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RA RA Rasputin

Much like the infamous Russian, RA's may be viewed as both good and bad. However, unlike Rasputin, RA's are for the good and the only "bad" are the rules that you have to obey and are there for your protection. Essentially, the good far outweighs the bad and when the day comes and it's time for your retirement you will be relieved that you played by the rules.

There are a number of ways to save and a retirement annuity fund, is one of the potential investment tools which offers a tax efficient way to save towards retirement.

You can invest lump sums or make regular contributions into your own investment portfolios within a retirement annuity. The earliest age you can retire from the fund and make withdrawals is 55 years old.

When you retire

At retirement you can take up to one third of your fund value in cash, subject to taxation, and the remainder can be used to either invest into a living annuity or purchase a fixed annuity, to pay yourself an income at retirement.

When choosing your investment portfolios for your retirement annuity, it is important to understand that a retirement annuity, as well as any other pre-retirement investment vehicles, follow Regulation 28, which limits the amount of exposure in certain asset classes. For example, you cannot have more than 75% in equities (includes local and offshore equities). This is to decrease risk for the investor and help protect and diversify portfolios.

What happens to your funds when you pass on?

The trustees of the retirement annuity fund will allocate your fund value to your dependents and nominated beneficiaries as is required by law. You can nominate beneficiaries for consideration with a retirement annuity and this nomination will assist the trustees of the fund in allocating the funds on your death. Typically, people whom are financially dependent on you will receive funds. Always ensure that you list all your beneficiaries for your retirement investments or contact your adviser for the necessary forms to have them listed.

Why save towards a retirement annuity?

Some of us might already have pension or provident funds which we use to save towards retirement and it might seem like you and/or your employer are making sufficient contributions, but in many cases this alone might not be enough to retire on, depending on your specific needs.

When your contributions for your pension or provident funds are calculated, it is based on your pensionable salary and not your cost to company. The rule of thumb

is that if you save 15% of your salary over 35 years, you could potentially receive 75% of your salary as a pension, as long as you received reasonable investment returns.

The problem is that your pensionable salary is usually only about 70% of your cost to company (depending on the company you work for). For example, if your monthly package is R15 000, you would need to retire on the equivalent of R11 250 (75%). However, your pensionable salary which your contributions are based on, is less at R10 500 (R15 000 x 70%). If we use the general rule of thumb it provides a pension income of only R7 875 (R10 500 x 75%), which is much lower than you might have thought.

You can make up the shortfall by investing additional contributions of your non-pensionable income into a retirement annuity.

Benefits of a RA

Besides making up shortfalls, probably the biggest benefit of a retirement annuity are the tax benefits and deductions individual tax payers get for investing in a retirement annuity. With a retirement annuity you can deduct your contributions from your taxable income. Currently the limit you can deduct is 27.5% of the greater of remuneration or taxable income limited to R350 000 per year. Excess contributions are carried forward to the next tax year.

Other advantages of a retirement annuity are:

- Compound interest - as you are investing over a long period, you earn growth on the growth.
- Supporting your dependents - you can provide for those you leave behind. Your RA benefit is not subject to estate duty, and creditors cannot access your hard earned retirement funds.
- Long-term stability - you can ride out short-term fluctuations in the market in order to target long-term real growth, which pays off when you retire.
- Freedom of choice subject to regulation 28 mentioned above - you can choose your underlying investment portfolios, giving you flexibility in how your contributions are invested and how they grow.
- Disciplined savings - not being able to access your retirement savings before age 55 is a good thing.

There is no tax on interest or capital gains on your investment in the fund.

According to Alexander Forbes Member Watch, only 6% of members retire with a replacement ratio of 75% or more. What this means is that if your pensionable salary is R20 000 then a 75% replacement ratio means an income of R15 000 in retirement. Therefore, keeping up with your contributions and preserving your benefits should be at the top of your list when it comes to saving for retirement.

Options at retirement

There are two main options when it comes to purchasing an annuity income: a guaranteed life annuity or a living annuity.

Guaranteed Annuity

In the case of a guaranteed annuity, you purchase an income for the rest of your life. It is not like a bank account for example, where there is a balance that earns an income. With a guaranteed annuity you hand over a lump sum in exchange for the guarantee that you will receive a set income, with the option of increasing with inflation, for the rest of your life. The annuity continues for as long as you live but stops when you die (or when the guaranteed period expires).

Living Annuity

With a living annuity you have an investment portfolio which means your income is determined in part by the return of the underlying investments. You can draw down between 2.5% and 17.5% of the capital each year. This allows more flexibility in terms of your income – so you could draw down less in your first years of retirement if you are supplementing with part-time work, and then increase the percentage in your later years. Any balance in your living annuity is paid to your beneficiaries when you pass away.

Taken on trust

Many people, when they hear the word "trust" in the context of financial planning, tend to think of a vague and mysterious concept which has no practical bearing on their lives. However, almost every one of us has been, or at some time will be, involved with some type of trust.

Some practical examples of trusts in "everyday" life are, for example, the parents of young children who provide in their Will for the creation of a trust to look after their offspring's future inheritance in the event of their simultaneous deaths. Another example of a trust structure in common use is that of the "unit trust" (officially called a "collective investment"): the shares held by the investors in a so-called "unit trust" are in law held in a special type of trust and every unit trust investor is effectively a beneficiary of a trust. Similarly, a pension fund is simply a statutory form of a trust.

Despite often appearing at first glance to be a complex structure, the trust is in fact one of the most powerful tools available to a person when planning an estate - but what exactly is a trust and how does it work?

Trusts 101

Simply put, a trust is a structure in which a person transfers assets to other parties, who then administer and control the assets on behalf of one or more beneficiaries, in accordance with the trust instrument (which could be a trust deed or a Will).

The person who initiates the trust agreement is known as the "founder" (also sometimes called "the settler" or "the donor"). The trustees are the people (and/or an institution) nominated by the founder to be the legal owners of the assets in the trust and are responsible for the administration of the trust and its assets.

The beneficiaries are the people who benefit from the assets in the trust by earning income or receiving the capital of the trust at some point. A trust beneficiary can also be a trustee, and the founder can also be both a beneficiary and a trustee.

Trusty types

The types of trusts one comes across can be described in various ways, depending on (a) how they are formed, or (b) what rights the beneficiaries have, or (c) for what purpose they are formed. These various tags which are commonly applied to trusts can lead to confusion. Simplistically, however, every trust can be categorised according to these criteria:

- Manner of formation - trusts can be formed during the founder's lifetime (known as an "inter vivos trust" – in Latin "between the living") or after his or her death based on instructions contained in a Will (known as a "will trust" or "testamentary trust")

Trustafarians

The spoiled trust fund baby is a stereotype, though, and not necessarily the norm. Lots of wealthy young people have gone on to become great successes. Consider Megan Ellison, daughter of **Oracle** co-founder and chairman Larry Ellison, recently the seventh-richest man in the world. Her company Annapurna Pictures has produced three films that were nominated for the Academy Award for best picture: *Zero Dark Thirty*, *Her*, and *American Hustle*.

Another independently successful trust fund baby is Caroline Kennedy Schlossberg, daughter of John F. Kennedy and Jackie Kennedy Onassis and our current ambassador to Japan. Gloria Vanderbilt (yes, *those* Vanderbilts) is another successful scion of the wealthy, having made her own fortune in the fashion industry. (Her son, CNN anchor Anderson Cooper, is *not* a trust fund baby, as his mother expected him to make his own way in the world.)

Gloria Vanderbilt's attitude is not uncommon among wealthy parents. Many wealthy people are on record saying they do not plan to leave

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- Rights of beneficiaries - trusts confer different rights on the beneficiaries concerning the distribution of income and capital. A "vesting trust" is one where the trust instrument stipulates precisely when and how income and capital is to be distributed to beneficiaries, whereas a "discretionary trust" allows the trustees to decide when and how such distributions are to be made
- Purpose of trust - trusts are also often described by the purpose for which they are formed, for example, “asset protection trust”, “trading trust” or “business trust”

Thus, for example, a traditional “family trust” is usually an inter vivos trust set up during the founder’s lifetime for the purpose of holding and protecting his family’s wealth, with the trustees being given a discretion to distribute the income and capital between the various family members as they see fit, during the founder’s lifetime or after his death (such a trust would thus be described as an inter vivos discretionary family trust).

A trust to die for - The Testamentary trust

In terms of estate planning, one of the most common forms of trusts is the testamentary trust. As this type of trust is created in the founder’s Will, it does not come into existence until the founder’s death.

A testamentary trust is most commonly used to administer and protect assets inherited by minor children or by anyone else not skilled at looking after money. Holding assets in a testamentary trust for minors until they reach their majority is the best way to protect the assets from being used for purposes other than their benefit and wellbeing. Furthermore, unless a testamentary trust of this nature is created in a Will, then there is a likelihood that a minor heir’s inheritance will have to be paid into the State administered Guardian’s Fund for the duration of the minor’s minority. This would require the child’s remaining guardian to approach the Fund whenever the child is in need, and fairly rigid and inflexible rules apply.

A living thing – The inter vivos Trust

An inter vivos trust is set up during the founder’s lifetime. It is usually created by a trust deed – an agreement between the founder and the trustees, who are appointed in the trust deed. The trustees, who manage the trust fund for the benefit of the beneficiaries, usually have extensive discretionary powers.

This type of trust is ideal for accumulating and holding growth assets such as shares, unit trusts and fixed property in order to keep the growth on these assets out of the founder’s estate. The increase in the value of the assets after they are placed in the trust occurs in the trust. This means that, at the founder’s death, no estate duty is levied on the assets in the trust and the beneficiaries get the full benefit of their inheritance. While the founder is alive, he usually remains a potential beneficiary of the trust and thus can still enjoy the benefits of the assets in the trust. This trust therefore offers an excellent way to limit estate duty. However, it is important to transfer the assets to the trust well in ad-

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great sums of money to their children. Warren Buffett famously said that he wanted to leave his kids -- now adults -- "enough money so that they would feel they could do anything, but not so much that they could do nothing." Several years ago it was reported that Bill and Melinda Gates planned to leave their kids $10 million each -- a pittance compared to their parents' billions.

A trust protects the financial interests of minor children and other vulnerable beneficiaries

vance in order for most of the growth in value of the assets to take place in the trust, rather than the founder's personal estate.

Other potential benefits obtained by placing one's assets and investments in an inter vivos trust include:

- Trust assets are excluded from the executorship process which occurs on one's death – these assets are thus not frozen in a deceased estate situation and are immediately available to surviving trust beneficiaries and executor's fees are not levied on the value of the trust assets
- The trustees appointed by the founder retain complete control throughout the whole process
- Due to the continuity of assets and property management with a trust, the founder's heirs enjoy uninterrupted income
- The founder's spouse and heirs avoid much of the emotional trauma, aggravation and frustration often associated with a normal Will
- If the founder becomes incapacitated, the trustees continue to handle the trust assets, avoiding the need to apply to the court for the appointment of a curator
- A trust protects the founder's children, and ensures his wishes are carried out after his death without being subject to outside attack. A trust allows the founder to control his wealth while he is alive and after his death through written instructions to his succeeding trustees.
- A trust offers protection from claims by the founder's personal creditors in some circumstances
- A trust protects the financial interests of minor children and other vulnerable beneficiaries
- A trust structure can prevent indiscriminate spending of the assets by less responsible heirs to the detriment of others
- The trust founder is assured of impartiality between beneficiaries after his death, as the decisions of objective trustees should not likely favour any beneficiary
- A trust facilitates multi-ownership of assets which may not be easy to split between heirs, such as a farm or block of flats - with a trust the beneficiaries can receive the income generated by the asset, while the asset itself is held intact in the trust
- In certain circumstances income from a trust can be split amongst beneficiaries, thus reducing income tax liability

Conclusion

A trust may have an important role to play in estate planning, even if this is limited to a simple testamentary trust in a Will to protect minors' inheritances; for the wealthier estate planner, trusts can be an invaluable tool for numerous reasons.