

BINDING CLASS RULING: BCR 056

DATE: 16 February 2017

**ACT : INCOME TAX ACT 58 OF 1962 (the Act)
SECURITIES TRANSFER TAX ACT 25 OF 2007 (STT Act)**

**SECTION : SECTIONS 1(1) – DEFINITION OF “PORTFOLIO OF A COLLECTIVE INVESTMENT SCHEME”, “PORTFOLIO OF A DECLARED COLLECTIVE INVESTMENT SCHEME”, AND “PORTFOLIO OF A HEDGE FUND COLLECTIVE INVESTMENT SCHEME”, 41(1) – DEFINITION OF “EQUITY SHARE” AND 44 OF THE ACT AND PARAGRAPHS 1 – DEFINITION OF “ASSET” AND “DISPOSAL”, 3, 10, 11 AND 61(3) OF THE EIGHTH SCHEDULE TO THE ACT
SECTION 8(1)(a)(ii) OF THE STT ACT**

SUBJECT : AMALGAMATION OF PORTFOLIOS OF DECLARED HEDGE FUND COLLECTIVE INVESTMENT SCHEMES WITH REGISTERED HEDGE FUND COLLECTIVE INVESTMENT SCHEMES

1. Summary

This ruling determines the income tax and securities transfer tax consequences resulting from the amalgamation of hedge fund portfolios that have been declared collective investment schemes (CISs) with registered hedge fund CISs pursuant to a change in the law governing hedge fund portfolios.

2. Relevant tax laws

This is a binding class ruling issued in accordance with section 78(2) and published in accordance with section 87(2) of the Tax Administration Act 28 of 2011.

In this ruling references to sections and paragraphs are to sections of the relevant Act and paragraphs of the Eighth Schedule to the Act applicable as at 30 September 2016.

Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of –

- the Act –
 - section 1(1), definition of –
 - “portfolio of a collective investment scheme”;
 - “portfolio of a declared collective investment scheme”; and
 - “portfolio of a hedge fund collective investment scheme”;

- section 41, definition of –
 - “asset”;
 - “company”;
 - “disposal”; and
 - “equity share”;
 - section 44; and
 - paragraphs 1 – definition of “asset” and “disposal”, 3, 10, 11 and 61(3).
- the STT Act –
 - section 8(a)(ii).

3. Class

The Class Members to whom this ruling applies are –

- five Product Trusts and their beneficiaries;
- seven Manager Trusts and their beneficiaries;
- five Fund of Funds (FOF) Registered Hedge Fund CISs; and
- seven Registered Hedge Fund CISs.

4. Parties to the proposed transaction

The Applicant:	A listed company incorporated in and a resident of South Africa, registered as a long-term insurer under the Long-Term Insurance Act 52 of 1998
Co-Applicant 1:	A company incorporated in and a resident of South Africa, authorised as a manager in terms of the Collective Investment Schemes Control Act 45 of 2002 (the Cisca) for five FOF Registered Hedge Fund CISs
Co-Applicant 2:	A listed company incorporated in and a resident of South Africa, registered as a bank under the Banks Act 94 of 1990
Co-Applicant 3:	A company incorporated in and a resident of South Africa, authorised as a manager in terms of the Cisca for the seven Registered Hedge Fund CISs
The Product Trusts:	Five trusts, each established in and a resident of South Africa
The Manager Trusts:	Seven trusts, each established in and a resident of South Africa
The FOF Registered Hedge Fund CISs:	Five FOF Registered Hedge Funds CISs nominated by the Product Trusts to which the trusts will transition their assets

The Registered Hedge Fund CISs: Seven Registered Hedge Fund CISs nominated by the Manager Trusts to which the trusts will transition their assets

5. Description of the proposed transaction

The Applicant is the sole beneficiary of four of the five Product Trusts and Co-Applicant 2 is the sole beneficiary of the remaining Product Trust. Each beneficiary of a Product Trust has vested rights to the income received by or accrued to the trustee and the capital of the Product Trust concerned.

The Applicant and Co-Applicant 2 funded each of the Product Trusts of which they are beneficiaries.

The Applicant issued policies which reference the investment performance of the Product Trusts.

The Product Trusts are the beneficiaries of the Manager Trusts and made capital contributions to the Manager Trusts. In accordance with the provisions of the trust deed of each of the Manager Trusts, the beneficiaries have, *pro rata* to their capital contribution to each Manager Trust, vested rights to the income received by or accrued to the trustees and to the capital of each relevant Manager Trust.

The Applicant and Co-Applicant 2 are therefore indirectly the ultimate investors in the Manager Trusts.

Each Product Trust and each Manager Trust is a “hedge fund” as defined in Government Notice 141, dated 25 February 2015 published in *Government Gazette* 38503 (notice). In terms of the notice, each Product Trust and each Manager Trust was declared to be a CIS under section 63 of the CISCAs with effect from 1 April 2015.

In order to comply with the notice, a person that conducted the business of a hedge fund was required, within 6 months as from 1 April 2015, to lodge with the Registrar of Collective Investment Schemes (the Registrar) an application for registration as a manager to operate a hedge fund in accordance with section 42 of the CISCAs. As an alternative to registration, the Registrar granted a general exemption under Board Notice 140 of 2015, published in *Government Gazette* 39220, in terms of which persons conducting the business of a hedge fund could notify the Registrar by not later than 30 September 2015 of a newly registered portfolio operated by a manager under the CISCAs, to which the applicable portfolio of the hedge fund that existed on 1 April 2015 would be transitioned.

The trustees of each Product Trust and each Manager Trust opted for the general exemption to apply to them and duly informed the Registrar of the newly registered portfolios to which they would transition their respective portfolios.

Pursuant to their elections, each Product Trust intends to transfer all of its assets and liabilities (other than assets required to settle debts incurred in the ordinary course of its trade and to satisfy reasonable anticipated liabilities for the administration of its liquidation or winding up) to a nominated newly registered portfolio of a FOF Registered Hedge Fund CIS, by way of an amalgamation contemplated in section 99 of the CISCAs and/or the Guidance Note on the

transition process issued by the Financial Services Board (FSB) on 16 August 2016 (number HF01A) (first amalgamation).

Similarly, each Manager Trust will transfer all of its assets and liabilities (other than assets required to settle debts incurred in the ordinary course of its trade and to satisfy reasonable anticipated liabilities for the administration of its liquidation or winding up) to a Registered Hedge Fund CIS by way of an amalgamation contemplated in section 99 of the CISCA and/or the already-mentioned Guidance Note (second amalgamation).

Each Product Trust will distribute the participatory interest it acquires in the FOF Registered Hedge Fund CIS to its beneficiary after which each Product Trust will be liquidated or its existence will be terminated. Similarly, each Manager Trust will distribute the participatory interest it acquires in the Registered Hedge Fund CIS to its beneficiaries and each Manager Trust will be liquidated or its existence will be terminated.

Subsequent to the second amalgamation, each Registered Hedge Fund CIS may be required to rebalance its portfolio by disposing of certain assets acquired in terms of that amalgamation transaction within 18 months of such acquisition as part of the normal investment authority of the portfolio.

The trustees of each Product Trust and each Manager Trust will take the following steps to terminate the respective trusts within the time periods as prescribed in section 41(4) of the Act –

- adopt resolutions to terminate and deregister the relevant trusts which will be adopted with the prior written consent of the relevant founder and relevant beneficiary of each trust;
- settle the liabilities of each trust from their assets and distribute the residual assets of each trust to the respective beneficiaries in accordance with the provisions of each trust deed; and
- once all of the assets have been so distributed, submit an application to the Master of the High Court having jurisdiction to deregister each trust.

6. Conditions and assumptions

This binding class ruling is subject to the additional conditions and assumptions that the liabilities which will be assumed by each Registered Hedge Fund CIS will constitute debt that was incurred by the relevant Manager Trust more than 18 months prior to the disposal of its assets to that Registered Hedge Fund CIS, or debt that was incurred within a period of 18 months before that disposal, but in that event it will either constitute the refinancing of the debt referred to already, or debt which arose in the ordinary course of the business undertaking which will be disposed of, as a going concern, to that Registered Hedge Fund CIS.

7. Ruling

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

- a) Both the first and the second amalgamation transactions, regarding the transfer of assets from each Product Trust to a FOF Registered CIS and from each Manager Trust to a Registered Hedge Fund CIS, will each

constitute an “amalgamation transaction”, as defined in paragraph (a) of the definition of that term in section 44(1) of the Act.

Consequently, section 44(2) will apply to each amalgamation transaction as follows –

- i) each trust will be deemed to have disposed of their assets to the respective registered CIS for amounts equal to their respective base costs on the date of disposal; and
 - ii) the trusts and the respective registered CISs must, for purposes of determining any capital gain or capital loss in respect of a future disposal by the registered CIS of any of those assets, be deemed to be one and the same person in respect of the date of acquisition of the asset in question by the trusts and the amount and date of incurral by the trusts of any expenditure allowable under paragraph 20 and any valuation effected under paragraph 29 by the trusts in respect of the asset.
- b) Any transfer of shares from each of the Product Trusts to a FOF Registered CIS and from the Manager Trusts to a Registered Hedge Fund CIS in terms of the first amalgamation transaction and the second amalgamation transaction respectively will qualify for an exemption from securities transfer tax under section 8(1)(a)(ii) of the STT Act.
- c) The distribution of the participatory interests acquired by each of the Product Trusts in a FOF Registered CIS and by each of the Manager Trusts in a Registered Hedge Fund CIS to the relevant beneficiaries will qualify for relief under sections 44(6)(a) and (b), and 44(8) of the Act respectively, in that –
 - i) each trust must disregard the relevant disposal for purposes of calculating its taxable income or assessed loss; and
 - ii) each beneficiary will be regarded as having disposed of its interest in the relevant Product Trust or Manager Trust at its base cost or the amount taken into account under section 11(a) or section 22(1) or (2) of the Act. The beneficiary will be regarded as having acquired the participatory interest in the relevant FOF Registered CIS or Registered Hedge Fund CIS on the date that the beneficiary acquired its interest in the relevant Product Trust or Manager Trust for a cost equal to its base cost or the amount taken into account under section 11(a) or section 22(1) or (2) of the Act.
- d) Despite the application of section 44(5) of the Act, no amount will be taken into account under paragraph 10, in respect of the disposals by the FOF Registered CISs of their interests in the Manager Trusts in terms of the second amalgamation transaction, as each of those disposals will not give rise to a capital gain as a result of section 44(2) of the Act applying to the disposals.
- e) Despite the application of section 44(5) of the Act, no amount will be taken into account under paragraph 10, in respect of the subsequent disposal of assets by the Registered Hedge Fund CISs after the second amalgamation transaction, as each of the Registered Hedge Fund CISs is

required to disregard capital gains or losses in accordance with paragraph 61(3).

- f) Provided the appropriate steps have been taken to terminate the Product Trusts and the Manager Trusts within the time period prescribed in section 44(13)(a) of the Act, section 44(13) of the Act will not apply to limit the application of the roll-over relief provided for under section 44(2) of the Act.

8. Period for which this ruling is valid

This binding class ruling is valid for a period of two years from 30 September 2016.

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