

BINDING PRIVATE RULING: BPR 340

DATE: 27 February 2020

ACT : INCOME TAX ACT 58 OF 1962 (the Act)
SECTION : SECTIONS 1(1) – DEFINITIONS OF “DIVIDEND” AND “GROSS INCOME”, 55(1), 58(1) AND PARAGRAPHS 11(1)(a), 11(2)(b) AND 38(1) OF THE EIGHTH SCHEDULE TO THE ACT
SUBJECT : SHARE BUY-BACK AT NOMINAL VALUE

Preamble

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

1. Summary

This ruling determines the income tax and donations tax consequences of a share-buy-back at nominal value pursuant to a proposed cancellation agreement.

2. Relevant tax laws

In this ruling references to sections are to sections of the Act and references to paragraphs are to paragraphs of the Eighth Schedule to the Act applicable as at 27 September 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) – definitions of “dividend” and “gross income”;
- section 55(1);
- section 58(1);
- paragraph 11(1)(a);
- paragraph 11(2)(b); and
- paragraph 38(1).

3. Parties to the proposed transaction

The applicant: A resident company

The co-applicant: A resident trust

Company A: A resident company

Company B: A resident company

4. Description of the proposed transaction

The applicant's shares are held as follows –

- 44.94% by Company A issued at a total subscription price of R1.00;
- 34.83% by the co-applicant issued at a total subscription price of R1.00; and
- 20.23% by Company B issued at a total subscription price of R1.00.

The subscription prices at which shares were issued to the co-applicant and Company B were determined by the board of directors of the applicant to be adequate consideration for purposes of section 40 of the Companies Act 71 of 2008 ("Companies Act").

The shares issued to the co-applicant were issued in terms of an employee share ownership programme in accordance with the Broad-Based Black Economic Empowerment ("BBBEE") Codes of Good Practice in terms of the Broad-Based Black Economic Empowerment Act 53 of 2003. The main objective of the establishment of the co-applicant was to provide sustainable equity-based participation in the applicant for the benefit of the beneficiaries of the co-applicant; to ensure that the business of the applicant remained sustainable and well-managed; and for the applicant to improve its ownership by black people in order to improve the applicant's Black Economic Empowerment rating.

The co-applicant has not yet appointed beneficiaries and the applicant has not declared a dividend since the co-applicant and Company B became shareholders.

The share subscription transaction involving the co-applicant was incorrectly implemented. The intention was that the co-applicant should acquire and hold the shares in the applicant in a nominee capacity only, on behalf of scheme beneficiaries yet to be appointed, but the transaction was structured and implemented in such a manner that the co-applicant holds the shares in the applicant as a discretionary trust only.

On the basis that the transaction was incorrectly structured and implemented, the applicant and co-applicant propose to unwind the transaction by entering into a restitution agreement aimed at terminating the subscription agreement previously entered into, and for each of them to be returned to the position prior to the implementation of the share subscription; and to then implement an employee share ownership plan in terms of which shares will be reserved for issue to qualifying black employees.

The restitution agreement will be effected by the applicant repurchasing all of its shares held by the co-applicant for a consideration of R1.00, which is the price at which the shares were issued. The applicant will cancel the repurchased shares and they will be returned to its authorised and unissued share capital in accordance with section 35(5) of the Companies Act.

Subsequent to the restitution transaction, the applicant will implement an employee share ownership plan in terms of which it will reserve shares in its authorised unissued share capital for allocation and issue, from time to time, to current and future qualifying black employees of the applicant at a subscription price to be determined by the board of directors of the applicant. The applicant will place restrictions on the vesting of the shares in qualifying employees and on transfer of the shares by the applicant to the employees.

5. Conditions and assumptions

This binding private ruling is subject to the following additional conditions and assumptions:

- a) The board of directors of the applicant must take a resolution authorising the repurchase of all the shares held by the co-applicant for a consideration of R1.00 in aggregate. The resolution of the board of directors must –
 - expressly state the reasons that necessitated the share repurchase and describe the proposed new structure that will be implemented subsequent to the implementation of the share repurchase; and
 - confirm that the share repurchase will reduce the contributed tax capital of the Applicant.
- b) The shareholders of the applicant must take a resolution approving the decision by the board of directors of the applicant authorising the applicant to repurchase all of the shares held by the co-applicant for consideration of R1.00.
- c) The trustees of the co-applicant must take a resolution authorising the repurchase of all of its shares held in the applicant for consideration of R1.00. The resolution of the trustees must expressly state the reasons that necessitated the share repurchase and the proposed new structure that will be implemented pursuant to the implementation of the share repurchase.
- d) The applicant must conclude, implement and give effect to the new employee share ownership plan within a period of 18 months from the date of the binding private ruling issued, or within such further period as may be approved by the Advance Tax Rulings Unit of SARS on application for an extension of the time-period for which this ruling is valid.

6. Ruling

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

- The share repurchase by the applicant of its shares from the co-applicant for a consideration of R1.00 will –
 - not constitute a disposal by the Applicant in terms of paragraph 11(2)(b);
 - constitute a disposal by the co-applicant in terms of paragraph 11(1)(a);
 - not, in the specific facts and circumstances, result in the application of paragraph 38(1) to the transaction;

- not give rise to a “dividend” as defined in section 1(1);
- not give rise to an inclusion in the “gross income” of the Co-applicant as defined in section 1(1);
- not give rise to a “donation” as defined in section 55(1); and
- not give rise to a deemed donation in terms of section 58(1).

7. Period for which this ruling is valid

This binding private ruling is valid for a period of 18 months from 27 September 2019.

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