Dear Sir

TAX IMPACT OF CORPORATE ACTIONS ON THE EXPENSE RELIEF RATIO OF LONG TERM INSURERS

Background:

Section 29A(11) of the Income Tax Act limits the amount of expenses that a policyholder fund can claim for income tax purposes by means of the following formulas:

\[
I + R + F / I + 2.5 R + 4.75F + 4.75 L \quad \text{for the Individual Policyholder Fund (IPF)}, \quad I + R + F / I + 2R + 3.5F + 3.5 L \quad \text{for the Company Policyholder Fund (CPF)},
\]

where:

- \( I \) = Interest income per section 24J
- \( R \) = Rental income after direct expenses
- \( F \) = Taxable foreign dividend income
- \( L \) = Dividend income other than taxable foreign dividends

Dividend income has an adverse effect on the amount of expenses that can be deducted to determine the taxable income attributable to the respective policyholder funds.

The recent unbundling in the market place by means of dividend distributions has resulted in a significant increase in the tax liability for the respective policyholders funds due to the negative impact on the expense ratio.

The income tax liability attributable to policyholder funds is an expense for policyholders. Policyholders benefits will accordingly be reduced in order to meet the additional tax liability.

Recommendation:
Policyholders have not gained any additional benefit compared to other investors, but have to pay additional tax as a result of the negative impact on the expense ratio. This is not equitable and fair towards policyholders. No basis exists to justify this cost to policyholders.

We therefore propose an enactment of a retrospective legislative amendment to exclude from “L” in the aforementioned formula extraordinary dividend distributions in respect of corporate actions.

Please do not hesitate to contact me should you require further information.

Yours faithfully

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