

BINDING PRIVATE RULING: BPR 356

DATE: 25 November 2020

ACT : INCOME TAX ACT 58 OF 1962 (the Act)
SECTION : SECTIONS 1(1) – DEFINITIONS OF “EQUITY SHARE”, “CONTROLLING GROUP COMPANY” AND “GROUP OF COMPANIES”; 8E(1) – DEFINITIONS OF “EQUITY INSTRUMENT”, “FINANCIAL INSTRUMENT” AND “HYBRID EQUITY INSTRUMENT”; 8EA(1) – DEFINITIONS OF “ENFORCEMENT RIGHT”, “OPERATING COMPANY”, “PREFERENCE SHARE”, “QUALIFYING PURPOSE” AND “THIRD-PARTY BACKED SHARE”; 8EA(2); AND 8EA(3)
SUBJECT : PREFERENCE SHARE – HYBRID EQUITY INSTRUMENT AND THIRD-PARTY BACKED SHARE

Preamble

This binding private ruling is published with the consent of the applicant(s) to which it has been issued. It is binding between SARS and the applicant and any co-applicant(s) only and published for general information. It does not constitute a practice generally prevailing.

1. Summary

This ruling determines whether the preference shares issued by the applicant are hybrid equity instruments or third-party backed shares.

2. Relevant tax laws

In this ruling references to sections are to sections of the Act applicable as at 19 November 2020. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of –

- section 1(1) – definitions of “equity share”, “controlling group company” and “group of companies”;
- section 8E(1) – definitions of “equity instrument”, “financial instrument” and “hybrid equity instrument”;
- section 8EA(1) – definitions of “enforcement right”, “operating company”, “preference share”, “qualifying purpose” and “third-party backed share”;
- section 8EA(2); and
- section 8EA(3).

3. Parties to the proposed transaction

The applicant: A resident company

Company A: A resident company

Company B: A resident company

4. Description of the proposed transaction

The applicant carries on no trade and its sole purpose is to act as a conduit for dividends. The applicant entered into an agreement with Company A, in terms of which the applicant issued preference shares to Company A in order to fund the acquisition of shares in Company B.

A trust is the 100% shareholder of the applicant and the trust beneficiaries are the members of a specified community.

In terms of the agreement any distributions made by Company B to the applicant must be on-distributed as follows:

- 90% of the amount to Company A; and
- 10% to the trust.

These dividend distribution ratios remain in place for as long as the preference shares are in issue.

As security for the applicant's obligations under the agreement, the trust has provided Company A with:

- A first ranking share pledge over the trust's shares in the applicant;
- A cession of the trust's loans to the applicant; and
- A limited guarantee by the trust in favour of Company A.

Company A has a tax indemnity in respect of any tax that may arise in the hands of the company on dividends paid to it in respect of the preference shares.

The indemnity period is aligned with the terminal redemption date, being 17 years from the issue date of the preference shares even if the agreement is terminated or the preference shares are redeemed earlier.

The applicant will declare a preference share dividend to Company A in the near future.

5. Conditions and assumptions

This binding private ruling is subject to the additional condition that the terms of the preference shares remain unchanged.

6. Ruling

The ruling made in connection with the proposed transaction is as follows:

- a) The preference shares are not hybrid equity instruments as defined in section 8E. Accordingly, section 8E will not apply in respect of future preference dividends declared and paid by the applicant; and
- b) The preference shares do not constitute third-party backed shares as defined in section 8EA. Accordingly, section 8EA will not apply in respect of future preference dividends declared by the applicant.

7. Period for which this ruling is valid

This binding private ruling is valid for a period of five years from 19 November 2020.

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