TAX

IN THIS ISSUE

SARS EXTENDS THE LIST OF REPORTABLE ARRANGEMENTS

SARS CLAMPS DOWN ON SHARE BUY BACKS FOLLOWED BY THE ISSUE OF SHARES

SARS EXTENDS THE LIST OF REPORTABLE ARRANGEMENTS

The Commissioner for the South African Revenue Service (SARS) issued an important notice (SARS Notice) on 16 March 2015. The SARS Notice was published in terms of s35(2) and s36(4) of the Tax Administration Act, No 28 of 2011 (TAA).

Sections 34 to 39 of the TAA deal with so-called 'reportable arrangements'. Essentially, if an arrangement has certain characteristics (as listed in s35(1) of the TAA) or if SARS has listed the arrangement in a public notice (in terms of s35(2) of the TAA), then the person who promotes the arrangement (called a promoter) and the person who may derive a tax benefit from the arrangement (called the participant) must report the arrangement to SARS.

In terms of s36(1) to (3) of the TAA, certain arrangements are excluded, and do not need to be reported. Promoters or participants need not report these types of arrangements to SARS. Section 36(4) of the TAA also allows SARS to exclude additional arrangements by way of public notice.

In terms of the SARS Notice, the following arrangements are now also reportable (in addition to the arrangements with the features set out in s35(1) of the TAA):

- Hybrid financial instruments: Certain arrangements that qualify as 'hybrid equity shares' in terms of s8E of the Income Tax Act, No 58 of 1962 (ITA) and certain 'hybrid debt instruments' in terms of s8F of the ITA (other than listed shares). Put simply, under those anti-avoidance provisions, the incidence of tax in relation to financial instruments which have certain features, is re-characterised.
- Share buy-backs: An arrangement in terms of which a company buys back its shares for a price of more than R10 million and the company issued or is required to issue shares within a period of 12 months of entering into the arrangement or the date of the buy-back.
- Offshore trusts: An arrangement in terms of which a local tax resident makes a contribution to a trust if: (i) the trust is a tax resident abroad; (ii) the resident making the contribution is a beneficiary of the trust; and (iii) the value of the contribution or the interest of the beneficiary in the trust exceeds R10 million. Investments in certain offshore collective investment schemes are excluded.
- Assessed losses: An arrangement in terms of which a person acquires a direct or indirect controlling interest in a company that has, or is likely to have, an assessed loss exceeding R50 million.
- Foreign insurance policies: An arrangement in terms of which a local tax resident pays more than R5 million to an offshore insurer and the return of the insurance policy is determined mainly with reference to the value of particular assets held by the insurer.

However, the SARS Notice does contain some good news: SARS has excluded from the operation of s35(1) of the TAA arrangements where the aggregate tax benefit which may be derived by all the participants to the arrangement is less than R5 million.

The SARS Notice replaces all previous notices issued in relation to reportable arrangements.

Section 38 of the TAA sets out the information that a promoter or participant must submit to SARS. The promoter or participant must submit the information within 45 business days of the date on which the arrangement becomes reportable or, if a person becomes a participant in an arrangement that is reportable, within 45 days of the person becoming a participant (s37 of the TAA).

On receipt of the relevant information SARS must allocate a reference number to the participant for administrative purposes only (s39 of the TAA).

What are the consequences of reporting an arrangement to SARS? Importantly, the fact that a person has reported an arrangement to SARS does not mean that the person thereby becomes subject to tax. The only effect of reporting an arrangement is that SARS will be notified of a transaction which it may be consider to be suspect from a tax perspective and enable SARS to investigate the transaction at an early stage.

What happens if a person does not inform SARS of an arrangement that is reportable? In terms of s212 of the TAA, a person who fails to disclose the information in respect of a reportable arrangement is liable to a penalty for each month that the failure continues (limited to 12 months). The amount

continue

of the penalty may be doubled or even tripled, depending on the amount of the anticipated tax benefit realised by the participant.

The SARS Notice raises a number of issues which we will consider in greater detail in our upcoming Tax Alerts.

Ben Strauss

SARS CLAMPS DOWN ON SHARE BUY BACKS FOLLOWED BY THE ISSUE OF SHARES

In practice taxpayers often enter into arrangements in terms of which a company buys back its own shares held by certain shareholders, and immediately thereafter issues new shares to new shareholders. This practice has long caused tax avoidance concerns for the South African Revenue Service (SARS), as it could circumvent the payment of capital gains tax (CGT) by the shareholder whose shares are bought back.

For example, company A holds shares in company B. Company A wishes to sell these shares to company C. Rather than entering into a sale of shares agreement with company C, company A opts to enter into a share buy back agreement with company B. Immediately thereafter, company C enters into a subscription agreement with company B.

The benefits of entering into the latter arrangement is that company A receives an exempt dividend from company B, and is not liable for CGT on the disposal of the shares to company B to the extent of the dividend. Similarly, company C is not liable for any tax in respect of the subscription for shares in company B and company B is not liable for CGT in respect of the issue of shares. One is therefore dealing with a very tax efficient and favourable arrangement for all parties concerned - except for SARS.

The risk is that SARS may view the share buy back and subsequent issue of shares as a disguised sale between company A and company C.

On 16 March 2015, SARS issued Government Notice No 38569 (Notice), in terms of which the following arrangement has been identified as a 'reportable arrangement' for purposes of s35 and s36 of the Tax Administration Act, No 28 of 2011 (TAA):

Any arrangement in terms of which-

(a) a company buys back shares on or after the date of publication of this notice from one or more shareholders for an aggregate amount exceeding R10 million; and

(b) that company issued or is required to issue any shares within 12 months of entering into that arrangement or of the date of any buy back in terms of that arrangement.

The effect of the Notice is that any share buy back and issue arrangement which falls within the ambit of the Notice now places a disclosure obligation on any 'participant' of information in respect of the 'arrangement' for purposes of Part B of Chapter 4 of the TAA. The 'participant' must disclose certain information within 45 business days of the 'arrangement' qualifying as a 'reportable arrangement' for purposes of the TAA, or must disclose the information within 45 days from the date of becoming a 'participant' to that 'reportable arrangement'.

Section 38 of the TAA sets out the information that needs to be submitted to SARS in relation to the 'reportable arrangement', which information must be submitted in the prescribed form and manner, and by the date specified, and must be as follows:

- a detailed description of all the steps and key features of the 'arrangement', including, in the case of an 'arrangement' that is a step or part of a larger 'arrangement', all the steps and key features of the larger 'arrangement';
- a detailed description of the assumed 'tax benefits' for all 'participants', including tax deductions and deferred income;
- the names, registration numbers and registered addresses of all 'participants';
- a list of all agreements of the 'arrangement'; and
- any financial model that embodies the projected tax treatment of the 'arrangement'.

Section 212 of the TAA previously stated that a 'participant' who fails to disclose the information in respect of a 'reportable arrangement', as required by s37 of the TAA, is liable for a penalty for each month that the failure continues (limited to 12 months), in the amount of:

- R50,000 in the case of a 'participant', other than the 'promotor' (ie the person principally responsible for organising, designing, selling, financing or managing the 'arrangement'); or
- R100,000 in the case of the 'promotor'.

The section further stated that the amount of the penalty is double if the amount of the anticipated tax benefit for the 'participant' due to the 'arrangement' exceeds R5 million and tripled if the benefit exceeds R10 million. However, the Notice

continue

has now amended the TAA by causing any arrangement referred to in s35(1) of the TAA to be an excluded 'arrangement', as contemplated in s36 of the TAA, if the aggregate tax benefit which is or may be derived from that 'arrangement' by all 'participants' to that 'arrangement' does not exceed R5 million. Thus, the Notice does provide some relief in respect of share buy back and issue transactions.

Taxpayers should bear in mind that s234 of the TAA makes it a criminal offence to wilfully and without just cause fail or neglect to disclose to SARS any material facts which should have been disclosed under the TAA or to notify SARS of anything which the person is required to notify SARS of under a tax act. If a person is convicted of such criminal offence, the person is subject to a fine or imprisonment for a period not exceeding two years.

Mareli Treurnicht

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

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

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

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

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

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

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

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

Nicole Paulsen
Associate
T + 27 (0)11 562 1386
E nicole.paulsen@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
Cliffe Dekker Hofmeyr is a member of DLA Piper Group, an alliance of legal practices.

DLA CLIFFE DEKKER HOFMEYR