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Securities transfer tax exemption where parties opt out of roll-over relief

By Heinrich Louw

23 Jul 2015

The South African Revenue Service (SARS) released Binding Private Ruling No 195 (Ruling) on 26 June 2015. The Ruling deals with the application of the exemption provision contained in s8(1)(a) of the Securities Transfer Tax Act, No 25 of 2007 (STT Act) in circumstances where parties have entered into an asset-for-share transaction as defined in s42 of the Income Tax Act, No 58 of 1962 (Act), but elected that any relief provided for in s42 of the Act should not apply.

The Applicant, a company incorporated and resident in South Africa, was a wholly owned subsidiary of HoldCo, a non-resident company incorporated in a foreign jurisdiction.

HoldCo also held all of the shares in Company X, and 90% of the shares in Company Y, both being private companies incorporated and resident in South Africa. Through its subsidiaries, HoldCo also held 57% of the shares in Company A, a public company incorporated and resident in South Africa. Company X and Company Y each held 30% of the shares in Company A.

For regulatory purposes, HoldCo sought to consolidate its stake in Company A by creating a "significant owner" of Company A's shares in South Africa.

It was proposed that the Applicant would purchase HoldCo's shares in Company X and Company Y. In exchange, the Applicant would issue further shares to HoldCo.

However, HoldCo and the Applicant would agree in terms of s42(8A) of the Act that the roll-over relief provided for in s42 of the Act would not apply to the transaction.

It appears that, even though the transaction would constitute an asset-for-share transaction for purposes of s42 of the Act, the parties did not require the capital gains tax relief provided for in that section because HoldCo was a non-resident, and the shares were not assets as contemplated in paragraph 2(1)(b) of the Eighth Schedule to the Act.

In fact, if s42 of the Act were to apply to the transaction, the base cost of the shares in the hands of the Applicant going forward would have been much lower than had the relief not applied.

The main concern seems to have been that, if the parties elected out of s42 of the Act, they would not qualify for the exemption from securities transfer tax contained in s8(1)(a) of the STT Act, and that the tax would be payable on the transfer of the shares in Company X and Company Y.

However, SARS ruled that the exemption in s8(1)(a) of the STT Act would apply to the transfer of the shares. Although SARS did not provide reasons for its Ruling, it appears that the wording of s8(1)(a) of the STT Act is such that it only requires the transaction to constitute an "asset-for-share transaction" as defined, and does not require that the actual relief provided for in s42 applies to the parties.

Additionally, SARS confirmed that:

- the shares in Company X and Company Y would not be regarded as assets contemplated in paragraph 2(1)(b) of the Eighth Schedule to the Act;
- the Applicant would get a step-up in its base cost in the shares of Company X and Company Y, as the base cost would be equal the market value of the Applicant's shares issued to HoldCo; and
- the Applicant would have a contributed tax capital in respect of the shares issued to HoldCo equal to the market value of the shares acquired in Company X and Company Y.

The Ruling is valid for a period of two years.

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