

## **BINDING PRIVATE RULING: BPR 124**

DATE: 22 October 2012

**ACT : INCOME TAX ACT, NO. 58 OF 1962 (the Act)**

**SECTION : SECTIONS 1(1), DEFINITION OF “CONTRIBUTED TAX CAPITAL” AND 20(1)(a)(ii), AND PARAGRAPHS 12(5) AND 20(1)(a) OF THE EIGHTH SCHEDULE TO THE ACT**

**SUBJECT : REPAYMENT OF SHAREHOLDERS’ LOANS FROM PROCEEDS OF A NEW ISSUE OF REDEEMABLE PREFERENCE SHARES**

### **1. Summary**

This ruling deals with the income tax and capital gains tax consequences arising from the repayment of shareholders’ loans from the proceeds of a new issue of redeemable preference shares (a new issue of shares) under technically insolvent circumstances.

### **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 to the Act applicable as at 2 April 2012 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 “contributed tax capital”;
- section 20(1)(a)(ii); and
- paragraphs 12(5) and 20(1)(a) of the Eighth Schedule.

### **3. Parties to the proposed transaction**

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

The Co-Applicant: A private company incorporated in and a resident of South Africa that holds a majority of the equity shares in the Applicant

Shareholders of the Applicant:

The Co-Applicant holds 51% of the equity shares in the Applicant

Two other companies incorporated outside South Africa that hold the balance of the equity shares in the Applicant

#### **4. Description of the proposed transaction**

The Applicant has an assessed loss brought forward from the previous years of assessment. The Applicant continued to trade in the current year of assessment, but is incurring further losses. The Applicant's operations are mostly financed through interest bearing loans from shareholders and from banks. The Applicant is heavily burdened with debt and interest payments arising therefrom to the point that its liabilities now exceed the book value of its assets.

In view of the Applicant's current financial position the shareholders wish to recapitalize the company with a new issue of shares. The Applicant will utilise the proceeds from the new issue to repay its shareholders' loans in order to improve the solvency of the company and reduce the interest burden on the company.

#### **5. Conditions and assumptions**

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

- The subscription price for the new issue of shares is to be settled in cash by the Applicant's shareholders.
- The shareholders' loans will be settled in full in cash by the Applicant.

#### **6. Ruling**

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

- The repayment of the shareholders' loans from the proceeds of the new issue of redeemable preference shares will not be regarded as a concession granted by or a compromise made by the Applicant's shareholders with the Applicant as envisaged in section 20(1)(a)(ii).
- Paragraph 12(5) of the Eighth Schedule will not be applicable to the repayment of the shareholders' loans.
- The payment of the subscription price to be made by the Applicant's shareholders in cash will qualify as expenditure actually incurred for

the acquisition of the new redeemable preference shares for purposes of paragraph 20(1)(a) of the Eighth Schedule.

- The fully paid subscription price for the new redeemable preference shares will qualify as “contributed tax capital” as defined in section 1(1).

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

This binding private ruling is valid for a period of 1 year from 2 April 2012.

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