

*SOUTH AFRICAN REVENUE SERVICE*

**BINDING PRIVATE RULING: BPR 060**

DATE: 30 October 2009

**ACT : INCOME TAX ACT, NO. 58 OF 1962 (the Act)**  
**SECTION : SECTION 1, DEFINITION OF “GROSS INCOME” AND SECTION 11(a) READ WITH SECTION 23(g)**  
**SUBJECT : “SHORT SALE” TRANSACTIONS AND SECURITIES LENDING ARRANGEMENTS**

**1. Summary**

This ruling deals with the income tax implication for vested beneficiaries entering into securities lending arrangements with the express purpose of facilitating “short sale” transactions.

**2. Relevant tax laws**

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

In this ruling legislative references to sections are to sections of the Act applicable as at 21 October 2008 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 1, definition of “gross income”; and
- section 11(a) read with section 23(g).

**3. Parties to the proposed transaction**

The Applicant: A trust (Borrower)

Co-Applicants: Vested beneficiaries of the trust

**4. Description of the proposed transaction**

The Borrower intends to enter into securities lending arrangements, in terms of which the Borrower will borrow fixed or variable interest rate bonds, and/or shares (bonds and/or shares) with the express purpose of facilitating

“short sale” transactions in respect of the borrowed bonds and/or shares, as the Borrower expects to profit from an expected decline in the prices of the borrowed bonds and/or shares.

In terms of a securities lending arrangement, the Borrower will have an “unconditional obligation”], to return the borrowed bonds and/or shares (close-out of the securities lending arrangement) to the lender on an agreed date (close-out date) which might be specified or un-specified.

The Borrower is further under an obligation to pay the lender a fee for agreeing to lend the bonds and/or shares.

For the term of the securities lending arrangement the Borrower will also be obliged to pay manufactured interest and/or dividends (whichever is applicable), in respect of the borrowed bonds and/or shares, to the lender.

The borrowed bonds and/or shares will be disposed of in terms of “short sale” transactions to be entered into in the year in which the securities lending arrangement is entered into.

The proceeds to be received from a “short sale” transaction will be invested in shares.

When the lender calls on the Borrower to close-out the securities lending arrangement, the bonds/shares will be purchased in the market by the Borrower and delivered to the lender in accordance with its obligations under the securities lending arrangement.

## **5. Conditions and assumptions**

This ruling is made subject to the conditions and assumptions that –

- an “unconditional obligation” on the Borrower, to return the borrowed bonds and/or shares to the lender, must exist on the day that the securities lending arrangement is entered into; and
- the estimated market value of the borrowed bonds and/or shares to be used in claiming the initial deduction under the provisions of section 11(a) must be the same as the estimated value to be used for management reporting purposes, when the securities lending arrangement is entered into.

## **6. Ruling**

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

- Any “short sale” transaction in respect of the borrowed bonds and/or shares will result in a receipt or an accrual of “gross income” as defined in section 1, in the hands of each Co-Applicant, equal to the Co-Applicant’s vested right in the amount received by or accrued to the Borrower.

- The Borrower's "unconditional obligation", to "close-out" any securities lending arrangement will be recognised as an expense to be allowed as a deduction (initial deduction), in the hands of the Co-Applicants, under the provisions of section 11(a) read with the provisions of section 23(g), in the year of assessment in which the securities lending arrangement is entered into. .
- The amount of the initial deduction to be allowed (referred to above) will be equal to the Co-Applicant's vested right in the estimated market value of the borrowed bonds and/or shares on the date the securities lending arrangement is entered into.
- In the year of assessment when the Borrower acquires the bonds and/or shares in order to close-out any securities lending arrangement, and the Co-Applicant's vested right in the cost of the bonds and/or shares so acquired is in excess of the initial deduction that was allowed that Co-Applicant will be entitled to a further deduction under the provisions of section 11(a) equal to the excess amount of the cost of the bonds and/or shares over the initial deduction that was allowed. If the cost of the bonds and/or shares so acquired is less than the initial deduction that was allowed, that Co-Applicant will have to recoup an amount under the provisions of section 8(4)(a), equal to the excess amount of the initial deduction that was allowed over the cost of the bonds and/or shares so acquired.

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

This binding private ruling is valid for a period of three (3) years as from 12 December 2008.

Issued by:

**Legal and Policy Division: Advance Tax Rulings  
SOUTH AFRICAN REVENUE SERVICE**