

BINDING PRIVATE RULING: BPR 255

DATE: 30 November 2016

ACT : INCOME TAX ACT 58 OF 1962 (the Act)
SECTION : SECTIONS 8(4)(a), 19, AND PARAGRAPHS 12A AND 20(3)(a) OF THE EIGHTH SCHEDULE
SUBJECT : DEBT REDUCTION BY MEANS OF SET-OFF

1. Summary

This ruling determines the tax consequences relating to the settlement of shareholder funding loans owed to the shareholder, being set-off against that shareholder's share subscription obligation in the same amount.

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 18 July 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 8(4)(a);
- section 19;
- paragraph 12A; and
- paragraph 20(3)(b).

3. Parties to the proposed transaction

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

Co-Applicant: A company incorporated in and a resident of South Africa that is a shareholder of the Applicant

4. Description of the proposed transaction

The Co-Applicant advanced interest bearing loans (shareholder funding loans and administration loans) to the Applicant. There are no fixed terms of repayment and the loans are repayable on demand.

The shareholder funding loans were applied by the Applicant for the acquisition of allowance assets or trading stock in prior years of assessment. All the allowances have been written off or deducted for income tax purposes.

The shareholder funding loans include capitalised interest which has been deducted for income tax purposes by the Applicant.

The Applicant does not have sufficient cash reserves to meet its financial obligations and it is unlikely that the Applicant will be in a position to repay the shareholder funding loans from its operating cash flows in the foreseeable future. The balance sheet of the Applicant has the potential to impair the company's ability to obtain credit for working capital requirements.

The proposed steps for achieving the settlement of the shareholder funding loans are as follows:

- The Co-Applicant, through a rights issue, will subscribe for equity shares in the Applicant.
- The Co-Applicant will settle its subscription obligation by way of set-off against its shareholder funding loans owed to it by the Applicant.

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) Section 19 and paragraph 12A will not be applicable to the proposed transaction to the extent that it relates to the settlement of the Applicant's shareholder funding loans owed to the Co-Applicant, being set-off against the share subscription obligation in the same amount.
- b) No amount will be included in the Applicant's income under section 8(4)(a) and no expenditure relating to an asset will be reduced as envisaged under paragraph 20(3)(b).

7. Note

This ruling does not cover the application of any general anti-avoidance provision to the proposed transaction.

8. Period for which this ruling is valid

This binding private ruling is valid for a period of three years from 18 July 2016.