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TAX & EXCHANGE CONTROL **ALERT**

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CLIFFE DEKKER HOFMEYR

INCORPORATING **KIETI LAW LLP, KENYA**

Swings and roundabouts of deregulation: Guidance issued on section 9K disposals following foreign re-listing of securities

Section 9K provides for a deemed disposal and reacquisition of securities held by a natural person or trust, where such securities are delisted from a South African exchange and relisted on a foreign exchange.

Agility in capital markets, including the ability for companies to easily raise capital from as broad a range of sources as possible, is a major positive for the ease of doing business in a country. South Africa is facing a constrained economic space, exacerbated by the effects of the COVID-19 pandemic. In this environment, listed companies may seek more liquid capital markets in foreign jurisdictions. Allowing companies to delist from a South African exchange and re-list their securities on a foreign exchange enables these companies to access fresh capital, while retaining local business operations.

Since the February 2020 Budget, the South African Government has undertaken a programme of modernising the exchange control regime. Section 9K of the Income Tax Act 58 of 1962 (Act) was introduced as part of these reforms. Section 9K provides for a deemed disposal and reacquisition of securities held by a natural person or trust, where such securities are delisted from a South African exchange and relisted on a foreign exchange. Its enactment was accompanied by a liberalisation of the requirement to obtain South African Reserve Bank (SARB) approval for the export of capital in the form of securities, where a delisting from a South African exchange and re-listing on a foreign exchange occurs.

The South African Revenue Service recently released Issue 8 of Interpretation Note 43 – Circumstances in which certain amounts received or accrued from the disposal of shares are deemed to be of a capital nature (IN43). The focus of this interpretation note remains section 9C of the Act, but has now been updated to provide guidance on the deemed disposal and re-acquisitions to take place under the newly introduced section 9K.

The provisions of section 9K

Section 9K(1) provides that where a natural person or trust holds a security in a company that is listed on an exchange, as defined in section 1 of and licenced under section 9 of the Financial Markets Act 19 of 2012, and that security is subsequently delisted and relisted on a foreign exchange, then such natural person or trust will be treated as having:

- disposed of that security for an amount equal to the market value of that security (i.e. price which could be obtained upon a sale of that security between a willing buyer and a willing seller dealing at arm's length in an open market) on the day on which the security is listed outside of South Africa; and
- reacquired that security for an amount expenditure equal to the market value on that same day.

The effect of the deemed disposal and reacquisition depends on whether the security is held as a capital or revenue asset by the particular taxpayer. Should it be held as a revenue asset, then an income tax event will be triggered with either taxable income or a potentially deductible loss accruing to the taxpayer. Should the security be held as a capital asset, a capital gains tax event is triggered and, depending on the base cost of the relisted security in the taxpayer's hands and the market value of the security on the day of relisting, a capital gain or loss may arise.

Swings and roundabouts of deregulation: Guidance issued on section 9K disposals following foreign re-listing of securities...*continued*

The modernisation of the exchange control system and particularly reductions in the scope of activities that require SARB approval is a welcome development. It ought to enable businesses to react to the needs of the day faster, having to traverse fewer regulatory hurdles.

Interpretation Note 43 and section 9K

While IN43 mainly deals with the interpretation of the deeming provisions in section 9C, Issue 8 includes guidance on the application of section 9K. It provides an authoritative, although non-binding, interpretation of the section 9K considerations to be applied where a natural person or trust holds a security which is delisted from a South African exchange and subsequently relisted on a foreign exchange.

IN43 provides guidance on the tax principles and related provisions of the Act to be considered for deemed disposals and reacquisitions under the provisions of section 9C. These same principles apply to the deemed disposal and reacquisition under section 9K.

As noted above, section 9K does not deem the disposal to be of a particular nature and therefore it may result in proceeds and expenditure of either a capital or revenue nature. Therefore, where section 9K applies the taxpayer must determine the nature of the deemed proceeds and expenditure in their hands regarding the relisted shares.

IN43 indicates that where section 9K(1) is triggered, section 9K(2) requires that the relisted security be treated as the same security as the delisted security for the purposes of section 9C(2). Section 9C(2) is also a deeming provision, which deems the proceeds or expenditure in relation to an equity share to be of a capital nature where that equity share is held by a taxpayer for three years or more.

It is important to note that section 9C(2) only applies to equity shares. Meaning that where an equity share, as defined in section 1 of the Act, is relisted on a foreign exchange, if the relevant shareholder has held that equity share for three years or longer, the deemed disposal under section 9K will result in capital proceeds.

Therefore, where any other type of listed securities is relisted the taxpayer must apply ordinary tax principles on capital and revenue to determine how to account for the deemed accrual and expenditure.

Comment

The modernisation of the exchange control system and particularly reductions in the scope of activities that require SARB approval is a welcome development. It ought to enable businesses to react to the needs of the day faster, having to traverse fewer regulatory hurdles. This will lead to better economic outcomes for South Africa at large.

With the introduction of section 9K, government may be seeking to cushion the potential unforeseen consequences of this deregulation by requiring natural persons and trusts to account for a deemed tax where a relisting of previously South African securities takes place.

However, this means that natural persons and trusts may have to pay a dry tax where securities they hold are relisted on a foreign exchange, as there will be no actual proceeds to fund this cost. Fortunately, taxpayers who bear this cost will enjoy the benefit of an increase in the base cost of their relisted securities, leading to a reduced tax cost when the securities are later disposed of or sold.

Tsanga Mukumba overseen by Louis Botha

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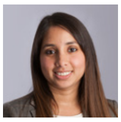

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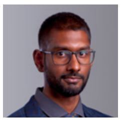

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BBBEE STATUS: LEVEL ONE CONTRIBUTOR

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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