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# TAX & EXCHANGE CONTROL ALERT

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### TLAB 2020: Proposed rollover relief amendments tabled

The rollover relief provisions contained in Part III of the Income Tax Act 58 of 1962 (the Act) provide valuable commercial flexibility to corporate groups. This is achieved by enabling corporate groups to undertake certain transactions in a tax neutral manner and defer the tax costs, where such transactions would otherwise give rise to immediate income tax and/or capital gains tax costs. The intra-group transactions covered by the rollover relief provisions include the introduction of assets into a group company, transfer of assets between group companies, and the unbundling of indirectly held subsidiaries to a group holding company.

## TLAB 2020: Proposed rollover relief amendments tabled

Two proposed amendments to the rollover relief provisions will be discussed here:

- Refinement of the interaction between the anti-avoidance provisions for intra-group transactions, and
- Clarifying rollover relief for unbundling transactions.

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In our Tax & Exchange Control Alerts of [6 August 2020](#), [13 August 2020](#), [20 August 2020](#), [27 August 2020](#), [3 September 2020](#) and [23 October 2020](#), a selection of the proposals introduced by the draft Taxation Laws Amendment Bill 2020 (Draft TLAB) were discussed.

The Taxation Laws Amendment Bill 27 of 2020 (TLAB) was tabled by the Minister of Finance during the presentation of the Medium-Term Budget Policy Statement on 28 October 2020. The TLAB represents the outcome of National Treasury and SARS' response to submissions made by the public on the proposals in the Draft TLAB. The outcomes of the public participation process regarding two proposed amendments to the rollover relief provisions will be discussed here:

- Refinement of the interaction between the anti-avoidance provisions for intra-group transactions, and
- Clarifying rollover relief for unbundling transactions.

### Section 45 – Refinement of the interaction between the anti-avoidance provisions for intra-group transactions

Section 45 of the Act allows one company to transfer an asset to another company forming part of the same group, on a tax neutral basis and defer the tax liability that would have been incurred in the ordinary course.

Section 45 however, contains anti-avoidance provisions aimed at preventing the abuse of the tax relief afforded to companies under these intra-group transactions. Namely:

- the "De-grouping Charge" contained in section 45(4), which applies where a group benefits from rollover relief under an intra-group transaction, but one of the companies subsequently ceases to form part of the group within 6 years. This triggers an imposition of the deferred tax in the hands of the company that qualified for the roll-over relief, and
- the "Zero Base Cost Rule" contained in section 45(3A) of the Act, which deems the base cost of debt or non-equity shares transferred under an intra-group transaction to be nil in the hands of the company that qualified for the roll-over relief. This is specifically in the context of intra-group transactions where the purchase of the asset is funded through the issuing of debt or non-equity shares.

### The Anomaly

The Draft TLAB identified an anomaly which arises where an asset for debt transaction benefits from rollover relief under section 45, but there is a subsequent de-grouping. In such circumstances there would be a reversal of the tax deferral under the De-grouping Charge and a

## TLAB 2020: Proposed rollover relief amendments tabled...*continued*

The TLAB proposes introducing a new subsection 3B into section 45, which links the base cost to the value of the debt or non-equity shares on the day of acquisition and provides for the relief to apply where:

- the transferee company ceases being part of a group of companies as contemplated in section 45(4); or
- the transferee company is deemed to have ceased to form part of the same group under section 45(4B)

greater capital gain will be realized on the disposal of the debt or non-equity shares, as the base cost of the debt or non-equity shares is deemed to be nil under the Zero Base Cost Rule.

### *Draft TLAB Proposals*

The Draft TLAB proposed amending the interaction between the two anti-avoidance provisions, to ensure that where the De-grouping Charge applies to a transaction where the Zero Base Cost Rule has previously applied, the taxpayer be put into the same position as if the rollover relief had not applied and a base cost be determined regarding the debt or non-equity shares.

### *Public Comments and TLAB Position*

Two notable comments were made during the public participation process.

First, that under the Draft TLAB proposals the starting point for determining the base cost of the debt or non-equity shares in the anomalous situation would be the market value. However, ordinarily the starting point would be the amount of debt incurred or capital subscribed for and therefore, the starting point for determining the base cost of the debt or non-equity shares in the anomalous situation ought to be the face value.

Secondly, the proposal in the Draft TLAB speaks to a situation where the transferee company ceases to form part of the same group of companies as the transferor company. However, section 45(4) refers to transferee company ceasing to form part of any group of companies in relation to the transferor company or a controlling group company in relation to the transferor company. The proposed wording in the Draft TLAB narrows the applicability of the proposed relief from the anomaly identified.

The comments were both accepted and the TLAB proposes introducing a new subsection 3B into section 45, which links the base cost to the value of the debt or non-equity shares on the day of acquisition and provides for the relief to apply where:

- the transferee company ceases being part of a group of companies as contemplated in section 45(4); or
- the transferee company is deemed to have ceased to form part of the same group under section 45(4B).

### **Section 46 - Clarifying rollover relief for unbundling transactions**

An unbundling transaction under section 46, is in brief where the shares in a lower tiered subsidiary (unbundled company), held by a mid-level subsidiary (unbundling company) are transferred to that mid-level subsidiary's shareholder(s), for example a holding company, in accordance with their effective interest. The unbundling results in the indirect shareholding of the holding company in the lower tiered subsidiary (unbundled company) – via the mid-level subsidiary – being converted into a direct shareholding. Where an unbundling transaction takes place in accordance with section 46, the tax consequences of the transfer of shares is tax neutral, with the tax costs deferred until the shares are transferred outside the group.

Section 46 also contains anti-avoidance provisions. Here the relevant one being the bar to unbundling transactions where immediately before the unbundling, 20% of the shares in the company to be unbundled are held by 'disqualified persons' alone or together with any connected persons who are similarly disqualified.

## TLAB 2020: Proposed rollover relief amendments tabled...*continued*

National Treasury proposed a pro rata version of the anti-avoidance provision which would bar the relief regarding any equity shares to be distributed by the unbundling company that are held by a shareholder that is a disqualified person and holds at least 5% of the equity shares in the unbundling company, immediately before the unbundling transaction.

'Disqualified persons' are defined in section 46(7)(b) of the Act and includes, amongst others, persons who are non-resident and public benefit organisations.

### *Draft TLAB Proposal*

The Draft TLAB proposed removing the alone or together with connected persons requirement from section 46(7)(a) which contains the anti-avoidance provision and replacing it with an aggregation. The effect of the proposal would be that unbundling transactions would not be possible where 20% of the unbundled company's shares are in aggregate held by disqualified persons.

It was proposed that these changes would take effect from the date the Draft TLAB was published, being 31 July 2020.

### *Public Comments and TLAB Position*

An in-depth public participation process was held regarding the proposed amendments to section 46. The main concerns raised by the public comments centered around the following:

- *that the removal of the connected person limitation from the anti-avoidance provision renders it overly punitive, as it is not sufficiently targeted at the disqualified persons. Mainly as that the qualifying shareholders - who may hold up to 79% of the shares in the unbundled company - are subject to anti-avoidance, rather than only the disqualified persons.*

National Treasury in response proposed a pro rata version of the anti-avoidance provision which would bar the relief regarding any equity shares to be distributed by the unbundling company that are held by a shareholder that is a disqualified person and holds at least 5% of the equity shares in the unbundling company, immediately before the unbundling transaction.

Further comments were received regarding the retrospectivity of the proposed changes, as there were unbundling transactions already underway and to make these subject to retrospective changes would be unduly burdensome.

This comment was accepted and the TLAB proposes these changes be effective as of 28 October 2020.

### **Comment**

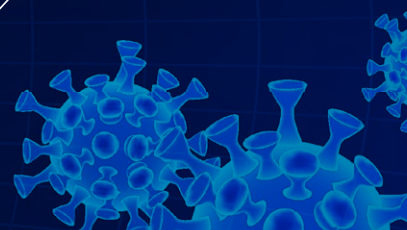
Ensuring a predictable outcome and presenting value to business in the form of reliable deferral of tax costs under the rollover relief provisions in the Act, is key to the effectiveness of the roll-over provisions, which are essentially a tax policy measure aimed at enhancing commercial activity.

The proposed amendments as contained in the TLAB may be subject to further alteration during the Parliamentary process and there is a prospect that further amendments may be made to the text of the TLAB.

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# CDH'S COVID-19 RESOURCE HUB

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### BBBEE STATUS: LEVEL TWO CONTRIBUTOR

Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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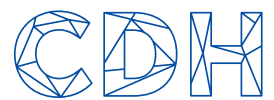
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