BINDING PRIVATE RULING: BPR 204

DATE: 24 August 2015

ACT	**:**	**INCOME TAX ACT NO. 58 OF 1962 (the Act)**
SECTION	**:**	**SECTIONS 1(1) – DEFINITION OF "REIT", 25BB, 42 AND 44 AND PARAGRAPHS 1, 11(1)(*a*) AND 13(1)(*a*) OF THE EIGHTH SCHEDULE TO THE ACT**
SUBJECT	**:**	**DEFINITION OF "DISPOSAL" FOR PURPOSES OF ASSET-FOR-SHARE AND AMALGAMATION TRANSACTIONS; "QUALIFYING DISTRIBUTION" UPON CONVERSION TO A CORPORATE REAL ESTATE INVESTMENT TRUST**

1. Summary

This ruling deals with –

- the conversion of a portfolio of a collective investment scheme in properties, currently listed as a Real Estate Investment Trust (REIT) on the JSE, to a corporate REIT. Prior to the conversion, immovable property will be transferred to a property company;

- whether the date of transfer of ownership in immovable property in the Deeds Office into the name of the property company impacts on the time of disposal of that immovable property for purposes of the asset-for-share transaction and the amalgamation transaction; and

- whether the declaration date of a distribution, as opposed to the date of payment, is the relevant time for determining if the distribution is a "qualifying distribution" under section 25BB.

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 Act and paragraphs of the Eighth Schedule thereto, applicable as at 23 June 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1), definition of "REIT";
- section 25BB;
- section 42;

- section 44;
- paragraph 1;
- paragraph 11(1)(*a*); and
- paragraph 13(1)(*a*).

3. Parties to the proposed transaction

The Applicant:	A listed collective investment scheme in properties (CISP) with its financial year ending on 31 December
The First Co-Applicant:	A private property company incorporated in South Africa, and a wholly-owned subsidiary of CISP (Property Company)
The Second Co-Applicant:	A corporate REIT, a public company incorporated in South Afica, with its financial year ending on 31 December, which will be listed on the JSE as a REIT pursuant to the proposed transaction (Corporate REIT)

4. Description of the proposed transaction

The proposed transaction is the effective conversion of the CISP to a corporate REIT in accordance with the procedure set out in Notice 42 of 2014 (Notice 42) issued by the Registrar of Collective Investment Schemes in terms of the Collective Investment Schemes Control Act No. 45 of 2002 (the CISC Act).

The CISP directly holds letting enterprises in relation to the immovable properties, which includes –

- immovable properties;
- the rights and obligations of the CISP as the lessor in terms of leases of the properties;
- assets which include cash on hand and certain contracts;
- liabilities which include all actual and contingent liabilities and obligations of the CISP relating to the properties and letting enterprises;
- goodwill; and
- shares in and loan accounts against wholly-owned subsidiaries, including the Property Company.

The proposed transaction will be achieved through the following transaction steps:

1) The CISP transfers the letting enterprises to the Property Company as going concerns by means of an asset-for-share transaction under section 42, in return for the issue of equity shares in the Property Company. A written asset-for-share agreement between the CISP and the Property Company was concluded and not subject to any suspensive conditions.

2) Two days prior to the effective date of the amalgamation transaction under section 44 (see 4 below), the subsidiaries will declare a distribution in relation to the first and second quarters of the current financial year to the CISP, as the beneficial shareholder of those subsidiaries.

3) One day before the effective date of the amalgamation transaction under section 44 (see 4 below), the CISP will declare a final profit distribution for the period 1 January 2015 to the date of the declaration, to be paid subsequently by the Corporate REIT to shareholders, once the audited financial statements of the CISP have been finalised.

4) The CISP will transfer all of its assets and liabilities, excluding bonds registered over the property which will remain in place until the date of transfer in the Deeds Office, to the Corporate REIT by means of an amalgamation transaction under section 44, in return for the issue of equity shares in the Corporate REIT. The assets include equity shares and loan accounts in the CISP's subsidiaries (including the shares and loan accounts in respect of the Property Company). The amalgamation agreement was concluded prior to the asset-for-share agreement, but contains a number of suspensive conditions, some of which were unfulfilled at the time of the conclusion of the asset-for-share agreement.

5) The CISP will declare a dividend *in specie* in respect of the equity shares in the Property Company, prior to it ceasing to be a REIT.

6) The existence of the CISP will be terminated once the equity shares in the Corporate REIT have been distributed on behalf of the CISP and the process has been completed to wind up the CISP pursuant to the requirements of the Registrar of Collective Investment Schemes, under the CISC Act.

7) The Corporate REIT is scheduled to be listed on the JSE as a REIT shortly after the effective date of the amalgamation transaction.

8) The units of the CISP will be suspended and delisted at the commencement of trade on the same day on which the Corporate REIT is listed.

It follows that the time and date on which the CISP will cease to be a REIT for income tax purposes is the commencement of trade on the listing date of the Corporate REIT. Therefore, the CISP's year of assessment will be deemed to end on that date, under section 25BB(7). There will, however, be no income derived by the CISP from the effective date of the amalgamation transaction to the deemed end date of its year of assessment.

5. Conditions and assumptions

This binding private ruling is subject to the following additional conditions and assumptions:

- The Corporate REIT complies with the JSE Listing Requirements for REITs.

- The CISP holds the immovable property and the shares in the wholly-owned subsidiaries on capital account.

- The amalgamation agreement becomes unconditional prior to the listing date of the Corporate REIT and the suspension of the CISP's units from the JSE.

- The CISP does not derive any imputed income from any controlled foreign company under section 9D.

- At least 75% of the gross income received by or accrued to the CISP or a 'subsidiary' (as defined in the International Financial Reporting Standards) of the CISP as a REIT, in the previous year of assessment, consisted of 'rental income', as defined in section 25BB(1).

- The amount of the CISP's final distribution as a REIT will be determined with reference to the financial results of the CISP, as reflected in the financial statements prepared for the year of assessment commencing on 1 January 2015 and deemed to end on the date on which the CISP ceases to be a REIT for income tax purposes.

6. Ruling

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

- In respect of the asset-for-share transaction under section 42, paragraph 13 of the Eighth Schedule will apply to the disposal of the immovable properties to the Property Company. The disposal of the immovable properties will be deemed to have occurred for income tax purposes on the date that the asset-for-share agreement is concluded.

- Irrespective of whether the transfer of ownership of the immovable properties has been registered in the name of the Property Company in the Deeds Office –
  - the Property Company will be entitled to issue the agreed number of equity shares to the CISP in exchange for the disposal of the letting enterprises as going concerns for income tax purposes to the Property Company, as the immovable properties would have been disposed of for income tax purposes;
  - the CISP will be regarded as having disposed of all of its assets for purposes of the amalgamation transaction under section 44, which would exclude such properties as already have been disposed of in terms of the asset-for-share transaction for income tax purposes; and
  - the Corporate REIT will be entitled to issue the agreed number of equity shares to the CISP as consideration for the disposal of the CISP's assets, in terms of the amalgamation transaction, for income tax purposes.

- For income tax purposes, at the time that the CISP ceases to be a REIT, the CISP will have disposed of all of its assets. Those assets include –
  - the immovable properties which have been disposed of to the Property Company in terms of the asset-for-share transaction (irrespective of the fact that the transfer of ownership of these properties may not yet have been registered in the Deeds Office);
  - the equity shares in and loans to the subsidiaries which have been disposed of to the Corporate REIT; and
  - the equity shares in the Corporate REIT which have been disposed of to the unit holders.

  It follows that no capital gains tax consequences will arise for the CISP pursuant to section 25BB(7).

- On the basis that the CISP declares the final profit distribution prior to its ceasing to be a REIT, the CISP will be able to deduct the distribution from its income for that year of assessment to the extent that all the requirements of the definition of 'qualifying distribution', in section 25BB(1), are met, even though payment in respect of the distribution will be made by the Corporate REIT in consequence of the proposed assignment of the liability to pay the distribution as part of the conversion to a corporate REIT under Notice 42.

- The settlement of the assumed liability under the CISP's final profit distribution to shareholders by the Corporate REIT is not a 'qualifying distribution', as defined in section 25BB(1), for the Corporate REIT and is, therefore, not deductible by the Corporate REIT under section 25BB(2)(*a*).

- Subsequent to its listing on the JSE, the Corporate REIT will qualify as a REIT for purposes of the Act. To the extent that the Corporate REIT then distributes an amount that is a 'qualifying distribution' as defined in section 25BB(1), that amount will be deductible under section 25BB(2)(*a*).

7. Period for which this ruling is valid

This binding private ruling is valid for a period of 3 years from 23 June 2015.

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