BINDING PRIVATE RULING: BPR 083

DATE: 25 May 2010

ACT	:	**INCOME TAX ACT, NO. 58 OF 1962 (the Act)**
SECTION	:	**PARAGRAPH 11(1) OF THE EIGHTH SCHEDULE TO THE ACT**
SUBJECT	:	**CAPITAL GAINS TAX IMPLICATIONS ON THE CONVERSION OF A COMPANY THROUGH THE AMENDMENT OF ITS INCORPORATION DOCUMENTATION**

1. Summary

This ruling deals with the question as to whether steps taken by a company to convert to a protected cell company (PCC) under legislation governing its commercial activities, entailing amendments to its incorporation documentation and other related administrative actions, will give rise to a "disposal" by the shareholders of that company as defined in paragraph 11(1) of the Eighth Schedule to the Act.

2. Relevant tax laws

This is a binding private ruling issued in accordance with section 76Q of the Act.

In this ruling legislative references to paragraphs are to paragraphs of the Eighth Schedule to the Act applicable as at 31 December 2006 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This ruling has been requested under the provisions of paragraph 11(1) of the Eighth Schedule.

3. Parties to the proposed transaction

The Applicant:	A contractual cell captive company incorporated outside South Africa and licensed to carry on insurance business in another jurisdiction
The Co-Applicant:	One of the shareholders of the Applicant who is resident in South Africa

4. Description of the proposed transaction

The Applicant is a contractual cell captive company, incorporated outside South Africa and is licensed to carry on insurance business. Various classes of shares have been issued by the contractual cell captive

company, some of which are issued to shareholders who are “resident” as defined in section 1, one of which is the Co-Applicant.

A cell captive insurance company enables clients to purchase separate classes of shares (a cell) in a registered insurance company which underwrites agreed insurance risk exposure for a particular cell. This arrangement and its terms are governed by a contract entered into between a registered insurance company and the cell owner/shareholder in terms of which the risks and the rewards associated with certain insurance activities accrue to the shareholder. The shareholders’ agreement provides for contractual ring-fencing between the various cells’ insurance activities and the promoter’s (shareholder’s) activities.

The jurisdiction in which the Applicant is located introduced protected cell company legislation (PCC legislation), providing for legal segregation of the assets and liabilities between cells and from those of the promoter cell. This type of legislation was first introduced, *inter alia*, for purposes of providing enhanced security to participating companies in cell captive insurers. The PCC legislation enables the assets of the individual cells to be legally insulated from the liabilities of other cells and the liabilities of the promoter cell. Although prior to the relevant PCC legislation coming into effect the shareholders in the company agreed to such an arrangement amongst themselves under a general shareholders’ agreement, its enforceability in relation to third parties has never been tested in a court.

The segregation of assets in terms of the PCC legislation provides additional legal protection to the shareholders in their judgment. Instead of the shareholders relying on a purely contractual arrangement between the shareholders, the legislative regime gives a statutory basis for the segregation of assets that binds third parties as well. By ring-fencing the assets of each cell such that they cannot be subject to a claim by a creditor of another cell, or be used to offset losses of another cell, the PCC legislation offers the protection of a clear segregation of assets within a single legal entity.

In order to provide this added legal protection to its shareholders (cell owners), the Applicant has to adopt this piece of legislation and effectively convert into a PCC, as required by the PCC legislation. In order to adopt this legislation, the Applicant must apply to the regulatory authorities and fulfil a few company secretarial procedures, including changing its name (to include reference to a PCC) and amending its Shareholders’ Agreement and the Memorandum and Articles of Association in order to incorporate the PCC legislation’s principles and terminology. The conversion will not change the Applicant into a different legal entity, nor will it in any way replace existing shares with new shares.

5. Conditions and assumptions

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

- The share agreement provided to SARS is currently in force and effect and is a sample of the standard agreement concluded between a registered insurance company and the various shareholders.
- This ruling will only apply to the Applicant and the shareholder comprising the Co-Applicant. No other party, including any other shareholders of the Applicant that have not specifically applied for a ruling on this matter, may place any reliance thereon.
- The proposed transaction is not part of or connected to any other transaction, operation or scheme.

6. Ruling

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

- The steps taken by the Applicant to be recognised as a PCC under the relevant PCC legislation will not give rise to a "disposal" as defined in paragraph 11(1) of the Eighth Schedule.

7. Period for which this ruling is valid

This binding private ruling, issued in December 2006, is valid as from the date the proposed transaction takes place, that is, the conversion of the Applicant to a PCC in accordance with the relevant PPC legislation, and applies in respect of the Applicant's and the Co-Applicant's relevant years of assessment.

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