

**BINDING PRIVATE RULING: BPR 304**

DATE: 20 June 2018

**ACT** : **INCOME TAX ACT 58 OF 1962 (the Act)**  
**SECTION** : **SECTIONS 1(1) – DEFINITIONS OF “CONTRIBUTED TAX CAPITAL” AND “DIVIDEND”, 8(4)(a), 19, 24J(4A), 36(11) – DEFINITION OF “EXPENDITURE” AND PARAGRAPHS 12A AND 20(1)(a) OF THE EIGHTH SCHEDULE TO THE ACT**  
**SUBJECT** : **DEBT REDUCTION AND SUBSEQUENT LIQUIDATION OF DEBTOR**

**1. Summary**

This ruling determines the income tax consequences of the settlement of a loan by way of set-off from the outstanding subscription price of a new issue of additional shares and the subsequent liquidation of the issuer.

**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 28 of 2011.

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 29 August 2017. 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) - the definitions of “contributed tax capital” and “dividend”;
- section 8(4)(a);
- section 19;
- section 24J(4A);
- section 36(11) – definition of “expenditure”;
- paragraph 12A; and
- paragraph 20(1)(a).

**3. Parties to the proposed transaction**

The applicant: A resident company

The co-applicant: A resident company that is the majority shareholder in the applicant

Trusts A, B and C: Three resident trusts, which are minority shareholders in the applicant

Companies D and E: Two resident companies, which are minority shareholders in the applicant

#### **4. Description of the proposed transaction**

The co-applicant holds 74% of the shares in the applicant. Trusts A, B and C and Company D and E (the minority shareholders) hold the remaining 26% in varying percentages.

The applicant holds a 26% undivided share in the assets of an unincorporated mining and production joint venture established between the applicant and co-applicant (the JV).

The applicant met its funding obligations towards the JV, both for operational and capital expenditure purposes, by utilising the monies advanced to it by the co-applicant on loan account. Interest is charged on the loan and capitalised interest amounts to roughly a quarter of the total amount outstanding.

Because of operational and economic difficulties, the applicant has accumulated a significant assessed loss and unredeemed capital expenditure balance under section 36. The mine which operated under the JV is currently in care and maintenance.

The applicant and co-applicant want to dispose of their respective interests in the assets of the JV to a non-connected third party. The sales price for the complete mine (including all the mining assets) operated through the JV provisionally agreed to, is less than 10% of the total loan balance owing to the co-applicant.

After the disposal of the mine the applicant will have no assets on its balance sheet except for the disposal proceeds. Upon completion of the disposal, the shareholders of the applicant wish to liquidate the applicant.

The transaction steps will be as follows:

- The co-applicant will waive its claim against the applicant for an amount representing accrued interest on its loan to the applicant.
- The applicant will receive its share of the sale proceeds from the disposal of the assets of the JV, put aside a portion of the proceeds for the repurchase of the minority shareholder's shares and use the remaining portion to repay part of the principal debt owing to the co-applicant.
- The co-applicant will subscribe for ordinary shares of the applicant for a subscription consideration equal to the applicant's principal debt owing to the co-applicant after the repayment of the sale proceeds and waiver of the capitalised interest.
- The subscription consideration owing by the co-applicant to the applicant will be settled by way of set-off against the remaining principal debt owing by the applicant to the co-applicant on loan account.
- The applicant will enter into a share buy-back agreement with the minority shareholders for the repurchase of the applicant's shares.
- The applicant will commence liquidation steps.

#### **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 payment of the share subscription price by way of set-off against the co-applicant's loan will qualify as expenditure actually incurred for the acquisition of the applicant's ordinary shares for purposes of paragraph 20(1)(a).
- b) The fully paid subscription price for the applicant's shares will qualify as "contributed tax capital" as defined in section 1(1).
- c) The payment by the applicant to the co-applicant in settlement of its loan owing to the co-applicant by way of set-off against its subscription claim, will be regarded as consideration for the reduction of the debt as contemplated in section 19 and paragraph 12A.
- d) Pursuant to the interest levied in respect of the loan by the co-applicant to the applicant being irrecoverable, the amount of interest claim against the applicant written-off by the co-applicant will be an amount included in the applicant's income by virtue of section 19 read with section 8(4)(a). The co-applicant will be entitled to a deduction of the amount of interest which will become irrecoverable under section 24J(4A)(a).
- e) The amount of the proceeds received by the minority shareholders that exceeds the subscription price paid for the acquisition of the shares will constitute a "dividend" as defined in section 1(1). Dividends received by trusts A, B and C will be subject to dividends tax at the rate of 20%. Dividends received by Companies D and E will be exempt under section 64F(1)(a).

**7. Period for which this ruling is valid**

This binding private ruling is valid for a period of three years from 29 August 2017.

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SOUTH AFRICAN REVENUE SERVICE**