



Fiduciary Insights

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NAVIGATING FOREIGN INHERITANCE AS AN SA TAX RESIDENT

Inheriting assets from abroad can be both a blessing and a challenge for South African residents. Consider, for example, an SA resident inheriting a flat in the UK from a relative who emigrated long ago. Suddenly, the resident now has a worldwide estate that includes an offshore asset. If he/she decides to rent the flat out, he/she will need to register as a UK taxpayer and include the foreign rental in his/her SA tax return. What are the estate planning considerations and options?

A BRIEF OVERVIEW OF SA LAW ON FOREIGN INHERITANCE

SA law offers specific provisions for handling foreign assets inherited from tax non-residents. These include exemptions from Exchange Control Regulations and Donations Tax, as well as certain deductions under the Estate Duty Act.

In a nutshell, an SA resident does not have to disclose an inheritance received from a non-resident if the inheritance is located outside SA. Furthermore, this foreign inheritance can also be disposed of without reporting the disposal to the SARB's Financial Surveillance Department. However, local tax disclosures and compliance will apply to the disposal.

While the foreign property inherited will form part of the resident's total estate, it is excluded by way of a deduction under section 4(1)(e) of the Estate Duty Act. Moreover, the foreign property inherited can be donated without triggering donations tax in South Africa, due to the exemption from donations tax under section 56(1)(e) of the Income Tax Act.

If the foreign property is sold, the base cost used in the calculation of capital gains is the market value of that property at the death of the non-resident plus costs incurred in respect of the foreign property by the executor, in the process of winding the estate down.



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If the foreign property is donated to a foreign trust, resulting in income distributions to a non-resident, the attribution rules apply, and the income distributed to the non-resident is included in the resident's income.

ESTATE PLANNING OPTIONS

One of the main objectives for residents inheriting foreign properties might be to avoid becoming subject to tax in foreign jurisdictions. Alternatively, they may seek to hold the property in a manner that reduces estate planning complexities. Whatever the objective, making an informed decision requires a thorough understanding of both SA law and the laws governing the jurisdiction where the property is situated.

Within the scope of SA law, residents have several options when dealing with inherited foreign assets, including:

- **Direct ownership:** Holding the property and renting it out may subject the resident to taxes in both SA and the foreign jurisdiction, requiring annual tax filings in both countries. A Section 6quat rebate may apply to foreign rental income taxed in SA. At death, there will be no estate duty on the foreign property in SA, however capital gains tax may be payable due to deemed disposal. As a result of a foreign estate created by the inheritance, the resident may need a will dealing with that offshore property. However, there should be no foreign tax rebate if there is a wealth tax on the foreign property – because the value of the foreign property never forms part of the dutiable estate in SA.
- **Immediate disposal:** Selling the inherited property upon acquisition can minimise capital gains tax exposure, though careful consideration of market

value and base cost is essential. The proceeds could be invested anywhere in the world, without applying for Financial Surveillance Department permission, and the replacement property is excluded from the SA estate – for estate duty purposes.

- **Transfer to a foreign company:** Transferring the property to a foreign company within which the resident is a majority shareholder could create a controlled foreign company, requiring compliance with the controlled foreign company provisions of the Income Tax Act.
- **Donation to a foreign trust:** The property could be donated to a foreign trust without triggering South African donations tax, but may result in income tax obligations for distributions from the trust to non-resident beneficiaries.

- **Sale to a foreign trust on a loan account:** Selling the property to a foreign trust on loan account can provide tax-efficient income streams, though careful structuring is necessary. Since the loan is based on foreign currency, market-related interest may be significantly lower than what could have been charged on an SA rand loan. The loan account will remain level over the lifetime of the resident taxpayer. At death, there is no capital gains tax on the disposal of a loan account and the loan account will not attract estate duty in SA. The foreign interest income will be included in the SA tax return, and if there are interest payments by the foreign trust to the resident taxpayer, the receipts should be sufficient to pay domestic tax. The tax payable to the tax authorities in the foreign jurisdiction could be reduced by claiming tax treaty benefits between SA and that foreign jurisdiction.

Each of the above options carry their own tax and legal implications, requiring careful evaluation based on individual circumstances and objectives. Professional advice is recommended to navigate both SA and foreign tax laws effectively. In conclusion, while inheriting foreign assets as an SA tax resident presents complexities, understanding the legal landscape can facilitate informed decision-making and optimal estate and tax planning.

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