

BINDING PRIVATE RULING: BPR 086

DATE: 28 May 2010

ACTS : **INCOME TAX ACT, NO. 58 OF 1962 (the Act)**
: **VALUE-ADDED TAX ACT, NO. 89 OF 1991 (the VAT Act)**

SECTIONS : **SECTIONS 1, 15, 24H, 36 AND 37A AS WELL AS PARAGRAPHS 1, 11, 33 AND 38 OF THE EIGHTH SCHEDULE TO THE ACT**
: **SECTIONS 1, 8(2), 10(4) AND (23), 16(3), 18, 23(1) AND 51(1) OF THE VAT ACT**

SUBJECT : **APPLICATION OF THE RELEVANT LEGISLATION WHERE TWO PARTIES CONDUCT MINING OPERATIONS IN TERMS OF AN UNINCORPORATED JOINT VENTURE AGREEMENT**

1. Summary

This ruling deals with the tax implications, arising from an Unincorporated Joint Venture Agreement (the UJV Agreement).

In relation to income tax, this ruling provides guidance as to –

- whether the income received by the parties to the UJV Agreement will be income derived from mining operations;
- whether the UJV will be considered to be carrying on a trade as a partnership; and
- whether there will be any disposal of assets by the parties to the UJV Agreement as a result of their having entered into the UJV Agreement.

In relation to VAT, this ruling provides guidance as to –

- whether the UJV is conducting an enterprise separate from its members;
- the supply of the right to use the members' assets by the members to the UJV; and
- the entitlement of the UJV to claim input tax in respect of the supply of the right to use the members' assets and its liability for output tax upon dissolution of the assets, excluding the members' assets for which the right of use is acquired.

2. Relevant tax laws

This is a binding private ruling issued in accordance with section 76Q of the Act.

In this ruling legislative references to sections and paragraphs are to sections of the relevant Acts and paragraphs of the Eighth Schedule to the Act applicable as at 22 July 2008 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in such Acts.

This ruling has been requested under the provisions of –

- section 1 of the Act, paragraph (j) of the definition of “gross income”;
- section 1 of the Act, definition of “person”, “mining operations” and “mining”;
- sections 15, 24H, 36 and 37A of the Act;
- paragraphs 1, 11, 33 and 38 of the Eighth Schedule to the Act;
- section 1 of the VAT Act, definition of “enterprise” and “input tax”; and
- sections 8(2), 10(4) and (23), 16(3), 18, 23(1) and 51(1) of the VAT Act.

3. Parties to the proposed transaction

The Applicant: A limited liability company that is resident in South Africa

The Co-Applicant: A limited liability company that is resident in South Africa

4. Description of the proposed transaction

The Applicant and the Co-Applicant intend to conclude a UJV Agreement.

Prior to the effective date of the UJV Agreement, the Applicant and Co-Applicant will be the legal and beneficial owners of all the rights, title and interest in 73,99% and 26,01% respectively of the undivided share in certain mining assets and mining right. As the mining right is a new order mining right, it will be registered in the names of both the Applicant and the Co-Applicant. The Co-Applicant has as a shareholder a Black Economic Empowerment Consortium (the Consortium) in order to meet the objectives of the Socio-economic Empowerment Charter as envisaged in section 100(2) of the Mineral and Petroleum Resources Development Act, No. 28 of 2002.

It is proposed that the Applicant and the Consortium (through the Consortium’s shareholding in the Co-Applicant) collectively have respective

participation interests in the UJV, which will entitle the Applicant to 73,99% and the Consortium to 26,01% of the economic interest in and voting rights in relation to the UJV.

In terms of the UJV Agreement –

- the Applicant and Co-Applicant will contribute the right of use, but not the ownership in respect of their respective 73,99% and 26,01%, of the mining right and mining assets in order to constitute the UJV;
- the Applicant and the Co-Applicant will contribute to the cost of the UJV and be responsible for the obligations and liabilities of the UJV, as well as participate in the profits generated from the conduct of the UJV business in the ratio of 73.99% to the Applicant and 26.01% to the Co-Applicant;
- the ultimate responsibility for the management, administration and operations of the UJV will vest in its executive committee. The members of the executive committee will consist of five (5) members appointed by the Applicant and three (3) members appointed by the Co-Applicant;
- the executive committee will, on and with effect from the commencement date of the UJV, delegate the responsibility for the day-to-day management, administration and operations of the mining activities of the UJV, the concentrating facilities and marketing, sales and distribution to the Applicant;
- the Applicant will do the day-to-day management, acting both in its capacity as participant in and representative of the UJV. The Applicant will be paid 3% of the production revenue of the UJV per month as compensation for its services;
- the UJV will keep a separate bank account and all the proceeds and all other revenues of the UJV will be paid by the Applicant on behalf of the Applicant and the Co-Applicant into that bank account and all the operational expenditure will be settled from that bank account;
- the Applicant will retain from all revenue, amounts for maintenance capital expenditure, improvement capital expenditure and for rehabilitation and environmental obligations;
- all surplus funds will be distributed proportionally between the Applicant and the Co-Applicant on a quarterly basis in accordance with its participation interest;
- neither the Applicant nor the Co-Applicant will be entitled to represent or hold itself out as being the partner or agent of each other; and

- neither the Applicant nor the Co-Applicant will acquire ownership of the interest in each other's assets. Ownership in those assets will remain vested in the Applicant or the Co-Applicant respectively.

5. Conditions and assumptions

This ruling is made subject to the conditions and assumptions that –

- it has been accepted, based on the application submitted, that the UJV is not a partnership from a common law perspective as both the Applicant and the Co-Applicant clearly stated that they have no intention of forming a partnership or being regarded as partners; and
- the management fee which will be received by the Applicant in terms of the UJV Agreement will not constitute mining income as envisaged in the Act.

6. Ruling

The ruling made in connection with the proposed transaction is as follows:

Income Tax

- The activities which will be performed by the Applicant and the Co-Applicant under the UJV Agreement during the period of the said agreement constitute "mining" and "mining operations" as defined in section 1 of the Act.
- The revenue or consideration which will be received by the Applicant and the Co-Applicant for producing and delivering the concentrate to the refinery under the UJV Agreement during the period of that agreement (other than the management fee receivable by the Applicant) will be regarded as income directly connected to such mining operations and as such will be regarded as income derived from mining.
- The Applicant and the Co-Applicant would be entitled to capital expenditure deductions or allowances under section 15 of the Act read with sections 36 and 37A of the Act, against such mining income during the period of the UJV Agreement.
- The Applicant and the Co-Applicant, as participants to the UJV, are not partners from a common law perspective and accordingly the provisions of section 24H of the Act will not be applicable.
- In the light of the fact that the Applicant and the Co-Applicant will each retain ownership of their respective existing mining assets, there will be no disposal of that assets by them as a result of them having entered into the UJV Agreement.

- In the event that an asset is wholly owned by one party, that is, it was owned at the date of entering into the UJV Agreement, the proceeds on disposal will accrue to that party only and must be dealt with under section 36 of the Act read with section 1, paragraph (j) of the definition of “gross income” of the Act.
- In the event that an asset is jointly purchased by the Applicant and the Co-Applicant, that is, it was acquired after the conclusion of the UJV Agreement, the proceeds will accrue to the Applicant and the Co-Applicant on a pro-rata basis and must be dealt with under section 36 of the Act read with section 1, paragraph (j) of the definition of “gross income” of the Act in accordance with the Applicant’s and the Co-Applicant’s participation rights.

VAT

- The UJV will be conducting an enterprise separate from its members, being the Applicant and the Co-Applicant, and the UJV will be required to register as a vendor for VAT purposes under section 23 of the VAT Act.
- The supply of the right to use the assets of the Applicant by the Applicant to the UJV and the supply of the right to use the assets of the Co-Applicant by the Co-Applicant to the UJV will be deemed to be a supply of goods for no consideration as envisaged in sections 8(11) and 10(23) of the VAT Act respectively.
- The supply of the right to use the assets of the Applicant by the Applicant to the UJV and the supply of the right to use the assets of the Co-Applicant by the Co-Applicant to the UJV will not give rise to the application of section 16(3)(f) of the VAT Act read with section 18(4) of the VAT Act in the hands of the UJV.
- On the dissolution of the UJV, output tax will only be declared on the joint assets acquired post the establishment of the UJV, under section 8(2) of the VAT Act, and not on the Applicant’s assets and the Co-Applicant’s assets for which the right of use is contributed.

7. Period for which this ruling is valid

This binding private ruling, issued in July 2008, will be valid for a period of five (5) years as from the effective date of the UJV Agreement.

Issued by:

**Legal and Policy Division: Advance Tax Rulings
SOUTH AFRICAN REVENUE SERVICE**