DRAFT

South African Revenue Service

DRAFT INTERPRETATION NOTE

DATE:

ACT	**:**	**INCOME TAX ACT NO. 58 OF 1962**
SECTION	**:**	**SECTIONS 1(1) – DEFINITION OF "REIT", 8F(3)(*d*), 8FA(3)(*d*), PARAGRAPH (*aa*) OF THE PROVISO TO SECTION 10(1)(*k*)(i), 23N(5)(*a*) 25BB, 41(4)(*a*)(iii), 43, PROVISO TO SECTION 44(4A), 46(2) and (6A), 64F(1)(*a*) AND (*l*) AND (2), 64FA(1)(*a*); SECTION 8(1)(*t*) OF THE SECURITIES TRANSFER TAX ACT; SECTIONS 1(1) – DEFINITION OF "RESIDENTIAL PROPERTY COMPANY" AND 9(1)(*l*) OF THE TRANSFER DUTY ACT; AND SECTIONS 2, 7(1)(*a*) AND 12(*a*) OF THE VALUE-ADDED TAX ACT**
SUBJECT	**:**	**TAXATION OF REITs AND CONTROLLED COMPANIES**

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Preamble

In this Note unless the context indicates otherwise –

- **"CGT"** means capital gains tax, being the portion of normal tax attributable to the inclusion in taxable income of a taxable capital gain;
- **"CISIP"** means a collective investment scheme in property for purposes of the JSE Limited Listings Requirements;
- **"Collective Investment Schemes Control Act"** means the Collective Investment Schemes Control Act No. 45 of 2002;
- **"Companies Act"** means the Companies Act No. 71 of 2008;
- **"Controlled company"** means a "controlled company" as defined in section 25BB(1) (see **4.2**);
- **"JSE"** means the securities exchange operated by JSE Ltd;
- "**linked unit**" means a "linked unit" as defined in section 1(1) (see **4.4.1**);
- **"paragraph"** means a paragraph of the JSE Limited Listings Requirements as defined in section 1(1);
- **"property company"** means a "property company" as defined in section 25BB(1) (see **4.4.1**);
- **"qualifying distribution"** means a "qualifying distribution" as defined in section 25BB(1) (see **4.4.1**);
- **"REIT"** stands for "Real Estate Investment Trust" but bears its meaning as defined in section 1(1) and can thus take the legal form of a company or a trust provided it is listed on the JSE as a REIT (see **4.1**); [1]

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[1] A REIT, whether in the legal form of a company or trust, is a company for tax purposes (see **4.1.1**).

- **“Schedule”** means a Schedule to the Act;
- **“section”** means a section of the Act;
- **“the Act”** means the Income Tax Act No. 58 of 1962;
- **“VAT Act”** means the Value-Added Tax Act No. 89 of 1991; and
- any other word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This Note –

- provides guidance on the interpretation and application of section 25BB which deals with the taxation of REITs and controlled companies;
- considers other selected provisions of the Act that are particularly relevant to REITs, controlled companies and the holders of shares or linked units in these companies;
- does not discuss all the sections which apply to REITs and controlled companies, such as sections 42, 45 and 47 of the corporate rules which, while not specifically referring to REITS and controlled companies, are nevertheless applicable to REITS and controlled companies; and
- reflects the amendments introduced by the Taxation Laws Amendment Act No. 25 of 2015.

2. Background

Before the introduction of specific REIT legislation in South Africa,[2] two forms of listed property investment entities existed in South Africa, namely, property loan stock companies and property unit trusts (collective investment schemes in property). These entities were subject to different regulatory controls and tax treatment. A collective investment scheme in property operated as a trust both in reality and for income tax purposes, while a property loan stock company operated as a company. A unified approach was adopted and REITs were introduced in South Africa with effect from 1 April 2013. The REIT is the international standard and more than 25 countries in the world use a similar REIT model.[3]

South African REITs own several kinds of commercial property like shopping centres, office buildings, factories, warehouses, hotels, hospitals and, to a lesser extent, residential property, in South Africa.[4] Some REITs also invest in property in other countries.[5] The objective of a REIT is to provide investors with steady rental income and capital growth in the underlying properties.

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2 Section 25BB and the JSE Limited Listings Requirements dealing with REITs.
3 **www.sareit.co.za** [Accessed 12 May 2016].
4 **www.sareit.co.za** [Accessed 12 May 2016].
5 **www.sareit.co.za** [Accessed 12 May 2016].

A REIT may be a company as commonly understood or may be deemed to be a company for taxation purposes.[6]

Both corporate and trust (collective investment schemes in property) REITs that comply with the JSE Limited Listings Requirements[7] may be listed and publicly traded on the JSE REIT board. Once the shares in a company or a trust which is deemed to be a company for tax purposes are listed as shares in a REIT as defined in paragraph 13.1(x), the company or trust will qualify as a REIT for income tax and CGT purposes.

A REIT, and a "controlled company" as defined[8] in relation to a REIT, are subject to a specific tax regime under section 25BB. In essence a REIT and a controlled company are treated as a conduit for the income derived by it, with the REIT or controlled company being granted a deduction, subject to various limitations, for the distributions it makes of such income. A resident investor is subject to normal tax on those distributions. By contrast, a non-resident investor would be liable for dividends tax on those distributions, not normal tax.

A REIT or controlled company is also subject to other specific tax provisions, for example dividends tax, transfer duty and securities transfer tax.

3. The law

Section 25BB is quoted in **Annexure A**.

4. Application of the law

4.1 General requirements of a "REIT" [definition of "REIT" – section 1(1)]

A "REIT" is defined in section 1(1) as –

> "…a company—
>
> (*a*) that is a resident; and
>
> (*b*) the shares of which are listed—
>
> (i) on an exchange (as defined in section 1 of the Financial Markets Act and licensed under section 9 of that Act); and
>
> (ii) as shares in a REIT as defined in the JSE Limited Listings Requirements;".

The requirements for a REIT are accordingly that –

- it must be a company as defined in section 1(1) (see **4.1.1**);
- it must be a resident as defined in section 1(1) (see **4.1.2**);
- its shares must be listed on an exchange as defined in section 1(1) (see **4.1.3**); and

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[6] A portfolio of a collective investment scheme in property that qualifies as a REIT as defined in paragraph 13.1(*x*) is deemed to be a "company" [paragraph (*e*)(iii) of the definition of "company" in section 1(1)].

[7] The term "JSE Limited Listings Requirements" is defined in section 1(1) and means the JSE Limited Listings Requirements, 2003, made by the JSE Limited under section 11 of the Financial Markets Act No. 19 of 2012.

[8] In section 25BB(1).

- its shares must be listed as shares in a REIT as defined in the JSE Limited Listings Requirements (see **4.1.4**).

These requirements are considered below.

4.1.1 The REIT must be a company [preamble to the definition of "REIT" – section 1(1)]

The term "company" is defined in section 1(1). In order to qualify as a "company" for purposes of the definition of "REIT", an entity must in essence either be –

- a company as defined in section 1 of the Companies Act [paragraph (*a*) of the definition of "company" in section 1(1)] [see **4.1.1 (a)**];
- a company incorporated under the law of any country other than the Republic [paragraph (*b*) of the definition of "company" in section 1(1)] [see **4.1.1 (b)**]; or
- a portfolio of a collective investment scheme in property that qualifies as a REIT as defined in paragraph 13.1(x) [paragraph (*e*)(iii) of the definition of "company" in section 1(1)][9] (see **4.1.1**).

(a) A company as defined in the Companies Act

A "company" is defined in section 1 of the Companies Act and means –

> "a juristic person incorporated in terms of this Act, a domesticated company, or a juristic person that, immediately before the effective date—
>
> (*a*) was registered in terms of the—
>
> (i) Companies Act, 1973 (Act No. 61 of 1973), other than as an external company as defined in that Act; or
>
> (ii) Close Corporations Act, 1984 (Act No. 69 of 1984), if it has subsequently been converted in terms of Schedule 2;
>
> (*b*) was in existence and recognised as an "existing company" in terms of the Companies Act, 1973 (Act No. 61 of 1973); or
>
> (*c*) was deregistered in terms of the Companies Act, 1973 (Act No. 61 of 1973), and has subsequently been re-registered in terms of this Act;"

A domesticated company referred to in the above definition is a company whose registration has been transferred to South Africa from a foreign jurisdiction. Under section 13(5) of the Companies Act such a company is treated as if it had been originally incorporated and registered under the Companies Act.

In essence only a "public company" that is a "profit company" as defined in section 1 of the Companies Act will qualify as a REIT.

[9] Paragraph (*e*) of the definition of "company" in section 1(1) was amended by the addition of paragraph (*e*)(iii) to include a portfolio of a collective investment scheme in property with effect from years of assessment commencing on or after 1 April 2013. Paragraph (*e*)(iii) was then amended with effect from years of assessment commencing on or after 1 January 2015 to refer to a portfolio of a collective investment scheme in property that qualifies as a REIT. Paragraph (*e*)(iii) was again amended with effect from 1 January 2015 so as to refer to a portfolio of a collective investment scheme in property that qualifies as a REIT as defined in paragraph 13.1(x) of the JSE Limited Listings Requirements.

(b) A company incorporated under the law of any country other than the Republic

A company incorporated under the law of any country other than the Republic is a "company" as defined for income tax purposes and can thus also qualify as a REIT provided that it complies with all the other requirements of the definition of "REIT". One such requirement is that it must be a resident (see **4.1.2**).

(c) A portfolio of a collective investment scheme in property that qualifies as a REIT as defined in paragraph 13.1(x)

A portfolio of a collective investment scheme in property is, with effect from years of assessment commencing on or after 1 January 2015, a company for income tax purposes if it qualifies as a "REIT" as defined in paragraph 13.1(x) [see **4.1.4** for the definition of "REIT" as defined in paragraph 13.1(x)].

A "portfolio of a collective investment scheme in property" is defined in section 1(1) as follows:

> " **'[P]ortfolio of a collective investment scheme in property'** means any portfolio comprised in any collective investment scheme in property contemplated in Part V of the Collective Investment Schemes Control Act managed or carried on by any company registered as a manager under section 51 of that Act for the purposes of that Part;"

The terms "portfolio" and "collective investment scheme" are defined in section 1 of the Collective Investment Schemes Control Act as follows:

> " **'[P]ortfolio'** means a group of assets including any amount of cash in which members of the public are invited or permitted by a manager to acquire, pursuant to a collective investment scheme, a participatory interest or a participatory interest of a specific class which as a result of its specific characteristics differs from another class of participatory interests;"
>
> " **'collective investment scheme'** means a scheme, in whatever form, including an open-ended investment company, in pursuance of which members of the public are invited or permitted to invest money or other assets in a portfolio, and in terms of which—
>
> (*a*) two or more investors contribute money or other assets to and hold a participatory interest in a portfolio of the scheme through shares, units or any other form of participatory interest; and
>
> (*b*) the investors share the risk and the benefit of investment in proportion to their participatory interest in a portfolio of a scheme or on any other basis determined in the deed,
>
> but not a collective investment scheme authorised by any other Act;"

A "collective investment scheme in property" as defined in section 47(1) of the Collective Investment Schemes Control Act includes a scheme the portfolio of which consists of the following assets:

- Property shares
- Immovable property
- Assets prescribed by the Registrar
- Investments outside the Republic

Property shares

The term "property shares" is defined in section 47(1) of the Collective Investment Schemes Control Act as follows:

> " **'[P]roperty shares'** means shares in and of—
>
> (*a*) a fixed property company; or
>
> (*b*) a holding company which has no subsidiaries other than fixed property companies which are wholly owned subsidiaries as referred to in section 3(1)(*b*) of the Companies Act;"[10]

A "fixed property company" is in turn defined in section 47(1) of the Collective Investment Schemes Control Act as follows:

> " **'[F]ixed property company'** means a company all the issued shares of which are included in a portfolio, and the principal business of which consists in the acquisition and holding of—
>
> (*a*) urban immovable property[11] or any undivided share or interest therein or leasehold in respect thereof; and
>
> (*b*) such other immovable property or any undivided share or interest therein or leasehold in respect thereof as the registrar may have approved;"

While "urban immovable property" is defined in section 47(1) of the Collective Investment Schemes Control Act, the words "other immovable property" are not defined. As to the meaning of "immovable property" see discussion below.

Immovable property

According to Silberberg and Schoeman's Law of Property[12] *corporeal* immovable things (property) consist of –

> "land and everything that is attached to land by natural or artificial means."

It would seem to be accepted that the answer as to whether incorporeal things (property) are movable or immovable "would depend on the nature of the object to which it pertains."[13] It is therefore considered that a usufruct over land constitutes immovable property as contemplated in the definition of "fixed property company" in section 47(1) of the Collective Investment Schemes Control Act.

Assets prescribed by the Registrar

The registrar of collective investment schemes may for purposes of Part V (sections 47 to 51) of the Collective Investment Schemes Control Act determine assets, other than property shares, immovable property or any investment permitted under section 49, which may be included in a portfolio of a collective investment scheme in property.

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[10] Section 3(1)(*b*) of the Companies Act provides that for the purposes of that Act, a subsidiary shall be deemed to be a wholly owned subsidiary of another company if all the general voting rights associated with issued securities of the company are held or controlled, alone or in any combination, by the other company or one or more subsidiaries of that other company.

[11] As defined in section 47(1) of the Collective Investment Schemes Control Act.

[12] D G Klein and A Boraine, *Silberberg and Schoeman's Law of Property* third edition (1993) at 32.

[13] Above at 33.

Investments outside the Republic

Under section 49 of the Collective Investment Schemes Control Act a manager may, subject to specific provisions or any other law, invest assets of a portfolio of a collective investment scheme in property in immovable property in a foreign country and property shares or participatory interests in a collective investment scheme in property in a foreign country if certain requirements are met.

4.1.2 The REIT must be a resident [paragraph (*a*) of the definition of "REIT" – section 1(1)]

Only a company that is a resident qualifies as a REIT. In relation to a juristic person, paragraph (*b*) of the definition of "resident" in section 1(1) defines a resident as a person that –

- is incorporated, established or formed in the Republic; or
- has its place of effective management in the Republic.[14]

A company that is deemed to be exclusively a resident of another country under a tax treaty is excluded from the definition of "resident" in section 1(1).

4.1.3 The shares of the REIT must be listed on an exchange [paragraph (*b*)(i) of the definition of "REIT" – section 1(1)]

In order to qualify as a REIT, the shares of the company must be listed on an exchange as defined in the Financial Markets Act No. 19 of 2012 and licensed under section 9 of that Act. An "exchange" is defined in section 1 of the Financial Markets Act as follows:

> " **'[E]xchange'** means a person who constitutes, maintains and provides an infrastructure—
>
> (*a*) for bringing together buyers and sellers of securities;
>
> (*b*) for matching bids and offers for securities of multiple buyers and sellers; and
>
> (*c*) whereby a matched bid and offer for securities constitutes a transaction;"

The JSE is licensed under section 9 of the Financial Markets Act No. 19 of 2012. On 8 March 2016 ZAR X (Pty) Ltd was granted conditional approval for a licence under section 9 of the Financial Markets Act to operate an exchange in South Africa. The approval is subject to a number of suspensive conditions which must be fulfilled by 31 August 2016.[15]

The shares of the company must be listed. A "share" is defined in section 1(1) to mean, in relation to any company, any unit into which the proprietary interest in that company is divided. A share, therefore, includes a participatory interest in a portfolio of a collective investment scheme in property.

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[14] See Interpretation Note No. 6 dated 26 March 2002 "Resident: Place of Effective Management (Persons Other Than Natural Persons)" and Interpretation Note No. 6 (Issue 2) dated 3 November 2015 "Resident – Place of Effective Management (Companies)" for a discussion of the term "place of effective management".

[15] Financial Services Board Press Release dated 31 March 2016.

A listed property entity or a property entity seeking a listing must comply with the requirements in section 13 of the JSE Limited Listings Requirements, in addition to all other applicable Listing Requirements.[16] A "property entity" is defined in paragraph 13.1(t) as a company or CISIP who is primarily engaged, directly or indirectly, in property activities including –

- the holding of properties and development of properties for letting and retention as investments; or
- the purchase of land for development of properties for retention as investments.

4.1.4 The shares of the REIT must be listed as shares in a REIT as defined in the JSE Limited Listings Requirements [paragraph (*b*)(ii) of the definition of "REIT" – section 1(1)]

The shares of the REIT must be listed on an exchange licensed under section 9 of the Financial Markets Act as shares in a "REIT" as defined in paragraph 13.1(x).

The term "REIT" is defined in paragraph 13.1(x) as follows:

> " **'REIT'** means Real Estate Investment Trust and is defined as an applicant issuer which receives a REIT status in terms of the Listings Requirements."

The term "applicant or applicant issuer" is defined in the definitions of the JSE Limited Listings Requirements and means an issuer, an issuer of specialist securities[17] or a new applicant.

REIT status listing criteria for property entities other than CISIPs are dealt with in paragraphs 13.46 to 13.54, 13.59 and 13.60 and those for CISIPs in paragraphs 13.55 to 13.59 and 13.61. These listing criteria are summarised in **Annexure B**.

4.2 General requirements of a "controlled company" [definition of "controlled company" – section 25BB(1)]

The term "controlled company" is defined in section 25BB(1) and means a company that is a subsidiary, as defined in IFRS,[18] of a REIT.

A "subsidiary", as defined in IFRS 10, means an entity that is controlled by another entity. The meaning of the word "control" is discussed in paragraphs 5 to 18 of IFRS 10. It is stated in paragraph 5 of IFRS 10 that an investor, regardless of the nature of its involvement with an entity (the investee), must determine whether it is a parent by assessing whether it controls the investee. Paragraph 6 of IFRS 10 stipulates that an investor controls an investee when it is exposed or has rights to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

A company will, therefore, be a "controlled company" if it is controlled by a REIT as contemplated in IFRS 10.

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16 Paragraph 13.2(*a*).

17 Specialist securities are dealt with in section 19 of the JSE Limited Listings Requirements.

18 The term "IFRS" is defined in section 1(1) and means the International Financial Reporting Standards issued by the International Accounting Standards Board.

The shares of a controlled company need not be listed on the JSE. It is furthermore not a requirement that a controlled company be a resident, although section 25BB(2), which provides for the deduction of qualifying distributions, applies only to a controlled company that is a resident (see **4.4**).

4.3 Time of determination whether a company qualifies as a REIT or a controlled company.

The determination whether a company is a REIT or a controlled company must be made on the following dates:

- For the purposes of section 25BB(2)(*a*), (4) and (5) a company must be a REIT or a controlled company on the last day of its year of assessment (see **4.4.1**, **4.6** and **4.7**).
- Section 25BB(6)(*b*) stipulates that a company must be a REIT or a controlled company at the time of receipt or accrual of interest on a debenture forming part of a linked unit in a property company (see **4.8.2**).
- For the purposes of section 25BB(5)(*a*), (6)(*a*), 6(*c*), (7) and (8) a company must be a REIT or a controlled company at the time the relevant amount is received or accrued, or when the relevant transaction or event takes place (see **4.7**, **4.8.1**, **4.8.3** and **4.10**).

4.4 Deduction of a qualifying distribution made by a REIT or a controlled company that is a resident [section 25BB(2)]

4.4.1 Qualifying distribution [section 25BB(2)(*a*)]

The amount of a "qualifying distribution" as defined (see below) made by a REIT or a controlled company that is a resident for a year of assessment must be deducted from the income of that REIT or controlled company for that year of assessment, but only if that company is a REIT or a controlled company that is a resident *on the last day of that year of assessment*.

A company that is not a REIT or not a controlled company that is a resident on the last day of the relevant year of assessment will *not* qualify for the deduction of a qualifying distribution for that year of assessment, even if the company was a REIT or a controlled company that is a resident for part of the year of assessment. A controlled company must be a resident to qualify for a deduction under section 25BB(2). A REIT is by definition a resident.

Meaning of "qualifying distribution"

The term "qualifying distribution" is defined in section 25BB(1). A distribution by a REIT or a controlled company must comply with the following requirements to be a "qualifying distribution":

- The distribution must consist of –
  - a dividend[19] paid or payable, excluding a share buy-back contemplated in paragraph (*b*) of the definition of "dividend" in section 1(1);[20] or
  - interest incurred on a debenture forming part of a linked unit (see below) in that company.[21]
- The distribution of the dividend and the interest referred to above which must be determined with reference to the financial results for the year of assessment, must be reflected in that year's financial statements. For example, when a distribution, the amount of which is determined with reference to the financial results of Year 1 as reflected in the financial statements of Year 1, is declared and actually paid in Year 2, it will be allowed as a deduction in Year 1 even though the actual distribution is made only in Year 2.
- At least 75% of the gross income[22] received by or accrued to a company during the first year of assessment in which the company qualifies as a REIT or controlled company must comprise rental income (see below on the meaning of "rental income").
- In any other case, at least 75% of any gross income received by or accrued to a REIT or a controlled company in the year of assessment preceding the year of assessment in which the distribution is paid or payable, if a dividend, or incurred if interest, must consist of rental income (see below).
- In determining a "qualifying distribution", an amount that must be included in the income of the REIT or controlled company under section 9D(2) must not be included in the gross income of that REIT or controlled company for that year of assessment. In essence, therefore, such amount must be ignored in applying the 75% of gross income rental income test. Under section 9D(2) a portion of the net income of a controlled foreign company must be included in the income of holders of shares who are residents, other than headquarter companies, if residents directly or indirectly hold more than 50% of the participation rights or voting rights in the controlled foreign company.

A company may lose its REIT status on the JSE if a distribution does not meet the requirements of the definition of "qualifying distribution" in section 25BB(1) (see **4.1.4** and **Annexure B**).

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[19] See paragraph 2.2.3 of the *Comprehensive Guide to Dividends Tax* dated 23 February 2015 for a discussion of the meaning of "dividend" as defined in section 1(1).

[20] A share buy-back by a REIT or a controlled company is exempt from normal tax in the hands of the holders of the shares or linked units under section 10(1)(*k*)(i) (see **5.4.1**).

[21] Any interest that forms part of "qualifying distribution" is not otherwise deductible under the Act.

[22] As defined in section 1(1).

Meaning of "rental income" referred to in the definition of "qualifying distribution"

The term "rental income" is defined in section 25BB(1) and means any of the following amounts received by or accrued to a REIT or a controlled company:

- An amount received or accrued for the use of immovable property, including any penalty or interest charged on the late payment of such amount.
- Any dividend, other than a share buy-back contemplated in paragraph (*b*) of the definition of "dividend" in section 1(1), from a company that is a REIT at the time of the distribution of that dividend. A share buy-back by a REIT is excluded from "rental income" because it is exempt from normal tax in the hands of the holders of the shares under section 10(1)(*k*)(i) (see **5.4.1**). A dividend received by or accrued from a REIT includes an amount of interest paid on a debenture forming part of a linked unit held in a REIT (see **4.8.1**).
- A qualifying distribution[23] from a company that is a controlled company at the time of that distribution.
- A dividend or foreign dividend from a company that is a property company (see below) at the time of that distribution.[24]

Meaning of a "property company" referred to in the definition of "rental income"

A "property company" is defined in section 25BB(1) and can be a resident company or a foreign company. It must, however, meet the following requirements:

- A REIT or a controlled company, whether alone or together with any other company forming part of the same group of companies (see below) as that REIT or that controlled company, must hold 20% or more of the equity shares (see below) or linked units (see below) in that company.
- At the end of the previous year of assessment of that company, 80% or more of the value of its assets, reflected in the annual financial statements prepared in accordance with the Companies Act or IFRS[25] for the previous year of assessment, must directly or indirectly (see below) be attributable to immovable property.[26] A company incorporated during the current year of assessment will be unable to meet this requirement even if 80% or more of its assets during the current year comprise immovable property. However, it is unlikely that such a company would distribute a dividend until after the end of its first year of assessment.

The requirements to be a property company must be met at the time of the happening of a specific event, for example when –

- a distribution in the form of a dividend or foreign dividend is made by the company to a REIT or a controlled company [paragraph (*d*) of the definition of "rental income" in section 25BB(1)];

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[23] As defined in section 25BB(1).

[24] The terms "dividend" and "foreign dividend" are defined in section 1(1).

[25] Reference to IFRS added by section 45(1)(*a*) of the Taxation Laws Amendment Act No. 43 of 2014 with effect from 1 April 2013 and applicable in respect of years of assessment commencing on or after that date. The financial statements of a foreign company will not be prepared in accordance with the South African Companies Act, but are generally prepared in accordance with IFRS.

[26] See **4.1.1(c)** for the meaning of the words "immovable property".

- a share or a linked unit in that company is disposed of by a REIT or a controlled company [section 25BB(5)(*c*)]; and
- an amount of interest is received by or accrues to a REIT or a controlled company on a debenture forming part of a linked unit in that company [section 25BB(6)(*b*)].

Meaning of "group of companies" in the definition of "property company"

A "group of companies" is defined in section 1(1) and means two or more companies in which one company (the controlling group company) directly or indirectly holds shares in at least one other company (the controlled group company), to the extent that –

- at least 70% of the equity shares in each controlled group company are directly held by the controlling group company, one or more other controlled group companies or any combination thereof; and
- the controlling group company directly holds at least 70% of the equity shares in at least one controlled group company.

Meaning of "equity share" referred to in the definition of "property company"

The term "equity share" is defined in section 1(1) and means any share in a company, excluding any share that, neither as respects dividends nor as respects returns of capital, carries any right to participate beyond a specified amount in a distribution.

A distribution from a company could take the form of a distribution of profits (dividends) or capital (return of contributed tax capital).[27] As long as the right to participate in either of these types of distribution is unrestricted, the share will be an equity share. The share will be an equity share if only one of these rights is restricted, but not if both of these rights are restricted.

Meaning of the words "directly or indirectly" as referred to in the definition of "property company"

It is a requirement that 80% or more of the value of the assets of a property company must directly or indirectly be attributable to immovable property. "Directly" attributable includes, for example, the value of immovable property owned directly by the property company and the value of leasehold rights. "Indirectly" attributable would, for example, include the market value of any shares held by a property company to the extent that the value is attributable, directly or indirectly, to immovable property.

Meaning of "linked unit" referred to in the definitions of "qualifying distribution" and "property company"

The term "linked unit" is defined in section 1(1) and means a unit comprising a share and a debenture (see below) in a company where that share and that debenture are linked and are traded together as a single unit. Certain REITs, previously known as property loan stock companies, issue linked units to their holders. Profits distributed by these companies comprise both dividend and interest elements. For example, a distribution of R100 may consist of a dividend of R1 and interest of R99.

[27] The term "contributed tax capital" is defined in section 1(1).

Meaning of "debenture" as referred to in the definition of "linked unit"

The word "debenture" is not defined in the Act. It is stated in *Henochsberg on the Companies Act 71 of 2008* that a "debenture" means –[28]

> "any document, however it may be described, and whatever form it may take, which creates or acknowledges indebtedness in the company to another for moneys advanced or to be advanced to the company".

4.4.2 Limitation of the deduction of the "qualifying distribution" [section 25BB(2)(*b*)]

The aggregate amount of qualifying distributions (dividends and interest on a debenture forming part of a linked unit) that may be deducted in any year of assessment may not exceed the taxable income of the REIT or the controlled company that is a resident for that year of assessment, before taking into account the following:

- Any deduction for the qualifying distribution.
- Any assessed loss brought forward under section 20. An assessed loss of a REIT or a controlled company before it became a REIT or a controlled company may be carried forward under section 20.
- The amount of a taxable capital gain included in taxable income under section 26A. A taxable capital gain will constitute an amount that is not disregarded under section 25BB(5) (see **4.7**).

Expenditure or allowances (other than certain specified capital allowances on immovable property, see **4.6**) that are deductible under other provisions of the Act must first be deducted from the REIT or controlled company's income before determining the taxable income limitation under section 25BB(2)(*b*). A REIT or a controlled company may, for example, claim a deduction for –

- salaries under section 11(*a*);
- a wear-and-tear or depreciation allowance under section 11(*e*);
- energy-efficiency savings under section 12L;
- foreign tax under section 25BB(2A)(*a*) and (*b*) (see **4.5.1** and **4.5.2)**; and
- *bona fide* donations made to certain organisations under section 25BB(2A)(*c*) (see **4.5.3)**.

Since the aggregate amount of qualifying distributions that may be deducted in any year of assessment may not exceed the REIT or controlled company's taxable income, the deduction of qualifying distributions under section 25BB(2)(*a*) cannot create an assessed loss or increase an assessed loss carried forward.

The amount of any qualifying distribution that is not deductible because it exceeds the REIT or controlled company's taxable income as determined under section 25BB(2)(*b*) is forfeited and cannot be carried forward to a subsequent year of assessment. Even so, the full amount of the qualifying distribution is taxable in the hands of resident holders of shares under paragraph (*k*) of the definition of "gross

[28] P M Meskin *et al Henochsberg on the Companies Act 71 of 2008* [online] (My LexisNexis: May 2015) in Commentary on section 43 of the Companies Act.

income" in section 1(1) (see **5.4.1**) while non-resident holders are subject to dividends tax.

Example 1 – Taxation of a REIT and the normal tax and dividends tax implications of dividends paid to the holders of shares in a REIT

Facts:

REIT A was incorporated on 10 January 2014 and its year of assessment ends on the last day of December. REIT A holds 51% of the equity shares in Controlled Company C and 20% of the equity shares in Property Company D. It also holds 10% of the linked units in REIT B. Residents hold 70% of the equity shares in REIT A and non-residents hold 30%. REIT A declared a dividend of R15,4 million on 15 March 2015 that was paid on 31 March 2015. The dividend was determined with reference to the financial results reflected in the 2014 financial statements.

The following gross income was received by or accrued to REIT A during its 2014 year of assessment:

	R
Rental income from letting of fixed property	2 000 000
Dividend received from REIT B	100 000
Interest on a linked unit in REIT B	9 900 000
Qualifying distribution from Controlled Company C	1 000 000
Dividend from Property Company D	300 000
Interest on loans	400 000
Dividends on investments in other companies	300 000
Total gross income	14 000 000

REIT A made the following capital gains on the disposal of assets during the 2014 year of assessment:

	R
Capital gain on disposal of fixed property	5 000 000
Capital gain on disposal of other assets	2 000 000
Sum of capital gains	7 000 000

REIT A incurred expenses of R1,5 million in the production of the rental income. REIT A owns fixed property with a cost price of R20 million and claimed an allowance of R1 million under section 13*quin*(1).

Result:

Calculation of the qualifying distribution

The dividend of R15,4 million will be a "qualifying distribution"[29] as defined in section 25BB(1) if at least 75% of the gross income of REIT A for its 2014 year of assessment consisted of rental income.

[29] Paragraph (*a*) of the definition of "qualifying distribution".

The following amounts of income received by or accrued to REIT A for the 2014 year of assessment constituted "rental income" as defined in section 25BB(1):

	R
Rental income from letting of fixed property	2 000 000
Dividend from REIT B (Note 1)	100 000
Interest on a linked unit in REIT B (Note 2)	9 900 000
Qualifying distribution from Controlled Company C	1 000 000
Dividend from Property Company D (Note 3)	300 000
Total amount of "rental income"	13 300 000

The "rental income" received by or accrued to REIT A constituted 95% (R13,3 million / R14 million) of the gross income received or accrued to it for the 2014 year of assessment.

The dividend of R15,4 million therefore constitutes a "qualifying distribution" in the 2014 year of assessment. Although the dividend was declared and paid in the 2015 year of assessment, on the basis that it was determined with reference to the financial results reflected in the financial statements prepared for the 2014 year of assessment, it is deductible in the 2014 year of assessment.

Limitation of the amount of the "qualifying distribution" under section 25BB(2)(b)

	R
Gross income	14 000 000
Less: Dividend exemption – section 10(1)(*k*)(i) (Note 4)	(600 000)
Less: Expenses incurred in the production of rental income	(1 500 000)
Less: Capital allowance under section 13*quin*(1) (Note 5)	0
Taxable income before taking into account the deduction under section 25BB(2)(*a*) and the taxable capital gain	11 900 000

The qualifying distribution of R15,4 million that is deductible in the 2014 year of assessment is therefore limited to R11 900 000 under section 25BB(2)(*b*). The shortfall of R3 500 000 (R15 400 000 – R11 900 000) is not carried forward to the 2015 year of assessment and is forfeited.

Calculation of taxable income of REIT A

	R
Taxable income before taking into account the deduction under section 25BB(2)(*a*) and the amount of the taxable capital gain	11 900 000
Less: Deduction of the qualifying distribution – section 25BB(2)(*a*)	(11 900 000)
Taxable capital gain (R2 million × 66,6%) (Note 6)	1 332 000
Taxable income of REIT A	1 332 000

Notes:

(1) Any dividend received or accrued from a REIT (other than in relation to a share buy-back) constitutes "rental income" as defined [paragraph (*b*) of the definition of "rental income" in section 25BB(1)].

(2) Interest on a debenture forming part of a linked unit in a REIT is deemed to be a dividend received or accrued under section 25BB(6)(*a*). A dividend received or accrued from a REIT (other than in relation to a share buy-back) in turn constitutes "rental income" as defined [paragraph (*b*) of the definition of "rental income" in section 25BB(1)].

(3) A dividend received or accrued from a property company constitutes "rental income" as defined [paragraph (*d*) of the definition of "rental income" in section 25BB(1)].

(4) The exemption under section 10(1)(*k*)(i) applies to the dividends received from Property Company D (R300 000) and the other companies (R300 000). The dividends and deemed dividends received from REIT B and Controlled Company C do not qualify for the exemption because of the exclusion provided for in paragraph (*aa*) of the proviso to section 10(1)(*k*)(i).

(5) Under section 25BB(4) REIT A may not claim the capital allowance of R1 million under section 13*quin*(1).

(6) Under section 25BB(5) the capital gain of R5 000 000 on disposal of the fixed property must be disregarded in determining the aggregate capital gain or aggregate capital loss of REIT A.

Normal tax and dividends tax implications for the resident holders of shares in REIT A

The dividends of R10 780 000 (R15,4 million × 70%) received by or accrued to the resident holders of the shares are included in their gross income under paragraph (*k*) of the definition of "gross income" in section 1(1). Under paragraph (*aa*) of the proviso to section 10(1)(*k*)(i) these dividends are not exempt from normal tax.

The dividends of R10 780 000 paid to the resident beneficial owners are exempt from dividends tax under section 64F(1)(*l*) because of their inclusion in income for normal tax purposes.

Normal tax and dividends tax implications for the non-resident holders of shares in REIT A

The dividends of R4 620 000 (R15,4 million × 30%) received by or accrued to the non-resident holders of shares are included in their gross income under paragraph (*k*) of the definition of "gross income" in section 1(1). These dividends are, however, exempt from normal tax under section 10(1)(*k*)(i).

The dividends of R4 620 000 paid to the non-resident beneficial owners are subject to dividends tax under section 64E(1). REIT A, or its regulated intermediary, is liable under section 64G(1) or section 64H(1) to withhold dividends tax of R693 000 (R4 620 000 × 15%) from the dividends paid to the non-resident beneficial owners. Dividends tax may be withheld at a reduced rate if the requirements of section 64G(3) or section 64H(3) are met.

4.5 Deduction of foreign taxes and *bona fide* donations [section 25BB(2A)]

Section 25BB(2A) provides for three types of deduction in determining a REIT or controlled company's taxable income. These deductions, which are discussed in **4.5.1**, **4.5.2** and **4.5.3**, must be deducted in the determination of a REIT or a controlled company's taxable income for years of assessment commencing on or after 1 January 2016.

The deductions must be claimed in the order specified in the subsection. In each case the deductions are determined before reducing taxable income by the amount of any qualifying distribution referred to in section 25BB(2)(*a*), but after taking into account any assessed loss brought forward from the previous year of assessment

and any taxable capital gain. The requirement to determine the deductions before taking into account any qualifying distribution is necessary because a qualifying distribution would typically result in a substantial reduction in taxable income thus severely curtailing the amount of the deductions that a REIT or controlled company could claim under section 25BB(2A).

4.5.1 Deduction of foreign taxes attributable to a REIT or controlled company's interest in a non-resident vesting trust [section 25BB(2A)(*a*)]

A REIT or a controlled company that is a beneficiary of a *vesting* trust that is not a resident may deduct any amount of tax *proved to be payable* by that trust to the government of a country other than South Africa that is attributable to the interest of that REIT or controlled company in that trust – provided the non-resident trust is *liable for or subject to tax on income* in the country in which that trust is established or formed.[30] A deduction will not be allowed if any person has any right of recovery of that tax.

This section will therefore apply only when –

- *income* is derived by a non-resident trust during a year of assessment;
- a REIT or a controlled company has a *vested right* in that income during the same year of assessment;
- the trust is "liable for or subject to" tax on that *income* in the country in which that trust is established or formed;
- the relevant tax is "proved to be payable" by the trust to a government other than South Africa; and
- no person has a right of recovery in relation to the taxes proved to be so payable.

Tax on income

It is only tax borne on *income* derived by the trust that will qualify for deduction under section 25BB(2A)(*a*). In determining whether or not a particular foreign tax qualifies as a tax on *income*, the basic scheme of application of the foreign tax must be compared with that of the Act. The foreign tax will be accepted as a tax on income only if the basis of taxation is substantially similar to that of the Act.

To a certain extent it is immaterial that the detail of a foreign tax law differs from South Africa's domestic tax law. The important consideration is whether the basis of taxation is substantially similar. For example, a foreign tax law may include certain items of income or may allow certain exclusions or deductions not included or allowed under South African domestic tax law but the relevant foreign tax could still be considered to be a tax on income.

In contrast, the mere fact that a foreign tax is regarded as a tax on income by the country levying the tax or that the same term is used is not sufficient. The precise nature of the foreign tax and the meaning of particular terms must be determined and considered. In other words, the foreign tax liability must be a tax on income within the South African concept of that term.

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[30] Any foreign taxes that are deductible under section 25BB(2A)(*a*) are not otherwise deductible under the Act.

SARS levies the following taxes on income:

- Normal tax on taxable income, which includes a taxable capital gain [section 5]
- Withholding tax on royalties, a final tax payable by non-residents on income derived from royalties or similar payments [section 49A – G]
- Withholding tax on interest, a final tax (effective 1 March 2015) [section 50(B)(1)]
- Withholding tax on service fees, a final tax (effective 1 January 2017)[31] [section 51(B)(1)]
- Withholding tax on foreign entertainers and sportspersons, a final tax [section 47B(2)]
- Turnover tax on micro businesses [section 48A]
- Dividends tax [section 64E(1)]

Any foreign taxes which are substantively similar in nature to these taxes will be considered a tax on income. Withholding taxes which constitute an advance payment on an ultimate foreign tax liability would not qualify as a foreign tax on income although the underlying ultimate foreign tax liability may itself qualify as a tax on income. For example, foreign taxes similar to employees' tax, provisional tax and section 35A withholding tax levied on payments made to non-resident sellers of immovable property in South Africa would not qualify as a tax on income.

A liability for interest, additional foreign taxes, fines, penalties or any other similar obligation imposed under the tax laws of a foreign country is not regarded as a tax on income and does not qualify for a deduction under section 25BB(2A)(*a*).

"Liable for or subject to" tax in the foreign jurisdiction

In order for a REIT or controlled company to qualify for the deduction of the foreign taxes under section 25BB(2A)(*a*), the non-resident trust must have been "liable for or subject to" tax on that income in the country in which the trust is established or formed.

The meaning of "liable for" and "subject to" is not defined in the Act. While these words have not received judicial consideration in South Africa, it is evident from an analysis of foreign case law[32] that what is required for the trust to be "*liable for*" the tax on the relevant income is that tax must have been imposed on the amount of the income. The fact that an exemption may apply in relation to the specific income and no tax may therefore be payable by the trust does not alter the fact that the trust is "liable for" the tax. By contrast, the non-resident trust will be regarded as "*subject to*" tax on the relevant income only if the trust is actually required to pay the tax. If an exemption applies in respect of the income, the non-resident trust is not "subject to" tax on the income. Practically, given that the foreign tax must also "be proved to be

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[31] Section 99 of the Taxation Laws Amendment Act No. 31 of 2013 read with section 149 of the Taxation Laws Amendment Act No. 25 of 2015. The withdrawal of withholding tax on service fees was proposed in the 2016 National Budget.

[32] See *Paul Weiser v HM Revenue and Customs* [2012] UKFTT 501 (TC) and L Kruger "Interest-free and Low-interest Shareholder Loans" (September 2014) 5 *Business Tax and Company Law Quarterly* 21.

payable" (see below), it is insufficient for the non-resident trust to be only "liable for" the tax; the non-resident trust must in fact be "subject to" tax on the relevant vested income.

"Proved to be payable"

A tax will be "proved to be payable" if the non-resident trust has an unconditional legal liability to pay the tax and the trust has either paid the tax or will have to pay the tax in the future. An unconditional legal liability to pay the foreign tax arises only once all the events that fix the amount of the foreign tax, and the non-resident trust's liability, have taken place.

Given that the relevant foreign tax will qualify to be dealt with under section 25BB(2A)(*a*) only if it is "proved to be payable" ***and*** no person has "any right of recovery" of the tax, it is apparent that an unconditional legal liability in the context of section 25BB(2A)(*a*) means that the foreign tax must have been levied legitimately under the foreign jurisdiction's tax law and tax treaty (if applicable) before it can qualify for a deduction under section 25BB(2A)(*a*). If the foreign tax has not been levied legitimately under the domestic law of the foreign jurisdiction or has been levied contrary to the clear provisions of a tax treaty (if applicable), it cannot be said that the foreign tax is "proved to be payable" or that the resident does not have a "right of recovery".[33]

Example 2 – Deduction of foreign taxes attributable to a REIT's interest in a non-resident vesting trust

Facts:

REIT A has a vested right of 100% in the rental income derived by a non-resident trust, Trust A, which was established in Foreign Country A. Trust A invested in immovable property in Foreign Country A. During REIT A's year of assessment ending on 31 December 2016, Trust A derived rental income of R100 000 which vested in REIT A. Trust A is subject to foreign tax in Foreign Country A on rental income received by or accrued to it at a rate of 10% and is therefore liable for tax of R10 000 on the rental income derived by it.

Result:

The rental income of R100 000 that vests in REIT A must be included in its gross income under section 25B(1) and the definition of "gross income" in section 1(1).

Under section 25BB(2A)(*a*) the foreign tax of R10 000 that is proved to be payable by Trust A on the rental income of R100 000 that vests in REIT A must be allowed as a deduction in determining REIT A's taxable income for the 2016 year of assessment. The foreign tax of R10 000 is allowed as a deduction in full since REIT A has an interest of 100% in the rental income derived by Trust A.

[33] See further paragraphs 4.3.1 and 4.3.2 of Interpretation Note No. 18 (Issue 3) dated 26 June 2015 "Rebates and Deductions for Foreign Taxes on Income" for a discussion regarding the meaning of "tax on income" and "proved to be payable".

4.5.2 Deduction of foreign taxes on income proved to be payable by a REIT or a controlled company to any sphere of government of a foreign country [section 25BB(2A)(*b*)]

A deduction must be allowed for the sum of any taxes on *income* "proved to be payable" (see **4.5.1**) by a REIT or controlled company to any sphere of government of any foreign country.[34] Such a deduction will not be allowed if any person has any right of recovery (see **4.5.1**) of those foreign taxes, other than a right of recovery under any entitlement to carry back losses arising during any year of assessment to any year of assessment before such year of assessment.

Example 3 – Deduction of foreign taxes on income proved to be payable by a REIT to any sphere of government of a foreign country

Facts:

REIT A's year of assessment ends on 31 December. During its 2016 year of assessment, foreign dividends of R100 000 accrued to REIT A from Foreign Company A. REIT A holds 5% of the equity shares in Foreign Company A. Foreign Company A withheld tax of R15 000 (15% × R100 000) from the dividend and paid the net amount of R85 000 (R100 000 – R15 000) to REIT A.

Result:

The foreign dividends of R100 000 that accrued to REIT A must be included in its gross income under paragraph (*k*) of the definition of "gross income" in section 1(1). The foreign dividends are not exempt from normal tax under section 10B(2) but are partially exempt under section 10B(3).

Under section 25BB(2A)(*b*) the foreign withholding tax of R15 000 must be allowed in full as a deduction in determining REIT A's taxable income for the 2016 year of assessment, even though a portion of the foreign dividend is exempt from tax under section 10B(3).

4.5.3 Deduction of *bona fide* donations made by a REIT or a controlled company [section 25BB(2A)(*c*)]

Any *bona fide* donations made by a REIT or controlled company during a year of assessment to any organisation as contemplated in section 18A(1)(*a*) or (*b*) must be allowed as a deduction under section 25BB(2A)(*c*).[35]

The organisations referred to in section 18A above are the following:

- A public benefit organisation which actively carries on in South Africa any public benefit activity listed in Part II of the Ninth Schedule [section 18A(1)(*a*)(i)].
- A public benefit organisation that does not itself carry on the public benefit activities listed in Part II but provides funds or assets to another approved public benefit organisation referred to in the preceding bullet, or to an

[34] Any foreign taxes that are deductible under section 25BB(2A)(*b*) are not otherwise deductible under the Act.

[35] Any donation that is deductible under section 25BB(2A)(*c*) is not otherwise deductible under the Act.

institution, board or body contemplated in section 10(1)(*c*A)(i) which carries on in South Africa any public benefit activity listed in Part II [section 18A(1)(*b*)].

- An institution, board or body established by or under law approved by SARS under section 10(1)(*c*A)(i) and which carries on any public benefit activity listed in Part II in South Africa [section 18A(1)(*a*)(ii)].

The following explanation is provided in the *Tax Exemption Guide for Public Benefit Organisations in South Africa* (Issue 4) in paragraph 23.11 on the meaning of "*bona fide* donation":

> "A donation[36] is a gratuitous disposal by the donor out of liberality or generosity, under which the donee is enriched and the donor impoverished. It is a voluntary gift which is freely given to the donee. There must be no *quid pro quo*, no reciprocal obligations and no personal benefit for the donor. If the donee gives any consideration at all it is not a donation.
>
> A PBO may not accept donations which are subject to conditions that could enable the donor or any connected person in relation to the donor to derive some direct or indirect benefit from the application of the donation. The donation may also, subject to limited exceptions, not be revocable by the donor."

Under the proviso to section 25BB(2A)(*c*) the deduction may not exceed 10% of the taxable income of a REIT or controlled company after taking into account any deduction for foreign taxes under section 25BB(2A)(*a*) and (*b*), but before taking into account any deduction of a qualifying distribution under section 25BB(2)(*a*). No provision is made for the carry-forward of any amount paid in excess of the 10% limitation to a subsequent year of assessment and any such excess will be forfeited.

Example 4 – Deduction of *bona fide* donations made by a REIT

Facts:

REIT A's year of assessment ends on 31 December. Its taxable income for the 2016 year of assessment is R920 000, after taking into account a taxable capital gain of R20 000 and the balance of an assessed loss brought forward from the 2015 year of assessment of R100 000.

REIT A qualifies for a deduction of foreign withholding taxes under section 25BB(2A)(*b*) of R10 000. REIT A made *bona fide* donations contemplated under section 18A(1)(*a*)(i) of R100 000. After the end of its 2016 year of assessment it declared a dividend of R900 000 which constitutes a "qualifying distribution" as defined in section 25BB(1). The foreign taxes, *bona fide* donation and qualifying distribution have not yet been taken into account in determining REIT A's taxable income.

The amount of the dividend was determined with reference to the financial results reflected in the 2016 financial statements.

[36] Defined in section 55.

Result:

Calculation of the amount of the donation that is allowable under section 25BB(2A)(c)

	R
Taxable income after taking into account the taxable capital gain and the balance of assessed loss brought forward, but before taking into account the deductions for foreign taxes, the donation and the qualifying distribution	920 000
Less: Foreign withholding taxes [section 25BB(2A)(*b*)]	(10 000)
Taxable income before donations and the qualifying distribution	910 000
Less: Deduction for the donation [limited to 10% of R910 000 under the proviso to section 25BB(2A)(*c*)]	(91 000)
Taxable income before the deduction for the qualifying distribution	819 000

Calculation of the qualifying distribution

	R
Taxable income calculated above	819 000
Less: Taxable capital gain included in taxable income	(20 000)
Add: Balance of assessed loss deducted from taxable income	100 000
Maximum amount to be allowed for the qualifying distribution under section 25BB(2)(*a*) and (*b*)	899 000

Calculation of taxable income after taking into account the qualifying distribution

	R
Taxable income before taking into account the qualifying distribution	819 000
Less: Qualifying distribution under section 25BB(2)(*a*) and (*b*)	(899 000)
Assessed loss (Note)	(80 000)

Note:

The deduction for the qualifying distribution has not created or increased the assessed loss, the assessed loss remaining relates to the assessed loss brought forward from 2015.

4.6 Prohibition of deduction of capital allowances on immovable property [section 25BB(4)]

Section 25BB(4) prohibits a company that is a REIT or a controlled company *on the last day of a year of assessment* from deducting an allowance on immovable property under the following sections:

- 11(*g*) – An allowance granted to a lessee for expenditure actually incurred in pursuance of an obligation to effect improvements on land or to buildings.
- 13 – Allowance on buildings used in a process of manufacture.
- 13*bis* – Allowance on buildings used by hotel keepers.
- 13*ter* – Allowance on residential buildings.
- 13*quat* – Allowance on erection or improvement of buildings in urban development zones.
- 13*quin* – Allowance on commercial buildings.

- 13*sex* – Allowance on certain residential units.

A depreciation allowance on assets, other than immovable property, may be claimed by a REIT or a controlled company under section 11(*e*).

While the building allowances described in section 25BB(4) are not deductible, this disadvantage is counterbalanced by the fact that any capital gains or capital losses on disposal of immovable property must be disregarded by a REIT or a controlled company for CGT purposes under section 25BB(5) (see **4.7**).

Even so, there will be a recoupment of capital allowances claimed as a deduction by a REIT or a controlled company before the company became a REIT or a controlled company when immovable property is disposed of (see **4.7**).

4.7 Disregarding of a capital gain or capital loss on the disposal of certain property by a REIT or a controlled company [section 25BB(5)]

A capital gain or capital loss determined on the disposal of an asset by a company that qualifies as a REIT or a controlled company *on the last day of a year of assessment*, must be disregarded in determining its aggregate capital gain or aggregate capital loss,[37] if the disposal comprises –

- immovable property of a company that is a REIT or a controlled company at the time of the disposal [section 25BB(5)(*a*)];
- a share or a linked unit in a company that is a REIT at the time of that disposal [section 25BB(5)(*b*)]; or
- a share or a linked unit in a company that is a property company at the time of that disposal [section 25BB(5)(*c*)].

The disposal of a share or a linked unit in a controlled company must not be disregarded under section 25BB(5) unless the controlled company qualifies as a property company at the time of disposal. A controlled company may own assets other than immovable property. The disposal by a REIT of a share or a linked unit in a controlled company that does not qualify as a property company at the time of disposal will accordingly be subject to CGT if the proceeds are of a capital nature.

While a capital gain or capital loss on disposal of the assets described above must be disregarded, any capital allowances allowed on immovable property before the company became a REIT or a controlled company must be recouped and included in the gross income of the REIT or controlled company under paragraph (*n*) of the definition of "gross income" in section 1(1).

A capital gain or capital loss determined on the disposal of an asset of a REIT or a controlled company that is not listed in section 25BB(5) will be subject to CGT. Assets not listed in section 25BB(5) could, for example, include motor vehicles and office equipment. A controlled company that is a foreign company will be subject to CGT on the disposal of assets referred to in paragraph 2(1)(*b*) of the Eighth Schedule. Since a capital gain or capital loss determined on disposal of immovable property is excluded under section 25BB(5), the only assets remaining

[37] The terms "aggregate capital gain" and "aggregate capital loss" are defined in paragraphs 6 and 7 of the Eighth Schedule, respectively.

under paragraph 2(1)(*b*) are assets which are attributable to a permanent establishment of the controlled company in South Africa.

Income of a revenue nature derived from the disposal of shares, fixed property and other assets that were, for example, held as trading stock must be included in a REIT or controlled company's gross income. Such income will be included in the gross income of a controlled company that is a foreign company if derived from a source within South Africa.[38]

Section 25BB(5) refers to immovable property of a company that is a REIT or a controlled company and as such envisages direct disposals of property and does not include –

- a capital gain determined on the vesting of an asset in a beneficiary which is a REIT or a controlled company under paragraph 80(1)(*b*) of the Eighth Schedule; or
- the distribution of a capital gain arising on the disposal of the assets referred to in section 25BB(5)(*a*) to (*c*) by a trust under paragraph 80(2)(*b*) of the Eighth Schedule to a beneficiary which is a REIT or a controlled company.

Such capital gains will be subject to CGT in the REIT or controlled company to which they are attributed.

4.8 Interest on a debenture forming part of a linked unit deemed to be a dividend [section 25BB(6)]

4.8.1 Interest received by or accrued to a person on a debenture forming part of a linked unit held in a REIT or a controlled company [section 25BB(6)(*a*)]

Section 25BB(6)(*a)* provides that any interest received by or accrued to a person during a year of assessment in respect of a debenture forming part of a linked unit held by that person in a company that is a REIT or a controlled company is, if that company or controlled company is –

- a resident, deemed to be a dividend received by or accrued to that person; or
- a foreign company, deemed to be a foreign dividend received or accrued to that person,

during that year of assessment.

Section 25BB(6)(*a*) generally applies to years of assessment of any person commencing on or after 1 April 2013.

By contrast, section 25BB(6)(*c*), which deems interest paid in respect of a linked unit in a REIT or controlled company to be a dividend for dividends tax purposes (see **4.8.3**), applies to the years of assessment commencing on or after 1 April 2013 *of the REIT or controlled company paying the interest.*

As a result, it was possible that interest paid on a linked unit by a REIT or a controlled company was deemed to be a dividend, for the purposes noted above, from the REIT or controlled company's perspective, but was not deemed to be a dividend from the perspective of the person that received the dividend or to whom it

[38] Paragraph (ii) of the definition of "gross income" in section 1(1).

accrued. This would arise if, for example, REIT A with a year of assessment commencing on 1 April 2013, paid interest on a linked unit to Resident B on 30 April 2013 that had a year of assessment commencing on 1 March 2013. Section 25BB(6)(*a*) did not apply to Resident B since Resident B's year of assessment commenced before 1 April 2013, while the provisions of section 25BB(6)(*c*) applied to REIT A because REIT A's year of assessment commenced on or after 1 April 2013.

This result could occur only in the first year of assessment of the REIT or controlled company commencing on or after 1 April 2013 when the year of assessment of the holder of a linked unit in the REIT or controlled company commenced before 1 April 2013. It will not occur when both the year of assessment of the holder of the linked unit and the year of assessment of the REIT or controlled company commenced on or after 1 April 2013.

See **5.4.1** for the normal tax implications of dividends received by or accrued to a person from a REIT or a controlled company and **5.10** for the dividends tax implications of such dividends.

4.8.2 Interest received by or accrued to a REIT or a controlled company that is a resident on a debenture forming part of a linked unit held in a property company [section 25BB(6)(*b*)]

Interest received by or accrued to a company that is a REIT or a controlled company that is a resident during a year of assessment on a debenture forming part of a linked unit held by that company in a property company is deemed to be –

- a dividend if the property company is a resident; or
- a foreign dividend if the property company is a foreign company

received by or accrued to that company during that year of assessment if that company is a REIT or a controlled company that is a resident *at the time of that receipt or accrual*.

Any such deemed dividends or deemed foreign dividends received by or accrued to a REIT or a controlled company must be included in the gross income of the REIT or controlled company. Dividends and foreign dividends (which would include such deemed dividends and deemed foreign dividends) are generally fully exempt from income tax under section 10(1)(*k*)(i) (domestic dividends) or fully or partially exempt under section 10B (foreign dividends).

See **5.10.2** for the dividends tax implications of dividends and foreign dividends received by or accrued to a REIT or a controlled company.

Dividends and foreign dividends received by or accrued to a REIT or a controlled company that is a resident from a property company qualify as "rental income" as defined in section 25BB(1) and are used to determine a "qualifying distribution" as defined in section 25BB(1) (see **4.8.1**).

4.8.3 Interest paid on a debenture forming part of a linked unit in a REIT or a controlled company [section 25BB(6)(*c*)]

Interest paid on a debenture forming part of a linked unit in a REIT or a controlled company is deemed –

- to be a dividend paid by that REIT or that controlled company for the purposes of dividends tax; and
- not to be an amount of interest paid by that REIT or that controlled company for the purposes of withholding tax on interest.[39]

Interest paid by a REIT or a controlled company that is a resident on a debenture forming part of a linked unit is, therefore, potentially subject to dividends tax. Interest paid by a controlled company that is not a resident on a debenture forming part of a linked unit will potentially be subject to dividends tax only if the controlled company's shares are listed on the JSE and if the "dividend" does not constitute the distribution of an asset *in specie*. See **5.10.1** for the dividends tax implications of dividends paid by a REIT or a controlled company.

Interest paid on a debenture forming part of a linked unit in a REIT or a controlled company may be a "qualifying distribution" as defined in section 25BB(1) and, if so, may, subject to certain limitations, be deducted from the income of the REIT or controlled company under section 25BB(2) (see **4.4**).

4.9 Cessation of a REIT or a controlled company [section 25BB(7)]

A REIT or a controlled company's year of assessment is deemed to end before the end of its financial year when –

- the REIT ceases to be a REIT and does not qualify as a controlled company; or
- the controlled company ceases to be a controlled company and does not qualify as a REIT.

These events will have the following consequences:

- The year of assessment of the REIT or controlled company is deemed to end on the day that the company ceases to be a REIT or a controlled company as indicated above; and
- the following year of assessment of the company is deemed to commence on the day immediately after the day that the company ceased to be either a REIT or a controlled company.

A company will cease to be a REIT when –

- the JSE removes the REIT status of an applicant issuer that fails to comply with paragraph 13.49;[40]

[39] The legislation for withholding tax on interest is contained in sections 50A to 50H and became effective on 1 March 2015.

[40] Paragraph 13.53(*a*).

- an issuer that received REIT status makes application to the JSE to have its status removed;[41] or
- it does not meet the requirements of a "REIT" as defined in section 1(1).

A company that ceases to be a REIT can still qualify as a controlled company if it is controlled by another company that is a REIT. Under these circumstances, section 25BB(7) will not apply.

A company will cease to be a controlled company when it ceases to be controlled by a company that is a REIT. A company that ceases to be a controlled company can still be a REIT if it satisfies the requirements of a "REIT" as defined in section 1(1). Under these circumstances, section 25BB(7) will not apply.

The remaining provisions of section 25BB do not apply to a company from the year of assessment following the year of assessment in which the company ceases to be a REIT or a controlled company.

After an entity ceases to be a REIT or a controlled company it will be subject to income tax under the general rules applicable to its legal form. In other words, a company will be taxed as a company and a trust will be taxed as a trust. The taxation of the holders of shares in a company and beneficiaries of a trust will follow the normal tax rules applicable to such persons.

4.10 Cancellation of the debenture part of a linked unit [section 25BB(8)]

Specific rules apply when a REIT or a controlled company cancels the debenture part of a linked unit and capitalises the issue price of the debenture to stated capital for the purposes of financial reporting in accordance with IFRS. After cancellation of the debenture part of a linked unit a person will hold only a share in the REIT or controlled company. The tax consequences of the cancellation of the debenture part of a linked unit are as follows:

- The cancellation of the debenture must be disregarded in determining the taxable income of the holder of the debenture and of the REIT or controlled company. No gain or loss on the cancellation of the debenture will, therefore, be determined for the holder of the linked unit and for the REIT or controlled company [section 25BB(8)(*a*)].
- Expenditure incurred by the holder of shares in the REIT or controlled company on the capitalised shares is deemed to be equal to the amount of the expenditure incurred on the acquisition of the linked unit. This expenditure will be used to determine the base cost of the shares held as a capital asset under paragraph 20(1) of the Eighth Schedule or the amount of expenditure actually incurred on the shares under section 11(*a*) for a share-dealer [section 25BB(8)(*b*)].
- The issue price of the cancelled debenture must be added to the contributed tax capital[42] of the class of shares that formed part of the cancelled linked unit. Contributed tax capital is a tax concept and broadly represents the amounts contributed to a company in exchange for the issue of its shares. Contributed tax capital of a company is increased by the consideration

[41] Paragraph 13.54.
[42] The term "contributed tax capital" is defined in section 1(1).

received by or accrued to that company for the issue of its shares on or after 1 January 2011. Contributed tax capital is determined per class of shares. The issue price of a cancelled debenture can, therefore, be added only to the contributed tax capital of the class of shares relating to the cancelled linked unit [section 25BB(8)(*c*)].

See **5.7** for the income tax implications of a "substitutive share-for-share transaction" under section 43 under which linked units in a company are exchanged for equity shares.

5. Selected other provisions affecting REITs, controlled companies and the holders of shares or linked units in REITs and controlled companies

5.1 The law

The relevant sections and other legislation are quoted in **Annexure A**.

5.2 Interest on hybrid debt instruments deemed to be dividends *in specie* [section 8F(3)(*d*)]

Under section 8F(2)(*a*) an amount of interest incurred by a company on a hybrid debt instrument[43] is, on or after the date that the instrument becomes a hybrid debt instrument –

- deemed for the purposes of the Act to be a dividend *in specie* declared and paid by that company on the last day of the year of assessment of that company; and
- not deductible under the Act.

The amount of the interest that is deemed to be a dividend *in specie* declared and paid by the company incurring the interest expense is potentially subject to dividends tax under section 64E(1). The company incurring the interest expense is the party that is liable under section 64EA(*b*) for any dividends tax that is payable because the interest expense is deemed to be a dividend *in specie*.[44] The deemed dividend will, however, qualify for an exemption from dividends tax under section 64FA(1)(*a*) read with section 64F(1)(*l*) because the deemed dividend will constitute income for the debenture holder (see below).

While section 8F(2)(*a*) provides that the interest on a hybrid debt instrument which is deemed to be a dividend *in specie* is not deductible under the Act, the deemed dividend may be deductible as part of a qualifying distribution under section 25BB(2)(*a*) if the requirements of that section are met.

Section 8F(2)(*b*)[45] provides that an amount of interest that accrues to a person to whom an amount is owed on a hybrid debt instrument is deemed for the purposes of

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43 The term "hybrid debt instrument" is defined in section 8F(1).

44 Section 64E uses the expression "distribution of an asset *in specie*" while section 8F refers to a "dividend *in specie*". Nothing turns on the difference in wording since both expressions bear the same meaning for the purpose of determining the liability for, and incidence of, dividends tax.

45 Section 8F(2)(*b*) was amended by section 8 of the Taxation Laws Amendment Act No. 43 of 2014 with effect from the date of promulgation of the Taxation Laws Amendment Act, 2014 namely 20 January 2015.

the Act to be a dividend *in specie* that is declared and paid to that person on the last day of the year of assessment of the company that incurred the interest.

The interest that accrues to a person and which is deemed to be a dividend *in specie* must be included in the person's "gross income" under paragraph (*k*) of the definition of "gross income" in section 1(1). The amount of the interest that is deemed to be a dividend *in specie* will not qualify for exemption [paragraph (*aa*) of the proviso to section 10(1)(*k*)(i)].

Section 8F(3)(*d*) provides that section 8F does not apply to an instrument that constitutes a linked unit in a company when the linked unit is *held* by a REIT, amongst other entities (but not a controlled company), if –

- the REIT holds at least 20% of the linked units in that company;
- the REIT acquired those linked units before 1 January 2013; and
- at the end of the previous year of assessment 80% or more of the value of the assets of the company incurring the interest expense, reflected in the annual financial statements prepared in accordance with the Companies Act for the previous year of assessment, is directly or indirectly attributable to immovable property.

Section 8F(3)(*d*) will be deleted with effect from 1 January 2017.[46] Section 8F will therefore apply to amounts of interest incurred on or after that date on linked units that constitute hybrid debt instruments that are *held* by a REIT, amongst other entities.[47]

Currently section 8F applies to hybrid debt instruments *issued* by a REIT and any hybrid debt instrument *issued or held* by a controlled company. In addition, as noted above, section 8F will also apply to any hybrid debt instrument *held* by a REIT with effect from 1 January 2017.

In summary, since the exclusion provided for in section 8F(3)(*d*) applies to hybrid debt instruments *held* by a REIT, any interest *paid* by a REIT or controlled company on a debenture forming part of a linked unit that constitutes a hybrid debt instrument under section 8F will be deemed to be a dividend *in specie* declared and paid by the REIT or controlled company and –

- although potentially subject to dividends tax, will qualify for an exemption under section 64FA read with section 64F(1)(*l*);
- will not be deductible under the Act but the REIT or controlled company may be entitled to a deduction for the deemed dividend as part of a "qualifying distribution" under section 25BB(2)(*a*); and
- will be included in the gross income of the debenture holder and will not be exempt from normal tax since it is excluded from the exemption in section 10(1)(*k*)(i) under paragraph (*aa*) of the proviso to section 10(1)(*k*)(i).

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46 Section 144 of the Taxation Laws Amendment Act No. 25 of 2015 extends the deadline of 1 January 2016 to 1 January 2017.

47 Section 8F(3)(*d*) is to be deleted with effect from 1 January 2017 by section 13(1)(*c*) of the Taxation Laws Amendment Act No. 31 of 2013, read with section 144 of the Taxation Laws Amendment Act No. 25 of 2015.

5.3 Hybrid interest deemed to be dividends *in specie* [section 8FA(3)(*d*)]

Under section 8FA(2)(*a*) an amount of interest *incurred* by a company that constitutes hybrid interest[48] is, on or after the date that the interest becomes hybrid interest –

- deemed for the purposes of the Act to be a dividend *in specie* declared and paid by that company on the last day of that year of assessment; and
- not deductible under the Act.

The amount of the interest that is deemed to be a dividend *in specie* declared and paid by the company incurring the interest expense is potentially subject to dividends tax under section 64E(1). The deemed dividend will, however, qualify for an exemption from dividends tax under section 64FA(1)(*a*) read with section 64F(1)(*l*) because the deemed dividend will constitute income for the debenture holder (see below).

Section 8FA(2)(*b*)[49] provides that an amount of hybrid interest that *accrues* to a person is deemed for the purposes of the Act to be a dividend *in specie* that is declared and paid to that person on the last day of that year of assessment of the company that incurred the interest.

See **5.2** for the dividends tax and normal tax implications of an amount of interest that is deemed to be a dividend *in specie*.

Section 8FA(3)(*d*) provides that section 8FA does not apply to interest owed on an instrument that constitutes a linked unit in a company that is *held by a REIT*, amongst other entities (but not including a controlled company), if certain requirements are met. These requirements are similar to those in section 8F(3)(*d*) (see **5.2**).

Section 8FA(3)(*d*) will be deleted with effect from 1 January 2017.[50] Section 8FA will therefore apply to amounts of hybrid interest incurred on or after that date on linked units held by a REIT, amongst other entities.[51]

In summary, since the exclusion provided for in section 8FA(3)(*d*) applies only to interest owed on an instrument that constitutes a linked unit in a company that is *held by a REIT*, any interest paid or derived on a debenture forming part of a linked unit *issued* by a REIT or controlled company that constitutes hybrid interest is deemed to be a dividend *in specie* declared and paid by the REIT or controlled company and –

- although potentially subject to dividends tax, will qualify for an exemption under section 64FA(1) read with section 64F(1)(*l*);
- will not be deductible under the Act, but the REIT or controlled company may be entitled to a deduction for the deemed dividend as part of a "qualifying distribution" under section 25BB(2)(*a*); and

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48 The term "hybrid interest" is defined in section 8FA(1).

49 Section 8FA(2)(*b*) was amended by section 9(1) of the Taxation Laws Amendment Act No. 43 of 2014 and applies to amounts of interest incurred on or after 1 April 2014.

50 Section 145 of the Taxation Laws Amendment Act No. 25 of 2015 extends the deadline from 1 January 2016 to 1 January 2017.

51 Section 8FA(3)(*d*) is to be deleted by section 15(1)(*c*) of the Taxation Laws Amendment Act No. 31 of 2013.

- will be included in the gross income of the debenture holder and will not be exempt from normal tax since it is excluded from the exemption in section 10(1)(*k*)(i) under paragraph (*aa*) of the proviso to section 10(1)(*k*)(*i*).

5.4 Receipt or accrual of dividends and foreign dividends [section 1(1) – paragraph (*k*) of the definition of "gross income" and paragraph (*aa*) of the proviso to section 10(1)(*k*)(i)]

5.4.1 Receipt or accrual of dividends from a REIT or a controlled company

Dividends received by or accrued to a person are included in that person's gross income under paragraph (*k*) of the definition of "gross income" in section 1(1).

Dividends received by or accrued to a resident that were distributed by a REIT or a controlled company that is a resident are not exempt from normal tax [paragraph (*aa*) of the proviso to section 10(1)(*k*)(i)]. Dividends distributed by a REIT or a controlled company that is a resident include amounts of interest (see **4.4.1**) paid on a debenture forming part of a linked unit that are deemed to be dividends received or accrued under section 25BB(6)(*a*). However, interest (see **4.4.1**) paid by a controlled company that is not a resident on a debenture forming part of a linked unit is deemed to be a foreign dividend and may be fully or partially exempt under section 10B. A dividend received by or accrued to a person from a REIT or a controlled company that is a resident that constitutes a share buy-back as contemplated in paragraph (*b*) of the definition of "dividend" in section 1(1) is, however, exempt from normal tax under section 10(1)(*k*)(i). A share buy-back by a REIT or a controlled company is excluded from a "qualifying distribution" as defined in section 25BB(1) made by a REIT or a controlled company and is, therefore, not deductible under section 25BB(2).

Dividends received by or accrued to a person that is not a resident that were distributed by a REIT or a controlled company that is a resident are exempt from normal tax under section 10(1)(*k*)(i).

See **5.10** for the dividends tax implications of dividends paid by a REIT or a controlled company.

5.4.2 Dividends and foreign dividends received by or accrued to a REIT or a controlled company

Dividends and foreign dividends received by or accrued to a REIT or a controlled company are included in the gross income of that REIT or controlled company under paragraph (*k*) of the definition of "gross income" in section 1(1). These dividends potentially qualify for the exemptions under section 10(1)(*k*)(i), while the foreign dividends potentially qualify for full or partial exemption under section 10B.

Dividends received by or accrued to a REIT or resident controlled company from another REIT or controlled company do not qualify for exemption under section 10(1)(*k*)(i) because of the exclusion provided for in paragraph (*aa*) of the proviso to section 10(1)(*k*)(i).

5.5 Tax implications for the holder of a share or a linked unit – Disposal of a share or a linked unit in a REIT or a controlled company and a return of capital

5.5.1 Disposal of a share or a linked unit in a REIT or a controlled company

The proceeds on disposal of a share or a linked unit in a REIT or a controlled company by the resident holder of the share or linked unit, will constitute gross income in that person's hands if the shares or linked units are held on revenue account. The proceeds on disposal of a share or a linked unit in these companies by a resident holder of such shares or linked units will be of a capital nature if the shares or linked units are held as capital assets. A capital gain or capital loss on disposal of these assets must be determined under paragraph 3 or 4 of the Eighth Schedule respectively (see **4.11** for the CGT implications if the holder of the share or linked unit is a REIT).

Non-resident holders of such shares or linked units that hold them on revenue account will be liable to tax in South Africa only if the proceeds are from a South African source (for example, if the relevant assets are traded through a permanent establishment in South Africa). Non-resident holders of such shares or linked units that hold them on capital account will be liable to CGT only if the shares are deemed to be an interest in immovable property under paragraph 2(2) of the Eighth Schedule (for example, if the holder holds, directly or indirectly, at least 20% of the equity shares in the company and 80% or more of the market value of those shares is directly or indirectly attributable to immovable property in South Africa), or if the shares or linked units form part of the holder's permanent establishment in South Africa.

5.5.2 Return of capital and foreign return of capital

A return of contributed tax capital to the holder of a share or linked unit in a REIT or a controlled company that is a resident constitutes a return of capital which must be accounted for under paragraph 76B of the Eighth Schedule.[52] A foreign return of capital by a controlled company that is not a resident must similarly be dealt with under paragraph 76B. See Chapter 18 of the *Comprehensive Guide to Capital Gains Tax* (Issue 5) for a discussion of paragraph 76B.

5.6 Limitation of interest deductions on reorganisation and acquisition transactions [section 23N(5)(*a*)]

Section 23N(2)[53] stipulates that the deduction for an amount of interest incurred by an acquiring company[54] on a debt is limited in specified circumstances to an amount determined under section 23N(3). Depending on the facts a REIT or controlled company may be an acquiring company.

Section 23N(5)(*a*) provides that section 23N does not apply to interest incurred before 31 December 2015 by an acquiring company on a debt contemplated in section 23N(2) when the interest is incurred on a linked unit in the acquiring company and that interest accrues to a REIT, amongst other entities, and –

- the REIT holds at least 20% of the linked units in that acquiring company;

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[52] The terms "contributed tax capital" and "return of capital" are defined in section 1(1).

[53] Section 23N was inserted by section 63(1) of the Taxation Laws Amendment Act No. 31 of 2013 and comes into operation on 1 April 2014.

[54] The term "acquiring company" is defined in section 23N(1).

- the REIT acquired those linked units before 1 January 2013; and
- at the end of the previous year of assessment 80% or more of the value of the assets of that acquiring company, reflected in the annual financial statements prepared in accordance with the Companies Act for the previous year of assessment, is directly or indirectly attributable to immovable property.

5.7 Substitutive share-for-share transactions [section 43]

Under section 43(2) roll-over treatment will apply when a person disposes of an equity share in the form of a linked unit in, amongst other companies, a REIT, a controlled company or a property company, and acquires an equity share other than a linked unit in that same company. This transaction is a "substitutive share-for-share transaction" as defined in section 43(1). Before the transaction a person held a share and a debenture in the company, but after the transaction a person holds only a share in the company.

A person that disposes of a share under a substitutive share-for-share transaction is deemed to have –

- disposed of the equity share for an amount equal to the expenditure allowable in respect of that share under paragraph 20 of the Eighth Schedule or taken into account under section 11(*a*), 22(1) or (2) [section 43(2)(*a*)];
- acquired the other equity share for the same expenditure referred to above on the latest date on which any of the equity shares disposed of were acquired [section 43(2)(*b*)]; and
- incurred the cost referred to in section 43(2)(*b*) on the same date on which the latest of the previous shares was acquired [section 43(2)(*c*)].

The cost attributable to the new equity shares acquired as –

- capital assets, is treated for purposes of paragraph 20 of the Eighth Schedule as expenditure actually incurred in respect of those equity shares; or
- trading stock, is treated for purposes of section 11(*a*) or 22(1) or (2) as the amount to be taken into account in respect of those equity shares.

Section 43(1A) provides that when a person disposes of an equity share in a company that comprises a pre-valuation date asset and acquires another equity share in that company under a substitutive share-for-share transaction, that person must, for the purposes of determining the date of acquisition of that equity share and the expenditure in respect of the cost of acquisition of that equity share, be treated as having –

- disposed of that equity share at a time immediately before the substitutive share-for-share transaction, for an amount equal to the market value of that equity share at that time; and
- immediately reacquired that equity share at that time at an expenditure equal to that market value.

The market value reacquisition cost must be reduced by any capital gain and increased by any capital loss arising from the deemed disposal. The resulting expenditure is treated as having been incurred for the purposes of paragraph 20(1)(*a*) of the Eighth Schedule. A pre-valuation date share is, therefore, converted to a post-valuation date share in order that section 43(2) can be applied.

Section 43(4) provides that when a person disposes of an equity share in a company under a substitutive share-for-share transaction and that person becomes entitled, in exchange for that equity share, to any consideration other than a dividend, foreign dividend or another equity share in that company, the roll-over treatment afforded under section 43(2) will not apply to the extent of the other consideration received.

The portion of the expenditure relating to the equity shares disposed of that must be attributed to the other consideration received is determined by multiplying the expenditure relating to those shares by the amount of the other consideration received divided by the sum of the market value of the equity shares acquired and the market value of the other consideration.

Section 43(4A) provides that when an equity share is issued under a substitutive share-for-share transaction, the issue price of the linked unit disposed of under that transaction is deemed to be contributed tax capital in respect of the class to which the equity share so acquired relates. Contributed tax capital of a company is increased by the consideration received by or accrued to that company for the issue of its shares on or after 1 January 2011 and is determined per class of shares.[55]

Example 5 – Substitutive share-for-share transaction

Facts:

Individual A acquired 2 000 linked units in REIT B on 1 March 2011 for R20 000 (R2 000 for the share and R18 000 for the debenture components of the linked units) and a further 1 000 linked units on 1 April 2011 for R10 100 (R1 000 for the share and R9 100 for the debenture components of the linked units). The linked units were held as capital assets.

On 1 August 2014 REIT B issued 3 000 equity shares with a market value of R50 000 to Individual A in exchange for the surrender of the 3 000 linked units held by Individual A.

Result:

The exchange of the linked units held by Individual A for equity shares qualifies as a "substitutive share-for-share transaction" as defined in section 43(1). Under section 43(2)(*a*) Individual A is deemed to have disposed of the linked units in REIT B for R30 100, being the base cost of the shares under paragraph 20 of the Eighth Schedule. The capital gain on disposal of the shares is nil (proceeds of R30 100 – base cost of R30 100).

Under section 43(2)(*b*) Individual A is deemed to have acquired the new equity shares in REIT B for R30 100 on 1 April 2011, being the latest date that the linked units were acquired by Individual A. Under section 43(2)(*c*) this cost of acquisition is treated for purposes of paragraph 20 of the Eighth Schedule as being the base cost for Individual A of the new equity shares acquired.

The contributed tax capital for REIT B of the newly issued shares is R30 100 under section 43(4A), being the price of the linked units previously issued by REIT B.

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[55] The term "contributed tax capital" is defined in section 1(1).

5.8 Amalgamation transactions [section 41(4)(*a*)(iii) and the proviso to section 44(4A)]

Both a company incorporated under the Companies Act and a portfolio of a collective investment scheme in property may qualify as a REIT (see **4.1.1**). A portfolio of a collective investment scheme in property that qualifies as a REIT is a "company" as defined[56] and may therefore use the roll-over relief provided under section 44 (amalgamation transactions). In essence an amalgamation transaction is any transaction under which a resident *company* (amalgamated company) disposes of all its assets (except those required to meet any debt obligations) to another resident company (resultant company), and as a result the existence of the amalgamated company is terminated.

The following provisions of sections 1(1), 41(1) and 44, deal specifically with a portfolio of a collective investment scheme in property:

- The definition of "equity share" in section 1(1) means any share in a company, excluding any share that, neither as respects dividends nor as respects returns of capital, carries any right to participate beyond a specified amount in a distribution. A "share" as defined in section 1(1) means, in relation to a company, any unit into which the proprietary interest in that company is divided. It is, therefore, clear that the definition of "equity share" in section 1(1) includes a participatory interest in a portfolio of a collective investment scheme in property which qualifies as a REIT.
- Under section 41(4)(*a*)(iii)[57] a company must for purposes of sections 41 to 47 be deemed to have taken steps to liquidate, wind up or deregister when in the case of a liquidation or winding-up the manager, trustee or custodian of the portfolio of a collective investment scheme in property has under section 102(1) or (2) of the Collective Investment Schemes Control Act applied for the winding-up of that portfolio. Such a portfolio would need to qualify as a REIT in order to constitute a company.
- The proviso to section 44(4A)[58] stipulates that when the amalgamated company is a portfolio of a collective investment scheme in property, the price at which the participatory interests in that collective investment scheme was issued must be added to the contributed tax capital[59] of the class of shares issued by the resultant company.

5.9 Unbundling transactions [section 46(2), (5) and (6A)]

Section 46(2) provides that an unbundling company must disregard the distribution of shares under an "unbundling transaction"[60] for purposes of calculating its taxable income or assessed loss, or its net income for purposes of section 9D.

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[56] Paragraph (*e*)(iii) of the definition in section 1(1).

[57] Section 41(4)(*a*)(iii) was inserted by section 90(1)(*j*) of the Taxation Laws Amendment Act No. 31 of 2013 with effect from 24 October 2013.

[58] The proviso to section 44(4A) was added by section 93(1)(*c*) of the Taxation Laws Amendment Act No. 31 of 2013 with effect from 24 October 2013.

[59] The term "contributed tax capital" is defined in section 1(1).

[60] The term "unbundling transaction" is defined in section 46(1).

Section 46 does not apply to an unbundling transaction on or after 20 January 2015 when the unbundling company is a REIT or a controlled company.[61] It follows that a REIT or a controlled company that distributes shares can no longer avail itself of the roll-over relief in section 46.

Before 20 January 2015[62] section 46 had the effect that a REIT or a controlled company that distributed shares under an "unbundling transaction" to its shareholders was not entitled to deduct this distribution from its income, even though it may have constituted a "qualifying distribution" as defined in section 25BB(1).

The distribution of shares as a dividend *in specie* by a REIT or a controlled company under an "unbundling transaction" before 20 January 2015 was included in the "gross income" of the holders of the shares under paragraph (*k*) of the definition of "gross income" in section 1(1). These dividends were not exempt from normal tax under section 10(1)(*k*)(*i*) if they were received by or accrued to holders of shares that are residents [paragraph (*aa*) of the proviso to section 10(1)(*k*)(i)].

The combined effect of section 46(2) and paragraph (*aa*) of the proviso to section 10(1)(*k*)(i) was that shares distributed by a REIT or a controlled company to resident holders of shares under an "unbundling transaction" were taxed twice for normal tax purposes, namely in the hands of –

- the REIT or controlled company because the distribution is disregarded in determining the taxable income or assessed loss of the REIT or controlled company; and
- the holders of the shares because the distribution did not qualify for the dividend exemption.

Section 46(5) stipulates that shares distributed by an unbundling company under an "unbundling transaction" must be disregarded for dividends tax purposes. It follows that shares distributed by a REIT or a controlled company under an "unbundling transaction" before 20 January 2015 must be disregarded for dividends tax purposes.

5.10 Dividends Tax and exemption from dividends tax [section 64F(1)(*a*), (*l*) and (2) and section 64FA(1)(*a*)]

Generally, dividends tax is levied under section 64E –

- on a dividend paid by a company that is a resident, other than a headquarter company; or
- on a foreign dividend paid by a company that is not a resident, if the share in respect of which that foreign dividend is paid is listed on the JSE and to the extent that that foreign dividend does not consist of a distribution of an asset *in specie*.

A dividend or interest deemed to be a dividend under section 25BB(6) (see **4.8**) paid by a REIT or, in certain circumstances, a controlled company, is therefore liable to

[61] Section 46(6A) was inserted by section 58 of the Taxation Laws Amendment Act No. 43 of 2014 and is effective from the date of promulgation of that Act, being 20 January 2015.

[62] With effect from 20 January 2015 section 46 is inapplicable when the unbundling company is a REIT or controlled company (section 58 of the Taxation Laws Amendment Act No. 43 of 2014).

dividends tax. The dividend may be exempt from dividends tax if it qualifies for an exemption from dividends tax. Some of the exemptions are discussed below.

See the *Comprehensive Guide to Dividends Tax* dated 23 February 2015 for a comprehensive discussion of dividends tax, including other exemptions which could apply to particular circumstances not discussed in this Note.

5.10.1 Dividends paid by a REIT or a controlled company [section 64F(1)(*l*) and (2)]

It is possible that a number of different exemptions may apply to a particular dividend, for example, depending on the facts it is possible that the exemption in section 64F(1)(*a*), section 64F(1)(*l*) and section 64F(2), discussed below, could apply to the same dividend. In this situation it is clear that an amount can be exempt only once.

A dividend or deemed dividend paid by a REIT or controlled company is exempt from dividends tax under section 64F(1)(*a*) if the beneficial owner of the dividend is a company that is a resident.

A dividend is exempt from dividends tax under section 64F(1)(*l*) to the extent that it does not consist of a dividend *in specie* and it constitutes "income" of the beneficial owner. Therefore, a dividend, excluding a dividend that constitutes a share buy-back and excluding a dividend to the extent the dividend is a dividend *in specie,* paid by a REIT or controlled company to a beneficial owner which is a resident is exempt from dividends tax under section 64F(1)(*l*) because it is included in the income of a recipient under paragraph (*k*) of the definition of "gross income" in section 1(1) and is not exempt under paragraph (*aa*) of the proviso to section 10(1)(*k*)(i) (see **5.4.1**). A dividend that constitutes a share buy-back does not qualify for the exemption under section 64F(1)(*l*) because it does not constitute income and it is therefore subject to dividends tax. It is exempt from normal tax (see **5.4.1**).

Dividends paid by a REIT or a controlled company which are received by or accrue to a non-resident beneficial owner constitute exempt income and are not subject to normal tax (see **5.4.1**). These dividends are subject to dividends tax because they do not qualify for the exemption under section 64F(1)(*l*) as they do not constitute "income".

In addition, a dividend paid by a REIT or a controlled company that was received by or accrued to a beneficial owner that is a resident or a non-resident before 1 January 2014 was exempt from dividends tax under section 64F(2), but only to the extent that the dividend did not consist of the distribution of an asset *in specie*. [63]

5.10.2 Dividends paid to a beneficial owner that is a REIT or a controlled company [sections 64F(1)(*a*) and (*l*) and 64FA(1)(*a*)]

A REIT and a controlled company qualify as a "company" as defined in section 1(1) and any dividend received by or accrued to a REIT or a resident controlled company will be exempt from dividends tax under sections 64F(1)(*a*) or 64FA(1)(*a*) if the REIT or a controlled company is the beneficial owner of the dividend.

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[63] Section 64F(1)(*l*) applied to dividends received or accrued on or after 1 April 2013. To the extent both section 64F(1)(*l*) and section 64F(2) applied, an amount can be exempt only once.

5.11 Exemption from securities transfer tax [section 8(1)(*t*) of the Securities Transfer Tax Act No. 25 of 2007]

Section 2(1) of the Securities Transfer Tax Act stipulates that securities transfer tax is levied at the rate of 0,25% of the taxable amount of a security on –

- every transfer of a security issued by –
  - a close corporation or company incorporated, established or formed inside the Republic; or
  - a company incorporated, established or formed outside the Republic and listed on the JSE; and
- any reallocation of securities from a member's bank restricted stock account or a member's unrestricted and security restricted stock account to a member's general restricted stock account.

Section 8(1)(*t*) of the Securities Transfer Tax Act provides that securities transfer tax is not payable on the transfer of a security that constitutes a share in a "REIT" as defined in section 1(1). Controlled companies are not included in this exemption and the transfer of a share in a controlled company may therefore be subject to securities transfer tax.

5.12 Exemption from transfer duty [sections 1(1) and 9(1)(*l*) of the Transfer Duty Act No. 40 of 1949]

Section 2(1) of the Transfer Duty Act stipulates that transfer duty is levied on the value of property acquired by a person, at a rate determined on a sliding scale, based on the value of the property acquired.

The term "property" is defined in section 1(1) of the Transfer Duty Act as land and any fixtures thereon, and includes in paragraph (*d*) of that definition a share (other than a share in a share block company) or member's interest in a *residential property company*.

The term "residential property company"[64] is defined in section 1(1) of the Transfer Duty Act and specifically excludes a REIT as defined in section 1(1). The acquisition of a share in a REIT is, therefore, not subject to transfer duty. A controlled company, which is not a REIT, is not excluded from the definition of "residential property company" and the transfer of a share in a controlled company may therefore be subject to transfer duty.

The acquisition of property by a company (including a REIT and a controlled company) under any of the following transactions is exempt from transfer duty under section 9(1)(*l*) of the Transfer Duty Act:

- An asset for-share transaction as defined in section 42.
- A substitutive share-for-share transaction as defined in section 43.
- An amalgamation transaction as defined in section 44.
- An intra-group transaction as defined in section 45.

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64 The definition of "residential property company" was amended by section 1 of the Taxation Laws Amendment Act No. 31 of 2013 with effect from 12 December 2013.

- A liquidation distribution as defined in section 47.
- A transaction which would have constituted a transaction or distribution in the bullets above regardless of whether that person acquired that property as a capital asset or as trading stock.

5.13 VAT treatment of REITs and controlled companies [sections 2, 7(1)(*a*) and 12(*a*) of the VAT Act]

Every supply of goods or services by a vendor in the course or furtherance of that vendor's enterprise is subject to VAT at the standard rate under section 7(1)(*a*) of the VAT Act, unless the supply is exempt or zero rated or falls outside the scope of the VAT Act.

Under section 12(*a*) of the VAT Act, the supply of "financial services" is exempt from VAT. The term "financial services" is defined in section 1(1) of the VAT Act as being the activities which are deemed by section 2 to be financial services.

It is assumed for purposes of the analysis that follows that the REIT, controlled company and linked unit holder are vendors for VAT purposes.

The issue and disposal of shares

Under section 2(1)(*d*) of the VAT Act, the issue, allotment or transfer of ownership of an "equity security" or a "participatory security" is deemed to be financial services and therefore exempt from VAT under section 12(*a*) of the VAT Act. In essence an "equity security"[65] would include a share in a REIT that is a juristic person or a controlled company, while a "participatory security"[66] would include a participatory interest in a portfolio of a collective scheme in property that qualifies as a REIT.

The issue or allotment of a share or participatory security in a REIT or a controlled company is therefore exempt from VAT under section 12(*a*) of the VAT Act. The subsequent disposal of such a share or participatory security by its holder similarly constitutes the supply of an exempt financial service.

The issue and disposal of linked units

A linked unit issued by a REIT that is a company contains both a share element (an "equity security") and a debenture element.

The issue, allotment or transfer of ownership of a "debt security" as defined for VAT purposes[67] is exempt from VAT under section 12(*a*) read with section 2(1)(*c*) of the VAT Act. A "debt security" is essentially defined[68] as a right or obligation to be paid, or to pay, money that is or is to be owing by any person. Thus, the issue of a

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[65] The term "equity security" is defined in section 2(2)(iv) of the VAT Act as "any interest in or right to a share in the capital of a juristic person or the interest in a close corporation of a member thereof".

[66] A "participatory security" is defined in section 2(2) of the VAT Act as "a participatory interest as defined in section 1 of the Collective Investment Schemes Control Act, 2002 (Act No. 45 of 2002), but does not include an equity security, a debt security, money or a cheque".

[67] The term "debt security" is defined in section 2(2)(iii)(*bb*) of the VAT Act as" as an interest in or right to be paid money; or…an obligation or liability to pay money that is, or is to be, owing by any person...".

[68] Section 2(2) of the VAT Act.

debenture by a REIT that is a company or a controlled company is deemed to be a financial service and is therefore exempt from VAT.

With regard to the "share element", as mentioned above, the issue or allotment of a share is exempt from VAT under section 12(*a*) read with section 2(1)(*d*) of the VAT Act.

The disposal of a linked unit by a REIT that is a company or a controlled company, which acquired the linked unit in another REIT or controlled company, similarly constitutes the supply of exempt financial services under section 12(*a*) read with section 2(1)(*c*) and (*d*) of the VAT Act.

Distributions

A dividend declared in respect of the share element by the REIT that is a company or controlled company is not consideration for a supply of goods or services and accordingly falls outside the scope of the VAT Act. The fact that the recipient of the dividend declared by the REIT or controlled company may be regarded as having derived "rental income" for purposes of section 25BB,[69] does not alter the fact that for VAT purposes the dividend receipt does not constitute taxable rental income in the hands of the recipient.

While any amount received by a REIT or a controlled company on disposal of a financial instrument must be included either in the gross income or taxable income of the REIT or controlled company, such amount may constitute consideration for the supply of an exempt financial service and, if so, will be exempt from VAT under section 12(*a*) read with section 2 of the VAT Act, or, as in the case of the receipt of dividends, fall outside the scope of the VAT Act.

Interest

The provision of credit (the linked loan provided by the holder of the linked unit) constitutes an exempt financial service under section 2(1)(*f*) of the VAT Act. Any consideration (interest) derived under a credit arrangement is accordingly exempt from VAT under section 12(*a*) read with section 2(1)(*f*) of the VAT Act. It follows that any interest received in respect of the "debenture element" constitutes consideration for the exempt supply of credit and no output tax need be accounted for on any interest received by the holder of the linked unit.

While interest payable by a REIT or a controlled company on a debenture that forms part of a linked unit constitutes a "qualifying distribution," and therefore "rental income" for purposes of section 25BB, the interest remains exempt interest for VAT purposes.

Rental income

The supply of commercial property by a REIT or a controlled company in the course or furtherance of its enterprise constitutes a taxable supply under section 7(1)(*a*) of the VAT Act. Rental income received in respect of such a supply is subject to VAT at the standard rate.

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[69] Section 25BB(1).

However, the supply by a REIT respectively of a dwelling under an agreement for its letting and hiring, and any "right of occupation" as defined in section 1 of the Housing Development Schemes for Retired Persons Act No. 65 of 1988, are exempt under section 12(*c*) of the VAT Act.

The fact that certain income of a REIT is defined as "rental income" in section 25BB for income tax purposes does not result in such income constituting rental income for VAT purposes. Thus, for example, while a dividend derived from a REIT falls within the ambit of the definition of "rental income" in section 25BB(1), it will constitute an out of scope receipt for VAT purposes.

Sale of fixed property

The supply of "fixed property"[70] by a REIT or a controlled company under an agreement of sale in the course or furtherance of its enterprise is subject to VAT at the standard rate under section 7(1)(*a*) of the VAT Act.

However, the sale of property used by a REIT *wholly* in the course and furtherance of making exempt supplies is not subject to VAT. The supply of fixed property that was used by the REIT or controlled company partly for the purpose of making taxable supplies and partly for some other (for example, exempt) purpose is deemed to have been made *wholly* in the course or furtherance of the REIT or controlled company's enterprise, that is, a taxable supply.[71] Thus, for example, if a REIT or a controlled company supplies fixed property that was used for both commercial (taxable) and residential (exempt) purposes, the REIT or controlled company will be required to account for output tax on the full consideration received for the supply, even though that part of the fixed property was used for an exempt purpose. The REIT or controlled company may, however, be entitled to VAT relief in terms of section 16(3)(*h*) of the VAT Act.

The supply of fixed property as a going concern may be subject to VAT at the zero rate if all the requirements of section 11(1)(*e*) of the VAT Act are met.

General

The supply of any other goods or services by a REIT or a controlled company in the course or furtherance of its enterprise is subject to VAT at the standard rate under section 7(1)(*a*) unless an exemption or zero-rating applies.

6. Conclusion

Section 25BB introduced a uniform set of rules for the taxation of REITs and their controlled companies as well as the holders of shares or linked units in such REITs and controlled companies with effect from years of assessment commencing on or after 1 April 2013. In order to qualify as a REIT, a company or portfolio of a collective investment scheme in property must be a resident, be listed on the JSE as a REIT and meet the JSE's listings requirements. A REIT in reality can be a trust if it takes the form of a portfolio, but for income tax purposes it is deemed to be a company.

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70 The term "fixed property" is essentially defined in section 1(1) of the VAT Act as land and any improvements to such land. Included in the definition is any sectional title unit, share in a share block company and a time-sharing interest.

71 Section 8(16) of the VAT Act.

The effect of section 25BB is to treat a REIT or a controlled company as a flow-through entity for income tax purposes. This treatment is achieved by allowing the REIT or a resident controlled company a deduction for a "qualifying distribution." The deductible amount of the qualifying distribution is limited to the taxable income of the REIT or controlled company before taking into account –

- the qualifying distribution;
- any assessed loss brought forward from the previous year of assessment; and
- any taxable capital gain.

A distribution by a REIT or a controlled company that was in existence at the end of the preceding year of assessment will constitute a deductible qualifying distribution only if at least 75% of any gross income derived by the REIT or controlled company for the preceding year of assessment consists of "rental income". A similar rule applies during the first year of assessment in which a company qualifies as a REIT or controlled company, but in such event the gross income derived by the REIT or controlled company for that year of assessment is used. Rental income includes dividends from another REIT, dividends or foreign dividends from a property company, a qualifying distribution from a controlled company and income from the use of immovable property.

The REIT and controlled company must disregard any capital gain or capital loss on disposal of shares or linked units in another REIT or a property company as well as any capital gain or capital loss on disposal of immovable property. However, a REIT or a controlled company must account for other capital gains and losses while proceeds of a revenue nature on the disposal of assets are included in gross income.

Interest received by or accrued to a person during a year of assessment on a debenture forming part of a linked unit in a REIT or a controlled company that is a resident is deemed to be a dividend. Such dividends are fully taxable for normal tax purposes in the hands of resident holders of shares but are exempt from dividends tax. Non-residents are exempt from normal tax on such dividends but are instead subject to dividends tax.

Interest received by or accrued to a person during a year of assessment on a debenture forming part of a linked unit in a non-resident controlled company is deemed to be a foreign dividend.

The other provisions of the Act and other legislation dealing with REITs, controlled companies and the holders of shares or linked units, as discussed in this Note, should also be considered.

Legal and Policy Division
SOUTH AFRICAN REVENUE SERVICE

Annexure A – The law

Section 8F(3)(*d*)[72]

(3) This section does not apply to any instrument—

(*d*) that constitutes a linked unit in a company where the linked unit is held by a long-term insurer as defined in the Long-term Insurance Act, a pension fund, a provident fund, a REIT or a short-term insurer as defined in the Short-term Insurance Act, if—

(i) the long-term insurer, pension fund, provident fund, REIT or short-term insurer holds at least 20 per cent of the linked units in that company;

(ii) the long-term insurer, pension fund, provident fund, REIT or short-term insurer acquired those linked units before 1 January 2013; and

(iii) at the end of the previous year of assessment 80 per cent or more of the value of the assets of that company, reflected in the annual financial statements prepared in accordance with the Companies Act for the previous year of assessment, is directly or indirectly attributable to immovable property.

Section 8FA(3)(*d*)[73]

(3) This section does not apply to any interest owed in respect of—

(*d*) an instrument that constitutes a linked unit in a company where the linked unit is held by a long-term insurer as defined in the Long-term Insurance Act, a pension fund, a provident fund, a REIT or a short-term insurer as defined in the Short-term Insurance Act, if—

(i) the long-term insurer, pension fund, provident fund, REIT or short-term insurer holds at least 20 per cent of the linked units in that company;

(ii) the long-term insurer, pension fund, provident fund, REIT or short-term insurer acquired those linked units before 1 January 2013; and

(iii) at the end of the previous year of assessment 80 per cent or more of the value of the assets of that company, reflected in the annual financial statements prepared in accordance with the Companies Act for the previous year of assessment, is directly or indirectly attributable to immovable property.

Paragraph (*aa*) of the proviso to section 10(1)(*k*)(i)

10. Exemptions.—(1) There shall be exempt from normal tax—

(*k*) (i) dividends (other than dividends paid or declared by a headquarter company) received by or accrued to any person: Provided that this exemption shall not apply

(*aa*) to dividends (other than those received by or accrued to or in favour of a person that is not a resident or a dividend contemplated in paragraph (*b*) of the definition of "dividend") distributed by a company that is a REIT, or a controlled company as defined in section 25BB;

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[72] Section 8F(3)(*d*) will be deleted with effect from 1 January 2017 and will not apply to amounts of interest incurred on or after that date.

[73] Section 8FA(3)(*d*) will be deleted with effect from 1 January 2017 and will not apply to amounts of interest incurred on or after that date.

Section 23N(5)(*a*)

(5) This section does not apply to any interest incurred by an acquiring company in respect of any debt contemplated in subsection (2)—

(*a*) where that interest is incurred in respect of a linked unit in the acquiring company and that interest accrues to a long-term insurer as defined in the Long-term Insurance Act, a pension fund, a provident fund, a REIT or a short-term insurer as defined in the Short-term Insurance Act, if—

(i) the long-term insurer, pension fund, provident fund, REIT or short-term insurer holds at least 20 per cent of the linked units in that acquiring company;

(ii) the long-term insurer, pension fund, provident fund, REIT or short-term insurer acquired those linked units before 1 January 2013; and

(iii) at the end of the previous year of assessment 80 per cent or more of the value of the assets of that acquiring company, reflected in the annual financial statements prepared in accordance with the Companies Act for the previous year of assessment, is directly or indirectly attributable to immovable property; or

Section 25BB

25BB. Taxation of REITs.—(1) For the purposes of this section—

"controlled company" means a company that is a subsidiary, as defined in IFRS, of a REIT;

"property company" means a company—

(*a*) in which 20 per cent or more of the equity shares or linked units are held by a REIT or a controlled company (whether alone or together with any other company forming part of the same group of companies as that REIT or that controlled company); and

(*b*) of which at the end of the previous year of assessment 80 per cent or more of the value of the assets, reflected in the annual financial statements prepared in accordance with the Companies Act or IFRS for the previous year of assessment, is directly or indirectly attributable to immovable property;

"qualifying distribution", in respect of a year of assessment of a company that is a REIT or a controlled company as at the end of a year of assessment, means any dividend (other than a dividend contemplated in paragraph (*b*) of the definition of "dividend") paid or payable, or interest incurred in respect of a debenture forming part of a linked unit in that company if the amount thereof is determined with reference to the financial results of that company as reflected in the financial statements prepared for that year of assessment if—

(*a*) at least 75 per cent of the gross income received by or accrued to a company during the first year of assessment that the company qualifies as a REIT or controlled company, consists of rental income; or

(*b*) in any other case, at least 75 per cent of the gross income received by or accrued to a REIT or a controlled company in the preceding year of assessment consists of rental income:

Provided that any amount that must be included in the income of the REIT or controlled company in terms of section 9D(2) must not be included in the gross income of the REIT or controlled company in respect of that year of assessment for the purposes of this definition;

"rental income" means any amount received or accrued—

(*a*) in respect of the use of immovable property, including a penalty or interest in respect of late payment of any such amount;

(*b*) as a dividend (other than a dividend contemplated in paragraph (*b*) of the definition of "dividend") from a company that is a REIT at the time of the distribution of that dividend;

(*c*) as a qualifying distribution from a company that is a controlled company at the time of that distribution; or

(*d*) as a dividend or foreign dividend from a company that is a property company at the time of that distribution.

(2)(*a*) There must be deducted from the income for a year of assessment of—

(i) a REIT; or

(ii) a controlled company that is a resident,

the amount of any qualifying distribution made by that REIT or that controlled company in respect of that year of assessment if that company is a REIT or a controlled company on the last day of that year of assessment.

(*b*) The aggregate amount of the deductions contemplated in paragraph (*a*) may not exceed the taxable income for that year of assessment of that REIT or that controlled company, before taking into account—

(i) any deduction in terms of this subsection;

(ii) any assessed loss brought forward in terms of section 20; and

(iii) the amount of taxable capital gain included in taxable income in terms of section 26A.

(2A) For the purposes of calculating the taxable income in respect of a year of assessment of a REIT or a controlled company as contemplated in subsection (2)(*b*)—

(*a*) where—

(i) a REIT or a controlled company is a beneficiary of a vesting trust that is not a resident; and

(ii) the trust contemplated in subparagraph (i) is liable for or subject to tax on income in the country in which that trust is established or formed,

so much of any amount of tax proved to be payable by that trust to the government of a country other than the Republic as is attributable to the interest of that REIT or controlled company in that trust, without any right of recovery of that tax by any person, must be allowed to be deducted by that REIT or controlled company before taking into account any deduction in terms of subsection (2)(*a*);

(*b*) there must be allowed as a deduction from the income of that REIT or that controlled company the sum of any taxes on income proved to be payable by that REIT or that controlled company to any sphere of government of any country other than the Republic, without any right of recovery by any person other than a right of recovery in terms of any entitlement to carry back losses arising during any year of assessment to any year of assessment prior to such year of assessment before taking into account any deduction in terms of subsection (2)(a); and

(*c*) where during any year of assessment a REIT or controlled company has made a bona fide donation to any organisation as contemplated in section 18A(1)(*a*) or (*b*) there must be allowed to be deducted an amount equal to the amount of that donation: Provided that the deduction so allowed may not exceed 10 per cent of the taxable income of that REIT or controlled company after taking into account any deduction in terms of paragraph (*a*) and (*b*) but before taking into account any deduction in terms of subsection (2)(*a*).

(3) …………….

(4) A company that is a REIT or a controlled company on the last day of a year of assessment may not deduct by way of an allowance any amount in respect of immovable property in terms of section 11(*g*), 13, 13*bis*, 13*ter*, 13*quat*, 13*quin* or 13*sex*.

(5) In determining the aggregate capital gain or aggregate capital loss of a company that is a REIT or a controlled company on the last day of a year of assessment for purposes of the Eighth Schedule, any capital gain or capital loss determined in respect of the disposal of—

(*a*) immovable property of a company that is a REIT or controlled company at the time of the disposal;

(*b*) a share or a linked unit in a company that is a REIT at the time of that disposal; or

(*c*) a share or a linked unit in a company that is a property company at the time of that disposal,

must be disregarded.

(6)(*a*) Any amount of interest received by or accrued to a person during a year of assessment in respect of a debenture forming part of a linked unit held by that person in a company that is a REIT or a controlled company must if that company or controlled company is a resident be deemed to be a dividend received by or accrued to that person or if that company or controlled company is a foreign company be deemed to be a foreign dividend received or accrued to that person, during that year of assessment.

(*b*) Any amount of interest received by or accrued to a company that is a REIT or a controlled company that is a resident during a year of assessment in respect of a debenture forming part of a linked unit held by that company in a property company must if the property company is a resident be deemed to be a dividend, or if the property company is a foreign company be deemed to be a foreign dividend, received by or accrued to that company during that year of assessment if that company is a REIT or a controlled company that is a resident at the time of that receipt or accrual.

(*c*) Any amount of interest paid in respect of a linked unit in a REIT or a controlled company must be deemed—

(i) to be a dividend paid by that REIT or that controlled company for the purposes of the dividends tax contemplated in Part VIII of this Chapter; and

(ii) not to be an amount of interest paid by that REIT or that controlled company for the purposes of the withholding tax on interest contemplated in Part IVB of this Chapter.

(7) If during any year of assessment a company that is a REIT ceases to be a REIT and that company does not qualify as a controlled company or a company that is a controlled company ceases to be a controlled company and that company does not qualify as a REIT—

(*a*) that year of assessment of that REIT or controlled company is deemed to end on the day that the company ceases to be either a REIT or a controlled company; and

(*b*) the following year of assessment of that company is deemed to commence on the day immediately after that company ceased to be either a REIT or a controlled company.

(8) If a REIT or a controlled company cancels the debenture part of a linked unit and capitalises the issue price of the debenture to stated capital for the purposes of financial reporting in accordance with IFRS—

(*a*) the cancellation of the debenture must be disregarded in determining the taxable income of the holder of the debenture and of the REIT or controlled company;

(*b*) expenditure incurred by the holder of a share in the REIT or controlled company in respect of the shares is deemed to be equal to the amount of the expenditure incurred in respect of the acquisition of that linked unit; and

(*c*) the issue price of the cancelled debenture must be added to the contributed tax capital of the class of shares that forms part of the linked unit.

Section 41(4)(*a*)(iii)

(4) A company must for the purposes of this Part, be deemed to have taken steps to liquidate, wind up or deregister, where—

(*a*) in the case of a liquidation or winding-up—

(iii) the manager, trustee or custodian of the portfolio of the collective investment scheme in property has in terms of section 102(1) or (2) of the Collective Investment Schemes Control Act applied for the winding up of that portfolio;

Section 43

43. Substitutive share-for-share transactions.—(1) For the purposes of this section—

"equity share" includes a linked unit;

"equity share interest" . . . . . .

"non-equity share" . . . . . .

"non-equity share interest" . . . . . .

"property linked unit" . . . . . .

"share interest" . . . . . .

"substitutive share-for-share transaction" means a transaction between a person and a company in terms of which that person disposes of an equity share in the form of a linked unit in that company and acquires an equity share other than a linked unit in that company.

(1A) Where a person disposes of an equity share in a company that constitutes a pre-valuation date asset and acquires another equity share in that company in terms of a substitutive share-for-share transaction, for the purposes of determining the date of acquisition of that equity share and the expenditure in respect of the cost of acquisition of that equity share, that person must be treated as having—

(*a*) disposed of that equity share at the time immediately before that substitutive share-for-share transaction, for an amount equal to the market value of that equity share at that time; and

(*b*) immediately reacquired that equity share at that time at an expenditure equal to that market value—

(i) less any capital gain, and

(ii) increased by any capital loss,

that would have been determined had that equity share been disposed of at market value at that time, which expenditure must be treated as an amount of expenditure actually incurred at that time for the purposes of paragraph 20(1)(*a*) of the Eighth Schedule.

(2) Subject to subsection (4), where a person disposes of an equity share in a company and acquires another equity share in that company in terms of a substitutive share-for-share transaction, that person must be deemed to have—

(*a*) disposed of that equity share so disposed of for an amount equal to the expenditure incurred by that person in respect of that equity share so disposed of which is or was allowable in terms of paragraph 20 of the Eighth Schedule or taken into account in terms of section 11(*a*) or 22(1) or (2), as the case may be;

(*b*) acquired that other equity share so acquired on the latest date on which that person acquired any share comprising the equity share so disposed of for a cost equal to the expenditure incurred by that person as contemplated in paragraph (*a*); and

(*c*) incurred the cost contemplated in paragraph (*b*) on the date contemplated in that paragraph, which cost must —

(i) if the equity share so acquired is acquired as a capital asset, be treated for the purposes of paragraph 20 of the Eighth Schedule as an expenditure actually incurred by that person in respect of the equity share so acquired; or

(ii) if the equity share so acquired is acquired as trading stock, be treated for the purposes of section 11(*a*) or 22(1) or (2) as the amount to be taken into account by that person in respect of the equity share so acquired.

(3) …..

(4) (*a*) This subsection applies where—

(i) a person disposes of an equity share in a company in terms of a substitutive share-for-share transaction; and

(ii) that person becomes entitled, in exchange for that equity share, to any consideration other than a dividend, foreign dividend or another equity share that is acquired by that person in terms of that substitutive share-for-share transaction.

(*b*) Where a person disposes of an equity share in terms of a substitutive share-for-share transaction and becomes entitled to consideration other than another equity share as contemplated in paragraph (*a*)(ii)—

(i) subsection (2) must not apply to the part of the equity share so disposed of that relates to that consideration; and

(ii) either—

(*aa*) where that equity share is so disposed of as a capital asset, the base cost at the time of that disposal of the part of the equity share contemplated in subparagraph (i) must be deemed to be equal to an amount which bears to the base cost of the equity share so disposed of the same ratio as the market value of that consideration bears to the sum of the market value of that consideration and the market value of the equity share acquired by that person in terms of that substitutive share-for-share transaction; or

(*bb*) where that interest is so disposed of as trading stock, the amount to be taken into account in terms of section 11(*a*) or 22(1) or (2) in respect of the part of the equity share contemplated in subparagraph (i) must be deemed to be equal to an amount which bears to the total amount taken into account in terms of section 11(*a*) or 22(1) or (2) in respect of the equity share so disposed of the same ratio as the market value of that consideration bears to the sum of the market value of that consideration and the market value of the equity share acquired by that person in terms of that substitutive share-for-share transaction.

(4A) If an equity share is issued in terms of a substitutive share-for-share transaction, the issue price of the linked unit disposed of in terms of that transaction is deemed to be contributed tax capital in respect of the class to which the equity share so acquired relates.

Proviso to section 44(4A)

Provided that where the amalgamated company is a portfolio of a collective investment scheme in property, the price at which the participatory interests were issued shall be added to the contributed tax capital in respect of the class of shares issued by the resultant company.

Section 46(2), (5) and (6A)

(2) Where an unbundling company distributes shares in terms of an unbundling transaction, that unbundling company must disregard that distribution for purposes of determining its taxable income or assessed loss, or its net income as contemplated in section 9D.

(5) Where shares are distributed by an unbundling company to a shareholder in terms of an unbundling transaction, the distribution by that unbundling company of the shares must be disregarded in determining any liability for dividends tax.

(6A) This section does not apply in respect of an unbundling transaction where the unbundling company is a REIT or a controlled company as defined in section 25BB(1).

Section 64F(1)(*a*) and (l) and (2)

64F. Exemption from tax in respect of dividends other than dividends *in specie*.—(1) Any dividend is exempt from the dividends tax to the extent that it does not consist of a dividend *in specie* if the beneficial owner is—

(*a*) a company which is a resident;

(*b*) to (*k*)…..

(*l*) any person to the extent that the dividend constitutes income of that person; or

(2) Any dividend paid by a REIT or a controlled company, as defined in section 25BB, and received or accrued before 1 January 2014 is exempt from the dividends tax to the extent that the dividend does not consist of a dividend *in specie.*

Section 64FA(1)(*a*)

64FA. Exemption from and reduction of tax in respect of dividends *in specie*.—(1) Where a company declares and pays a dividend that consists of a distribution of an asset *in specie*, that dividend is exempt from the dividends tax to the extent that it constitutes a distribution of an asset *in specie* if—

(*a*) the person to whom the payment is made has, by the date of payment of the dividend, submitted to the company—

(i) a declaration by the beneficial owner in such form as may be prescribed by the Commissioner that the portion of the dividend that constitutes a distribution of an asset *in specie* would, if that portion had not constituted a distribution of an asset *in specie*, have been exempt from the dividends tax in terms of section 64F; and

(ii) a written undertaking in such form as may be prescribed by the Commissioner to forthwith inform the company in writing should the circumstances affecting the exemption applicable to the beneficial owner referred to in subparagraph (i) change or the beneficial owner cease to be a beneficial owner;

Section 8(1)(*t*) of the Securities Transfer Tax Act No. 25 of 2007

8. Exemptions.—(1) The tax is not payable in respect of a transfer of a security—

(*t*) if that security constitutes a share in a REIT as defined in section 1 of the Income Tax Act;

Section 9(1)(*l*) of the Transfer Duty Act No. 40 of 1949

9. Exemptions from duty.—(1) No duty shall be payable in respect of the acquisition of property by—

(*l*) any company in terms of—

(i) an asset for- share transaction as defined in section 42 of the Income Tax Act, 1962 (Act No. 58 of 1962);

(iA) a substitutive share-for-share transaction as defined in section 43 of the Income Tax Act, 1962 (Act No. 58 of 1962);

(iB) an amalgamation transaction as defined in section 44 of the Income Tax Act, 1962 (Act No. 58 of 1962);

(ii) an intra-group transaction as defined in section 45 of the Income Tax Act, 1962 (Act No. 58 of 1962);

(iii) a liquidation distribution as defined in section 47 of the Income Tax Act, 1962 (Act No. 58 of 1962); or

(iv) a transaction which would have constituted a transaction or distribution contemplated in subparagraphs (i) to (iii) regardless of whether that person acquired that property as a capital asset or as trading stock,

where the public officer of that company has made a sworn affidavit or solemn declaration that such acquisition of property complies with the provisions of this paragraph;

Section 7(1)(*a*) of the VAT Act

7. Imposition of value-added tax.—(1) Subject to the exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the National Revenue Fund a tax, to be known as the value-added tax—

(*a*) on the supply by any vendor of goods or services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him;

Section 12(*a*) of the VAT Act

12. Exempt supplies.—The supply of any of the following goods or services shall be exempt from the tax imposed under section 7(1)(*a*):

(*a*) The supply of any financial services, but excluding the supply of financial services which, but for this paragraph, would be charged with tax at the rate of zero per cent under section 11;

Annexure B – Summary of the JSE Limited Listings Requirements

REIT status listing criteria for property entities other than CISIPs [paragraphs 13.46 to 13.54, 13.59 and 13.60]

An applicant issuer (that is, a new issuer) seeking to obtain REIT status from the JSE must satisfy the following criteria listed in paragraph 13.46:

- Under paragraph 13.46(a) the directors of the applicant must provide an undertaking and must ensure that the applicant issuer complies with the following distribution provisions set out in paragraph 13.47:
  - ➢ The company must distribute at least 75% of its total distributable profits as a distribution to the holders of its listed securities (which includes shares and linked units) by no later than six months after its financial year end, subject to the solvency and liquidity test.[74]
  - ➢ Interim distributions may occur before the end of a financial year end.
  - ➢ The company will procure that, subject to the solvency and liquidity test and section 46 of the Companies Act, those of its subsidiaries that are property entities incorporated in South Africa will distribute at least 75% of their total distributable profits as a distribution by no later than six months after their financial year ends.
  - ➢ Distributable profits for a financial year is defined as gross income[75] less deductions and allowances that are permitted to be deducted by a REIT under the Act, other than a qualifying distribution.[76]
- It must have gross assets of at least R300 million as reflected in either its audited or reviewed consolidated financial statements or a *pro forma* consolidated balance sheet compiled under paragraph 13.16, whichever reflects the more recent financial position [paragraph 13.46(b)].
- It must be a property entity [paragraph 13.46(c)].[77]
- At least 75% of the revenue as reflected in the statement of comprehensive income of the applicant issuer's group must be derived from rental revenue. The term "rental revenue"[78] means group revenue that is derived from the owning or leasing of immovable property which is let or sub-let to tenants plus dividends received from another REIT when the investment in that REIT is not consolidated in the group accounts [paragraph 13.46(d)].
- It must qualify for a listing on the Main Board under paragraph 4.2.8 or on ALT^{X} under paragraph 21.3, read together with paragraph 13.3 [paragraph 13.46(e)].
- The directors must each confirm that the applicant issuer will to the best of their knowledge and after making all reasonable enquiries to ascertain such facts, qualify for a tax deduction of distributions under section 25BB(2) for the current or future financial year end [paragraph 13.46(f)].

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74 As defined and applied in section 46 of the Companies Act.
75 As defined in section 1(1).
76 As defined in section 25BB(1).
77 As defined in paragraph 13.1(*t*).
78 As defined in paragraph 13.1(*z*).

- The directors of the applicant must provide an undertaking to the JSE that its consolidated liabilities will not exceed 60% of its gross asset value or consolidated assets, as the case may be, at a specific date [paragraph 13.46(g)].
- It must ensure that the audit committee or a separate risk committee of the board is responsible for adopting and implementing an appropriate risk management policy in accordance with industry practice [paragraph 13.46(h)].

An *existing issuer*, other than a CISIP, wishing to make application to obtain REIT status must –

- comply with the provisions of paragraph 13.46 (see above);
- not have failed the REIT tax test[79] for the last two consecutive financial years; and
- not have been in breach of the distribution provisions, set out in paragraph 13.47, in the last 24 months provided that it was classified as a REIT during that period.[80]

An applicant issuer, other than a CISIP, must on an on-going basis meet the following criteria listed in paragraph 13.49 in order to retain REIT status:

- It must comply with the distribution requirements in paragraph 13.47.
- It must qualify for a tax deduction of an amount equal to its distributions under section 25BB(2) for the immediately preceding financial year end *or* must not have failed the REIT tax test[81] for the last two consecutive financial year ends.
- The directors of the REIT must ensure that the total consolidated liabilities of the issuer will not be more than 60% of the total consolidated assets, or that they complied with their undertaking mandated in paragraph 13.46(g)(i).
- The directors of the REIT must submit the compliance declaration contemplated in paragraph 13.49(d) to the JSE within six months of the issuer's financial year end.

Paragraph 13.51 stipulates that in every announcement issued by a REIT it must make reference to the fact that it has a REIT status with the JSE. Announcements that deal with distributions must specify –

- that the distribution is regarded as –
  - a taxable dividend for income tax purposes for residents (see **5.4.1** for the income tax implications of dividends paid by a REIT); and
  - a taxable dividend for dividends tax purposes from 1 January 2014 for persons who are not residents (distributions made before that date to persons who are not residents are exempt from dividends tax) (see **5.10.1** for the dividends tax implications of dividends paid by a REIT); and
- the financial period to which the distribution relates.

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[79] The term "failed the REIT tax test" is defined in paragraph 13.1(i) and means that the applicant issuer was granted REIT status by the JSE, but on assessment by SARS, did not qualify for a deduction under section 25BB(2).

[80] Paragraph 13.48.

[81] The term "failed the REIT tax test" is defined in paragraph 13.1(i) and means that the applicant issuer was granted REIT status by the JSE, but on assessment by SARS, did not qualify for a deduction under section 25BB(2).

Under paragraph 13.52 an issuer with REIT status must keep the market informed regarding its tax status. In this regard the issuer must release an announcement containing full details of the implications for the issuer and its security holders, if it –

- fails the REIT tax test or believes that it will not qualify for a tax deduction of distributions under section 25BB(2);
- has breached the distribution provisions in paragraph 13.47; or
- has breached the gearing provisions of paragraph 13.49(c).

Paragraph 13.53(a) stipulates that the JSE will withdraw the REIT status of an applicant issuer if the applicant issuer fails to comply with the requirements of paragraph 13.49 at any time.

Paragraph 13.54 provides that an issuer who has received REIT status may at any time make application to the JSE to have this status removed.

Any applicant issuer that applies to receive REIT status must make application for a primary listing on the JSE.[82]

Certain transitional provisions under paragraph 13.60 applied to property entities, other than CISIPs. Provided the relevant property entity met the following requirements, it would have received REIT status from the commencement of its first financial year commencing on or after 1 April 2013, even though it did not necessarily meet all the criteria set out in paragraph 13.46.[83] The requirements may be summarised as follows:

- The property entity must have been listed on the Main Board of the JSE in the financials-real estate sector before 30 November 2012.
- The listed securities of the property entity must have been comprised of an ordinary share linked to a debenture and traded as a linked or combined unit at that time.
- The property entity must have applied on or before 1 July 2013 to receive a REIT status under these transitional provisions.
- The application letter must have complied with the requirements set out in paragraph 13.60(c).

REIT status listing criteria for CISIPs [paragraphs 13.55 to 13.59 and 13.61]

A CISIP is regulated by the Collective Investment Schemes Control Act, notices issued under that Act, a deed and supplemental deeds approved by the Registrar of Collective Investment Schemes and must comply with the Listings Requirements.[84]

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82 Paragraph 13.59.
83 Paragraph 13.60(*d*) and (*e*).
84 Paragraph 13.32.

Paragraph 13.55 stipulates that to receive REIT status a CISIP must apply to the JSE and comply with the following requirements:

- The CISIP must provide evidence that it complies with the following requirements in paragraphs 13.46(b) to (*e*) and (h):
  - It must have gross assets of at least R300 million as reflected in either its audited or reviewed consolidated financial statements or a *pro forma* consolidated balance sheet compiled under paragraph 13.16, whichever reflects the more recent financial position [paragraph 13.46(b)].
  - It must be a property entity [paragraph 13.46(c)].[85]
  - At least 75% of the revenue as reflected in the statement of comprehensive income of the applicant issuer's group must be derived from rental revenue. The term "rental revenue"[86] means group revenue that is derived from the owning or leasing of immovable property which is let or sub-let to tenants plus dividends received from another REIT when the investment in that REIT is not consolidated in the group accounts [paragraph 13.46(d)].
  - It must qualify for a listing on the Main Board under paragraph 4.2.8 or on ALT[X] under paragraph 21.3, read together with paragraph 13.3 [paragraph 13.46(e)].
  - It must ensure the responsibilities of an audit committee or a separate risk committee of the board [paragraph 13.46(h)].
- The CISIP must provide evidence of registration as a CISIP from the registrar of collective investment schemes.
- The CISIP must confirm that the CISIP deed has been approved by the registrar of collective investment schemes.[87]

A CISIP with REIT status must on an on-going basis comply with the following requirements set out in paragraphs 13.56 to 13.58:

- A CISIP must submit a compliance declaration referred to in paragraph 13.56 to the JSE within six months of the issuer's financial year end.
- In every announcement issued by a CISIP with a REIT status, it must make reference to the fact that it has a REIT status with the JSE.
- An issuer that is a CISIP with a REIT status must keep the market informed regarding its REIT status. In this regard the issuer must release an announcement containing full details of the implications for the issuer and its holders of securities, if it –
  - fails the REIT tax test[88] or believes that it will not qualify for a tax deduction of distributions under section 25BB(2);
  - has breached the provisions of its trust deed; or

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85 As defined in paragraph 13.1(*t*).

86 As defined in paragraph 13.1(*z*).

87 Paragraph 13.55.

88 The term "failed the REIT tax test" is defined in paragraph 13.1(i) and means that the applicant issuer was granted REIT status by the JSE, but on assessment by SARS, did not qualify for a deduction under section 25BB(2).

- has breached the provisions of the Collective Investment Schemes Control Act (see **4.9** for the income tax implications if a company ceases to be a REIT).

An applicant issuer that applies to receive REIT status must make application for a primary listing on the JSE.[89]

Transitional provisions applied under paragraph 13.61 to CISIPs seeking to obtain REIT status. In short, the relevant CISIPs were required to –

- be listed on the JSE before 30 November 2012;
- have applied on or before 1 July 2013 to receive a REIT status under these transitional provisions; and
- ensure that the application letter complied with the requirements set out in paragraph 13.61(c).

An applicant issuer that made application to the JSE and met the transitional Listings Requirements received REIT status from the commencement of its first financial year commencing on or after 1 April 2013, even though it did not necessarily meet all the criteria set out in paragraph 13.55.[90]

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89 Paragraph 13.59.

90 Paragraph 13.61(*d*) and (*e*).