



The New R3,5 million abatement

One of the first questions that an estate planner will have to ask a client is “do you have a predeceased spouse?”

The 2009 Taxation Laws Amendment Bill will introduce a new way of applying the R3,5 million estate duty abatement and with it, significant and unexpected estate duty savings for some estates.

In this issue of *Estate Planning Essentials* we look at the technical background to the amendment as well as at some of the considerations which should be taken into account when reaching a decision regarding the use of the abatement as an estate planning tool.

The R3,5 million abatement

Before looking at the application of this provision it is necessary to make two points.

- (i) For an estate of a deceased person who had a predeceased spouse - the abatement will apply on a look back basis, in that it is applied by looking at the abatement in the deceased's estate and determining the abatement with reference to the abatement amount as used in the estate of any one predeceased spouse or spouses.
- (ii) There is no longer any requirement that the whole estate has to be bequeathed to a surviving spouse (as was indicated in the initial draft of the bill).

How will it work?

For persons who die on or after 1 January 2010 we can distinguish between one of three scenarios:

- (i) The first scenario applies to single persons or first-dying spouses. The abatement in his or her estate will be R3,5 million.
- (ii) The second scenario applies to a “second-dying spouse” who has survived one or more predeceased spouses. In this case the second-dying spouse will qualify for an abatement of R7 million. This R7 million must be reduced by the amount of the abatement actually used in the estate of any one or more, previously deceased spouse/s.

Example 1: Mr Marais dies on 2 January 2010. His only predeceased spouse, Mrs S Marais' estate used R1,5 million as an abatement available at the time of her death. The abatement in Mr Marais' estate will be R5,5 million (R7 million reduced by the already utilised R1,5 million).

Example 2: Mr Marais survives two predeceased spouses. Mrs S Marais, whose estate utilised the R1,5 million abatement, and Mrs J Marais who left everything to Mr Marais (therefore no abatement could be applied). The abatement in Mr Marais' estate will be R7 million reduced by either R1,5 million or nil. It would make sense to use the lesser amount, being nil. Therefore the abatement in his estate will be R7 million.

- (iii) The last scenario applies in the estate of a person who was one of a number of spouses (polygamous or polygamous marriages) of a predeceased spouse. In this case the abatement amount will be:

R3,5 million

Plus

R3,5 million divided by the number of spouses, minus the portion of the abatement used by the predeceased spouse, divided by the number of spouses of that predeceased spouse.

Example : Mrs Smit dies and she is one of two wives of a predeceased Mr Smit. When Mr Smit died his estate qualified for a R1,5 million abatement.

The estate duty abatement in Mrs Smit's estate will be:

R3,5 million

Plus

$(R3,5 \text{ million} \div 2) \text{ minus } (R1,5 \text{ million} \div 2)$

i.e. R1 750 000 minus R750 000

= R1 million

The abatement in Mrs Smit's estate will be R4,5 million.

Important Note: The concessions referred to under points (ii) and (iii) above will only apply if the executor of the current deceased estate is able to submit a copy of the estate duty addendum of the first dying spouse to the Commissioner.

Estate planning considerations

(for the sake of avoiding using his/her I will assume that the surviving spouse is female)

Firstly, a "surviving spouse" should, as part of her current estate planning, ensure that she has a copy of her predeceased spouse's estate duty addendum and file it with her important documents or even record as an annexure to her will.

For spouses doing estate planning now the question will be whether to use the abatement as a rollover to the estate of the second dying spouse, or to use a discretionary trust as a means of using the abatement in the first-dying spouse's estate.

In this regard there are two important considerations:

1. Growth in the value of the asset

While the unused portion of the R3,5 million will qualify as an abatement in the second-dying spouse's estate, the growth on that amount will not. So where the asset is a growth asset and the spouses are relatively young i.e. the surviving spouse has a potentially long life expectancy, it may still make sense to use a trust to limit the estate duty position of the second dying spouse.

2. Asset protection

The primary consideration when contemplating a trust remains protection of assets. Where it is a testator's wish to protect assets for future generations a trust remains the most effective estate planning instrument in achieving this objective.

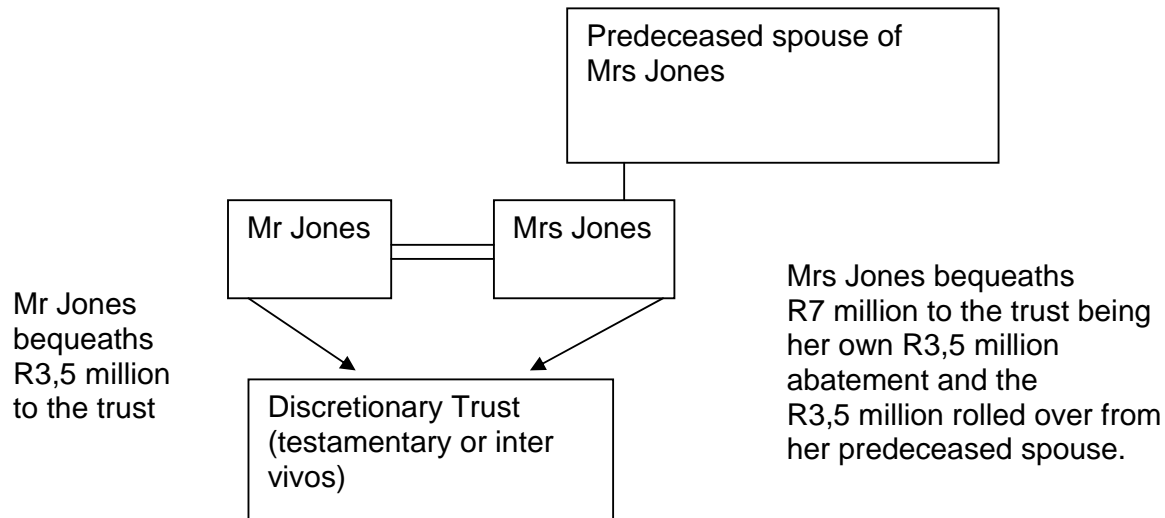
Is it possible to qualify for a R10,5 million abatement?

Instead of closing the door on the use of trusts in the abatement scenario, the new provisions have opened the door to a host of new opportunities. This is best explained by way of an example:

Mr and Mrs Jones are doing their estate planning. Mrs Jones was married before. Her predeceased husband bequeathed his whole estate to her (thus no part of the abatement amount was used in his estate). If Mr Jones leaves his estate to Mrs Jones as a rollover she (using their combined estates) would qualify for a R7 million abatement. (See scenario 2 above).

However, if Mr Jones leaves R3,5 million to a discretionary trust and Mrs Jones does the same, their combined estates would qualify for a R10,5 million abatement, as follows:

Mr Jones has his own abatement of R3,5 million in respect of the bequest to the trust. Mrs Jones will still qualify for a R7 million abatement, being her R3,5 million plus the R3,5 million unused portion of her predeceased spouse's abatement.



Conclusion

The answer to the question regarding a predeceased spouse can result in estate duty savings amounting to hundreds of thousands of rand. Don't forget to ask the question.

Any queries may be directed to:
Eugene Ward (041) 365 1303