



THE POWER
OF INDEPENDENT ADVICE

IN THIS ISSUE

“ *For an investor committing a large lump sum to an offshore investment, an offshore endowment wrapper with a South African insurer can offer estate planning and tax advantages.* ”

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ENDOWMENTS UNDER THE MICROSCOPE

By Gustav Reinach, Financial Planner at Brenthurst Wealth Management

Investing locally or offshore can be challenging with so much more to consider than just market returns and costs. Various structures are available to make offshore allocations, whether it is a share portfolio, unit trust or structured note, with different tax regimes applicable to respective jurisdictions like inheritance tax in the UK or estate duties in the US, as well as capital gains and income taxes back home.

If you are a higher income earner looking for an investment that will result in you paying less tax, while still following a growth investment strategy, and where maximum liquidity is not essential, then an endowment may just be the right investment option for you.

Two options for liquidity are available within the first five years of this investment option. One full or partial withdrawal of the capital or one partial interest free loan is available. After five years the investor has access to the liquidity of capital, but with the tax benefits.

An endowment policy is a type of vehicle that is often misunderstood.

A common misconception is that an endowment is a type of investment. It is not an investment in itself – it is rather an investment vehicle that holds an underlying investment fund. A decision to use an endowment vehicle should primarily be made for both tax and estate planning reasons, in addition to investment reasons.

It is important to emphasise that endowment policies have changed over the years. It is no longer the structured life and disability instruments of the past, which were usually long term policies. These days they are pure investment products, which cost structures have become rather competitive over time.

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An endowment makes sense when you have an individual marginal tax rate of over 31%, as it simplifies offshore investments tax implications – because it is taxed within the product itself – thus transferring the onus of the calculation and payment of tax on offshore investment earnings to an investment administrator. Furthermore, it is easy to appoint a beneficiary – where proceeds could therefore be paid relatively quickly to a on death and where no executor fees are payable.

More and more South Africans are using their investment allowances to invest offshore. To this end they use either the R1 million single discretionary allowance or the R10 million allowance that requires a tax clearance certificate allowance, or both. This article will attempt to identify some of the advantages of using an offshore endowment policy with a South African insurer.

An endowment policy with a life assured allows the owner to nominate a beneficiary. This is the person to whom the proceeds will be paid on death of the life assured. In the offshore world this is a major advantage as it helps to avoid the problem of probate. Probate is the process whereby a foreign estate has to be wound up and can prove particularly problematic.

Let us look at an example where John dies in South Africa. He has two offshore investments not in an endowment wrapper: One is in the UK and one in Jersey. John's local executor has to engage with two offshore executors to help wind up the foreign portion of the estate. This can be time consuming, especially given the fact that the South African Master requires an original will, and so do the offshore authorities. It can also be expensive. In addition, if the offshore amounts are small, it will be difficult to find anyone offshore willing to do the work. Because the amount they will be able to charge is limited, it will not be worth their time.

IF, HOWEVER, THE TWO OFFSHORE INVESTMENTS ARE IN AN ENDOWMENT WRAPPER, THEN THE NOMINATED BENEFICIARY IS SIMPLY PAID. THERE IS NO NEED TO GO THROUGH THE FOREIGN PROBATE OR WINDING-UP PROCESS.

This is obviously much quicker and cheaper. It should also be noted that most South African insurers have very creative products that allow the proceeds, or the actual policy itself, to move to nominated beneficiaries without having to pass through the estate. This applies in the case of both a beneficiary for proceeds (where the life assured dies) and a beneficiary for ownership (where the policy owner, who is not the life assured, dies). The ability to nominate a beneficiary also ensures that the proceeds will not be subject to executor's fees. Estate duty will, however, not be avoided as the policy is still an asset in the estate, even though the executor is not handling the proceeds.



A similar structure is available to local investors to access the tax benefits.

Although, as discussed above, the policy will be estate dutiable in the deceased South African estate, at least there will not be any estate duty offshore because all these policies are registered in tax centres.

CONCLUSION

For an investor committing a large lump sum to an offshore investment, an offshore endowment wrapper with a South African insurer can offer estate planning and tax advantages. However, make sure to check the costs on such an investment and also take professional tax advice. Each case is dependent on its own facts and there should not be a “one-size-fits-all” approach.

AS WITH ANY INVESTMENT DECISION, CHANGES TO PORTFOLIOS OR ASSET CLASS SELECTION MUST FIT THE INDIVIDUAL INVESTOR’S RISK PROFILE, INVESTMENT GOALS AND LONG-TERM FINANCIAL PLANNING STRATEGY.

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He obtained a B.Com Economics degree from the University of the Free State with a focus on key subjects such as Investment Management & International Economics.

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Gustav’s previous experience includes the analysis of white label and hedge funds, as well as financial planning for individual clients focusing on their investment portfolios.

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