

BINDING PRIVATE RULING: BPR 178

DATE: 14 August 2014

ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
SECTION : SECTIONS 1(1) DEFINITION OF “COMPANY”, “EQUITY SHARE”, “FOREIGN COMPANY”, “GROUP OF COMPANIES” AND “SHARE”, 42 AND 45
SUBJECT : INTERNATIONAL CORPORATE RESTRUCTURING

1. Summary

This ruling deals with a corporate restructuring of a multi-national group of companies.

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 are to sections of the Act applicable as at 23 April 2014 and 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), the definition of “company”, “equity share”, foreign company”, “group of companies” and “share”;
- section 42; and
- section 45.

3. Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa that holds 100% of the partnership interest in KG

The Co-Applicants:

KG: A German Kommanditgesellschaft (KG) partnership that is effectively managed in Germany

German Company: A company incorporated in and a resident of Germany that is effectively managed in Germany

Foreign Holdco: A company incorporated in and a resident of another Foreign Country that is effectively managed outside South Africa and is a wholly-owned subsidiary of SA Holdco

SA Holdco:	A private company incorporated in and a resident of South Africa that holds 100% of the shares in the Applicant and Foreign Holdco
Target:	A company incorporated in and a resident of the same country as Foreign Holdco

4. Description of the proposed transaction

Background information

The group to which the Applicant belongs (the Applicant group) has an investment in Germany. The investment is structured as follows:

- The Applicant is the limited partner in KG (KG is known as a “GmbH & Co. KG”, a subset of the German KG).
- KG owns all the issued shares of German Company.
- German Company owns all the issued shares of Target.

The shares in Target are held as a capital investment and do not secure any debt.

On the date of the proposed corporate restructuring the market value of the shares in Target will exceed their base cost in the hands of German Company.

The shares in German Company and the shares in Target are “equity shares”, as defined, for South African tax purposes.

KG, German Company, Foreign Holdco and Target are currently treated as controlled foreign companies (CFCs) by the Applicant group for purposes of section 9D.

From a German tax perspective, KG is tax transparent for German corporate income tax purposes but not for German trade tax purposes. In other words, the Applicant is liable to corporate income tax in Germany on the income derived by KG, but KG is liable for the German trade tax on their business income.

KG and German Company have formed a so-called tax consolidation, with the effect that the taxable income of German Company for each tax year is allocated to KG and the commercial (accounting) profit derived by German Company annually must be transferred to KG. The profit transfers are ignored for tax purposes in Germany.

The taxable income of German Company, allocated to KG, is subject to German corporate income tax in the hands of the Applicant and to German trade tax in the hands of KG, as described above.

The Applicant group has identified a commercial need, based on its foreign expansion initiatives, to consolidate certain non-German businesses under one single holding company in a specific foreign jurisdiction, to be held directly from South Africa. Given that Target is in the German group, there is a need to move it to such foreign jurisdiction. Target will remain a wholly-owned investment of the Applicant group in South Africa.

The shares in Foreign Holdco are “equity shares”, as defined, for South African tax purposes.

Proposed transaction steps

The parties propose to achieve the internal restructuring in the following manner:

- German Company sells its shares in Target to SA Holdco at market value and the consideration is settled by means of a loan note equal to the market value of Target, using the tax relief provided for in section 45.
- German Company transfers the loan to KG, which then transfers the loan to the Applicant. The Applicant distributes the loan as a dividend *in specie* to SA Holdco. The transfer between members of the tax consolidation is in settlement (in kind) of a contractual obligation to transfer profits.
- SA Holdco is then both the creditor and the debtor in terms of the loan, with the result that the loan is extinguished.
- SA Holdco capitalises Foreign Holdco with the Target shares in exchange for equity shares in Foreign Holdco, using the tax relief provided for in section 42.

5. Conditions and assumptions

This ruling is subject to the additional condition and assumption that the parties to the various transactions, taking advantage of the provisions of sections 42 and 45, do not trigger any of the anti-avoidance provisions in section 42 or 45, with the exception of section 45(3A), which is the subject of ruling 6.4 below.

6. Ruling

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

- 6.1 KG is a company, and hence a foreign company, for South African tax purposes.
- 6.2 The Applicant, SA Holdco, KG and German Company form part of the same “group of companies” as defined in section 1(1).
- 6.3 The disposal of the Target shares by German Company to SA Holdco, on loan account, will qualify as an “intra-group transaction” under paragraph (b) of the definition of “intra-group transaction” in section 45(1) and will consequently qualify for the tax relief as set out in section 45.
- 6.4 Section 45(3A) will not apply to deem the loan to have a base cost of nil in the hands of the holder of the loan, and therefore the loan will have a base cost equal to its face value. As this loan is distributed up the line to SA Holdco, the cessionary in each case will be able to access this face value as base cost.
- 6.5 The profit transfer by German Company to KG under the tax consolidation, and the subsequent transfers of such profits up the line to SA Holdco where all such transfers are to be effected *in specie* by way of a cession of the loan, will not give rise to a liability for South African income tax, including capital gains tax.

- 6.6 The contribution of the Target shares by SA Holdco to Foreign Holdco will qualify as an asset for share transaction under paragraph (b) of the definition of “asset for share transaction” in section 42(1), and will consequently qualify for the tax relief as set out in section 42.

7. Period for which this ruling is valid

This binding private ruling is valid for the year(s) of assessment during which the proposed transactions are implemented.

Issued by:

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