LEGAL UPDATE

Investec Living Annuity – Options for beneficiaries

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The Investec Investment Linked Life Annuity (ILLA) is a 'living annuity' as defined in the Income Tax Act 58 of 1962 (ITA), and is governed by the ITA and the Long Term Insurance Act 52 of 1998. It is administered by Investec Investment Management Services (Pty) Limited (Investec).

In order to assist you when advising your clients, we have produced this document which summarises the options available to clients invested in the ILLA (annuitants) in respect of beneficiary nominations, as well as the options available to beneficiaries after the death of the annuitant.

Beneficiary nominations

Who can be nominated as beneficiaries?

The annuitant may nominate primary and alternative beneficiaries by completing the relevant section in the ILLA application form. Beneficiaries can be natural persons or trusts (inter vivos and testamentary trusts where the beneficiaries of the trust are natural persons). The annuitant may also amend the beneficiary nomination at a later stage by completing and submitting the required form.

Where no beneficiary has been nominated in the application form or subsequent transaction form, Investec may only pay a commuted cash lump sum (less tax according the retirement tax table) to the deceased annuitant's estate.

Are the nominated beneficiaries guaranteed to receive the ILLA benefit on death of the annuitant?

As the ILLA is a member-owned living annuity, it is not subject to section 37C of the Pension Funds Act. This means that the nominated beneficiary will receive the benefit on the death of the annuitant, provided the beneficiary survives the annuitant and accepts the benefit.

Should one of the primary beneficiaries predecease the annuitant and that beneficiary had not been replaced prior to the annuitant's death, the predeceased beneficiary's share will be divided proportionately between the surviving primary beneficiary/ies.

When will alternative beneficiaries receive the ILLA benefit?

Alternative beneficiary nominations will only apply if there are no surviving primary beneficiaries on death of the annuitant. In the event of the simultaneous death of the annuitant and all primary beneficiaries, or in the event that all primary beneficiaries predecease the annuitant (without having nominated new primary beneficiary/ies, the benefit will be paid to the alternative beneficiaries (if nominated).

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Options available to primary or alternative beneficiaries

In terms of the ITA nominated beneficiaries have the following options on death of the annuitant:

Option 1: Receive benefit as a lump sum (commutation); or

Option 2: Transfer the annuity into a compulsory annuity in his/her own name (for example a living annuity); or

Option 3: A combination of option 1 and option 2.

The above options are available to all beneficiaries, whether a natural person or a trust.

How will a lump sum under option 1 or 3 above be taxed?

If the beneficiary chooses to receive a lump sum, the lump sum will be taxed in the hands of the deceased annuitant. This means that the retirement tax table (see below for the steps to be followed) will be applied in respect of the total lump sums payable to all beneficiaries. The deceased annuitant's contributions to retirement funds which did not rank for a deduction previously in terms of the ITA ("disallowed contributions"), will qualify as a deduction before applying the retirement tax table. The tax payable will then be deducted from the lump sum and the beneficiary will receive the benefit net of tax.

The above also applies to trusts nominated as beneficiaries, if the trustees elect to receive the benefit as a lump sum.

RETIREMENT LUMP SUM

TAXABLE INCOME (R)	TAX
0 – 500 000	0% of taxable income
500 001 – 700 000	18% of taxable income above R500 000
700 001 – 1 050 000	R36 000 + 27% of taxable income above R700 000
1 050 001+	R130 500 + 36% of taxable income above R1 050 000

Steps needed to calculate tax in respect of the lump sum:

1	2	3
Add current lump sum to all previous lump sums* and apply current retirement tax tables.	Add all previous lump sums* and apply current retirement tax tables.	Answer in step 1 minus answer in step 2 = tax payable on current lump sum.

*Only the following lump sums must be taken into account:

- retirement lump sums after 1 October 2007,
- withdrawals after 1 March 2009, and
- severance benefits after 1 March 2011

How will an annuity under option 2 or 3 above be taxed?

If the beneficiary chooses to transfer the annuity to a compulsory annuity in his/her own name, the transfer is tax neutral and the income payable from the annuity will be taxed in the hands of the new annuitant (the beneficiary), according to his/her marginal tax rate. In this scenario the deceased's "disallowed contributions" will not be taken into account, as the tax exemption for annuities as set out in section 10C of the ITA is only be available to the person who actually made those contributions.

How will an annuity received by a trust (the new annuitant) be taxed?

In the normal course, a trust (other than a special trust) is taxed at a rate of 45% on income received. At the end of the tax year, if distributions were made to the trust's beneficiaries in the year the incomes were received, the trustees of the trust may be able to claim back tax from SARS.

However, trustees of trusts who distribute annuity incomes to its beneficiaries in the year in which the income is received, may approach SARS for a tax directive. The tax directive will stipulate the rate of tax (if any) to be deducted by Investec from the annuity income before payment to the trust's bank account.

The process to be followed, as outlined by SARS, for a trust to obtain a tax directive is as follows:

- The trust must register for PAYE
- Once the trust has been registered for PAYE, the trustees must request a tax directive from SARS in writing.

The trustees may still have an obligation to withhold PAYE from the income distributed to beneficiaries and to issue the applicable tax certificate (IRP5/IT3(a)).

What happens to the ILLA if the trust is wound up?

The trustees of the trust may nominate beneficiaries when completing the ILLA application form, which may also be amended at a later stage.

If the trust is wound up, the nominated beneficiaries will have the same 3 options mentioned above. If the trust did not nominate a beneficiary/ies or the nominated beneficiary/ies are deceased, Investec will pay the benefit as a lump sum (less tax at the trust's rate of 45%) to the trust's bank account.

If the nominated beneficiary chooses to receive a lump sum, the lump sum will be taxed according to his/her marginal rate. The retirement lump sum tax table cannot be applied here because the lump sum is payable as a result of the trust being wound up (as opposed to an annuitant passing away).

If the nominated beneficiary chooses to receive the benefit as a compulsory annuity, the annuity income will be taxed in the hands of the new annuitant (nominated beneficiary) according to his/her marginal tax rate.

Are living annuities subject to estate duty?

All compulsory annuities (including living annuities) are exempt from estate duty in terms of section 3(2) of the Estate Duty Act, 45 of 1955, regardless of whether an annuity or lump sum is selected by the nominated beneficiary.

However, the deceased annuitant's 'disallowed contributions' will be included in his/her dutiable estate for estate duty purposes.

CONTACT INFORMATION

Please visit our website at **www.investecassetmanagement.com** for more information on our range of funds and portfolio products.

For more information and assistance with investing, call the Advisor Service Centre T 0860 444 487

Alternatively, please contact your Investec investment consultant.

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