

BINDING PRIVATE RULING: BPR 212

DATE: 10 December 2015

**ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
VALUE-ADDED TAX ACT NO. 89 OF 1991 (the VAT Act)**

**SECTION : SECTIONS 1(1) – DEFINITION OF “GROSS INCOME”, 24J AND
PARAGRAPHS 3, 4, 12A AND 20(3)(b) OF THE EIGHTH SCHEDULE
TO THE ACT
SECTIONS 2 AND 12(a) OF THE VAT ACT**

**SUBJECT : TAX CONSEQUENCES FOR THE ISSUER AND SECURITY
COMPANY OF LISTED CREDIT LINKED NOTES**

1. Summary

This ruling determines the tax consequences for the Issuer of listed credit linked notes (notes) that are enhanced by the conclusion of a credit default swap (CDS) with the Applicant, as well as the tax consequences that will arise for the Issuer and the Security Company in the event of default.

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 relevant Acts and paragraphs of the Eighth Schedule to the Act applicable as at 22 October 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of the following provisions of –

- the Act –
 - section 1(1) – definition of “gross income”;
 - section 24J;
 - paragraph 3;
 - paragraph 4;
 - paragraph 12A; and
 - paragraph 20(3)(b).
- the VAT Act –
 - section 2; and
 - section 12(a).

3. Parties to the proposed transaction

The Applicant:	A company incorporated in and a resident of South Africa
The Issuer:	A special purpose company incorporated in and a resident of South Africa
The Security Company:	Another special purpose company incorporated in and a resident of South Africa

4. Description of the proposed transaction

The Issuer intends to issue listed notes and to hold the underlying assets. The Applicant will administer the notes and the underlying assets while the Security Company will guarantee the obligations of the Issuer.

The purpose of the notes is to provide capital market investors (investors) with an opportunity to access bankruptcy remote corporate credit exposures. The notes will be registered on the Interest Rate Market of the JSE.

The Issuer and the Security Company are not connected persons in relation to the Applicant.

The proposed transaction steps are as follows:

- The Issuer will issue the notes to investors and will enter into a CDS with the Applicant. The coupon rate of the notes will be determined with reference to the income under the CDS and the interest under the debt instruments, to be acquired by the Issuer.
- The Security Company will issue guarantees in favour of the investors and the Applicant, in respect of the Issuer's obligations under the notes and the CDS.
- The Issuer will indemnify the Security Company in relation to the guarantees and will provide security in the form of a security cession of the debt instruments and the rights under the CDS.
- Under the CDS, the Issuer will assume the credit risk of corporate debtors in relation to the CDS reference assets and will receive a monthly payment from the Applicant.
- In the event of a default in relation to any of the CDS reference assets, the Issuer will take transfer of the defaulting reference asset(s), or will make a lump sum payment. The amount of the lump sum will be derived from the extent of the default in relation to the CDS reference asset(s).
- On the redemption of the notes and in the absence of a default event in relation to the CDS reference asset(s), the investors will be entitled to a redemption amount, to be determined according to the priority of payments set out in the transaction documentation. This amount should correspond to the realisable value of the debt instruments and the rights under the CDS at that time.

- On the redemption of the notes, following a default event in relation to the CDS reference asset(s), the redemption amount due to the investors will be limited by the prior ranking claim of the Applicant under the CDS.

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:

- The interest payments to be made by the Issuer to the investors pursuant to the notes will be allowed as a deduction under section 24J(2) of the Act to the extent of the income received by or accrued to the Issuer from the CDS and debt instruments. These amounts may be set-off against each other.
- In the event that the Issuer becomes obliged to perform under the CDS, it will not realise a capital loss in relation to the settlement of the CDS, whether in cash or otherwise.
- There will be no capital gain for the Issuer if the notes are redeemed for less than the issue price because the Issuer's obligation towards the investors will be limited to the value of the debt instruments after the Issuer's obligations under the CDS has been fulfilled. There will be no "reduction amount" under paragraph 12A.
- In the event that the Security Company must perfect the security, the Security Company will neither receive, nor pay any amount on its own behalf. No tax consequences will arise for the Security Company.
- The issue of the notes will constitute a financial service as contemplated in section 2(1) of the VAT Act. The supply thereof is exempt under section 12(a) of the VAT Act.

7. Period for which this ruling is valid

This binding private ruling is valid for a period of 5 years from 22 October 2015.