29 July 2021 – Trusts & Tax Obligations Webinar

If you have missed the live webinar, go to our SARS TV YouTube channel.

Below are the Questions & Answers discussed during the webinar.

	Question	Answer
1	What types of trusts are provided for in the Income Tax Act (ITA)?	The ITA refers to and defines the term "trust". Where the term "trust" is used it may be necessary to determine the specific application for the specific situation. In section 25B the ITA provides for rights that are vested either in terms of a relevant trust instrument (section 25B (1)) or vesting that occurred in terms of the discretionary right of trustees (section 25B (2)). It is important to note that these rights may be found in either an *inter vivos* or testamentary (will) trust. The ITA also refers to a special trust (discussed in more detail below). The ITA also makes reference to collective investment scheme trusts (section 25BA) and real estate investment trusts (section 25BB).
2	Why is apportionment applied on the income and expenditure of trusts?	Expenditure is allocated to the streams of income earned by a trust. Expenditure may either be direct or indirect in nature. Direct expenditure relates to a specific stream of income (e.g. municipal charges in relation to rental income) whereas indirect expenses are expenses that cannot be associated to a specific stream of income (e.g. office rental, accounting and auditing fees). The allocation of these expenses is done to calculate the amount of expenditure that follows a specific stream of income. When a specific stream of income is vested to a beneficiary, the expenditure related to that stream of income must follow the income (section 25B (3)). This means that the beneficiary will receive the income but will also have to account for the related expenditure. In addition, this calculation is necessary to determine the expenditure that will not be allowable as a deduction in the determination of taxable income (section 23).
3	Please clarify how apportionment works when dealing with income and expenditure in a trust.	The first step in apportioning expenditure is to determine the streams of income within the trust. This is done to calculate the contribution made by the different streams of income to the total income of the trust. The second step would be to analyse the expenditure to identify expenditure directly linked to a stream of income and those expenses that cannot be directly attributable to a specific stream of income (see question 2 above). The third step would be to apply the percentage/fraction of the different streams of income to the indirect expenses. The net result of this calculation will be the amount of indirect expenses that may be offset against the different streams of income. Once this calculation (income stream - direct and indirect expenses related to the income stream) was done and the effect of vesting has been considered, the taxable income of the trust can be determined. Please note that apportionment is not applied in respect of Capital Gains reflected in the income statement of a trust.

4	Are foreign trusts required to register for tax purposes?	The public notice issued in terms of section 25 of the Tax Administration Act, 2011 (on 14 May 2021) is clear in par 2. c) ii: **2. Persons who must submit an income tax return** The following persons must submit an income tax return: *(a)* Every company or other juristic person, which was a resident during the 2021 year of assessment that— (i) derived gross income of more than R1 000; (ii) held assets with a cost of more than R1 000 or had liabilities of more than R1 000 at any time; (iii) derived any capital gain or capital loss of more than R1 000 from the disposal of an asset to which the Eighth Schedule of the Income Tax Act applies; or (iv) had taxable income, taxable turnover, an assessed loss or an assessed capital loss; *(b)* Every trust that was a resident during the 2021 year of assessment; *(c)* Every company, trust or other juristic person, which was not a resident during the 2021 year of assessment, that— (i) carried on a trade through a permanent establishment in the Republic; (ii) derived income from a source in the Republic; or (iii) derived any capital gain or capital loss from the disposal of an asset to which the Eighth Schedule to the Income Tax Act applies; Insofar as non-resident/foreign Trusts are concerned, these Trusts must submit a return and hence register for tax if they: "(i) carried on a trade through a permanent establishment in the Republic; (ii) derived income from a source in the Republic; or (iii) derived any capital gain or capital loss from the disposal of an asset to which the Eighth Schedule to the Income Tax Act applies".
5	What is the implication of section 7C on a loan made to a trust?	Section 7C was introduced with effect from 1 March 2017. This section is applicable to low interest or interest-free loans. Section 7C applies to loans, advances or credit made by a connected person to a trust. Section 7C refers to an "affected loan" which also includes loans made by a company at the insistence of a connected person as well as loans made by companies of which the trust holds at least 20% of the equity shares or voting rights (refer section 7C of the ITA). (see detailed definition in section 7C of the ITA) There are certain loans that are excluded (refer section 7C of the ITA). The net effect of such a loan is that the foregone interest, due to no interest or low interest being charged on the loan, will be subject to tax at the rate of donations tax. The formula for the calculation of the foregone interest is detailed in section 7C of the ITA. This formula determines that the foregone interest should be calculated, that the annual donations tax exemption (if not already used) should be utilized and that donations tax be calculated at 20%. Should the loan have fluctuated, ceased to exist or originated during the year of assessment the calculation should be made on a pro-rata basis. The interest rate applied is the official rate of interest, and as this interest rate may also fluctuate, it may impact the calculation. Please note that loans that are subject to interest at the rate equal or above the official rate of interest will not be subject to section 7C. Also note that the donations tax is payable in the month following the year-end of the trust.
6	How are Special Trusts beneficial	Special Trusts are defined in in section 1(1) of the ITA Two types of Special Trusts are provided for:

	from a tax perspective?	• A Special Trust for a mentally or physically disabled person (as defined in section 6 of the ITA) – Type (a) Special Trust • A Special Trust in terms of the will of a deceased person set up for relatives (as defined in the ITA) who are alive on the date of death of the deceased person – Type (b) Special Trust These types of trusts have beneficial treatment in terms of the rate of tax that is applied to its taxable income. In addition, favourable capital gains tax (CGT) treatment is available. Please note that Special Trusts do not qualify for any rebates in terms of section 6 of the ITA. A guide on Special Trusts and the tax treatment thereof is available on the SARS website. **https://www.sars.gov.za/lapd-it-g20-guide-to-the-taxation-of-special-trusts/**
7	How do I comply with the filing requirements for my trust of which the year-end is not end February?	All trusts are required to have an end February year-end. However, the Commissioner may approve the drawing up of trust accounts to a date other than end of February. From a SARS perspective these trusts should submit the standard tax return (ITR12T). Practically this means that a Trust with a different year-end should determine in which tax cycle the Trust's return should be included. For this purpose, the Trust should apply a 6 months ahead and 6 months backwards test (and therefore the end of September is the test). Should the year-end be any period before on or before 30 September, the return must be filed for year of assessment ending in February of the same calendar year. In the event that the accounts are drawn up in the period after 1 October, the return will be filed for the year of assessment ending in February of the next calendar year. Example: Trust A has a 30 June 2021 year-end. Trust A will compile their financial statements as at 30 June 2021 but will submit the tax return for 28 February 2021. Trust B has a 31 December 2021 year-end. Trust B will compile their financial statements as at 31 December 2021 but will submit a 28 February 2022 return. Refer to Interpretation Note 19 (https://www.sars.gov.za/lapd-intr-in-2012-19-year-assessment-accounts-accepted-other-than-last-day-february/)
8	What is the tax consequences if a resident trust vests an amount of income or capital gain in a non-resident beneficiary?	In determining the **income tax** consequences of a distribution to a non-resident beneficiary the following aspects should be considered: • Was the income the result of a donation, settlement or other similar disposition (section 7 of the ITA) • The nature of the income distributed • The timing of the distribution of the income (Revenue vs retained income) • The existence of a Double Taxation Agreement (DTA) The non-resident beneficiary should register for tax purposes in South Africa as the income would be from a South African source and thus subject to tax in South Africa. In determining the **CGT** consequences: • Was the capital gain (CG) the result of a donation, settlement or other similar disposition (paragraph 68-72 of the Eighth Schedule to the ITA)

		• What is the nature of the asset that resulted in the CG (paragraph 2 of the Eighth Schedule to the ITA) • The timing of the distribution of the CG (Capital gain vs retained earnings) Paragraph 80 of the Eighth Schedule of the ITA does not provide for the vesting of a CG in a non-resident beneficiary. This translates to the taxing of the CG in the trust. Refer to the Comprehensive Guide on Capital Gains Tax and other capital gains tax material on the SARS website for further detail https://www.sars.gov.za/types-of-tax/capital-gains-tax/