South African Revenue Service

BINDING CLASS RULING: BCR 069

DATE: 23 October 2019

ACT	**:**	**INCOME TAX ACT 58 OF 1962 (the Act)**
SECTION	**:**	**SECTIONS 1(1) – DEFINITION OF "DIVIDEND", 8C, 10(1)(*k*)(i), 11(*a*), 23(*g*), 23H AND PARAGRAPHS 13(1)(*a*)(iiB) AND 38 OF THE EIGHTH SCHEDULE TO THE ACT**
SUBJECT	**:**	**EMPLOYEE SHARE OWNERSHIP PLAN**

Preamble

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

1. Summary

This ruling determines the income tax consequences for the applicant, employer companies, employees of the employer companies and the trusts through which employee share schemes will be implemented.

2. Relevant tax laws

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule to the Act applicable as at 16 April 2019. 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) – definition of "dividend";
- section 8C;
- section 10(1)(*k*)(i);
- section 11(*a*);
- section 23(*g*);
- section 23H;
- paragraph 13(1)(*a*)(iiB); and
- paragraph 38.

3. Class

The class members to whom this ruling will apply are –

- the employee share ownership trusts listed in **4**;
- the employer companies; and
- the employees of the applicant and the employees of the employer companies who are participants in share incentive schemes administered by the employee share ownership trusts.

4. Parties to the proposed transaction

The applicant:	A listed resident company
The trusts:	Two resident employee share ownership trusts
Employer companies:	Companies in the same group of companies as the applicant
Participants:	The employees of the applicant and the employees of the employer companies who are participants in share incentive schemes administered by the trusts

5. Description of the proposed transaction

The applicant intends to implement new share incentive schemes which will be administered by the trusts. The participants of the employee share schemes are the employees of the applicant and of the other employer companies.

The objects of the trusts are to acquire, subscribe for, and be registered in the securities registers as the legal owners of, and to dispose and deal with, the shares (plan shares), in terms of the share incentive schemes (the plans). The trusts will operate primarily as conduits for the acquisition of the shares by participants who will eventually be entitled to these shares in terms of the rules. These rules are the employee share option plan (ESOP) and the long-term incentive plan (LTIP) which will apply to both trusts.

The plan shares will be the ordinary shares of the applicant or another class of shares which may be designated as such by the rules. The shares will not be limited to specified amounts as respects their rights to receive either dividends or returns of capital.

The trusts will be funded by the applicant or another employer company in the same group of companies as the applicant with grants made to the trusts in order for the trustees to –

- administer the plans in terms of the rules;
- acquire or subscribe for the plan shares in relation to awards granted to the participants as prescribed by the rules;
- defray the costs and expenses arising out of and in connection with the administration of the trusts, the execution of their duties and powers in terms of the trust deeds of the trusts and the giving effect to of the objects of the trusts; and

- otherwise give effect to the plans, the trust deed and objects of the trusts.

The trustees will have the authority to acquire or subscribe for shares in terms of or for the purposes of any plans and to pay distributions received on any shares acquired for purposes of the plans to the participants who are unconditionally entitled to the amounts in terms of the rules. The trustees will also be obliged to deliver the shares to the participants in terms of the rules.

The rules will provide for awards to be granted to eligible participants, being conditional share awards and forfeitable share awards. A participant granted a conditional share award will not have any rights, conditional or otherwise, to the shares prior to settlement (when registering the participant as owner of the shares in the securities register on vesting of the shares).

The conditional share award will lapse immediately if the participant ceases to be an eligible employee prior to settlement due to a reason listed as an “ineligible termination” reason. These are terminations due to resignation, dismissal for misconduct, proven poor performance, dishonest or fraudulent conduct, or abscondment.

However, the portion of the conditional share award which has not vested will vest (unless the trustees determine otherwise) if the termination is due to a reason listed as an “eligible termination” reason. These are terminations due to death, retirement, retrenchment, ill-health, injury or disability, or a participant’s employer company ceasing to be part of the same group of companies as the applicant. In case of such terminations, the unvested portion of the award will vest on the date the employment terminated.

The remuneration committee will be entitled, but not obliged, to require that a trust holds a share in respect of any conditional share award that has been granted. Any such shares held by a trust shall be beneficially owned by the trust until disposed of by the trust. However, it is understood that this will only happen in exceptional cases. In most instances the trusts will only acquire the shares on settlement date.

The remuneration committee may direct upon vesting that a payment be made by an employer company for the payment of a dividend equivalent in cash following each vesting date. Vesting in relation to an award will be defined in the rules to mean that the participant is entitled to registration of a share in his / her name in the securities register or payment of cash. Should vesting take place, the award will also become unrestricted in terms of section 8C.

On vesting, the relevant employer company must procure the settlement of the shares on the participant through the trust, free of any further restrictions. Each trust will be entitled on vesting to dispose of enough shares to enable it to pay the employees’ tax and to satisfy any other withholding obligation then due. No consideration will be payable by a participant on the vesting of the conditional share award.

The participant of a forfeitable share award will become the beneficial owner of each share from the acceptance date until the share is settled. There are two types of forfeitable share awards, namely annual discretionary forfeitable share awards and on-appointment forfeitable share awards. Both of these types of awards will be subject to the same rules. The difference between these two types of awards is the date on which the shares are awarded and the section 8C vesting date.

On-appointment share awards may be made to new external or internal appointments at specified grade level or "role size". These awards can vest in tranches or at a certain point, depending on the type of appointment.

Annual discretionary share awards may be made on special nomination and based on specific criteria. These share awards vest in full on the third anniversary. These awards are part of the LTIP. The shares forming the subject matter of a forfeitable share award must be registered in the name of the relevant trust up to settlement.

Settlement or vesting of shares will occur on the later date on which the -

- participant has fulfilled the employment conditions as specified in the award letter; and
- the trustees determine that the relevant performance condition has been fulfilled.

The forfeitable share award is designed to ensure that the participants become the beneficial owners of the shares from acceptance date. The rules to the scheme state that beneficial ownership transfers to the participant on acceptance date and the participants will be entitled to the ordinary distributions in terms of the forfeitable share awards. In terms of the rules, the participants do not have the right to participate in special distributions and certain repurchases in terms of section 48 of the Companies Act 71 of 2008. However, trustees may in their discretion make special distributions, which could be distributions *in specie* or special dividends in cash, or returns of capital excluding issues of shares. The shares can also lapse where the performance condition relating to an award has not been fulfilled in whole or in part.

Even though participants will be the beneficial owners of shares after the award date, they are prohibited from disposing of the shares until settlement date. The benefits terminate if the conditions are not met during the vesting period. Thus, by the nature of a forfeitable share award, the beneficial ownership will pass on the acceptance date and the participant will enjoy the dividends and voting rights in respect of the shares from that date, and the right to dispose of the shares and the right to participate in special distributions will be restricted from acceptance to vesting date.

The participant will, however, forfeit the award (prior to settlement date) in the event of ineligible termination. Ineligible terminations are terminations due to resignation, dismissal for misconduct, proven poor performance, dishonest or fraudulent conduct, or abscondment.

On the section 8C vesting date, those shares held by the trust on behalf of a participant will be registered in the name of the participant, except for the shares that must be sold to pay employees' tax and to satisfy other withholding obligations. No consideration will be payable by the participant on the vesting of the forfeitable share award.

Once the share has vested, the risk of forfeiture will terminate.

6. Conditions and assumptions

This binding class ruling is not subject to any additional conditions and assumptions.

7. Ruling

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

a) The contributions made by the applicant or an employer company to the trusts to acquire or subscribe for shares in the applicant and to pay for scheme administration costs incurred by the trusts, will be deductible under section 11(*a*) read with section 23(*g*), provided that only contributions made by an employer company in respect of persons directly employed by it will be so deductible.

b) Section 23H will apply to those contributions made by the applicant or employer company to the trust in respect of the forfeitable share awards. The years prior to the allocation of the share award must not be taken into account in determining the apportionment method provided for under section 23H(1).

c) Section 23H will not apply to expenditure in respect of any share that forms the subject-matter of a conditional share award, on condition that the share is acquired by a trust and vested in a participant in the same year of assessment or awarded within six months after the end of the year of assessment during which the expenditure was incurred (see paragraph (*aa*) of the proviso to section 23H(1)(*b*)).

d) The vesting of the shares on the award date in terms of the forfeitable share award will be regarded as a disposal under paragraph 11(1)(*d*). However, under section 8C vesting will only take place after the restrictions have been lifted. Under paragraph 13(1)(*a*)(iiB), the time of disposal will be deferred until the date that the shares vest for purposes of section 8C.

e) The participants and the trustees of the trusts will be acting at arm's length and the Rnil consideration paid by the participants for the transfer of the shares under the forfeitable share award will be an arm's length price. Paragraph 38 will thus not apply.

f) The vesting of the shares in terms of the conditional share awards, whether the trust acquires the shares prior to vesting date or not, will result in a disposal under paragraph 11(1)(*d*). The time of disposal will remain subject to paragraph 13(1)(*a*)(iiB).

g) The participants and the trusts will be acting at arm's length and the Rnil consideration paid by the participants for the transfer of the shares in terms of the conditional share awards will be an arm's length price. Paragraph 38 will thus not apply.

h) Ordinary distributions which are dividends, as defined in section 1(1), received by the participants who are beneficially interested in the shares, as contemplated in section 1 of the Companies Act 71 of 2008, will be exempt from normal tax under section 10(1)(*k*)(i), subject to paragraph (*jj*) of the *proviso* to section 10(1)(*k*)(i). The dividends will be subject to dividends tax.

8. Period for which this ruling is valid

This binding class ruling is valid for a period of five years from 16 April 2019.

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SOUTH AFRICAN REVENUE SERVICE