

**BINDING PRIVATE RULING: BPR 402**

DATE: 14 December 2023

- ACT : INCOME TAX ACT 58 OF 1962 (the Act)  
VALUE ADDED TAX ACT 89 OF 1991 (VAT Act)**
- SECTION : SECTIONS 1(1) – DEFINITION OF “GROSS INCOME”, 11(a), 25B(1),  
28(1) – DEFINITIONS OF “SHORT-TERM INSURER”, “SHORT-TERM  
INSURANCE BUSINESS”, “SHORT-TERM POLICY” AND “BRANCH  
POLICY”, 28(2), 28(3A), 28(4), 29A(1) – DEFINITIONS OF “ADJUSTED  
IFRS VALUE” AND “NEGATIVE LIABILITY”, 29A(12), PARAGRAPHS  
11(1), AND 11(2)(a), OF THE EIGHTH SCHEDULE TO THE ACT  
SECTIONS 2(1)(c), 2(1)(d), 2(1)(f), 2(1)(l), 8(16), 10(4), 12(a), 16(3)(h),  
AND 23(1) OF THE VAT ACT**
- SUBJECT : TRANSFER OF LONG-TERM INSURANCE BUSINESS TO A LOCAL  
BRANCH OF A FOREIGN REINSURER**

***Preamble***

This binding private ruling is published with the consent of the Applicant(s) to which it has been issued. It is binding between SARS, the Applicant and any Co-Applicant(s) only and published for general information. It does not constitute a practice generally prevailing.

**1. Summary**

This ruling determines the tax implications of the transfer of life reinsurance business from a resident reinsurer to a local branch of a foreign company.

**2. Relevant tax laws**

In this ruling references to sections and paragraphs are to sections of the relevant Act and paragraphs of the Eighth Schedule to the Act applicable as at 1 January 2023. 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 Act
  - section 1(1) – definition of “gross income”;
  - section 11(a);
  - section 25B(1);
  - section 28(1), – definitions of “short-term insurer”, “short-term insurance business”, “short-term policy” and “branch policy”;
  - sections 28(2);
  - section 28(3A);

- section 28(4);
  - section 29A(1), – definitions of “adjusted IFRS value” and “negative liability”;
  - section 29A(12);
  - paragraph 11(1); and
  - paragraph 11(2)(a).
- the VAT Act –
    - section 2(1)(c);
    - section 2(1)(d);
    - section 2(1)(f);
    - section 2(1)(i);
    - section 8(16);
    - section 10(4);
    - section 12(a);
    - section 16(3)(h); and
    - section 23(1).

### 3. Parties to the proposed transaction

The Applicant:	A resident and licensed life reinsurer that is a wholly-owned subsidiary of Company A
Company A:	A resident that is a wholly-owned subsidiary of Company B
Company B:	A foreign reinsurance company that is the ultimate holding company of the group to which the Applicant and Company A belongs
The Branch:	A permanent establishment of Company B in South Africa
The Trust:	A resident trust established for insurance regulatory purposes as required by section 40 of the Insurance Act 18 of 2017

### 4. Description of the proposed transaction

The Applicant has active business operations (including employees, facilities, and infrastructure) in South Africa. Its main business is long-term reinsurance and it, in turn, reinsures a significant portion of its business with foreign group companies.

The Applicant is currently registered for Value-Added Tax (VAT). The Applicant currently makes both taxable and exempt supplies and its main business (i.e. more than 50%) is to provide long-term insurance which is an exempt supply for VAT purposes. The Applicant applies the standard turnover-based method to apportion VAT incurred on mixed-use expenses.

In addition to its reinsurance business, the Applicant also earns fee income relating to services performed by the Applicant for the benefit of foreign group companies. Most of which relates to the reinsurance business which the Applicant has reinsured with foreign group companies and a small proportion of which relates to services rendered to foreign group companies unrelated to the business underwritten by the Applicant.

The introduction of the Insurance Act 18 of 2017 (the Insurance Act), effective from 1 July 2018, affords foreign reinsurers the opportunity to conduct long-term reinsurance business in South Africa through a branch of the foreign reinsurer, provided the relevant licence is acquired.

Company B wishes to convert the ownership of its operations in South Africa from a company to a Branch, a foreign connected person in relation to the Applicant for tax purposes.

The Applicant will implement the proposed transaction on terms set out in the Sale of Enterprise Agreement (the Agreement) between the Applicant and the Branch. The salient terms of the agreement are as follows:

- The Applicant will make a cash payment to the Branch in exchange for the Branch assuming all the Applicant's liabilities. The cash consideration will be equal to the market value of the liabilities assumed, net of any negative liabilities as defined in section 29A of the Act.
- The Applicant will dispose of all its assets (other than certain cash balances) at market value to the Branch in exchange for the Branch making a cash payment. Assets required to be held as security for regulatory purposes by the Trust will be transferred directly to the Trust by the Applicant.

Regulatory approval is required from the Prudential Authority (PA) to proceed with the restructure of the Applicant. It is a regulatory requirement that a South African trust be established to hold certain assets of the Branch as security. The legal structure of the Trust must be approved by the PA and must comply with the legislative requirements of the Trust Property Control Act 57 of 1988 and the Insurance Act.

The Branch will continue to carry on the business previously conducted by the Applicant in South Africa in the same manner but as a foreign reinsurer conducting an insurance business through a Branch in South Africa in terms of section 6 of the Insurance Act. It is intended that the Branch be registered for VAT in South Africa prior to the transaction being implemented. The enterprise activities of the Branch will consist of, amongst others, premiums received from both local and cross border insurers, interest income earned on invested assets, cash and inter unit charges paid for services rendered to the Branch by other Company B group companies.

The Branch will be required to ensure that assets are held in the Trust at all times to the extent that such assets are at least equal to the technical provisions for the reinsurance business of the Branch calculated in accordance with the Insurance Act, as contemplated in section 40(1) of the Insurance Act (the Security). For these purposes, it is envisaged that the Branch may transfer further assets to the Trust to ensure that this requirement remains satisfied.

The Trust Deed will stipulate that the assets and income of the Trust will be held as security in a representative capacity on behalf of the Branch and that any of the assets, claims and rights comprised in the Security, interest and other returns on the Security, proceeds of any disposal by the Trust of any assets, claims and rights comprised in the Security, shall not be received by or otherwise accrue to the Trust, but shall be received by or otherwise accrue to the Branch. However, the Insurance Act requires that the Branch must comply with all requirements under the Insurance Act before giving instruction to the trustee(s) to release assets, claims and rights comprised in the Security held in Trust to the Branch, including the requirement that the Branch may not access or withdraw funds held in the Trust without the approval of the PA.

## **5. Conditions and assumptions**

This binding private ruling is subject to the additional condition and assumption that the Branch will meet the requirements to be deemed a person separate from the Company for the purposes of paragraph (ii) of the proviso to the definition of "enterprise" in section 1(1) of the VAT Act.

## **6. Ruling**

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

### **The Act**

- a) The difference in the market value of net insurance liabilities assumed by the Branch from the Applicant and the IFRS value of such net insurance liabilities must be allocated to the Untaxed Policyholder Fund and the Risk Policy Fund. Any surplus in those funds must then be transferred to the Corporate Fund and taxed in the Corporate Fund in accordance with section 29A(7).
- b) The cash payment received by the Branch from the Applicant as consideration for the assumption of insurance liabilities of the Applicant constitute a receipt of a capital nature and must not be included in the gross income of the Branch as defined in section 1(1).
- c) The Branch will constitute a short-term insurer conducting short-term insurance business as contemplated in section 28 and should be taxed in accordance with the provisions of section 28.
- d) The claims paid in respect of the short-term insurance policies issued and or assumed from the Applicant are deductible under section 11(a) read with section 28(2)(c).
- e) The Branch will be allowed a deduction for technical liabilities assumed in terms of section 28(3A) in respect of the Branch policies transferred and must include such amounts deducted in income in the following year of assessment under section 28(4).
- f) The amount in respect of liabilities to be deducted in terms of section 28(3A) must be determined in accordance with IFRS as prescribed in the formula in section 28(3A).

- g) The transfer of non-cash capital assets by the Branch to the Trust to ensure the required level of assets are held as security by the Trust for regulatory purposes will not be a disposal under paragraph 11(2)(a) for purposes of the Eighth Schedule.
- h) As the transfer of assets by the Branch to the Trust will not result in a disposal for purposes of the Eighth Schedule, any income and gains attributable to the assets held in the Trust will be attributed to the Branch and taxed accordingly.

### **The VAT Act**

- a) Paragraph (v) of the proviso to the definition of “enterprise” specifically excludes from the definition any activity to the extent that it involves the making of exempt supplies and as such, to the extent that any assets are applied exclusively for exempt purposes, those assets would not form part of the enterprise of a vendor.

As the enterprise or business is being sold and such enterprise consists of assets and liabilities, section 8(16) applies to the supply of the enterprise as a whole and does not apply to the individual assets. Notwithstanding the Agreement the assets exclusively used for exempt purposes will not form part of the enterprise for VAT purposes.

The supply of the remainder of the business as a whole (which includes the mixed-use assets) will be deemed to be made wholly in the course or furtherance of the Applicant’s business and VAT must be accounted for on the full selling price at the standard rate of 15%.

The Applicant can therefore claim an input tax deduction under section 16(3)(h) in respect of the mixed-use assets sold by the Applicant to the Branch, if the documentary requirements under Interpretation Note 92 are obtained.

- b) The payment by the Applicant to the Branch for the Branch assuming the insurance liabilities of the Applicant, subsequent to reducing the insurance liabilities with the negative liabilities, will not be consideration in respect of a separate supply of services. Consequently, the Applicant and the Branch do not need to account for VAT.
- c) The Delegation Payment which relates to the Branch assuming other free-standing liabilities of the Applicant will be an exempt supply and as a result the Branch does not need to account for VAT on that portion of the Delegation Payment.
- d) The Branch will be required to register for VAT if it will have taxable supplies exceeding R1 million in a 12-month period in South Africa and Company B will not be required to register as a VAT vendor in South Africa.
- e) To the extent that the supply of the assets comprises financial services which are exempt supplies, the supply of those assets for regulatory purposes will be exempt from VAT and therefore the value of supply rules for connected parties will also not apply.

**7. Period for which this ruling is valid**

This binding private ruling is valid in respect of the year of assessment ending 31 December 2023.

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