

BINDING PRIVATE RULING: BPR 241

DATE: 13 June 2016

ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
SECTION : SECTIONS 1(1) – DEFINITION OF “GROSS INCOME”, 10(1)(k), 24C, 25B OF THE ACT AND PARAGRAPHS 11(1)(d), 13(1)(a)(iiA), 38, 75 AND 80 OF THE EIGHTH SCHEDULE TO THE ACT
SUBJECT : AWARD RECEIVED FOR A BLACK ECONOMIC EMPOWERMENT (BEE) TRAINING INITIATIVE

1. Summary

This ruling determines the income tax and capital gains tax consequences for the recipient of an award of participation units in a trust received in pursuance of a BEE training initiative and its entitlement to claim a section 24C allowance against the award.

2. Relevant tax laws

This is a binding private ruling issued in accordance with section 78(1) and published in accordance with section 87(2) of the Tax Administration Act No. 28 of 2011.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule thereto applicable as at 26 January 2016. 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 the provisions of –

- section 1(1) – definition of “gross income”;
- section 10(1)(k);
- section 24C;
- section 25B;
- paragraph 11(1)(d);
- paragraph 13(1)(a)(iiA);
- paragraph 38;
- paragraph 75; and
- paragraph 80(1).

3. Parties to the proposed transaction

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| The Applicant: | A private company incorporated in and a resident of South Africa |
| Trust A: | A trust established in and a resident of South Africa of which the Applicant is a beneficiary |
| Company A: | A listed company incorporated in and a resident of South Africa |
| SPV Co: | A private company incorporated in and a resident of South Africa |
| BEE Co: | A private company incorporated in and a resident of South Africa that is the majority shareholder of the Applicant |
| Company B: | A public company incorporated in and a resident of South Africa within the same group of companies as Company A |

4. Description of the proposed transaction

Company A implemented a BEE initiative. For this purpose SPV Co was incorporated. SPV Co acquired 10% of the issued ordinary shares (shares) of Company A at market value. The acquisition of the shares was funded by third party funding. The funding was to be repaid from dividends received by SPV Co from the shares and the proceeds from the disposal of some or all of the shares.

Upon settlement of the funding SPV Co is required to distribute the remaining shares, if any, as a dividend *in specie* to its shareholders.

Three trusts with specific BEE aims were established as the shareholders of SPV Co. Trust A holds 49% of the ordinary shares in SPV Co. Trust A was established to facilitate the participation of qualifying business partners of Company A (business partners) in the BEE initiative.

In terms of the deed of Trust A (the deed):

- a) A number of units were created, conferring on their holders *pro rata* entitlements to participate in the net assets of Trust A (trust fund).
- b) The trustees are obliged to make an *in specie* distribution of the trust fund.
- c) The trust fund vests in the holders of the units on the same date on which SPV Co distributes the remaining shares to Trust A and the other shareholders (distribution date).

BEE Co and Company B incorporated the Applicant for the purpose of recruiting, appointing and training individuals to become economically independent (training initiative).

The Applicant received an award of units from Trust A. The award was made unconditional, free of charge and subject to the terms and conditions of the deed and it entitles the Applicant to participate in the trust fund.

The memorandum of incorporation of the Applicant and the shareholders agreement entered into by the Applicant's shareholders limit the activities of the Applicant to that of conducting the training initiative and provide that the benefits available from participation in the trust fund are used only for this purpose.

The Applicant will not operate to generate any profit or earn any income for its shareholders. Any subsequent amounts generated through its operations must be used in full for the training initiative.

SPV Co settled its funding obligation and subsequently made an *in specie* distribution of the remaining shares to its shareholders.

In accordance with the terms of the deed a number of the shares proportionate to the Applicant's unit-holding vested in the Applicant on the distribution date.

The Applicant's operational activities will be funded by the benefits accruing to it pursuant to the receipt of the *in specie* distribution of the shares. The Applicant will dispose of a sufficient number of shares annually to fund its operations.

Until such time as the Applicant is in a position to dispose of some of the shares its shareholders or a company within the group will provide bridging finance to the Applicant. This financing will be settled by the Applicant from the proceeds realised from the disposal of the shares.

5. Conditions and assumptions

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

6. Ruling

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

- a) The award of the Units gives rise to an amount that must be included in the gross income of the Applicant.
- b) The Applicant will qualify for an allowance in respect of future expenditure under section 24C against the amount referred to in a) to be included in gross income. The amount of the allowance in each year of assessment remains subject to the discretion of SARS.
- c) The shares to be distributed to the Applicant and any surplus cash vesting in the Applicant will constitute income in the form of a dividend *in specie*, which will be regarded as having accrued to the Applicant under section 25B(1). The shares and surplus cash will retain their nature as a dividend. The market value of the shares and the cash distribution must be included in the gross income of the Applicant in the year of assessment in which the distribution is made.
- d) The shares and any surplus cash vesting in the Applicant as a dividend *in specie* will be exempt under section 10(1)(k).

- e) Trust A will be deemed to have acquired the shares distributed to it by SPV Co (and which include the Applicant's shares) on the distribution date for an expenditure equal to the market value of those shares on that date, for purposes of paragraph 75(1)(b). The expenditure must be treated as an amount actually incurred for the purposes of paragraph 20(1)(a).
- f) Trust A must be treated as having disposed of the shares to the Applicant immediately upon receipt of those shares as a dividend *in specie*, for purposes of paragraph 11(1)(d), read with paragraph 13(a)(iiA).
- g) Paragraph 38 will apply to the vesting and resultant disposal of the shares. Therefore Trust A will be deemed to have disposed of the shares for proceeds equal to the market value of those shares on the distribution date and the Applicant will be deemed to have acquired the shares for a cost equal to the market value of those shares on the distribution date.
- h) No capital gain will arise or be attributed to the Applicant for purposes of paragraph 80(1) on the basis that the shares will be treated as having been acquired at their market value and simultaneously treated as having been disposed of by Trust A at their market value.
- i) The cancellation of the units following the distribution of the shares and any surplus cash will not give rise to any capital gains tax in the Applicant.

7. Period for which this ruling is valid

This binding private ruling is valid for a period of 5 years from 26 January 2016.