

BINDING PRIVATE RULING: BPR 226

DATE: 1 March 2016

**ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
VALUE-ADDED TAX ACT NO. 89 OF 1991 (the VAT Act)
SECURITIES TRANSFER TAX ACT NO. 25 OF 2007 (the STT Act)**

**SECTION : SECTIONS 29A, 41(3) AND 45 OF THE ACT; PARAGRAPHS 10(b)(ii),
12A, 35(1)(a) AND 55(1)(a)(i) OF THE EIGHTH SCHEDULE TO
THE ACT
SECTIONS 1(1), 2(1)(c), 2(1)(d), 2(1)(f), 7(1)(a) AND 12(a) OF THE
VAT ACT
SECTIONS 2(1) AND 8(1)(a)(iii) OF THE STT ACT**

**SUBJECT : TRANSFER OF THE LONG-TERM INSURANCE BUSINESS, PARTLY
TO A THIRD PARTY AND PARTLY INTRA-GROUP**

1. Summary

This ruling determines the income tax, value-added tax (VAT) and securities transfer tax (STT) consequences of the transfer of the business of a long-term insurer, in part to a third party long-term insurer and the remainder to a long-term insurer that forms part of the same group of companies as the transferor.

2. Relevant tax laws

This is a binding private ruling issued in accordance with section 78(1) and published in accordance with section 87(2) of the Tax Administration Act No. 28 of 2011.

In this ruling references to sections and paragraphs are to sections of the relevant Acts and paragraphs of the Eighth Schedule to the Act applicable as at 26 November 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of the provisions of –

- the Act –
 - section 29A;
 - section 41(3);
 - section 45;
 - paragraph 10(b)(ii);
 - paragraph 12A;
 - paragraph 35(1)(a); and
 - paragraph 55(1)(a)(i).

- the VAT Act –
 - section 1(1) – paragraph (v) of the proviso, to the definition of “enterprise”;
 - definition of “financial services” and “supply”;
 - section 2;
 - section 7(1)(a);
 - section 12(a) read with section 2(1)(i); and
 - section 12(a) read with section 2(1)(c) or (d).
- the STT Act –
 - section 1 – paragraph (a) of the definition of “transfer”;
 - section 2(1); and
 - section 8(1)(a)(iii).

3. Parties to the proposed transaction

The Applicant:	A long-term insurer incorporated in and a resident of South Africa and the seller of its business
Company A:	A long-term insurer incorporated in and a resident of South Africa that does not form part of the same group of companies as the Applicant
Company B:	A long-term insurer incorporated in and a resident of South Africa that forms part of the same group of companies as the Applicant

4. Description of the proposed transaction

4.1 Third party transaction

In terms of a substitution agreement, the Applicant and Company A wish to substitute the rights and obligations of the Applicant in relation to the policyholders under certain annuity policies, with the rights and obligations of Company A in relation to the same policyholders in terms of replacement policies, to be issued by Company A. The annuity policies are backed by a reinsurance policy issued to the Applicant by Company A. The policyholders are all pensioners who were members of pension funds. The annuity policies are annuity contracts in respect of which annuities are paid and the reinsurance policy issued by Company A is thus accounted for in the Applicant's untaxed policyholder fund (UPF).

Company A holds assets, including securities, to back its obligations under the reinsurance agreement. Following the proposed transaction, Company A will be the primary insurer towards the policyholders and the reinsurance policy will be cancelled. Company A remains the owner of the underlying assets, including securities.

4.2 Intra-group transaction

The Applicant's group, of which Company B forms part, seeks to rationalise the life licences in the group and the proposed restructuring involves the transfer of all of the Applicant's identifiable businesses, other than the subject of the third party transaction, to Company B. Any value left in the Applicant after the transfer of its businesses (that is, the corporate fund) will be distributed to its shareholder prior to deregistration.

The intra-group transaction comprises of three distinct, but inter-related transactions:

- (a) Transaction 1: Termination of the reinsurance policy issued by Company B (T1 reinsurance policy) and assumption by Company B of the rights and obligations under linked insurance policies.
- (b) Transaction 2: Transfer by the Applicant of the direct asset portfolio, including the underlying assets, and assumption by Company B of the rights and obligations under linked insurance policies.
- (c) Transaction 3: Transfer by the Applicant of its reinsurance asset portfolio and termination of the reinsurance policy issued by the Applicant to Company B (T3 reinsurance policy).

The assets to be transferred by the Applicant as part of the proposed transaction do not include any exchange items for purposes of section 24I, or instruments for purposes of section 24J of the Act.

The following is relevant in relation to the Intra-group transaction:

(a) Transaction 1

- The rights under the T1 reinsurance policy are held by the Applicant and the portfolio of assets backing the T1 reinsurance policy is held by Company B in their respective untaxed policyholder fund (UPF), individual policyholder fund (IPF) and company policyholder fund (CPF).
- The linked policies will be transferred by the Applicant to Company B in terms of a transfer agreement. The T1 reinsurance policy will simultaneously be terminated and Company B will, thereafter, act as primary insurer towards the policyholders, instead of reinsurer.

(b) Transaction 2

- The Applicant is the primary insurer and has issued living annuity policies and linked pure endowment policies (linked policies). The Applicant holds the assets backing these liabilities in its UPF, IPF and CPF. These assets comprise listed and unlisted shares, preference shares, listed debentures, interests in unit trust funds and cash.
- These linked policies, the assets and all asset management and broker agreements will be transferred by the Applicant to Company B in terms of a transfer agreement.

(c) Transaction 3

- Company B is the primary insurer of a pensioner portfolio and has issued linked insurance policies. The liabilities in terms of these linked insurance policies are fully reinsured by the Applicant in terms of the T3 reinsurance policy. The Applicant holds the assets backing the linked liabilities via the T3 reinsurance policy. The Applicant holds the reinsurance assets in its UPF. Company B holds the T3 reinsurance policy in its UPF.
- The reinsurance assets will be transferred by the Applicant to Company B in terms of a transfer agreement and the T3 reinsurance policy will consequently be terminated.
- All asset management agreements in respect of the management of the reinsurance assets will be transferred by the Applicant to Company B.

5. Conditions and assumptions

This binding private ruling, insofar as it relates to the third party transaction, is not made subject to any additional conditions and assumptions.

This binding private ruling, insofar as it relates to the intra-group transaction, is subject to the following additional conditions and assumptions:

- The Applicant and Company B each holds all relevant assets, appropriately held in the UPF, IPF or CPF, on capital account.
- The transfer of the policyholder businesses by the Applicant is allocated in such a manner that –
 - the policyholder businesses, assets and liabilities previously allocated to the UPF of the Applicant are allocated to the UPF of Company B;
 - the policyholder businesses, assets and liabilities previously allocated to the CPF of the Applicant are allocated to the CPF of Company B; and
 - the policyholder businesses, assets and liabilities previously allocated to the IPF of the Applicant are allocated to the IPF of Company B.
- Capital assets of the Applicant will be held as capital assets by Company B following the proposed transaction.
- No ruling is sought or made in relation to the ultimate winding-up, liquidation or deregistration of the Applicant and the potential impact this event may have on relief obtained under section 45 of the Act.
- No ruling is sought or made in relation to a potential disposal of an asset acquired under section 45 of the Act by Company B within 18 months of the proposed intra-group transaction as contemplated in section 45(5) of the Act.

6. Ruling

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

- The substitution by the Applicant of its rights and obligations in terms of the annuity policies for replacement policies to be issued by Company A to the policyholders will not result in any taxable capital gain for the Applicant.
- The termination of the Applicant's reinsurance policy, issued by Company A, will not result in any taxable capital gain for the Applicant due to the operation of paragraph 55(1)(a)(i) of the Eighth Schedule to the Act.
- The proposed third party transaction will not result in a "reduction amount" for purposes of paragraph 12A of the Eighth Schedule to the Act for Company A.
- No STT consequences will ensue from the proposed transaction for Company A.
- The transfer of ownership by the Applicant of the annuity policies, being long-term insurance policies, to Company A by way of substitution will be exempt from VAT in terms of section 12(a) read with section 2(1)(i) of the VAT Act.
- Paragraph (v) of the proviso to the definition of "enterprise" in section 1(1) of the VAT Act provides that any activity shall, to the extent to which it involves the making of exempt supplies, not be deemed to be the carrying on of an enterprise. In light of the fact that the termination of the Applicant's reinsurance policy, issued by Company A, is done in the course and furtherance of an exempt activity, it will not be subject to VAT.

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

(a) Transaction 1

- The transfer by the Applicant of any assets held in the UPF, IPF and CPF in terms of the linked insurance policies to Company B and the termination of the T1 reinsurance policy will not result in any taxable capital gain for the Applicant.
- The assumption by Company B of the linked insurance policies and the termination of the T1 reinsurance policy do not result in any taxable capital gain or loss for Company B.
- The transfer of the linked long-term insurance policies from the Applicant to Company B will be exempt from VAT under section 12(a) read with section 2(1)(i) of the VAT Act.
- Paragraph (v) of the proviso to the definition of "enterprise" in section 1(1) of the VAT Act provides that any activity shall, to the extent to which it involves the making of exempt supplies, not be deemed to be the carrying on of an enterprise. In light of the fact that the termination of the T1 reinsurance policy is done in the

course and furtherance of an exempt activity, it will not be subject to VAT.

(b) Transaction 2

- The transfer by the Applicant of assets associated with the living annuity policies and linked pure endowment policies comprising transaction 2 will not result in any taxable capital gain for the Applicant due to the application of section 45 of the Act, to the extent that these assets are transferred from the IPF and CPF. To the extent that these assets are transferred from the UPF, no taxable capital gains are included for tax purposes under paragraph 10(b)(ii) of the Eighth Schedule to the Act.
- The disposal of the securities (listed shares, unlisted shares and preference shares) and unit trusts units to Company B will be exempt from STT under section 8(1)(a)(iii) of the STT Act.
- The transfer of the living annuity policies and linked pure endowment insurance policies from the Applicant to Company B will be exempt from VAT under section 12(a) read with section 2(1)(j) of the VAT Act.
- The transfer by the Applicant to Company B of the assets associated with the living annuity policies and linked pure endowment policies, which comprise of equity securities, participatory securities, debt securities and cash, will be exempt from VAT under section 12(a) read with section 2(1)(c) or (d) of the VAT Act.

(c) Transaction 3

- The transfer of the reinsurance assets and the termination of the T3 reinsurance policy do not result in any taxable capital gain for the Applicant.
- The termination of the T3 reinsurance policy will not result in any taxable capital gain for Company B.
- The disposal of the securities (listed shares, unlisted shares and preference shares) and unit trusts to Company B will be exempt from STT under section 8(1)(a)(iii) of the STT Act.
- The transfer by the Applicant to Company B of the reinsurance assets held in respect of the T3 reinsurance policy will, to the extent that they comprise of equity securities, participatory securities, debt securities and cash, be exempt from VAT under section 12(a) read with section 2(1)(c) or (d) of the VAT Act.
- Paragraph (v) of the proviso to the definition of “enterprise” in section 1(1) of the VAT Act provides that any activity shall, to the extent to which it involves the making of exempt supplies, not be deemed to be the carrying on of an enterprise. In light of the fact that the termination of the T3 reinsurance policy is done in the

course and furtherance of an exempt activity, it will not be subject to VAT.

7. Period for which this ruling is valid

This binding private ruling is valid for the year of assessment during which the proposed transaction takes place for tax purposes.

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