TAX

IN THIS ISSUE

DEBT REDUCTION AND MINING ASSETS

On 18 February 2015, the South African Revenue Service (SARS) released Binding Private Ruling 187 (Ruling), which dealt with the waiver of a loan subsequent to the implementation of an intra-group transaction.

The facts were as follows:

- Company A held 74% of the shares in Company B, and Company C held 26% of the shares in Company B.
- In terms of a Black Economic Empowerment transaction, Company A sold its business to Company B.
- The business that Company A sold to Company B was effectively a prospecting and mining business, comprising various assets, including allowance assets, property, debtors, contracts and goodwill.
- Company A had no unredeemed capital expenditure at the time of the sale. The purchase price was to remain outstanding on loan account, which loan account attracted interest.
- Section 45 of the Income Tax Act, No 58 of 1962 (Act) applied to the transfer of the assets as Company A and Company B formed part of the same group of companies.
- Due to various factors impacting the mining industry, Company B had struggled to repay the capital and interest, and a portion of the unpaid interest had been written off by Company A as a bad debt.
- It was proposed that Company A waive the entire loan owing by Company B.

Taking cognisance of the above, it was clear that the parties were concerned about the application of the debt reduction provisions contained in s19 of the Act and paragraph 12A of the Eighth Schedule to the Act. Generally, where there is a reduction of debt that has been used to fund deductible expenditure or allowance assets, a recoupment could arise in the hands of the debtor in terms of s19 of the Act. Similarly, where there is a reduction of debt that has been used to fund capital assets, it could result in a reduction of base cost and/or a capital gain for the debtor in terms of paragraph 12A of the Eighth Schedule to the Act.

SARS ruled that paragraph 12A would not be applicable at all, presumably because of the group company exemption contained in paragraph 12A(6)(d). However, there is no similar group company exemption available in terms of s19 of the Act. Accordingly, SARS ruled that s19 of the Act would be applicable, but only to the extent that the loan related to allowance assets, other than mining assets in terms of which a deduction was claimed under s15(a) of the Act.

Section 19 would be applicable to the extent that the loan related to mining assets in respect of which a deduction was claimed under s15(a) of the Act as read with s36 of the Act.

In other words, s19 would only apply to non-mining allowance assets and not to mining assets. Unfortunately the Ruling does not elaborate on the reason for making the distinction between mining and non-mining allowance assets.

SARS indicated that s19 will not result in recoupments for Company A in respect of any non-mining allowance assets for which Company A claimed allowances and which were transferred in terms of s45. SARS also ruled that s19 would apply to trading stock still on hand as well as trading stock that had been disposed of.

SARS further indicated that the waiver of the loan would not constitute 'gross income' for Company B to the extent that it does not otherwise constitute a recoupment.

Additionally, and in terms of paragraph 56(1) of the Eighth Schedule to the Act, any capital loss in the hands of Company A in respect of the waiver of the loan must be disregarded to the extent that there are no recoupments or adjustments for Company B.

It is not clear from the Ruling whether s45(3A) of the Act applied to the loan. If it did, Company A would have had a base cost of nil in respect of the loan because it was used to fund the intra-group transaction, and Company A would not have been able to generate a capital loss.

Interestingly, SARS also indicated that paragraph 38 of the Eighth Schedule of the Act would not apply, implying that the waiver would neither constitute a donation, nor a disposal between connected persons not at an arm's length price.

Heinrich Louw

DLA CLIFFE DEKKER HOFMEYR

SALE OF SHARES SUBJECT TO SUSPENSIVE CONDITIONS

The South African Revenue Service (SARS) released Binding Private Ruling No 189 on 19 February 2015, which dealt with the sale of shares subject to suspensive conditions.

Two trusts had acquired certain ordinary shares in a listed company as part of a Black Economic Empowerment (BEE) transaction. The shares were subject to certain restrictions, but it was anticipated that the restrictions would soon lapse and the two trusts would be able to dispose of their shares.

A certain Company X intended to make an offer to the trusts to purchase some of the shares once the restrictions lapsed.

However, the listed company had a call option in respect of the shares, which related to the financing of the BEE transaction, and which it could exercise.

The trusts also held call options – should the listed company exercise its call option, the trusts would be entitled to re-subscribe for the same number of shares that were subject to the listed company's call option.

Before the trusts could determine the number of shares that they would have available for sale to Company X, the call options would first need to be exercised (or not, as the case may be).

It was proposed that the trusts enter into separate sale agreements with Company X, subject to various suspensive conditions, in respect of the shares. The agreements would provide that, after the suspensive conditions had been fulfilled, and over a period of approximately three months, the trusts may present Company X with a so-called 'trigger notice,' specifying the number of shares available for sale to Company X. Within the said period, the trusts may sell their available shares to Company X in three such tranches.

If no trigger notice had been presented by the end of the period for a certain minimum number of shares, the trusts would be deemed to have presented a trigger notice for all the available shares in terms of the sale agreements.

The agreements would also provide that:

- ownership, risk and benefit in respect of the shares will only pass to Company X once the trigger notice is presented, payment has been made, and the shares have been delivered; and
- the purchase price be determined with reference to a formula that takes into account a 30 day volume weighted average share price during the period, less any distributions during the period, and less a discount, as well as the current average trading price.

It appears that the parties were concerned about the time of disposal of the shares for purposes of capital gains tax. For a sale of any of the shares to be successfully completed:

- the option transactions would first have to be completed;
- the suspensive conditions in terms of the sale agreements would have to be fulfilled;
- the trigger notices would have to be presented;
- if no trigger notices are presented, the three month period would have to expire for a trigger notice to be deemed to have been presented;
- the price per share needs to be determined; and
- payment for and delivery of the shares would have to take place.

The exact time of disposal of any of the shares by the trusts is therefore, at first sight, not clear.

SARS ruled that:

- in terms of paragraph 13(1)(a)(i) of the Eighth Schedule to the Income Tax Act, No 58 of 1962 (Act), the time of disposal by the trusts of their shares will be the date on which the suspensive conditions in terms of the sale agreements are fulfilled;
- the base cost of the shares in the hands of Company X will be the purchase price payable under each trigger notice;
- the trusts and Company X are not connected persons, even though a fellow subsidiary of Company X holds an equity interest in a company that is a beneficiary of one of the trusts; and
- section 24J of the Act would not apply to the transaction.

Heinrich Louw

CONTACT US

For more information about our Tax practice and services, please contact:

Emil Brincker
National Practice Head
Director
T +27 (0)11 562 1063
E emil.brincker@dlacdh.com

Andrew Lewis
Director
T + 27 (0)11 562 1500
E andrew.lewis@dlacdh.com

Tessmerica Moodley
Senior Associate
T +27 (0)21 481 6397
E tessmerica.moodley@dlacdh.com

Ben Strauss
Director
T +27 (0)21 405 6063
E ben.strauss@dlacdh.com

Mareli Treurnicht
Senior Associate
T + 27 (0)11 562 1103
E mareli.treurnicht@dlacdh.com

Ruaan van Eeden
Director
T +27 (0)11 562 1086
E ruaan.vaneeden@dlacdh.com

Gigi Nyanin
Associate
T + 27 (0)11 562 1120
E gigi.nyanin@dlacdh.com

Lisa Brunton
Senior Associate
T + 27 (0)21 481 6390
E lisa.brunton@dlacdh.com

Nicole Paulsen
Associate
T + 27 (0)11 562 1386
E nicole.paulsen@dlacdh.com

Heinrich Louw
Senior Associate
T +27 (0)11 562 1187
E heinrich.louw@dlacdh.com

BBBEE STATUS: LEVEL THREE CONTRIBUTOR

JOHANNESBURG
1 Protea Place Sandton Johannesburg 2196, Private Bag X40 Benmore 2010 South Africa
Dx 154 Randburg and Dx 42 Johannesburg
T +27 (0)11 562 1000 **F** +27 (0)11 562 1111 **E** jhb@dlacdh.com

CAPE TOWN
11 Buitengracht Street Cape Town 8001, PO Box 695 Cape Town 8000 South Africa
Dx 5 Cape Town
T +27 (0)21 481 6300 **F** +27 (0)21 481 6388 **E** ctn@dlacdh.com

cliffedekkerhofmeyr.com

DLA CLIFFE DEKKER HOFMEYR