

AN ANALYSIS OF THE TRANSFER DUTY IMPLICATIONS ON THE 'SALE' OF A TRUST

by

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DEDICATION

I dedicate this work to our Father who art in heaven, Hallowed be Thy name, who gave me my loving and incredible wife, Liesl le Grange, and my two children Limoné and Leandri. Thank you for the unselfish love that is poured out to me every day. I love you more than you can imagine.

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DECLARATION

I, ANDRIES JOHANNES LE GRANGE, hereby declare that this dissertation is my own, unaided work. It is being submitted in partial fulfilment of the requirements for the Master's degree in Tax Law at the University of Pretoria. It has not been submitted before for any degree or examination at any other university.

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12 November 2013

LIST OF ABBREVIATIONS

AJ	Acting Judge
AJA	Acting Judge of Appeal
DJP	Deputy Judge President
J	Judge
JA	Judge of Appeal
LAWSA	The Law of South Africa
SARS	The South African Revenue Service
TA Act	Tax Administration Act
TDA	Transfer Duty Act 40 of 1949
TPCA	Trust Property Control Act 57 of 1988
VAT	Value-Added Tax

ABSTRACT

This dissertation is mainly a study of the nature of trusts and their daily operational limitations, which are frequently misunderstood and/or misused. My research question was whether a trust could be sold, and if so, what the tax implications of such a 'sale' would be. The overall approach was to perform a literature review and a critical analysis of current information available on South African trust law and the Transfer Duty Act 40 of 1949.

Many studies have been undertaken in the past on various aspects of my subject, but the subject has never been studied as a cohesive whole. These studies formed the basis of the literature review. To arrive at an answer, an analysis of the available literature and South African judgments was undertaken.

My concluding chapter gives an indication of whether a trust can be 'sold', what the current transfer duty implications are and what it is submitted they should be.

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CHAPTER 1. INTRODUCTION TO THE RESEARCH

1.1 Introduction

In the course of my legal career I have come across many instances where parties, assisted by their attorneys and/or counsel, have concluded agreements whereby the trustees and/or beneficiaries of a trust have agreed, against payment of an amount, to resign as trustees and/or beneficiaries, and to be substituted by the purchaser and/or his nominees.

These agreements are mainly concluded where the trust is the owner of immovable property and the keeper(s) (as I will call them for the time being) of the trust intend to sell the property to another, with the intention of keeping, and not terminating, the trust.

1.2 Research question

The question that I have been pondering for many years is whether such an agreement, which is a 'sale' in essence, would be lawful and what the tax implications would be in compliance with the agreement.

The in-depth question resulting from this is: What is the legal nature of an agreement (to be called a 'sale') whereby a trust instrument is varied (to substitute trustees and beneficiaries) outside the parameters of the trust instrument, and what are the legal and tax consequences of such a 'sale'?

1.3 Value of the proposed study

The information and guidelines available on this topic are currently very limited, and accordingly there is much confusion and uncertainty. While the trust law is still evolving in South Africa it is of the utmost importance that all those concerned should ensure that it evolves properly.

This study will address the issues of when trustees and beneficiaries may or may not be substituted; what the consequences would be of invalid substitutions; what the transfer duty implications would be; and lastly, who the appointed 'watch dogs' are who are responsible for protecting trusts in South Africa.

A further aim of this study is to carry out an in-depth analysis of the decision by Mbha J in *The T Trust v The Commissioner for the South African Revenue Service*,¹ and I will discuss whether the judgment has any merit.

The envisaged value of the study would therefore be to make colleagues (including those employed by SARS who will draft legislation in future that will have an impact on trusts) aware of a possible 'red light' in the sphere of trust law.

1.4 Delimitations

The proposed dissertation will be limited to trusts in general and the tax implications pertaining to the transfer duty levied on the transfer of residential immovable property held in trust by a trustee (as owner of the property in his official capacity), where such trust is covered by the Trust Property Control Act.²

¹ In the South African Tax Court (Johannesburg) under case number 11286 [2007].

² Act 57 of 1988.

CHAPTER 2. THE LEGAL NATURE OF A TRUST

2.1 Introduction

To put forward an answer to my research question it is important to know and understand the origin and legal nature of trusts.

The law of trusts originated in England, and not only is English trust law the foundational law of trusts but it makes a unique contribution to the global legal system. Trusts are part of the law of property, and arise where one person (a 'settlor') gives assets (e.g. some land) to another person (a 'trustee') to keep safe or to manage on behalf of a third person (a 'beneficiary').³

³ http://en.wikipedia.org/wiki/English_trust_law:

The law of trusts first developed in the 12th century from the time of the crusades under the jurisdiction of the King of England. The 'common law' regarded property as an indivisible entity, as had been done through Roman law and the continental version of civil law. Where it seemed 'inequitable' (i.e. unfair) to let someone with legal title hold onto it, the King's representative, the Lord Chancellor who established the Courts of Chancery, had the discretion to declare that the real owner 'in equity' (i.e. in all fairness) was another person. When a landowner left England to fight in the Crusades, he conveyed ownership of his lands in his absence to manage the estate and pay and receive feudal dues, on the understanding that the ownership would be conveyed back on his return. However, Crusaders often encountered refusal to hand over the property upon their return. Unfortunately for the Crusader, English common law did not recognize his claim. As far as the King's courts were concerned, the land belonged to the trustee, who was under no obligation to return it. The Crusader had no legal claim. The disgruntled Crusader would then petition the king, who would refer the matter to his Lord Chancellor. The Lord Chancellor could decide a case according to his conscience. At this time, the principle of equity was born. The Lord Chancellor would consider it 'unconscionable' that the legal owner could go back on his word and deny the claims of the Crusader (the 'true' owner). Therefore, he would find in favour of the returning Crusader. Over time, it became known that the Lord Chancellor's court (the Court of Chancery) would continually recognize the claim of a returning Crusader. The legal owner would hold the land for the benefit of the original owner, and would be compelled to convey it back to him when requested. The Crusader was the 'beneficiary' and the acquaintance the 'trustee'. The term 'use of land' was coined, and in time developed into what we now know as a 'trust'.

In many respects trusts in South Africa operate in a similar way to the way they operate in other common law countries, although the law of South Africa is actually a hybrid of the British common law system and the Dutch civil law.⁴

2.2 Definition and nature of a trust

In South African Law a 'trust' is defined in section 1 of the TPCA⁵ as follows:

'[T]rust' means the arrangement through which the ownership in property of one person is by virtue of a trust instrument made over or bequeathed –

- (a) to another person, the trustee, in whole or in part, to be administered or disposed of according to the provisions of the trust instrument for the benefit of the person or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument;*
- (b) to the beneficiaries designated in the trust instrument, which property is placed under the control of another person, the trustee, to be administered or disposed of according to the provisions of the trust instrument for the benefit of the person or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument,*

⁴ http://en.wikipedia.org/wiki/Trust_law:

In South Africa, in addition to the traditional living trusts and will trusts there is a 'bewind trust' (arising from Dutch law bewind and Roman-Dutch bewindhebber) in which the beneficiaries own the trust assets while the trustee administers the trust, although this is regarded by lawyers in the Netherlands as not actually a trust. Bewind trusts are created as trading vehicles providing trustees with limited liability and certain tax advantages. In South Africa, minor children cannot inherit assets and in the absence of a trust and assets held in a state institution, the Guardian's Fund, and released to the children in adulthood. Therefore testamentary (will) trusts often leave assets in a trust for the benefit of these minor children. There are two types of living trusts in South Africa, namely vested trusts and discretionary trusts. In vested trusts, the benefits of the beneficiaries are set out in the trust deed, whereas in discretionary trusts the trustees have full discretion at all times as to how much and when each beneficiary is to benefit.

⁵ Act 40 of 1949.

but does not include the case where the property of another is to be administered by any person as executor, tutor or curator in terms of the provisions of the Administration of Estates Act, 1965 (Act 66 of 1965).

In the recent matter of *Land and Agricultural Bank of South Africa v Parker and Others*⁶ Cameron JA elaborated on Honoré and stated:

'[A trust] is an accumulation of assets and liabilities. These constitute the trust estate, which is a separate entity. But though separate, the accumulation of rights and obligations comprising the trust estate does not have legal personality. It vests in the trustees, and must be administered by them – and it is only through the trustees, specified as in the trust instrument, that the trust can act.

The **essentials for a valid trust** to be created were formulated by Honoré⁷ as follows:

- The founder must intend to create a trust.
- The founder's intention must be expressed in a mode appropriate to create an obligation.
- The property that is the subject of the trust must be defined with reasonable certainty.
- The trust object, which may be either personal or impersonal, must be defined with reasonable certainty.
- The trust object must be lawful.

Some of these essentials are straightforward and need no further discussion. Failure to discuss every essential must not be regarded as an indication that I disagree with, or have discarded, any of them.

⁶ 2005 (2) SA 77 (SCA) ([2004] 4 All SA 261) at paras [10] and [11]. Own emphasis added.

⁷ Cameron *et al.* Honoré's *South African Law of Trusts*. 5th ed. at 117.

For the purposes of this dissertation, however, greater emphasis is placed on the essential that the trust object must be defined with reasonable certainty, and it will be discussed in the framework of the following long-standing principles of trusts and trust law:

- Trusteeship as an office.
- Variation or termination of a trust.
- The effect of an invalid variation or termination.
- Sham trusts.
- Duty of auditors, trustees, the Master and the court regarding trusts.

Each of these aspects will now be dealt with in more detail:

2.3 The object of a trust must be sufficiently certain

To illustrate this requirement, reference can be made to the well-known English case of *Morice v Bishop of Durham*⁸ where the testator's intention was to create a trust '*for such objects of benevolence and liberality as the trustee in his own discretion shall most approve*'. The court found that notwithstanding the testator's intention to create a trust, '*...the object being too indefinite, has failed*'.

The court in the *Morice* case referred to *Brown v Yeall*, and stated:

In Brown v. Yeall (7 Ves. 50, n.) the object was held so vague that it could not be executed: not, that the distribution of such books as were in the view of that testator was a vague object: but the mode was not pointed out. It was thrown entirely upon

⁸ [1805] EWHC Ch J80.

the Court of Chancery to say, who were the persons, what the books, and what the manner of distribution. Though the general object was pointed out, yet its nature was vague and uncertain. No case has yet overturned that decision...

It follows in English law that:

*... every trust (other than a charitable one) must have a definite object. There must be somebody in whose favour the court can decree performance. If there are no beneficiaries, nobody can enforce the trust in the event that the trustees fail to carry out their duties.*⁹

In South African law the trust object may consist of: (i) the benefit of one or more names or ascertainable persons or classes of person, including juristic persons; and/or (ii) one or more impersonal object.

When the trust objective is to benefit persons or classes of person, it follows that if the person or classes of person for whose benefit the trust is intended are not named or determinable, the trust will fail for lack of a certain object.¹⁰ The founder need not list each and every beneficiary. It is sufficient if he describes the class of beneficiary and then leaves the selection to the trustees, provided the class is reasonably clearly defined. If no distinct class is indicated, nor any particular beneficiary designated, the trust will fail.¹¹

In the well-known case of *Harter v Epstein*,¹² the testator appointed executors and trustees, made a specific bequest to his daughter, and then added: '*The balance of my estate to be left to the discretion of my executors*'. It was held that the balance of the estate went on intestacy

⁹ http://en.wikipedia.org/wiki/Purpose_trusts_in_English_law#cite_note-9.

¹⁰ Cameron *et al.* (2002). *Honoré's South African Law of Trusts*. 5th ed. Cape Town, paras 86–89 at 151–152. See also <http://www.jutalaw.co.za/products/3607-honore-the-south-african-law-of-trusts#sthash.1tLnP3mK.dpuf>; re *Estate Grayson* 1937 AD 96; *Dempers v The Master* 1977 (4) (SWA) where it was held *per Hart* AJP that the trust was meaningless and impracticable and therefore invalid.

¹¹ Joubert *et al.* LAWSA. 2nd ed. Vol 31 para 536 at 340.

¹² 1953 (1) SA 287 (A).

since no valid trust was created (for lack of a sufficiently certain object), nor could it be implied that the daughter was heir to the residue.

If the trust object fails because the beneficiary cannot take, or because the object is insufficiently defined, the trust itself falls away.¹³ (See also the reference by Honoré of the *Verseput* case¹⁴).

From what has been stated above, it follows that each trust is formed with a different and distinct clearly defined object and purpose, and if this object and purpose fails, then the trust in effect fails.

For example: Trust A is formed by the donor Mr X for the sole benefit of his children XY and XZ and is to be managed by trustee T. If both children die, the object of the trust is destroyed and the trust accordingly fails. A new trust could be formed by the same donor Mr X for the benefit of his grandchildren XYY and XZZ, to be managed by trustee T. Logic dictates that as the objects of the trusts differ materially the two trusts could not be the same.¹⁵

2.4 Trusteeship as an office

Both the legislature and the courts have acknowledged that a trustee acts in an official capacity,¹⁶ which Honoré refers to as a *'quasi-public office'*,¹⁷ while proceeding to describe trusteeship as follows:

An office and a trust, though usually created by a private individual or group, is an institution of public concern, so that the public authority as represented by the Master

¹³ Cameron *et al.* Honoré's *South African Law of Trusts*. 5th ed. at 171, para 106.

¹⁴ *Verseput v De Gruncy* NO 1977 (4) SA 440 (W) at 445 where the daughter (beneficiary) died during her father's (founder's) lifetime.

¹⁵ *Die Meester v Meyer en Andere* 1975 (2) SA 1 (TPA) at 12.

¹⁶ Section 6(1), 10 and 11(1)(a) of the TPCA; *Jowell v Bramwell-Jones* 1998 (1) SA 836 (W) at 884E; *Land and Agricultural Development Bank of SA v Parker* 2005(2) SA 77 (SCA) at 84.

¹⁷ Cameron *et al.* Honoré's *South African Law of Trusts*. 5th ed. at 11, 12 and 57.

and the courts has jurisdiction to take necessary steps to ensure that the trust is properly administered.

A trustee holds an office and is not merely party to a contract with the founder. Fleming DJP formulated the point in *Joubert v Van Rensburg*¹⁸ as follows:

When B is in such a contract called a 'trustee' the word, because of the purely contractual basis, signifies that B is a contracting party who is bound to some fiduciary component in applying himself to the arrangement. It has a parallel in its fiduciary element to the duty of a trustee in a testamentary trust (where the trustee legally starts off as a 'burdened legatee').

Ultimately, it is said that the trustee must in the performance of duties and the exercise of powers, act *'with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another'*.¹⁹

This duty is also enshrined in the definition of a 'trust'²⁰ where it is stated that the assets of the trust:

... should be administered or disposed of according to the provisions of the trust instrument for the benefit of the person or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument.

¹⁸ 2001 (1) SA 753 (W) at 768.

¹⁹ Section 9 of the TPCA sets out the care, diligence and skill that are required from a trustee as follow:

- (1) *A trustee shall in the performance of his duties and the exercise of his powers act with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another.*
- (2) *Any provision contained in a trust instrument shall be void in so far as it would have the effect of exempting a trustee from or indemnifying him against liability for breach of trust where he fails to show the degree of care, diligence and skill as required in subsection (1).*

²⁰ Section 1 of the TPCA.

Honoré²¹ accordingly formulates the first principle of trust administration as follows:

[T]he duty of the trustee(s) to give effect to the trust instrument, properly interpreted, as far as it is lawful and effective under the law, the trust instrument forms the statute under which the trustee acts.

The relevant question is then what the effect would be if the trustee(s) fail(s) to administer the trust in accordance with the trust instrument by varying or attempting to vary the trust instrument outside the parameters of the trust instrument.

2.5 Sham trusts

A trust is regarded as a 'sham trust' when the founder (or the trustees) has too much control, mainly in the form of decision-making powers, over the trust and its assets, with the result that the trustees or remaining trustees act as mere nominees and not as independent trustees exercising their own independent judgment.²²

This principle was *inter alia* dealt with in *Land and Agricultural Bank of South Africa v Parker and Others*²³ and formulated by Cameron JA as follows:

The core idea of the trust is the separation of ownership (or control) from enjoyment. Though a trustee can also be a beneficiary, the central notion is that the person entrusted with control exercises it on behalf of and in the interests of another. This is why a sole trustee cannot also be the sole beneficiary. Such a situation would

²¹ Cameron *et al.* *Honoré's South African Law of Trusts*. 5th ed., at 262. Own emphasis added.

²² This concept is also common in corporate law. Joubert *et al.* (2013). *LAWSA*. 2nd ed. Vol 4 Part 1, para 85 at 119 state that:

The separate existence of the corporation is, by way of metaphor, conceived of as creating a 'veil' separating the company from its members and concealing them from those who deal with it. The veil is said to be 'pierced' when, in certain exceptional circumstances, the court either ignores the company and treat its members as if they were the owners of its assets and were conducting its business in their personal capacities, or attributes rights or obligations of the members to the company.

²³ 2005 (2) SA 77 (SCA) at 86E. Own emphasis added.

embody an identity of interests that is inimical to the trust idea, and no trust would come into existence. It may be said, adapting the historical exposition of Tony Honoré, that the English law trust, and the trust-like institutions of the Roman and Roman-Dutch law, were designed essentially to protect the weak and to safeguard the interests of those who are absent or dead. This has not changed. The essential notion of trust law, from which the further development of the trust form must proceed, is that enjoyment and control should be functionally separate. The duties imposed on trustees, and the standard of care exacted of them, derive from this principle. And it is separation that serves to secure diligence on the part of the trustee, since a lapse may be visited with action by beneficiaries whose interests conduce to demanding better. The same separation tends to ensure independence of judgment on the part of the trustee – an indispensable requisite of office – as well as careful scrutiny of transactions designed to bind the trust, and compliance with formalities (whether relating to authority or internal procedures), since an independent trustee can have no interest in concluding transactions that may prove invalid.

The consequences of 'sham trusts' are that the court will have regard to substance over form. For example, it was held in *Zandbergh v Van Zyl*²⁴ that: 'an agreement will be ignored and not given effect to if it does not reflect the true intention of the parties'.

Joffe²⁵ sums this up as follows:

... in South Africa, just as required by offshore jurisdictions, for a valid trust to exist, the founder must properly divest himself of the trust property. Failing that, and if the founder maintains control over the assets, the courts validly have the power under South African law to declare the trust a sham, and allow the assets to be attacked by a spouse or creditors.

In *Badenhorst v Badenhorst*²⁶ the court also dealt with this aspect and found that the assets²⁷ of the *inter vivos* trust were to be regarded as Mr Badenhorst's own property, and had to be taken

²⁴ 1910 AD 302.

²⁵ Joffe, H. (2007). Sham Trusts. *De Rebus*, Jan/Feb, at 25. Own emphasis added.

²⁶ 2006 (2) SA 255 (SCA).

into account for purposes of a redistribution order. The court in this matter established the following principles:

- To succeed in a claim that the trust assets must be included in the estate of one of the parties to a marriage there needs to be evidence that such party controlled the trust.
- Control must be *de facto* and not necessarily *de iure*.
- To determine whether a party has such control it is necessary:
 - first to have regard to the terms of the trust deed, and
 - secondly to consider the evidence of how the affairs of the trust were conducted during the marriage.

The court *per* Combrinck AJA found that the following evidence supported the view that the trust was a sham and that Mr Badenhorst ('B') retained full control of the assets of the trust and used the trust merely as a vehicle for his business activities:

- The founder of the trust was B's father, whose only contribution to the trust property was an initial amount of R1 000.00.
- B and his brother were the only trustees.
- B has the right to discharge his co-trustee and appoint someone else in his place.

²⁷ It was stated *obiter* that:

It may be that in terms of the trust deed some or all the assets are beyond the control of the founder, for instance where a vesting has taken place by a beneficiary, such as a charitable institution accepting the benefit. In such a case, provided the party had not made the bequest with the intention of frustrating the wife's or husband's claim for a redistribution, the asset or assets concerned cannot be taken into account.

- From the evidence it is clear that in his conduct of the affairs of the trust, B seldom consulted or sought the approval of his co-trustee.

- B paid scant regard to the difference between trust assets and his own assets in that:
 - In an application for credit facilities, B listed the trust assets and the income generated as his own.

 - At one stage B insured a trust asset (a beach cottage) in his own name.

 - A property registered in B's name was financed by the trust.

 - B received an income of R50 000.00 per month from a company despite the fact that the shares in the company were owned by the trust.

In the premise, if it is found that a trust is a 'sham' the trust would be regarded as the *alter ego* of the founder and/or trustees and/or beneficiaries, with the consequence that the trust would be regarded as non-existent.

SARS have repeatedly indicated that they intend to 'sink their teeth' into sham trusts. I submit, for reasons that will later become apparent, that the 'sale' of a trust should raise a red flag for SARS.

2.6 Variation or termination of a trust

A clear distinction must be drawn between the terms 'variation' and 'termination'.

A **variation** on something is the same thing presented in a slightly different form.

When you **terminate** something or when it terminates, it ends completely.²⁸

Termination of a trust brings the trust to an end and takes place by either revocation or discharge.

Variation consists in the alteration of the terms of a trust deed and is permitted in appropriate circumstances which are governed by (i) the common law; and (ii) statute.²⁹

Whether it is possible to vary the trust instrument or terminate a trust altogether (except for a variation in terms of section 14 of the TPCA³⁰) depends on whether the trust is a testamentary trust (created by the provisions of a will) or an *inter vivos* trust.

2.6.1 Variation of a testamentary trust

Section 13 of the TPCA gives the court certain powers regarding the variation of a trust deed. The section provides that:

If a trust instrument contains any provision which brings about consequences which in the opinion of the court the founder of a trust did not contemplate or foresee and which –

- (a) *hampers the achievement of the objects of the founder; or*
- (b) *prejudices the interests of beneficiaries; or*

²⁸ Collins. (2006). *Cobuild Advanced Learner's English Dictionary*. 5th ed. (2006), Mumbai: Thomson Press (India) Ltd.

²⁹ Sections 13 and 14 of the TPCA and the Immovable Property Act 94 of 1965.

³⁰ Act 40 of 1949. Section 14 provides that:

... whenever a trust beneficiary under tutorship or curatorship becomes entitled to a benefit in terms of a trust instrument, the tutor or curator of such a beneficiary may on behalf of the beneficiary agree to the amendment of the provisions of a trust instrument, provided such amendment is to the benefit of the beneficiary.

(c) *is in conflict with the public interest,*

the court may, on application of the trustee or any person who in the opinion of the court has a sufficient interest in the trust property, delete or vary any such provision or make in respect thereof any order which such court deems just, including an order whereby particular trust property is substituted for particular other property, or an order terminating the trust.

To protect the long-standing and well-established principle of freedom of testation, the court will not easily vary the terms of a trust created by a will and will allow the variation only *ob causam necessariam*; in other words, in cases of dire necessity.³¹

From the aforementioned it is clear that the termination of a testamentary trust or any variation of its provisions not authorised by the trust instrument or without recourse of the court would be invalid.

2.6.2 Variation of an *inter vivos* trust

Section 13 of the Trust Property Control Act also applies to *inter vivos* trusts. But, unlike a testamentary trust, an *inter vivos* trust may be varied or terminated without recourse to a court of law if the founder is still alive.

A distinction should therefore be drawn between **variations made during the lifetime of the founder** of the trust and those made **after his/her death**.

If the **founder has passed away** the trustees,³² like those of a testamentary trust, are limited by statute or by the authority granted to them in terms of the trust deed itself³³ in their power to vary the terms of the trust instrument or terminate the trust altogether.

³¹ *Ex Parte Strauss* 1949 (3) SA 929 (O) at 945.

The situation changes and the problems start when **variations** are made, or the trust is terminated, **during the lifetime of the founder**.

In *Hofer and Others v Kevitt NO 1998 (1) SA 382 (SCA)*, the deed of an *inter vivos* trust, at the initiation of the founder and with the consent of the trustees, had been varied to the prejudice of the beneficiaries. Three important facts in this case need to be highlighted: (i) the beneficiaries had never accepted any benefits under the trust; (ii) no provision was made in the trust deed for the amendment of its terms nor was there any reservation of a unilateral right of revocation for the donor; and (iii) the trust was amended on the instructions of the donor, and the trustees, for the time being, consented thereto.

The applicants (beneficiaries) argued that the rights of trustees to vary the deed were not unfettered, and if the proposed variations were not in the interests of both the founder and the discretionary beneficiaries, then it was the duty of the trustees not to agree to them. It was argued that the trustees had not even considered the interests of the discretionary beneficiaries and had acted directly on the founder's request for a variation.

³² Be advised that the trustees must act together and where one of them has not so consented, the variation will be invalid. See in this regard Cameron et al. Honoré's South African Law of Trusts, 5th ed., at 320 para 197; *Land and Agricultural Bank of South Africa v Parker and Others* 2005 (2) SA 77 (SCA) in which Cameron JA stated at 85 para [15]:

Joint action requirement entails that trustees must act together... It is a fundamental rule of trust law, which this Court recently restated in Nieuwoudt and Another NNO v Vrystaat Mielies (Edms) Bpk, that in the absence of contrary provision in the trust deed the trustees must act jointly if the trust estate is to be bound by their acts. The rule derives from the nature of the trustees' joint ownership of the trust property. Since co-owners must act jointly, trustees must also act jointly. Professor Tony Honoré's authoritative historical exposition has shown that the joint action requirement was already being enforced as early as 1848. It has thus formed the basis of trust law in this country for well over a century and half. See also Potgieter v Potgieter 2012(1) 637 (SCA); See also Steyn and Others NNO v Blockpave (Pty) Ltd 2011 (3) SA 528 (FB) at para [18] 'These comments concerning the exclusion of the third applicant from decision-making processes relating to the affairs of the trust were disturbing. ...The trust required the full and complete participation of all its trustees in order to function legally....The comments of the first applicant show a lack of understanding of the juristic nature and functioning of the trust. The trustees have to decide, participate, and act together, as one, in dealing with the affairs of the trust, even where they are not all agreed, or even where they are not all present at a meeting under the same roof. (Own emphasis added.)

³³ *Tijmstra NO v Blunt-MacKenzie NO 2002 (1) SA 458 (T)* at 468J:

... trustees are bound by the powers invested upon them in terms of the trust deed.

The court in the *Hofer* case referred to *Crookes, NO and Another v Watson and Others*³⁴ where it was accepted that a trust *inter vivos* is a contract for the benefit of a third person, and unless the beneficiaries have accepted the benefit stipulated for them, then it can be varied by agreement between the founder and the trustee.

It further appears that the founder may, in the trust deed, reserve the right to vary the provisions of that trust.³⁵ The classic example is the 'testamentary reservation' in terms of which a founder testator reserves the right to determine in his will the formula for the distribution of trust benefits to defined beneficiaries after his demise.³⁶ It is submitted, however, that this is a dangerous reservation in that the court could regard this reservation, with or without other factors, as proof that the particular trust is a 'sham'. The principle that operates here will be discussed more fully further on.

The current law accordingly permits the founder of an *inter vivos* trust to make variations to the deed, apparently without limit, or even terminate the trust if he so chooses (i) if the right was expressly reserved, or (ii) if not so reserved, then by agreement with the trustees, if the

³⁴ 1956 (1) SA 277 (A) where Centlivres CJ stated at 285:

Under clause 1 of the deed the settlor donated 'irrevocably' to the trustees the shares mentioned in that clause. I do not think that the word 'irrevocably' is of any significance as far as the present proceedings are concerned. If A enters into a contract with B and the contract purports to be irrevocable that does not mean that the contract may not be cancelled or amended with the consent of both A and B. Similarly when a contract is entered into between A and B for the benefit of C and C has become a party thereto by acceptance such a contract can, notwithstanding that it purports to be irrevocable, be cancelled or amended if A, B and C agree to such cancellation or amendment. Speaking generally, every contract, whether it purports to be irrevocable or not, is irrevocable in the sense that it cannot be revoked by the unilateral act of one of the parties...If the beneficiaries (either vested or discretionary) have accepted the benefits which have or may accrue to them in the terms of the trust deed, then the beneficiaries became part of that contract (i.e. part of the trust), and any variations or amendments thereto can only be made with their approval.

³⁵ *Crookes, NO and Another v Watson and Others* 1956 (1) SA 277 (A) at 285:

The next provision of the deed to be considered is clause 3 which provides that: 'the settlor shall have no power wholly or partly to revoke, cancel or annul any of the trusts or provisions hereby declared'. This provision applies in my opinion only to unilateral action on the part of the settlor. In the present appeal he is not asking for an order declaring that he, acting alone, is entitled to amend the trust deed.

³⁶ Pace, R.P. & Van der Westhuizen, W.M. (1995), *Wills and Trusts*. (Loose-leaf service issue 10) Durban: Butterworth, at 62(1).

beneficiaries have not yet accepted the benefit stipulated for them, or if the beneficiaries did accept, then with their further consent.

Consequently, any variation or termination without consensus between the founder and trustee(s) or the beneficiaries who have accepted the benefits will be invalid, as was confirmed by Brand JA in *Potgieter v Potgieter*³⁷ as follows:

As a matter of law, the deceased and the trustees had no authority to amend the trust deed without the appellants' consent. Their attempt to do so can therefore not be categorized as breach of contract. As a matter of positive law, they had no power to do what they purported to do. Their agreement to do so was therefore without any force and effect. This means that the variation agreement was invalid.

2.6.3 Variation of trustees

Trustees may freely resign or be appointed and/or substituted in accordance with the general trust instrument, and if the trust instrument is silent then by the Master in terms of section 7 of the TPCA, which provides that:

If the office of trustee cannot be filled or becomes vacant, the Master shall, in the absence of any provision in the trust instrument, after consultation with so many interested parties as he may deem necessary, appoint any person as trustee.

Section 23 of the TPCA even provides a remedy for invalid, illegal or improper variations:

Any person who feels aggrieved by an authorization, appointment or removal of a trustee by the Master or by any decision, order or direction of the Master made or issued under this Act, may apply to the court for relief, and the court shall have the

³⁷ 2012 (1) SA 637 at 652H. Own emphasis added.

*power to consider the merits of any such matter, to take evidence and to make any order it deems fit.*³⁸

2.6.4 Variation of beneficiaries

As is apparent from the above, it is permissible in law to substitute trustees with relative ease; the same does not apply where beneficiaries are concerned.³⁹

Again, a distinction must be drawn between situations where the **founder has passed away** and those where he is **still alive**.

When the **founder has passed away** the position is clear.

The definition⁴⁰ of a 'trust' clearly stipulates that the trust assets must be:

... administered or disposed of according to the provisions of the trust instrument for the benefit of the person or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument.

Any variation in the form of a substitution of beneficiaries after the death of the founder must accordingly be in accordance with the object and purpose of the trust as provided for in the specific trust instrument.

With the founder's consent, as previously discussed, a variation in the form of a substitution of a beneficiary would be possible. I submit, however, that this variation would be limited to the point where the trust is no longer being varied but terminated. This will be illustrated further on.

³⁸ Section 23 of the TPCA.

³⁹ Cameron *et al.* (2002). *Honoré's South African Law of Trusts*. 5th ed. Cape Town: Juta, at 506–508.

⁴⁰ Section 1 of the TPCA. Own emphasis added.

2.7 Variation outside the parameters of the trust instrument

It is clear from the nature of a trust, as well as the limitations to the variation thereof, that the trustee or any other relevant person may not tamper with the object and purpose of the trust as laid down by the founder and which the trustees have agreed to uphold.

The problem starts when the net effect of the variation is so substantial that the principal object and purpose of the original trust, as envisaged by the donor, have failed.

It was held by Margo J in *Die Meester v Meyer en Andere*,⁴¹ where two provisions of a trust in regard to who the beneficiaries should be were in direct conflict with each other, that one could not be regarded as *pro non scripto* but that the trust had failed:

Die eenvoudige posisie is dat sodra para. C pro non scripto beskou word is die trust soos in die testament voorgeskryf onuitvoerbaar en verval dit. Al mag dit moontlik wees om 'n trust te administreer ooreenkomstig die oorblywende bepalings sou dit nie die trust wees wat in die testament voorgeskryf is nie. Dit is nie nodig om enige mening uit te spreek oor wat die regsposisie sou gewees het as die bepaling wat geskrap word nie essensieel of wesenlik was nie.

An action (variation) can therefore not be undertaken which would cause the failure of the object and purpose of a trust (and therefore the failure of the trust). This action would be invalid.

The question which suggests itself is what the effect of such an invalid variation would be.

2.8 The effect of an invalid variation

It is a fundamental principle of our law that a thing done in a manner contrary to the direct prohibition of the law is void and has no effect.⁴²

⁴¹ 1975 (2) SA 1 (TPA) at page 12. Own emphasis added.

The same principle applies in respect of the invalid variation of a trust instrument, as was held in *Potgieter v Potgieter*.⁴³ The court *per* Brand JA found that where the consensus of a beneficiary was needed and not obtained:

... the variation agreement was invalid and that the provisions of the original trust deed must be applied in unamended form.

If an action (variation) is undertaken whereby a new object and purpose are implemented in the place of the original object and purpose, the latter effectively die. It is submitted that this action, which caused the demise of the old object and purpose, would effectively amount to a termination of the trust itself.⁴⁴

The invalid variation will therefore have the effect not of variation but of a termination.

It must be kept in mind that a termination (which we can label the aforesaid as) is possible if the founder consents thereto, but then it is a (valid) termination of the trust and not an (invalid) variation.

For example: If a trust were created for the sole benefit of grandchildren XY and XZ, who subsequently died, a substitution of 'the Church of England' as the beneficiary would defeat the object of that trust, resulting in the failure of the trust. The founder could create a new trust, with the same asset(s) or benefit(s) that the grandchildren would have received, with the object of benefiting the Church of England, but an amendment that merely substitutes the beneficiaries and is not in accordance with the object of the trust would be invalid. Thus the net effect of

⁴² *Schierhout v Minister of Justice* 1926 AD 99 109 where the following was stated *inter alia*:

The rule is thus stated: Ea quae lege fieri prohibentur, si fuerint facta, non solum inutilia, sed pro infectis habeantur; licet legislator fieri prohibuerit tantum, nec specialiter dixerit inutile esse debere quod factum est.' (Code 1.14.5). So that what is done contrary to the prohibition of the law is not only of no effect, but must be regarded as never having been done – and that whether the lawgiver has expressly so decreed or not; the mere prohibition operates to nullify the act.

⁴³ 2012(1) SA 637 at 649 F-G. Own emphasis added.

⁴⁴ *The T Trust v The Commissioner for the South African Revenue Service*, in the South African Tax Court (Johannesburg) under case number 11286 [2007].

such a variation (outside the parameters of the object and purpose of the trust) is in fact a termination of the old trust. If the founder so intends, a new trust could be created with a new and distinct object and purpose.

It is submitted that it can be argued that an invalid variation (which is done outside of the parameters of the trust object as defined in the trust instrument) should, on the same basis, be null and void *ab origine* and without the effect of a variation, with the initial terms being regarded as unamended or that an invalid variation could be considered to have the effect of terminating the trust.

It is submitted that a substantial variation or termination of a trust instrument outside the parameters of the trust instrument could also be a clear indication that the founder and/or trustees did not properly divest himself/themselves of the trust property and in fact maintain(s) control over the assets, which could lead to a finding that the trust is a 'sham'.

2.9 The 'watch dogs' of a trust

As previously indicated, the trustee(s) has/have a duty to uphold the trust instrument and not to allow invalid variations or terminations.

A further duty is imposed on persons who audit trusts in terms of section 15:⁴⁵

If an irregularity in connection with the administration of a trust comes to the notice of a person who audits the accounts of a trust, such person shall, if in his opinion it is a material irregularity, report it in writing to the trustee, and if such irregularity is not rectified to the satisfaction of such person within one month as from the date upon which it was reported to the trustee, that person shall report it in writing to the Master.

I submit that SARS does indeed fall into the category of persons who audit trusts⁴⁶ and accordingly has a duty.

⁴⁵ Of the TPCA. Own emphasis added.

Let us now consider the Master⁴⁷ and the court⁴⁸ whose duty it is to protect the trust. *Per Honoré*:⁴⁹

Trusteeship is an office and a trust, though usually created by a private individual or group, is an institution of public concern, so that the public authority as represented by the Master and the courts has jurisdiction to take necessary steps to ensure that the trust is properly administered.

It is submitted that in view of the duties with which they are charged, these entities should not merely frown upon invalid variations or terminations or tax around it, but should enter the arena and take the further necessary steps to undo and discourage invalid variations or terminations.

⁴⁶ See inter alia ss 40 and 41 in Ch 5 of the Tax Administration Act 28 of 2011, which provide that SARS

may select a person for inspection, verification or audit on the basis of any consideration relevant for the proper administration of a tax Act, including on a random or a risk assessment basis.

It also provides that:

A senior SARS official may grant a SARS official written authorisation to conduct a field audit or criminal investigation, as referred to in Part B.

⁴⁷ The Master may in terms of s 16 of the TPCA call a trustee to account:

- (1) *A trustee shall, at the written request of the Master, account to the Master to his satisfaction and in accordance with the Master's requirements for his administration and disposal of trust property and shall, at the written request of the Master, deliver to the Master any book, record, account or document relating to his administration or disposal of the trust property and shall to the best of his ability answer honestly and truthfully any question put to him by the Master in connection with the administration and disposal of the trust property.*
- (2) *The Master may, if he deems it necessary, cause an investigation to be carried out by some fit and proper person appointed by him into the trustee's administration and disposal of trust property.*
- (3) *The Master shall make such order as he deems fit in connection with the costs of an investigation referred to in subsection (2).*

⁴⁸ Section 23 of the TPCA.

⁴⁹ Cameron *et al. Honoré's South African Law of Trusts*. 5th ed. at 11–12. See also s 13 of the TPCA. Own emphasis added.

2.10 Conclusion

It is extremely important, when dealing with a trust, to distinguish between the variation of a trust deed and the termination altogether of the trust.

Any variation outside the parameters of the trust object, as contained in the trust instrument, would be invalid and would not have the effect of a variation. Such a variation would therefore be null and void and without effect, and the provisions of the original trust deed would be applied in unamended form. The action could, however, have the effect of terminating the trust or may even cause the trust to be regarded as a 'sham'.

In view of the numerous possibilities that have been mentioned, it is important that the auditors of trust accounts, the trustees, the court, and the Master should scrutinise the actions of trusts and prohibit invalid variations or terminations for the sake of safeguarding the unique concept of a trust.

CHAPTER 3. CAN A TRUST BE SOLD?

3.1 Introduction

The 'sale of a trust' refers to the practice of replacing existing trust beneficiaries and trustees with new beneficiaries and trustees against monetary compensation.⁵⁰ The reason for this kind of agreement could be either to save the buyer the trouble of registering a new trust or to avoid payment of transfer duty (or possibly both).

3.2 What is sold?

What in effect is sold, against payment (or another form of compensation such as taking over debt), is:

- The office of trusteeship, and
- The rights to any benefit(s) (or possible benefits) from the trust

to a third person (the buyer) who, with his nominees, will substitute the trustees and beneficiaries.

3.2.1 *Sale of the office of trusteeship*

It is submitted that the office of trusteeship cannot be sold for the following reason:

⁵⁰ Du Toit, F. (2007). *South African Trust Law Principles and Practice*. 2nd ed. Durban: Lexis Nexis, at 195.

As mentioned, 'trusteeship is an official capacity', which warrants the trustee(s) in the performance of their duties and the exercise of powers to act '*with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another*'.⁵¹

Because of the nature of this office, it is submitted that it would be absurd to think that a person can sell his office (or duty) against monetary compensation to another. This would in effect mean that you can buy a trustee's statutory and common law duty and loyalty towards others.

Logic dictates that you cannot sell the office of your trusteeship and that such an action would be a breach of trust and *contra bonos mores*.

3.2.2 Sale of the beneficiaries' rights/benefits

If a trustee sells (which implies that he as a trustee receives the purchase price or gain from the sale) the beneficiary's right to benefit (or possible benefit) from a trust, this would entail a breach of trust as the trustee would be failing in his duty to act with the requisite impartiality, which implies the avoidance of a conflict between the trustee's personal interests and those of the beneficiary, as well as not making any undue profit from his trusteeship.⁵²

If the trust is not declared a 'sham' for this reason and other consequential factors, the 'sale' (in terms of the substitution of the beneficiary outside the object and purpose of the trust) would be invalid in any case, as the object and the trust will in effect have terminated.

Nothing prevents a beneficiary from selling his own right to a benefit(s) after it has accrued to him or from selling his right to future benefits. This is unlikely as most of the trust instruments (more specifically those of a discretionary trust) forbid such a sale or the parting of such a right(s) to a benefit, prior to accrual of the said right.

⁵¹ See also s 7 of the TPCA where this is expressed in unequivocal form.

⁵² Du Toit, F. (2007). *South African Trust Law Principles and Practice*. 2nd ed. Durban: Lexis Nexis, at 82–83.

3.3 Analytical discussion of the term ‘sale’

As stated, a ‘sale of a trust’ refers to the practice of replacing existing trust beneficiaries and trustees with new beneficiaries and trustees against monetary compensation. The intention is therefore that the trust should continue and not terminate. **The term ‘sale’ consequently excludes the practice of terminating a trust.**

Such a replacement can only be done by a variation of the trust instrument (agreement), which variation (in the form of replacement or substitution of trustees and beneficiaries) I submit would by design entail that it is done outside the parameters of the object and purpose of the specific trust.

This submission is based on the principle that a **living founder** cannot authorise a variation that exceeds the boundaries of his principal object and purpose so that it becomes a future determinable object and purpose or the object and purpose of another person. This would automatically entail that, (i) either no valid trust is formed (if the authorisation is contained in the deed) for the lack of a sufficiently certain object; or (ii), (where the founder authorised the act with ‘consent’ [*sic*] after the creation of the trust) that the principal object and purpose has in fact terminated.⁵³

This is also in line with the *Die Meester v Meyer en Andere*⁵⁴ matter where the court in effect said that if the object is unclear because of irreconcilable provisions, one provision cannot just be regarded as *pro non scripto*, as this would result in the lapse of the trust as the trust is just not the same as the one created in the testament.

Consequently, and following the discussion of the nature of a trust, it is submitted that a ‘sale of a trust’ (with the ‘consent or authorisation’ of the founder) in the form of a substitution is not possible since the object would no longer be the same and accordingly, the trust would not be

⁵³ *The T Trust v The Commissioner for the South African Revenue Service* where Mbha J stated:

that the principal object and purpose of the original trust as envisaged by the donor had been terminated in that a different ascertainable object and purpose to the original trust had been effected. (Own emphasis added.)

⁵⁴ 1975 (2) SA 1 (TPA) at 12.

the same either. Such a sale is invalid, null and void *ab origine* and can have no legal effect as it would bring about the failure of the trust. As no substitution can take place, there cannot be a 'sale' as intended.

Where the **founder has passed away** an intended 'sale' would be invalid and the court should regard the trust as being in its unamended form.

The problem is that most, if not all, of these 'sales' are only dissected after the contract is no longer in existence as the seller will have received payment and the contract been discharged by performance.

It is submitted that the net effect should then be determined (on the principle of 'substance over form') which I submit is that: (i) the trust has effectively failed and has been terminated against payment of compensation, and (ii), the buyer and his nominees are what they regard themselves as being. If the buyer intends to create a trust (which is one of the essentials for the creation of a valid trust), he would be the founder and so on, but to regard the trust as the same, merely with a variation, is submitted to be wrong.

3.4 Conclusion

It is therefore concluded that a trust, because of its nature, cannot be sold. Such an agreement would be invalid, null and void *ab origine* and can have no legal effect as it would bring about the failure of the specific trust. No substitution can be effected from such a 'sale'.

CHAPTER 4. THE T TRUST v THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE

4.1 The facts and findings of the judgment

Before further discussion, it must be kept in mind that the facts of *The T Trust v The Commissioner for the South African Revenue Service*⁵⁵ date back to before the implementation of the amendment of the definitions of 'transaction' and 'property' in the Trust Duty Act,⁵⁶ (2002 amendments) which will be dealt with later.

The *T Trust* case, notwithstanding the fact that it pertained to a tax question, did deal directly with a 'sale' agreement (in terms of which the trustees and beneficiaries were substituted) and the nature thereof.

In casu SARS claimed payment of transfer duty from the T Trust on the grounds that transfer of property had taken place when trustees and beneficiaries were substituted in terms of a 'sale' agreement of this nature.

It is important to highlight the fact that the **variations** (in terms of which the trustees and beneficiaries were substituted) **were effected with the consent of the founder**, who was still alive.

SARS argued *inter alia* that:

- *the agreement constituted a transaction as contemplated in section 1 of the Transfer Duty Act, 40 of 1949 ('Act'); and/or*

⁵⁵ In the South African Tax Court (Johannesburg) under case number 11286 [2007].

⁵⁶ Act 40 of 1949.

- *the agreement, viewed holistically, constituted a scheme tantamount to the disposal of the property to a new trust clearly with other trustees and beneficiaries. (Own emphasis added.)*

T Trust argued *inter alia* that it was never the intention of the parties to create a new trust but to take over a trust and that the agreements were incorrectly drafted. It is appropriate to state here that this contention was dismissed by the court after it was found that the agreements had been drafted in accordance with the intention of the parties and that a new trust had been created.

The court *per* Mbha J ultimately gave judgment in favour of SARS and found as follows:⁵⁷

- *I am satisfied that viewed holistically, the agreements constitute a transaction as contemplated in the Act and transfer duty on the value of the property is payable.*
- *In casu the beneficiaries [sic] in effect varied the trust. They used the trust property and set up a new trust that differed from the old.*
- *The net effect of the agreements was that the principal object and purpose of the original trust as envisaged by the donor had been terminated in that a different ascertainable object and purpose to the original trust had been effected.*
- *This new trust is in law liable for transfer duty.*

4.2 Analysis of the effect of the judgment

As stated, the court found that the net effect of the agreements was that the principal object and purpose of the original trust, as envisaged by the donor, had been terminated in that a different ascertainable object and purpose to those of the original trust had been effected and the new trust was liable in law for transfer duty.

The effect of the judgment is that the court *de facto*:

- (a) allowed the substitution of the trustees and beneficiaries in terms of the ‘sale’;

⁵⁷ At paras [26], [51], [52], [53]. Own emphasis added.

- (b) found that a new trust had been born; and thereafter
- (c) held the new trust liable for transfer duty.

The *dictum* is problematic and questionable for the following reasons:

- The court allowed the substitution, which I submit cannot be done for the reasons already discussed.
- The court did not distinguish between variation and termination of a trust.⁵⁸ The court found that the trust ceased to exist (terminated) in that a different ascertainable object and purpose to those of the original trust had been effected but then ultimately permitted the variation or substitution as the parties intended.
- The court found that a new trust was born while:
 - Factually there is no 'new trust' as the same T Trust ('the accumulation of assets and liabilities'⁵⁹) with the same IT number and in all probability the same trust provisions is alive and operating and has in fact been held liable for transfer duty by the same court.
 - Logic dictates that the founder can never be substituted because of the fact that he is the creator and the source of the distinct object and purpose of the trust. This will mean that notwithstanding the finding that a 'new trust' had been created, the founder remained the same because only the trustees and beneficiaries were substituted.
 - The founder's (seller's) name factually still exists in the trust instrument in that capacity.

In discussing this point it must be remembered that it is an essential for the creation of a valid trust that the founder intends to create a trust, and that the founder's intention must be expressed in a mode appropriate to create an obligation. The **founder (seller)** could surely

⁵⁸ See para [51] which is in contrast with para [52] regarding this.

⁵⁹ *Land and Agricultural Development Bank of SA v Parker* 2005(2) SA 77 (SCA) at paras [10] and [11].

not have had the intention to create a new trust for the benefit of the new beneficiaries and to be managed by the new trustees.

The **buyer** also had no intention of creating a new trust, and therefore argued that the intention was to take the trust over. If he (the buyer) had intended to create a valid trust his name would be pinned up on a trust instrument in that capacity. The 'new trust' may become embroiled in a predicament in that any further variation would need the consent of the founder (seller).

I submit that the neither the parties nor the court could have had the intention that the founder should still, even after receiving his share, have the ultimate say.

- The agreements did not constitute a transaction in terms of the provisions of the TDA before the 2002 amendments as acknowledged by the learned judge. This aspect is dealt with in more detail in Chapter 5.

As there was no new trust formed, the court should have established who the real buyer or buyers were, and should have held them liable for transfer duty.

The argument by the T Trust legal representatives that it was never the intention of the parties to create a **new trust** but to **take over a trust** is, for the same reasons that apply in respect of a 'sale', also flawed and *contra* trust law.

The court's argument in regard to the termination of the trust followed by the birth of a new trust is identical to the statement by Cameron:⁶⁰

It follows that they [beneficiaries] can in effect vary the trust, because they can use the trust property to set up a new trust that differs from the old.

⁶⁰ Cameron *et al.* *Honoré's South African Law of Trusts*. 5th ed., para 310 at 506.

Neither of the cases referred to by the learned author deal specifically with this statement. It is submitted that this statement is flawed by reason of the arguments already advanced. It is one thing to terminate a trust (which may be valid) but another to bring about, under the ‘variation-flag’, a totally different trust.

4.3 Conclusion

It is submitted that the court was correct in its finding that the trust terminated because the object failed, but the remainder of the finding and arguments are *contra* trust law and accordingly without merit.

It is further submitted that both the court and SARS disregarded their common law and statutory duty as they, as ‘watch dogs’, should have investigated and corrected the position and/or have referred the matter to the Master.

CHAPTER 5. TRANSFER DUTY

5.1 Historical background

The land shall not be sold for ever: for the land is Mine, for ye are strangers and sojourners with Me.

– Leviticus 25:23

After the conquest of the land of Canaan by the Israelites, 40 years after the Exodus from Egypt around 1280 BC, it was divided among the tribes of Israel according to the instructions⁶¹ of YHWH.⁶² The farmland was to be passed down within each specific tribe through inheritance alone and no other person could buy the farmland. Owners in the generation were, however, allowed to sell leasehold on their property but with the limitation that all leaseholds terminated at the same time, namely every 50 years, in the year of Jubilee. This prevented fathers from disinheriting subsequent generations.

This dispensation, where income accrued to the owner (at the time) through lease, was the root of transfer duty, descriptively called 'God's right' (or 'Hereregte' in Afrikaans).

SARS's *Transfer Duty Guide*⁶³ states that:

Transfer duty (originally referred to as the '40th penny' – because of a 2.5% tax rate at the time) was introduced in Holland in 1598. It was also introduced in the former Dutch colonies of Batavia (in 1623), Surinam (in 1684), Cape of Good Hope (in 1686) and Curaçau (in 1741). Transfer duty is one of the oldest taxes still levied in present-

⁶¹ According to the Fourth Book of Moses, Numbers, ch 34.

⁶² The Second Book of Moses, Exodus, ch 3 v 14 - The Hebrew name of the God of Israel, probably originally pronounced Yahweh. See Youngblood, R.F. (1995). *Nelson's New Illustrated Bible Dictionary*. USA: Thomas Nelson.

⁶³ SARS. *Transfer Duty Guide*, March 2013 <http://www.sars.gov.za/Pages/Find-a-Publ.aspx?sq=1&k=guide%20to%20transfer%20duty>.

day South Africa and was modelled on the Dutch and Batavian examples. The Transfer Duty Act became law on 1 January 1950 and applies to all acquisitions of property on or after that date. Any acquisitions before 1 January 1950 remain liable to duty under the relevant laws ... The Act is still in force today and was promulgated in Gazette Extraordinary 4193 on 28 July 1949.

5.2 Transfer Duty Act 40 of 1949

Transfer duty is levied in South Africa on the value of property acquired by any person by way of a transaction in terms of the Transfer Duty Act⁶⁴ (TDA). Section 2 of the Act currently provides as follow:

Subject to the provisions of section 9, there shall be levied for the benefit of the National Revenue Fund a transfer duty (hereinafter referred to as the duty) on the value of any property (which value shall be determined in accordance with the provisions of sections 5, 6, 7 and 8) acquired by any person on or after the date of commencement of this Act by way of a transaction or in any other manner, or on the amount by which the value of any property is enhanced by the renunciation, on or after the said date, of an interest in or restriction upon the use or disposal of that property, at the rate of...

Section 3 provides that:

The duty shall within six months of the date of acquisition be payable by the person who has acquired the property or in whose favour or for whose benefit any interest in or restriction upon the use or disposal of property has been renounced. (Own emphasis.)

Joubert summarises the imposition of transfer duty in LAWSA⁶⁵ as follows:

⁶⁴ Act 40 of 1949.

⁶⁵ Joubert *et al.* LAWSA. 2nd ed. Replacement volume 2012, Vol 22, Part 2 para 86 at page 36.

The intention and purpose of the legislation, when read with the opening words of the definition of 'property', is to tax the acquisition of land and the fixtures thereon. The definition of 'property' has however been expanded to include related concepts: a real right in land, a lease or sublease of a lot or stand registrable under the mining laws and a right to minerals as well as a lease or sublease of such a right. Other leases are excluded from the definition ... (Own emphasis added.)

It is a duty imposed on the consideration given by the person acquiring the fixed property for the right conferred on him or her to acquire the ownership of the property at the time stipulated in the transaction. The term 'acquire' is loosely used, meaning 'becoming entitled to', for the transaction gives rise to the liability to pay the duty whether or not transfer of ownership in fact ensues. The word 'acquire' does not include the purchasing of property under a contract of sale that is subject to a suspense condition that is not fulfilled.

There are, however, transactions which are exempt from the payment of transfer duty, the most relevant for our purposes and also the most common being transactions that would also attract value-added tax (VAT).⁶⁶ The sale of property cannot be subject to both. If the person who is selling the property is a registered VAT vendor and the property falls within his enterprise, then VAT will be levied on the transaction. If the person who is selling the property is not a registered VAT vendor, or the property falls outside his enterprise, then VAT will not be levied

⁶⁶ Section 15 provides that:

No transfer duty shall be payable in respect of the acquisition of any property under any transaction which for purposes of the Value-Added Tax Act, 1991, is a taxable supply of goods to the person acquiring such property if-

the transferor of the property under such transaction, in a declaration in such form as the Commissioner may prescribe, certifies that value-added tax payable under the said Act has been paid to him in respect of the said supply by the transferee and has been accounted for by him in a relevant return required to be furnished by him under the said Act or will be so accounted for in such return within the time allowed under that Act for the rendering of such return, or where such supply was subject to the said tax at the rate of zero per cent, such information regarding such supply as the Commissioner may require has been furnished to him;

any security required by the Commissioner for the payment of such tax has been lodged, if such tax has not yet been paid; and

the Commissioner has issued a certificate to the effect that the requirements of this subsection for the granting of the exemption have been met.

but transfer duty will be. Thus, VAT takes preference over transfer duty, and the seller will have to determine whether the transaction will be subject to transfer duty or VAT.

5.3 Tax Administration Act 28 of 2011

The general administration of all taxes in the Republic (including transfer duty) is governed primarily by the TA Act.

In terms of Proclamation 51 (GG 35687 dated 14 September 2012) the provisions of TA Act came into effect on 1 October 2012, except for –

... certain provisions relating to interest in sections 187 to 189 of the TA Act; and any amendment listed in Schedule 1 to the TA Act which relates to interest. Consequently, with effect from 1 October 2012, the general administration of all taxes in the Republic is governed primarily by the TA Act. The TA Act only deals with tax administration, and incorporates into one piece of legislation certain administrative provisions that are generic to all tax Acts. It also seeks to align the various administrative provisions which were previously duplicated in the different tax Acts, and to simplify and harmonise the provisions as far as possible.⁶⁷ (Own emphasis.)

5.4 A trust's liabilities in terms of the Transfer Duty Act

The position regarding the liability of a trust in terms of the TDA has changed substantially with the implementation of the Revenue Laws Amendment Act⁶⁸ (2002 amendments), as stated as follows by Mbha J in *The T Trust v The Commissioner for the South African Revenue Service*:⁶⁹

Section 2 of the Transfer Duty Act 40 of 1949 provided – prior to the amendments given effect to by the Revenue Laws Amendment Act, 74 of 2002 – as follows:

⁶⁷ SARS. *Transfer Duty Guide*, March 2013.

⁶⁸ Act 74 of 2002.

⁶⁹ At para [21].

'Subject to the provisions of section 9, there shall be levied for the benefit of the National Revenue Fund a transfer duty on the value of any property which shall be determined in accordance with the provisions of sections 5, 6, 7 and 8 acquired by any person on or after the date of commencement of this Act by way of a transaction or in any other manner, or on the amount by which the value of any property is enhanced by the renunciation, on or after the said date, of an interest in or restriction upon the use or disposal of that property, at the rate of –

- (a) *10% of the said value or the said amount, as the case may be, if the person by whom the property is acquired or in whose favour or for whose benefit the said interest or restriction is renounced is a person other than a natural person or ...'*

At the time the agreements in question were concluded the words 'property', 'person' and 'transaction' were defined as follows:

property –

'land in the Republic and any fixtures thereon and includes –

any real right in the land but excluding any right under a mortgage bond or a lease of property other than a lease referred to in paragraph (b) or (c)...'

person –

'includes the estate of the deceased or insolvent person or any trust.'

transaction –

'any agreement whereby one party thereto agrees to sell, grant, donate, cede, exchange, lease or otherwise dispose of property to another, or act whereby any person renounces any interest in or restriction in favour upon the use or disposal of the property.'

It is trite that the aim of the Revenue Laws Amendment Act, 74 of 2002 was, in accordance with the explanatory memorandum to such amending Bill, to extend the ambit of the circumstances in which transfer duty is payable to include circumstances where there is no registration of transfer of the immovable property.

This explanatory memorandum recognised that where properties were held in companies or trusts, a change in the shareholding or beneficiaries did not give rise to the payment of transfer duty. Thus, the definitions referred to above were amended to include for example the following:

'Property' - a contingent right to any residential property held by discretionary trust; and

'Transaction' - the substitution or addition of one or more of the beneficiaries with a contingent right to any property of that trust which property constitutes residential property. (Own emphasis added.)

The learned Professor F du Toit⁷⁰ concurred with this view:

*Until the amendment of the Transfer Duty Act in 2002 the acquisition of a contingent right by the new beneficiaries did not attract liability for transfer duty.*⁷¹ *However, the amendment in 2002 made important changes in respect of the sale of trusts under which beneficiaries only enjoy contingent rights to property. The relevant changes were, first, an addition to the definition of 'property' in section 1 of the Act. The definition now includes a contingent right to any residential property or share or member's interest, as contemplated in paragraphs (d) and (e) of the definition, held by discretionary trust (other than a special trust as defined in section 1 of the Income Tax Act). For this purpose the acquisition of the contingent right must be a consequence of or attempt upon the conclusion of any agreement for consideration with regard to property held by that trust; or be accompanied by the substitution or addition of any*

⁷⁰ Du Toit, F. (2007). *South African Trust Law Principles and Practice*. 2nd ed. Durban: Lexis Nexis, at 196. Own emphasis added.

⁷¹ This is contrary to the finding of Mbha J in the *T Trust* case, which I submit to be correct.

mortgage bond creditor; or be accompanied by the change of any trustee of that trust. Secondly, 'transaction' is now defined, in relation to a discretionary trust, as the substitution or addition of one or more beneficiaries with a contingent right to any property of the trust – be it residential property, shares or member's interest as contemplated in paragraph (d) and (e) of the definition of 'property', or contingent right as contemplated in paragraph (f) of that definition. A consequence of the acquisition of contingent rights in the aforementioned circumstances.

Transfer duty is payable in consequence of the 2002 amendments. SARS formulates this as follows in their *Transfer Duty Guide*:⁷²

Paragraphs (b) and (c) of the definition of the term 'fair value' refer to the situations in paragraphs (d), (e) and (f) of the definition of the term 'property'. This deals with the trading of shares in companies, interests in close corporations and contingent rights in trusts which are associated with the use or ownership of 'residential property' through the holding of those shares, interests or rights. These rules were introduced with effect from 13 December 2002 along with other amendments to the Act as antiavoidance measures to deal with transactions which had the effect that the use or enjoyment of 'residential property' could be obtained either –

- directly, by purchasing shares in a 'residential property company' which owns the residential property; or*
- indirectly, by acquiring shares in a holding company which would, together with its subsidiaries, have been regarded as a 'residential property company' had they not been separate entities; or*
- by substituting a beneficiary or trustee of a discretionary trust which owns residential property through its ownership of shares or interests in a 'residential property company'. (Own emphasis.)*

The effect of these provisions is that the person acquiring rights to 'residential property' in this manner can no longer avoid the payment of transfer duty on the basis that no 'property' had been acquired.

⁷² 13 March 2013 at 19 and 30. Own emphasis added.

... These provisions ensure that the acquisition of an interest in a 'residential property company' to the extent that it relates to 'residential property' is a 'transaction' for transfer duty purposes, regardless of whether that property is held directly or indirectly via an entity or a multi-tiered structure, or whether that structure contains companies, close corporations, trusts or combinations thereof. However, not all changes with regard to trusts holding residential property are transactions which give rise to tax events. For example, the birth of a child may create changes in the number and status of trust beneficiaries of a family trust, but that event would not be a taxable event, because of the requirements contained in paragraph (f) of the definition of a 'property'.

CHAPTER 6. TRANSFER DUTY IMPLICATIONS ON THE 'SALE' OF A TRUST

6.1 Introduction

It is clear from what has been stated, that prior to the 2002 amendments, a change in the beneficiaries would not have given rise to payment of transfer duty and that is precisely the reason for the 2002 amendments.

Although Mbha J referred in *The T Trust v The Commissioner for the South African Revenue Service*⁷³ to the 2002 amendments, the facts of the particular case were prior to the implementation of the said amendments. Mbha J, with this in mind and notwithstanding the learned judge's reference to the explanatory memorandum and to the fact that a change of beneficiaries would not give rise of the payment of transfer duty, made a finding contrary thereto (I submit, erroneously) to the effect that the agreements constituted a transaction as contemplated in the TDA.

Du Toit⁷⁴ sums up the liability to pay transfer duty (after implementation of the 2002 amendment) on such a 'sale' in the following statement:

The avoidance of transfer duty cannot always be achieved by means of such a scheme. It is submitted that the definition of 'transaction' and 'property' in the Transfer Duty Act, read with section 2(1) of the Act in respect of the imposition of transfer duty, are sufficiently wide to incorporate the disposal of certain interests under a trust and the acquisition of those interests by another. Liability for payment of transfer duty will depend on the nature and extent of the interests or rights enjoyed by the existing beneficiaries under the trust. In the case of a bewind trust, the acquisition of ownership in the trust property by new beneficiaries will occasion transfer-duty liability because they have obtained real rights (iura in rem) in land within the meaning of the definition of

⁷³ At para [53].

⁷⁴ Du Toit, F. (2007). *South African Trust Law Principles and Practice*. 2nd ed. Durban: Lexis Nexis, at 195 and 196. Own emphasis added.

'property' in section 1 of the Act. The acquisition of the rights of existing beneficiaries under an ownership trust by new beneficiaries, each of whom enjoys a vested ius in personam ad rem acquirendam to trust benefits, will also incur transfer-duty liability because 'acquire' in section 2(1) of the Act is interpreted as including the acquisition of a right to obtain ownership in property. However, should each of the existing beneficiaries enjoy a vested personal right to the trust benefits other than a ius in personam ad rem acquirendam and the trust deed be amended to substitute new beneficiaries, whereupon the distribution of the purchase price to the former beneficiaries is undertaken, it would appear that no transfer duty is payable. In this instance, persons who no longer qualify as trust beneficiaries will receive benefit of the purchase price. As this is likely to occur under a donation, the liability for payment of donations tax may well ensue, as may income tax liability.

I submit that it is evident from this statement, as well as from the 2002 amendments⁷⁵ of the definitions of *'property'* and *'transaction'* in the TDA, that SARS identified the 'sale' schemes and amended the law accordingly, which amendments were made around the time when SARS claimed payment of transfer duty from the *T Trust*.

This invites the conclusion that the *dictum* in the *T Trust* case, namely that the agreement referred to by the court constituted a transaction as contemplated in section 1 (as it stood before the 2002 amendments), was *prima facie* wrong. Why would SARS amend the Act, if such a substitution ('sale') constituted a transaction in terms of the old provisions?

6.2 Criticism of the current views on a 'sale' and the transfer duty legislation

It is interesting that not only SARS and Mbha J in the *T Trust* case, but also Du Toit regards the agreement as a scheme without pronouncing on what exactly is meant by the word 'scheme'. This suggests that they were all of the opinion that there was some kind of scam going on but that nobody knew what the real position should have been. SARS simply incorporated the scam into the TDA by way of the 2002 amendments.

⁷⁵ In terms of the Revenue Law Amendment Act 74 of 2002.

The problem with Du Toit's statement, as well as the *dictum* in the *T Trust* case and SARS's view after the 2002 amendments and the amendments itself, is that Du Toit, Mbha J and SARS all regard the 'sale' as valid and allow the substitution of the trustees and beneficiaries, after which the 'new trust' is taxed.

This validation of the substitution made outside the parameters of the trust instrument is, as discussed, neither possible nor sustainable. These substitutions would leave all the 'new trusts' with the predicament which the *T Trust* case created or permitted to be created, which would boomerang somewhere as it is *contra* the nature of a trust.

It is consequently submitted that the 2002 amendments do not have the effect which SARS sought. The legislator's point of entry was wrong as the 'sale' (in the form of substituting trustees and beneficiaries outside the parameters of the object and purpose of the specific trust which all these 'sale' agreements specifically entail) is invalid, *ab origine* null and void and can there accordingly never be or have been a **substitution as required by the new definition of 'transaction' in the TDA.**⁷⁶ This is not to say that there could not have been a termination, but the tax implications would surely have been different then.

The further problem is that the person or persons who are acquiring the rights to 'residential property' (and who are liable for transfer duty within six months) are, according to this view, the new trustees or beneficiaries (in that capacity and not their own personal capacity), who at the time of the agreement had no authority to bind a trust not yet formed.⁷⁷

⁷⁶ Act 40 of 1949, which defines 'transaction' *inter alia* as:

(c) *in relation to a discretionary trust, the substitution or addition of one or more beneficiaries with a contingent right to any property of that trust, which constitutes residential property or shares or member's interest contemplated in paragraph (d) or (e) of the definition of 'property' or a contingent right contemplated in paragraph (f) of that definition.* (Own emphasis added.)

⁷⁷ *Transfer Duty Guide*, March 2013 at 38:

Therefore, any transaction entered into by a person purporting to act on behalf of that trust, without the requisite authority, is invalid. A 'trust to be formed' may accordingly not be nominated as a purchaser for transfer duty purposes, not even when using the wording 'stipulatio alteri', as the trustees will not be in a position to ratify the purported act on behalf of the trust with retroactive effect. In such a case there will be no transaction as the contract is void ab initio. The trustee (once appointed as such) will therefore be required to enter into

6.3 Possible solution

It is submitted that this predicament could be resolved by adhering to the nature of a trust.

If the action of a 'sale' (which can in itself indicates a total disregard for the trust and its object and purpose) has the result that the trust is effectively managed by the founder and/or trustees for their own object and purposes, the trust should be declared a 'sham'. The trust should then be disregarded and the assets and liabilities should be the person's who has as an *alter ego*, i.e. the trust.

If the trust is not a 'sham', the scheme would, holistically viewed (substance over form), not be an invalid substitution but a valid termination of the trust. It should then be established who the real parties are; namely, who would be favoured by the sale (either by receiving the purchase price or by release from liability for debt) and who the buyer or buyers are, in order to hold the real perpetrator(s) liable for tax. The 'new trust' should be frowned upon and deregistered.

SARS regards a transaction entered into by an agent of a trust which has not been formed as no transaction and the contract as void *ab initio*. Where such an agreement is entered into, SARS will insist on a new contract with the seller if the ultimate intention is for the trust concerned to take transfer of the property.⁷⁸

It is submitted that SARS, as 'watch dog' should also regard the 'sale of a trust' as invalid and void *ab origine and* insist on a proper and valid agreement.

a new contract with the seller if the ultimate intention is for the trust concerned to take transfer of the property. (Own emphasis added.)

⁷⁸ See footnote 77.

CHAPTER 7. CONCLUSION

Transfer duty liability of trusts has given rise to an incorrect and unsustainable taxation system, principally because of a lack of understanding of the vitally important essentials of a trust and the principles surrounding trusts.

Transfer duty liability for trusts when the beneficiaries change originated with the practice of founders and/or trustees 'selling a trust' by replacing existing trust beneficiaries and trustees with new beneficiaries and trustees against monetary compensation. This practice did not give rise to payment of transfer duty in terms of the TDA prior to the 2002 amendments, and accordingly resulted in a tax benefit in a 'sale' agreement.

This practice in itself is, however, invalid and impermissible and should have been recognised by the legislature when the amendments were framed in 2002.

The nature of a trust does not allow a 'sale' of a trust (in terms whereof the trustees and beneficiaries are substituted and which by design entails that a trust instrument is varied outside the parameters of the specific trust's object and purpose) because every trust is formed with a different and distinct clearly defined object and purpose and if this object and purpose fails then the trust in effect fails.

The above conclusion does not negate the fact that agreements of this kind have been concluded and will still be attempted, or even entered into, in future. Current views and judgments, as well as the relevant transfer duty tax sections, however, in dealing with this, disregard the nature of a trust, which will ultimately result in uncertainty and confusion.

These 'sales' should be identified and dissected by the appointed 'watch dogs', which I submit include SARS,⁷⁹ to prevent the misuse of the trust form and to secure the proper evolution of the trust within other legislation in South Africa.

⁷⁹ See *inter alia* Chapter 5 of the Tax Administration Act 28 of 2011.

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