

National Treasury proposes roll-over relief for conversion of unregulated hedge funds

In the recently released draft of the Taxation Laws Amendment Bill, National Treasury has proposed significant concessions which address the tax consequences which hedge fund managers may face in complying with the new hedge fund regulations.

The new hedge fund regulations require any entity conducting the business of a hedge fund to register as a manager of a collective investment scheme. Hedge funds will thus be governed by the Collective Investment Schemes Control Act.

Existing hedge funds will be able dispose of their assets to an approved collective investment scheme for no consideration other than the right to receive a participatory interest in that approved collective investment scheme without incurring any tax at the time of disposal. On the transfer of the assets from existing hedge funds, the fund will be deemed to transfer their assets to the collective investment scheme at the base cost if the assets are capital assets or at cost if the assets are held as trading stock.

The approved collective investment scheme will be deemed to acquire the assets:

- at the base cost from the transferring hedge fund if the assets are capital assets; and
- at acquisition cost from the transferring hedge fund if the assets are held as trading stock.

The transferring hedge fund and the approved collective investment scheme are deemed to be the same person when determining the approved collective investment scheme's capital gains tax or income tax liability on future disposals of the assets.

The amendments do not appear to apply to the disposal of any assets that registered funds will not be able to trade in. Once registered, these funds will fall within the existing provisions set out in section 25BA of the Act which apply to registered collective investment schemes.

The explanatory memorandum to the draft bill notes that the provisions are transitional and will be repealed when the Financial Services Board determines that unregulated hedge funds may no longer apply for conversion to an approved collective investment scheme. Therefore, hedge funds should consider converting to an approved collective investment scheme sooner rather than later.

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