then the legal guardian must sign the claim forms on behalf of the minor.

b) Pay to a trust established either inter vivos or in the deceased’s will specifically for the proceeds of the policy payable to the minor child. A formal request will need to be made to the insurance company.

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to make payment to the trust. In most instances payment is made to the trust – especially where the minor is the only beneficiary or the minor and the guardian are the only beneficiaries of that trust. However, whether they will apply their discretion to favour the trust and not the minor’s guardian or the minor themselves will depend on the insurance company in question and the circumstances of the case.

c) Pay to the guardian’s fund. Where there is no guardian and no trust was created for the benefit of the minor child, the life company may pay to the guardian’s fund. This will generally be a last resort. The disadvantages of the guardian’s fund are that the benefits are invested with the Public Investment Commission at a fixed rate of interest (7.25% for 2014/2015 year). The Master is entitled to pay all accrued interest as well as up to R250 000 from the invested capital for maintenance needs (that can be motivated). Ordinarily a minor can claim the invested money as well as the accrued interest on reaching the age of majority (generally at age 18).
Note: that payment to a beneficiary fund, as provided for in terms of the Pension Fund Act cannot be used as a beneficiary for life insurance policy proceeds.

If you want the proceeds of a retirement fund or life policy to go to a testamentary trust created in your will, it is recommended that the beneficiary nomination specifically state: “my children, Jack and Jill, to be paid to the testamentary trust created in my will” or alternatively, “the testamentary trust created in terms of my will for the benefit of all my minor children”. The will may also specifically state that the testamentary trust will be the recipient of any amounts intended for the minor children (or children whilst they are still below a specified age) from clients’ personal estates as well as any amounts payable for their benefit in terms of any life policy or retirement fund, or otherwise a consequence of the testator’s death. The executors will then create the testamentary trust and thereafter any life policy or retirement fund death benefits can be paid directly by the relevant life companies to the testamentary trust. They will thereby be excluded from clients’ estates for the purposes of executor’s fees.

Another option to consider would be nominating an inter vivos trust. The disadvantage of this option is that an
inter vivos trust will not qualify for the ‘special trust’ tax

dispensation that a testamentary trust for minors would.

‘Special trusts’ are (in general terms) taxed at the same

rates as individuals, rather than the higher inter vivos

trust tax rates.

Note: Where a testamentary trust is nominated it is

common practice for the life office to request a copy

of the will and the identity documents of the minor

children.

Conclusion

It is therefore very important to consider the practical

implications of inheritances intended for minor children

so that clients can make informed decision and ensure

that the funds actually benefit those it was intended for.

Fiduciary Corner

More information on beneficiaries

Life insurance policies: Alternate beneficiaries

Most life companies do not provide for the nomination of alternate beneficiaries, for example, nominating “my son,

failing him my sister”. If the nominee pre-deceases the testator and they die before changing the nomination, then the
nomination ‘fails’. The proceeds will then be paid as if the nomination was not made, that is to the estate of the deceased and therefore in terms of the will.

Additional beneficiary nomination wording

Where a nomination reads ‘estate’ – it is the same as where no beneficiary is nominated. The proceeds will be paid into the estate. Where a nomination reads ‘as per my will’ – most life companies do not provide for the nomination of a beneficiary by way of reference to another document, for example the will of the client. The risk for a life insurance company where reference is made to another document is that there may be contradiction between the policy beneficiary nomination and what that other document states, for example the will. Alternatively, there may be interpretation problems with the will which the life company will not want to take responsibility for.
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