BINDING PRIVATE RULING: BPR 113

DATE: 15 March 2012

ACT	**:**	**INCOME TAX ACT, NO. 58 OF 1962 (the Act)**
SECTION	**:**	**SECTIONS 11(*a*), 23(*g*) and 23H**
SUBJECT	**:**	**EXPENDITURE ASSOCIATED WITH BROAD BASED BLACK ECONOMIC EMPOWERMENT**

1. Summary

This ruling deals with the deductibility of expenditure incurred in attaining the requisite points per the scorecard prescribed in association with Broad Based Black Economic Empowerment.

2. Relevant tax laws

This is a binding private ruling issued in accordance with section 76Q of the Act.

In this ruling legislative references to sections are to sections of the Act applicable as at 24 August 2011 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This ruling has been requested under the provisions of –

- section 11(*a*);
- section 23(*g*); and
- section 23H.

3. Party to the proposed transaction

The Applicant: A private company that is incorporated in and a resident of South Africa

4. Description of the proposed transaction

From a compliance and commercial perspective the Applicant requires Black Economic Empowerment (BEE) points in order to conduct business in the South African environment. As a multinational, however, the Applicant is bound by the policies of its principals, one of which states that equity will not be sold in any of its subsidiaries.

In order to address the ownership component of the BEE scorecard prescribed by the Broad Based Black Economic Empowerment Act the Applicant proposed an alternate approach by means of an Equity Equivalent programme (EE programme).

The proposed EE programme entails the investment of 4% of the Applicant's annual turnover, over a period of seven years, into selected qualifying small black owned Independent Vendors (the Vendors). This investment includes financial, infrastructure, dedicated personnel, marketing, sales and intellectual support to these Vendors.

The implementation of the EE programme will enable the Applicant to receive the full 20 BEE points per annum for the ownership component of the BEE scorecard, subject to the Applicant meeting annual agreed milestones with the Department of Trade and Industry (DTI). The attainment of the 20 BEE points will enable the Applicant to attain level 2 compliance as per the said BEE scorecard.

The necessary approval for the EE programme was granted by the DTI and the Applicant entered into its first Equity Equivalent Investment Agreement with the DTI in 2011 and received the relevant BEE points upfront. This agreement with the DTI expires eight to nine months after the Applicant's year-end and may be renewed on an annual basis. The BEE points for the ownership component will in future be granted by the DTI on an annual basis following a review of the Applicant. The BEE points for ownership are, therefore, only valid for a year and future agreements need to be signed in order for the Applicant to qualify for the BEE points.

The proposed transaction involves the selection of a minimum of five black owned and black managed Independent Vendors that will meet a set of pre-determined criteria. They will not necessarily form part of the Applicant's existing value chain.

The programme consists of the Vendors incurring expenditure in respect of infrastructure, recruitment and employment of black graduates, relevant sales and marketing, software development, training and skills development, travelling and other external services that will include but will not be limited to legal, accounting, tax, advertising, public relations and management consulting expenditure.

These Vendors will be reimbursed for the agreed and approved expenditure incurred (the Applicant's EE expenditure), by requesting purchase orders via the Applicant's global accounting system, and upon presentation of the relevant invoices, the Applicant will settle such expenditure. The EE expenditure will be incorporated under a separate cost centre and paid for via the Applicant's normal payment processes. The budget allocated to the separate cost centre will be the agreed 4% of the Applicant's annual turnover.

The management and governance of the EE programme will thus be incorporated within the Applicant's accounting framework to leverage the current internal control infrastructure and system resources.

The Applicant will appoint managers for each Vendor, namely, a technology specialist, a finance manager and a programme manager, to manage the Vendor and implement the EE programme.

The Applicant will not subscribe for equity in the companies of these Vendors.

A separate contract will be drafted and entered into with each Vendor.

The terms of the contracts with these Vendors will be reviewed annually based on the renewal or granting of the annual BEE ownership point allocation by the DTI.

5. Conditions and assumptions

This ruling is subject to the conditions and assumptions that –

- the ruling is only made in respect of the EE expenditure incurred in years two to seven; and
- the contracts to be entered into between the Applicant and the DTI, for years two to seven, will be on the same terms and conditions as the Equity Equivalent Investment Agreement entered into in 2011 (year one) between the Applicant and the DTI.

6. Ruling

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

- The Applicant may claim the EE expenditure in years two to seven as a deduction under section 11(*a*), read with section 23(*g*).
- The deduction of the EE expenditure, in years two to seven, will be spread in terms of section 23H.

7. Period for which this ruling is valid

This binding private ruling is valid for a period of seven (7) years from August 2011.

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