

BINDING PRIVATE RULING: BPR 187

DATE: 18 February 2015

ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
SECTION : SECTIONS 1(1), DEFINITION OF “GROSS INCOME”, 8(4)(a), 15(a) 19, 36, 45 AND PARAGRAPHS 12A, 38(1) AND 56(1) OF THE EIGHTH SCHEDULE TO THE ACT
SUBJECT : WAIVER OF AN INTRA-GROUP LOAN THAT FUNDED THE ACQUISITION OF A MINING OPERATION

1. Summary

This ruling deals with the waiver of a loan that funded the acquisition of a mining operation as a going concern under an intra-group transaction contemplated in section 45 of the Act.

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 Act and paragraphs of the Eighth Schedule thereto applicable as at 8 September 2014 and 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 1(1), definition of “gross income”;
- section 8(4)(a);
- section 15(a);
- section 19;
- section 36;
- section 45; and
- paragraphs 12A, 38(1) and 56(1).

3. Parties to the proposed transaction

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

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

4. Description of the proposed transaction

Following the introduction of the Mineral and Petroleum Resources Development Act No. 28 of 2002 and the Broad-Based Socio-Economic Empowerment Charter for the South African Mining and Minerals industry as contemplated in section 100(2)(a) of that Act, the Co-Applicant entered into a Broad-Based Black Economic Empowerment (BBBEE) transaction in terms of which the Co-Applicant sold its mining operations to the Applicant on loan account. The parties elected that the provisions of section 45 would apply to the transaction.

The shares in the Applicant are held 74 per cent by the Co-Applicant and 26 per cent by a company that is classified as a black owned company under the BBBEE Codes of Good Practice issued under section 9 of the Broad-Based Black Economic Empowerment Act No. 53 of 2003.

The material terms of the sale of business agreement were as follows:

- The “business” for purposes of the sale agreement was defined as the business of prospecting, mining and beneficiating, marketing and selling of the commodity and all related activities, that was conducted by the Co-Applicant.
- All the sale assets, being the fixed assets comprising mining and non-mining allowance assets, the properties, the debtors book, the sale contracts, the goodwill and all other assets utilised in relation to the conduct of the business as defined were sold to the Applicant.
- The outstanding balance of the purchase price was to bear interest at the same interest rate as was charged to the Co-Applicant by its financial institution in respect of local borrowings, the nominal annual rate compounded monthly, which interest would be payable by the Applicant to the Co-Applicant monthly and in arrears.

The unredeemed balance of “capital expenditure” as defined in section 36(11) was nil at the date of transfer of the assets and mining operations. Consequently, no further allowances under section 15(a) were available to be claimed by the Applicant in respect of the assets transferred.

As a result of the global financial crisis and the radical decline in commodity prices in recent years, the Applicant has been negatively impacted in that it has been unable to ensure full payment of the capital and the interest charged on the loan account. To date the Applicant has only been able to service part of the interest and the unpaid interest has been written off as a bad debt by the Co-Applicant.

The Co-Applicant therefore proposes to waive the loan account in order to strengthen the balance sheet of the Applicant.

5. Conditions and assumptions

This binding private ruling is not subject to any additional conditions and assumptions.

6. Ruling

6.1 Ruling applicable to the Applicant

The ruling made in connection with the proposed transaction, as applicable to the Applicant, is as follows:

- (a) Paragraph 12A will not be applicable to the waiver of the loan account owing by the Applicant to the Co-Applicant.
- (b) Section 19 will be applicable to the waiver of the loan account, to the extent that the debt was used to acquire non-mining allowance assets in respect of which allowances were claimed by the Applicant under the Act, other than deductions under section 15(a).
- (c) Section 19 will not be applicable to recoup or recover allowances claimed as a deduction by the Co-Applicant for the non-mining allowance assets acquired under section 45.
- (d) In respect of trading stock:
 - (i) Section 19(3) and (4) will be applicable to trading stock still on hand that was acquired under the sale of business agreement.
 - (ii) Section 19(5) will be applicable to trading stock acquired that has been sold and in respect of which a deduction or an allowance was granted under the Act.
- (e) Section 19 will not be applicable to the waiver of the loan, to the extent that the debt was used to acquire mining assets, that is, expenditure on assets qualifying as “capital expenditure” as defined in section 36(11), in respect of which allowances were claimed by the Co-Applicant under section 15(a).
- (f) To the extent that there is no recoupment under section 8(4)(a), the waiver of the loan account will not fall within the ambit of “gross income” as defined in section 1(1).

6.2 Ruling applicable to the Co-Applicant

The ruling made in connection with the proposed transaction, applicable to the Co-Applicant, is as follows:

- (a) The waiver of the loan account will result in a capital loss in the hands of the Co-Applicant, but this loss must be disregarded in accordance with the provisions of paragraph 56(1). To the extent that an amount is included in the income of the Applicant in respect of the debt waiver or an adjustment is made to the carrying value of trading stock under section 19(3), the Co-Applicant may take into account a corresponding amount of the capital loss.
- (b) The waiver of the loan account will not be subject to the provisions of paragraph 38(1).

7. Period for which this ruling is valid

This binding private ruling is valid for a period of 3 years from 8 September 2014.

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