

SOUTH AFRICAN REVENUE SERVICE

BINDING PRIVATE RULING: BPR 073

DATE: 29 January 2010

ACT : INCOME TAX ACT, NO. 58 OF 1962 (the Act)
: VALUE-ADDED TAX ACT, NO. 89 OF 1991 (the VAT Act)
SECTION : SECTIONS 8(4)(m) AND 20(1)(a)(ii) AND PARAGRAPH 12(5) OF
THE EIGHTH SCHEDULE TO THE ACT
: SECTION 22(1) OF THE VAT ACT
SUBJECT : EXTINCTION OF INTER-COMPANY LOANS AS A RESULT OF
VOLUNTARY WINDING-UP

1. Summary

This ruling deals with the potential adjustment of the balance of assessed loss and the recoupment of amounts previously allowed as deductions against income when inter-company loans are extinguished as a result of a voluntary winding-up. This ruling also deals with the VAT consequences relating to a potential input tax deduction in respect of taxable supplies previously made, which will become irrecoverable in the future.

2. Relevant tax laws

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

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 20 November 2009 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 8(4)(m) of the Act;
- section 11(i) of the Act;
- section 20(1)(a)(ii) of the Act;
- paragraph 12(5) of the Eighth Schedule to the Act; and
- section 22(1) of the VAT Act.

3. Parties to the proposed transaction

The Applicant: V, a company incorporated in South Africa

The Co-Applicants: W, X, Y and Z, companies incorporated in South Africa which are wholly owned subsidiaries of the Applicant

4. Description of the proposed transaction

With regard to the Co-applicants:

- Z has a balance of assessed loss and traded during the current year of assessment. Z will, therefore, retain its balance of assessed loss, which will be available for set-off against income derived by it during future years of assessment.
- W and Y each has a balance of assessed loss but did not trade during the current year of assessment. Both W and Y will, therefore, not retain their balance of assessed loss and no balance of assessed loss will be carried forward to their future year of assessment.
- X has no balance of assessed loss and did not trade during the current year of assessment. X will, therefore, have no balance of assessed loss to be carried forward to its future year of assessment.

The Applicant advanced working capital to the Co-Applicants over the years, and charged interest on the capital so advanced. The Applicant also charged them an administration fee, rent, and insurance over the years (hereinafter referred to as 'on-charged expenditure'), which was not paid by them, but credited to their respective loan accounts with the Applicant.

The Co-Applicants do not have the means to settle any amount owing to the Applicant.

The Applicant intends to wind up the Co-Applicants by way of a voluntary creditors' or members' winding-up in terms of sections 79 and 80 of the Companies Act, No. 71 of 2008, once proclaimed, or sections 349, 350 and 351 of the Companies Act, No. 61 of 1973.

The Applicant has not finally decided whether it will initiate a voluntary winding-up of the Co-Applicants by their members or creditors. The Applicant is both the member and the creditor of the Co-Applicants.

5. Conditions and assumptions

This ruling is not subject to any conditions and assumptions.

6. Ruling

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

6.1 The winding-up of the Co-Applicants that do not have the means to settle any amount owing to the Applicant will extinguish the Applicant's claims against them, resulting in a benefit to each of them that will have to be taken into account under sections 20(1)(a)(ii) and 8(4)(m) of the Act. It follows that:

- The balance of the assessed loss of Z will have to be reduced, to the extent indicated in section 20(1)(a)(ii) of the Act.
- Z will have to take that portion of its benefit, that is not set off against its balance of assessed loss under section 20(1)(a)(ii) of the Act, which relates to expenditure that has been set off by Z against actual income into account as a recoupment.
- Section 20(1)(a)(ii) of the Act will not apply in respect of W and Y, as they do not have any balance of assessed loss as a result of having not carried on any trade during the current year of assessment.
- W, X and Y must take into account as a recoupment the portion of its benefit that relates to expenditure that has been set off by each of them against actual income.
- Paragraph 12(5) of the Eighth Schedule to the Act will not apply to the debts which will be discharged as a result of the proposed winding-up, as the Applicant and Co-Applicants form a "group of companies" as defined in section 1 of the Act and the debts arose at the time when they formed part of that group of companies.
- The Applicant will be entitled to deduct the amounts relating to on-charged expenditure, which became bad during the current year of assessment under the provisions of section 11(1) of the Act, to the extent that the Applicant can prove that the amounts had been included in income.

6.2 The Applicant will be entitled to deduct input tax, under the provisions of section 22(1) of the VAT Act, in respect of the taxable supplies previously made to the Co-Applicants, to the extent that –

- the taxable supplies have not been paid for by the Co-Applicants;
- the unpaid taxable supplies are to be included in the balance of the loan accounts; and

- the Applicant will write off so much of the said amount, included in the loan accounts, as has become irrecoverable.

7. Period for which this ruling is valid

This binding private ruling is valid for a period of five (5) years as from 20 November 2009.

Issued by:

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