

BINDING PRIVATE RULING: BPR 261

DATE: 30 January 2017

ACT : INCOME TAX ACT 58 OF 1962 (the Act)
SECTION : SECTION 8C AND PARAGRAPHS 20(3)(b) AND 80(2) AND (2A) OF THE EIGHTH SCHEDULE
SUBJECT : REPURCHASE OF RESTRICTED EQUITY INSTRUMENTS

1. Summary

This ruling determines the tax consequences for an employee share trust that is obliged to repurchase restricted equity instruments.

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 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 12 January 2017. 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 8C;
- paragraph 20(3)(b); and
- paragraph 80(2) and (2A).

3. Parties to the proposed transaction

The Trust:	A trust registered in and a resident of South Africa
Company A:	A company incorporated in and a resident of South Africa
Company B:	A company incorporated in and a resident of South Africa
The Participants:	Beneficiaries who are holding vested interests in the Trust

4. Background

The Trust was created to benefit certain key employees (Participants) of a group of companies (group) of which Company A forms part. The Trust is a black empowerment employee share incentive trust established to acquire, hold and, in appropriate circumstances, sell equity shares for the benefit of its beneficiaries.

The Trust holds shares in Company A. Company A in turn holds 26% of the shares in Company B and is the empowerment shareholder for the group.

The beneficiaries have all been awarded personal rights against (units in) the Trust. A beneficiary becomes a Participant only upon the vesting of those rights which entitle him or her to participate in the income and capital of the Trust in accordance with his or her proportional interest.

A unit represents the rights of a beneficiary to benefit from the sale of the shares in Company A, as and when a sale occurs and if the beneficiary's rights have vested at that point. Once a unit has vested, it is referred to as a "trust interest" as opposed to a unit.

A Trust Interest is the personal right of a Participant (in his or her capacity as a vested beneficiary), enforceable against the trustees to participate in the income and capital (including capital gains) of the Trust, based on the number of units of the Participant's trust interest. A trust interest is expressed as a percentage determined by dividing the number of units constituting a Participant's trust interest by the total number of units held in the pool at the relevant time.

A Participant can forfeit his or her trust interest under certain circumstances and may not freely dispose of it. Specifically, the Participant will forfeit his or her vested interest upon lawful termination of his or her employment or when he or she is declared insolvent or commits an act of insolvency. Under these circumstances, the Participant will forfeit his or her trust interest and any allocated units for no consideration. A Participant is also only allowed to dispose of his or her trust interests to the Trust and even then, subject to certain restrictive conditions regarding the process, the timing and the trustees' ability to dispose of the Company A shares to fund the repurchase.

A Participant is entitled to receive all cash dividends and other cash payments of any nature whatsoever in respect of the Company A shares. The Participant is also entitled to receive all cash payments or distributions of the capital or premium received by the Trust in relation to the Company A shares less certain amounts deducted from those cash distributions, in proportion to each Participant's trust interest. Where cash distributions are paid on the sale of Company A shares, those cash distributions will, after the deduction of certain amounts like realisation costs and taxes, be deemed to have vested in the Participants in proportion to each Participant's trust interest.

5. Proposed transaction

The proposed transaction entails the trustees making an award to the Participants by selling certain of its Company A shares and by repurchasing the whole or any portion of their trust interests from them, depending on what the trustees can afford out of the sale proceeds. The trust interest will be repurchased at the fair value of the Company A shares associated with the portion of each Participant's total trust interest, after deducting from the sale proceeds the costs and the taxes which may be incurred in order to raise the funds required to purchase the trust interests (including any capital gains tax which may be payable to procure the sale of the underlying Company A shares), and the repurchase price will be paid in cash.

A Participant will, on and with effect from the date specified in the notice signifying the trustees' intention to purchase his or her trust interest, cease to be a Participant in respect of the trust interests repurchased.

The proposed transaction will be implemented through the following transaction steps:

- i) The trustees will give written notice to the Participants of their intention to repurchase a portion of each Participant's trust interest.
- ii) The trustees will use their endeavours to sell sufficient Company A shares to fund the purchase of the trust interests.
- iii) Upon the successful sale of the Company A shares, the trustees will purchase the identified trust interests from the relevant Participants.

6. Conditions and assumptions

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

7. Ruling

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

- a) The proceeds received by the Trust on the disposal of the Company A shares will accrue to the Trust, which will calculate any capital gain or capital loss that arise as a result of the disposal.
- b) Paragraph 20(3)(b) will apply to reduce the base cost of the Company A shares held by the Trust, by the proportionate contributions made by the group companies to enable the Trust to acquire the Company A shares.
- c) If the Trust derives any capital gains from the disposal of the Company A shares linked to the trust interests, those gains will not be taxable in the Trust under paragraph 80(2) and paragraph 80(2A) will also not apply.
- d) Section 8C will apply in respect of the vesting of the Participants' restricted equity instruments. Any gain or loss determined in respect of the vesting of those restricted equity instruments will be subject to employees' tax to be withheld by the Trust.

8. Period for which this ruling is valid

This binding private ruling is valid for a period of five years from 12 January 2017.