

BINDING PRIVATE RULING: BPR 110

DATE: 01 March 2012

ACT : INCOME TAX ACT, NO. 58 OF 1962 (the Act)
SECTION : SECTION 9D(9)(b)(ii)(bb)
**SUBJECT : TOLL MANUFACTURING AGREEMENT AND THE
ATTRIBUTION OF THE GLOBAL SALES OF SOUTH
AFRICAN MANUFACTURED PRODUCTS TO A FOREIGN
BUSINESS ESTABLISHMENT**

1. Summary

This ruling deals with the question as to whether –

- a toll manufacturing agreement (an agreement under which one entity, that is a resident and has specialized equipment, processes raw material or semi finished goods into manufactured products on behalf of another entity that is a controlled foreign company) will be regarded as a service agreement or a sale agreement; and
- the global sales of the manufactured products will constitute outbound sales. (Outbound sales exist when a South African resident sells products to a controlled foreign company which on sells the same products to a person other than a connected person in relation to the controlled foreign company who is a South African resident). Outbound sales may not be attributed to a foreign business establishment.

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 are to sections of the Act applicable as at 1 January 2011 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This ruling has been requested under the provisions of section 9D(9)(b)(ii)(bb).

3. **Parties to the proposed transaction**

The Applicant: A resident company owning more than 50% of the participation rights in the Controlled Foreign Company

The Controlled Foreign Company: A foreign company selling the South African manufactured products to the global market from a foreign business establishment

The Contract Manufacturer: A resident company which is wholly owned by the Applicant and which manufactures the products on behalf of the Controlled Foreign Company

4. **Description of the proposed transaction**

The Controlled Foreign Company intends to enter into a toll manufacturing agreement with the Contract Manufacturer.

The ownership and risks in relation to the manufactured products will at all times be that of the Controlled Foreign Company. The Controlled Foreign Company will provide the principal materials for the manufacturing of the products. The other materials and the packaging for the manufactured products will be provided by the Contract Manufacturer.

The Controlled Foreign Company will own all intellectual property in relation to the manufactured products. The Controlled Foreign Company will provide the Contract Manufacturer with the know-how and a manufacturing license to manufacture the products. The manufactured products will be shipped directly to the end client. All global sales and marketing in relation to the manufactured products will be performed by the employees of the Controlled Foreign Company from a foreign business establishment.

5. **Conditions and assumptions**

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

- the ruling does not, in any way, deal with or provide any opinion or certainty as to whether a foreign business establishment exists or whether the requirements in the Act are adhered to in this regard; and

- the attribution of the net income amounts to the so called “foreign business establishment” was not evaluated and no opinion or ruling is issued in this regard.

6. Ruling

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

- The proposed toll manufacturing agreement will be a service agreement as opposed to a sale agreement to be entered into between the Controlled Foreign Company and the Contract Manufacturer. As such, the Applicant, in relying on the foreign business establishment exemption under section 9D(9)(b) (provided all the other requirements thereof are met), may disregard the exclusion to the foreign business establishment exemption in section 9D(9)(b)(ii)(bb) in the context of the proposed toll manufacturing agreement.

7. Period for which this ruling is valid

This binding private ruling is valid for a period of five (5) years as from January 2011.

Issued by:

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