South African Revenue Service

DRAFT INTERPRETATION NOTE

DATE:

ACT : INCOME TAX ACT 58 OF 1962
SECTION : SECTIONS 23M, 23N, 24O AND 31
SUBJECT : LIMITATION OF INTEREST DEDUCTIONS

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Preamble

In this Note unless the context indicates otherwise –

- **"acquisition transaction"** means an "acquisition transaction" as defined in sections 23N(1)[1] and 24O(1)[2] respectively;
- **"CFC"** means a "controlled foreign company" as defined in section 1(1);
- **"reorganisation transaction"** means a "reorganisation transaction" as defined in section 23N(1), that is, an "intra-group transaction" as defined in

[1] See **4.4.1 (c)**.
[2] See **4.3.1 (a).**

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section 45(1) to which section 45 applies or a "liquidation distribution" as defined in section 47(1) to which section 47 applies;

- **"Schedule"** means a Schedule to the Act;
- **"section"** means a section of the Act;
- **"tax treaty"** means an agreement for the avoidance of double taxation entered into between South Africa and another country;
- **"the Act"** means the Income Tax Act 58 of 1962;
- **"the TA Act"** means the Tax Administration Act 28 of 2011; and
- any other word or expression bears the meaning ascribed to it in the Act.

All interpretation notes referred to in this Note are available on the SARS website at **www.sars.gov.za**. Unless indicated otherwise, the latest issue of these documents should be consulted.

1. Purpose

This Note provides guidance on the interpretation and application of –

- section 24O, deeming the incurral of interest on debt relating to the finance of an "acquisition transaction" as defined in section 24O(1) to be in the production of income;
- section 23N, which limits interest deductions on "reorganisation transactions" and "acquisition transactions" as defined in section 23N(1); and
- section 23M, which limits interest deductions on debt owed to certain persons not subject to tax.

This Note also addresses the interaction between sections 23M, 23N, 24O and 31 (international transactions to be based on arm's length principle) and the order in which sections 23M, 23N and 31 must be applied.

2. Background

The Explanatory Memorandum on the Taxation Laws Amendment Bill, 2015,[3] states that debt is often used to fund business acquisitions, which can be achieved by either purchasing the business assets of a company or by purchasing the shares in that company. Interest incurred by a purchaser when using debt to finance the acquisition of a business can be deducted from income to the extent that such interest expense is incurred in the production of income.

Since "income"[4] excludes exempt amounts, interest incurred on debt used to acquire shares in resident companies is generally not deductible where the purpose of the acquisition is to derive exempt dividends rather than income. To obtain interest deductions in respect of debt-financed share acquisitions, taxpayers have commonly implemented multi-step debt-push-down structures. Under such structures, the debt and related interest are effectively transferred to an operating subsidiary that acquires the target company's underlying assets on a tax-deferred basis, thereby creating an interest deduction in respect of debt linked to those assets and funds that ultimately

3 See paragraph 2.1.
4 Definition in section 1(1).

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replace the acquiring company's temporary loan originally raised to acquire the target company shares.

More specifically, a debt-push-down transaction generally involves the following:

- The acquisition by an acquiring company of all the shares of a target company using a temporary loan.
- The acquiring company (or a newly established subsidiary of the acquiring company) acquires the business assets of the target company under an intra-group transaction under section 45. The business assets of the target company are generally acquired using long-term debt-financing.
- The target company distributes the proceeds from the disposal of its assets, the disposal falling under section 45, as a dividend to the acquiring company. The funds are used by the acquiring company to repay the temporary loan. (There were also alternative structures involving the acquisition of the shares in the target company and the subsequent distribution of the business assets as a liquidation dividend under section 47).
- The dividend being exempt from normal tax under section 10(1)(*k*)(i) and from dividends tax under section 64F(1)(*a*).
- Interest incurred on the debt that financed the acquisition of the assets of the target company potentially being deductible if incurred in the production of income.

The reorganisation rules in section 41 – section 46A were intended to facilitate the transfer of assets in specified circumstances, but not to be used to potentially facilitate interest deductions. The real danger to the *fiscus* was, however, not debt push-down structures but rather the use of excessive debt to fund these structures. An interim measure in the form of section 23K denied the deduction of interest incurred on debt that financed reorganisation transactions.[5] A directive could, however, be issued by the Commissioner, after taking specific criteria into account, ruling that section 23K(2) would not apply to an amount of interest incurred.

An anomaly in the law was created, since interest associated with direct share acquisitions was not deductible while interest associated with indirect debt-financing through the use of tax-deferred debt-push-down structures may have been deductible in certain circumstances if a directive was obtained under section 23K. As a result, section 24O[6], which generally facilitates resident companies claiming an interest deduction on debt used to acquire controlling share interests in resident operating companies by deeming the interest to be in the production of income and for the purposes of trade, was enacted. The introduction of section 24O was aimed at addressing the anomaly and removing the need to implement multiple-step, debt-push-down structures.

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5 Reorganisation transactions entered into on or after 3 June 2011 and on or before 31 March 2014.

6 Acquisition transactions entered into on or after 1 January 2013.

Section 23K was amended to also deny a deduction for interest incurred on debt that financed acquisition transactions under section 24O.[7] A directive could, however, be issued by the Commissioner as with reorganisation transactions. Section 23K was subsequently replaced by section 23N.[8]

Generally, under section 23N the amount of interest incurred on reorganisation and acquisition transactions that may be deducted under the Act, for example, under section 11(*a*) or section 24J(2), is subject to a limitation calculated in accordance with the formula included in section 23N. The purpose of section 23N is to reduce the risk of the use of excessive debt to finance reorganisation and acquisition transactions, similar to that intended under section 23M in relation to debts owed to persons not subject to tax.

In this regard, generally, section 23M[9] was enacted to limit the deduction of interest incurred on debt when the interest is not subject to either normal tax or withholding tax on interest in the hands of the person to whom the interest accrues or which is not included in the net income of a CFC.

3. The law

The relevant provisions of the Act are quoted in the **Annexure**.

4. Application of the law

4.1 The deductibility of interest under section 11(a) or 24J(2)

Section 24J regulates the timing of the accrual and incurral of interest on an instrument and provides that it is spread over the term of the instrument.

Under section 24J(2) an issuer in relation to an instrument is deemed to have incurred an amount of interest during a year of assessment which is equal to –

- the sum of all accrual amounts in relation to all accrual periods falling, whether in whole or in part, within such year of assessment in respect of such instrument; or
- an amount determined in accordance with an alternative method in relation to such year of assessment in respect of such instrument,

which must be deducted from the income of that person derived from carrying on any trade, if that amount is incurred in the production of income.[10]

An instrument includes, amongst other things, any interest-bearing arrangement or debt.[11]

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7 Acquisition transactions entered into on or after 1 January 2013 and on or before 31 March 2014.

8 With effect from 1 April 2014.

9 Interest incurred on or after 1 January 2015.

10 The terms “accrual amount”, “accrual period”, “alternative method”, “instrument”, “interest” and “issuer” are defined in section 24J(1). These terms are not considered for purposes of this Note.

11 Paragraph (*c*) of the definition of “instrument” in section 24J(1).

Section 24J(12) provides that section 24J must not apply to an instrument if –

- the holder of the instrument has, throughout any period during a year of assessment during which the holder holds the instrument, a right to require the redemption of the instrument at any time during that period; and
- the instrument does not provide for the payment of any deferred interest.

The definition of "deferred interest" in section 24J(1) includes –

- any interest when such interest (or any portion thereof), calculated in respect of any accrual period falling within the term of any instrument by applying a constant interest rate throughout the term of such instrument, is not payable or receivable in terms of such instrument within one year from the date of the commencement of such accrual period; and
- any interest payable or receivable in terms of any instrument when such interest is not calculated by applying a constant interest rate throughout the term of the instrument.

Interest that is not deductible under section 24J(2) may be deductible under section 11(*a*) if the requirements of that section are met. In order to be deductible under section 11(*a*), an amount of interest must not be of a capital nature and must be actually incurred in the production of income which is derived from the carrying on of a trade.

Further, under section 23(*f*), any expenses incurred in respect of any amounts received or accrued which do not constitute "income" as defined in section 1(1), are not deductible. Under section 23(*g*), a deduction is denied to the extent moneys are not laid out or expended for the purposes of trade.

To qualify for a deduction, interest expenditure must meet the requirements of section 24J(2), or failing that the requirements of section 11(*a*), and must not fall foul of section 23(*f*) or section 23(*g*). Interest incurred on the funding used to acquire shares for the purpose of generating exempt dividends is not incurred in the production of income and may also not be incurred for the purposes of trade. However, in the case of interest incurred on an "acquisition transaction" as defined in section 24O(1), if all the requirements of section 24O are met, the interest is deemed to have been incurred in the production of income and laid out or expended for the purposes of trade under section 24O(2) (see **4.3**).

For completeness, it is noted that section 23(*q*) prohibits the deduction of any expenditure incurred in the production of income in the form of foreign dividends. For example, section 23(*q*) will deny a deduction for interest incurred on a loan used to purchase shares that give rise to foreign dividends that are not exempt under section 10B.

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4.2 Case law dealing with the deductibility of interest incurred on debt that financed the acquisition of shares

For interest to be deductible under section 11(*a*) or 24J(2), as indicated in **4.1**, it must, amongst other things, be incurred in the production of income which is derived from the carrying on of a trade.[12] The question whether interest incurred on debt to finance the acquisition of shares is deductible, is a factual one.

The deductibility of interest incurred on debt to finance the acquisition of shares has received considerable judicial consideration in South African courts.

It was held in *Producer v COT*[13] that the critical inquiry in determining whether an amount of interest is incurred in the production of income, is the purpose for which the money on which the interest is incurred, has been borrowed. Hudson CJ stated it as follows:

> "It is clear that if a taxpayer borrows a specific sum of money and applies that sum to a purpose unproductive of income, and not directly connected with the income-earning part of his business, then the interest paid on the borrowed money cannot be deducted as expenditure incurred in the production of income."

In *CIR v Standard Bank of South Africa*, Corbett JA stated that:[14]

> "In regard to the general deduction formula, it is settled law that generally in order to determine in a particular case whether moneys outlaid by the taxpayer constitute 'expenditure incurred in the production of the income' important, sometimes overriding, factors are the purpose of the expenditure and what the expenditure actually effects. And in this connection the court has to assess the closeness of the connection between the expenditure and the income-earning operations."

A sufficiently close connection between the purchase of the shares and the production of income is required for interest incurred on debt, that financed the acquisition of shares, to be incurred in the production of income.

In *CIR v Nemojin (Pty) Ltd*[15] shares were acquired with a dual purpose and effect of the receipt of proceeds on disposal of the shares (income) and dividend stripping (exempt income). On the facts neither of the purposes was incidental. The court recognised that the shares had a close connection to income and a close connection to exempt income. Accordingly, the interest expenditure was apportioned with only the portion closely connected to income meeting the requirement of being in the production of income and qualifying for a deduction.

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12 See Interpretation Note 33 "Assessed Losses: Companies: The 'Trade' and 'Income from Trade' Requirements" for the meaning of "Carrying on of a Trade".

13 1948 (4) SA 230 (SR), 15 SATC 405 at 408. The purpose for which money was borrowed was also held to be the critical inquiry in *CIR v Allied Building Society* 1963 (4) SA 1 (A), 25 SATC 343 and *CIR v Standard Bank of SA Ltd* 1985 (4) SA 485 (A), 47 SATC 179.

14 1985 (4) SA 485 (A), 47 SATC 179.

15 1983 (4) SA 935 (A), 45 SATC 241.

In *CIR v Shapiro Shapiro v CIR*[16] the taxpayer purchased shares in a company, the purchase of the initial holding of shares entitled the taxpayer to be appointed managing director for which services he would receive a salary, commission and housing benefits. In determining taxable income, the taxpayer claimed a deduction for certain amounts of interest paid on the money borrowed to acquire these shares. Based on the facts, Matthews J held that the interest was not deductible, since the taxpayer's trade was his continuous occupation as managing director and the interest paid on borrowed moneys to acquire the shares was not really incidental to that trade itself. Otherwise viewed, on the facts of the case the salary, commission and housing benefits were closely connected to the services rendered by the taxpayer as a managing director, but not to the holding of the shares which produced exempt dividend income.

In *CIR v Drakensberg Garden Hotel (Pty) Ltd*[17] the taxpayer leased a hotel and a store from a company to whom it paid rent. It sublet the hotel to a partnership comprising its two shareholders from which it derived rental income and ran the trading store for its own account from which it derived business profits. The taxpayer subsequently purchased all the shares in the lessor company. Interest was payable on the outstanding balance of the purchase price. It is the amount of this interest that the taxpayer sought to deduct from its income.

Schreiner JA held as follows:[18]

> " … on the findings contained in the stated case the respondent's purpose in buying the shares was to ensure the continuance of its income from sub-letting and trading and to secure an increased income therefrom.
>
> That there was a connection between the purchase of the shares and the production of the respondent's income seems to be clear. The question whether, having regard to the factors relied upon by the Commissioner, taken singly or together, the connection was close enough appears to be essentially a question of degree, in regard to which it is not possible to say that it would be erroneous in law to hold one opinion rather than the other. The Special Court has held that the connection is close enough and this is a finding which cannot be held to be one at which no Court could reasonably arrive."

There are several tax court judgements in which shareholders have been able to secure a deduction for interest incurred in acquiring shares when the purpose of the borrowing was not to generate exempt dividends but rather to generate increased emoluments from the company.[19]

The case of *Financier v COT*[20] dealt with a situation in which it was not possible to determine for which purpose moneys were borrowed. The nature of an investment management company is such that when it borrows generally for its business, it is often not known with certainty whether the money might be invested in investments which produced income or exempt income and whether that investment will change over

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16 1928 NLR 436, 4 SATC 29. See also *Natal Laeveld Boerdery BK v KBI* 1998 (1) SA 639 (SCA), 60 SATC 81; ITC 1602 (1995) 58 SATC 205 (N) and *C: SARS v 121 Castle Street Cape Town CC* 2002 (1) SA 198 (C), 63 SATC 185 dealing with the disallowance of interest on debt that funded the acquisition of shares in a company.

17 1960 (2) SA 475 (A), 23 SATC 251.

18 At SATC 259.

19 ITC 1428 (1985) 50 SATC 34 (C); ITC 1504 (1991) 53 SATC 349 (C); ITC 1604 (1995) 58 SATC 263 (EC) and ITC 1694 (1999) 63 SATC 127 (C).

20 1950 (3) SA 294 (SR), 17 SATC 34.

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time. Tredgold J held[21] that in the facts of the case it was impossible to apply the "purpose test". He held further[22] that the onus is on the taxpayer to show that a deduction is permissible and that the only practicable basis to determine this issue is by reference to the use to which the money is put. A similar line of reasoning was followed in ITC 1171[23] in which a taxpayer had borrowed money to fund the purchase of trading stock in the taxpayer's general dealer's business. After the business had closed the taxpayer sought to continue deducting the interest. The court dismissed the taxpayer's appeal, holding that it was not the initial borrowing but his decisions from day to day to retain the use of the money which entailed the expenditure.

Interest incurred on money that financed fixed or floating capital assets may be deductible if incurred in the production of income. In *CIR v Genn & Co (Pty) Ltd* Schreiner JA held that –[24]

> "[i]nterest paid on money borrowed and used for the purposes of a business would appear to be expenditure actually incurred in the production of the income of the business, whether the loan was for the acquisition of fixed or floating capital."

4.3 Incurral of interest on certain debt deemed to be in the production of income (section 24O)[25]

Section 24O introduced special rules applying to interest incurred on debt used to finance the acquisition of equity shares under an "acquisition transaction" as defined in section 24O(1) or to substitute such debt. Under section 24O(2) any interest incurred by a company on such debt must, to the extent to which the amount thereof relates to a period during the year of assessment during which the company held the equity shares and the equity shares constituted a qualifying interest (see **4.3.3**) in an operating company as determined at the date referred to in section 24O(2)(ii), be deemed to have been incurred in the production of income and laid out or expended for the purposes of trade.

4.3.1 Definitions [section 24O(1)]

The definition of "acquisition transaction" (see **(a)** below) and "operating company" (see **(b)** below) contained in section 24O(1) is critical for purposes of section 24O.

(a) Definition of "acquisition transaction"

The term "acquisition transaction" means any transaction under which a company (Co. A) acquires from a person that does not form part of the same "group of companies", as defined in section 1(1), as that company, an equity share in any of the following companies:

- A company (Co. B) that is an operating company [see **4.3.1 (b)**] on the date of acquisition of that share and as a result of which, at the end of the day of that transaction, that company (Co. A) –

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21 At SATC 37.

22 See above.

23 (1971) 34 SATC 80 (C).

24 1955 (3) SA 293 (A), 20 SATC 113 at 121.

25 Section 24O was inserted by section 57(1) of the Taxation Laws Amendment Act 22 of 2012 and applied to acquisition transactions entered into on or after 1 January 2013. It was substituted by section 46(1) of the Taxation Laws Amendment Act 25 of 2015 with effect from years of assessment ending on or after 1 January 2016 and amended by section 46(1) of the Taxation Laws Amendment Act 23 of 2018 and section 31 of the Taxation Laws Amendment Act 34 of 2019.

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- is a controlling group company in relation to the operating company (Co. B); and
- forms part of the same "group of companies" as defined in section 41(1) as the operating company (Co. B) [paragraph (*a*) of the definition of "acquisition transaction"].

(Paragraph (a) of the definition of "acquisition transaction")

- A company (Co. C) that is a controlling group company in relation to a company that is an operating company (Co. B) on the date of acquisition of that share and which forms part of the same "group of companies" as defined in section 41(1) as that controlling group company and as a result of which, at the end of the day of that transaction –
  - that company (Co. A) is a controlling group company in relation to that other controlling group company (Co. C); and
  - both controlling group companies (Co. A and Co. C) form part of the same "group of companies" as defined in section 41(1) [paragraph (*b*) of the definition of "acquisition transaction"].

(Paragraph (b) of the definition of "acquisition transaction".)

Any interest incurred on debt that funded the acquisition of equity shares in a transaction that does not meet the definition of an "acquisition transaction" will not be deemed to be incurred in the production of income and laid out or expended for the purposes of trade under section 24O(2) (see **4.3.2**), since the acquisition of the related equity shares in an acquisition transaction is one of the requirements in section 24O(2). If the definition of an "acquisition transaction" is met, the company incurring the interest expense will need to meet all of the requirements in section 24O before section 24O(2) applies.

Meaning of "equity share"

The term "equity share" is defined in section 1(1)[26] and means any share in a company, excluding any share that, neither in respect of dividends or foreign dividends, nor in respect of return of capital or foreign returns of capital, carries any right to participate beyond a specified amount in a distribution.

A distribution by a company could take the form of a distribution of profits (dividends) or capital (return of capital). As long as the right to participate in either of these types of distribution is unrestricted, the share will qualify as an equity share. The share will not be an equity share if both these rights are restricted.

Meaning of "group of companies"

The Act contains two definitions of "group of companies", namely, a wider definition in section 1(1) and a narrower definition in section 41(1).

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[26] This definition is quoted in the **Annexure**.

The term "group of companies" as defined in section 1(1) means two or more companies in which one company (the controlling group company) directly or indirectly holds shares in at least one other company (the controlled group company), to the extent that –

- at least 70% of the equity shares in each controlled group company are directly held by the controlling group company, one or more other controlled group companies or any combination thereof; and
- the controlling group company directly holds at least 70% of the equity shares in at least one controlled group company.

It is thus a requirement of a "controlling group company" that it must directly hold at least 70% of the equity shares in at least one controlled group company.

The definition of "group of companies" in section 41(1) starts with the definition in section 1(1) and then excludes certain companies and shares by way of a proviso. The following companies, amongst others, are excluded:

- Any association, corporation or company incorporated under the law of any other country other than South Africa or any body corporate formed or established under such law unless the association, corporation, company or body corporate has its place of effective management[27] in South Africa.[28]
- Any company that has its place of effective management outside South Africa.[29]

Therefore, when the definition of "acquisition transaction" in section 24O(1) refers to the definition of "group of companies" in section 41(1), it will often mean both the controlling group company and the operating company are residents[30] with their places of effective management in South Africa.

See Interpretation Note 75 "Exclusion of Certain Companies and Shares from a 'Group of Companies' as Defined in Section 41(1)" for details on the meaning of "group of companies".

Meaning of "controlled group company"

A controlled group company means a controlled group company contemplated in the definition of "group of companies".[31]

Meaning of "controlling group company"

A controlling group company means a controlling group company contemplated in the definition of "group of companies". [32]

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27 See Interpretation Note 6 "Resident – Place of Effective Management (Companies)".

28 Paragraph (i)(*ee*) of the proviso to the definition of "group of companies" in section 41(1).

29 Paragraph (i)(*ff*) of the proviso to the definition of "group of companies" in section 41(1).

30 The term "resident" is defined in section 1(1) and means in relation to a person other than a natural person, a person which is incorporated, established or formed in South Africa or which has its place of effective management in South Africa but does not include any person who is deemed to be exclusively a resident of another country for the purposes of the application of a tax treaty.

31 Section 1(1).

32 Section 1(1).

Meaning of "as a result of which, at the end of the day of that transaction"

As noted above, the requirements of an acquisition transaction include that *as a result of which* at the end of the day of that transaction –

- the company (Co. A) is a controlling group company in relation to the operating company (Co. B) or the other company (Co. C); and
- the companies concerned (as appropriate, Co. A and Co. B; or Co. A and Co. C) form part of the same "group of companies" as defined in section 41(1).

The relevance of the words "as a result of which" is that the two requirements referred to above must be met because of a specific share acquisition transaction. An acquisition of equity shares in circumstances where these two requirements were already met before the transaction or one in which after the transaction the two requirements are not met, will not qualify as an acquisition transaction. Only a transaction which gives rise to the controlling relationship and causes the companies concerned to form part of the same "group of companies" as defined in section 41(1), is an acquisition transaction. Importantly, both requirements must be met as a result of the share acquisition. For example, if a company borrows funds to acquire the shares in an operating company that is already a member of the same group of companies as that company, the transaction will not be an acquisition transaction because the transaction did not result in the operating company and that company becoming members of the same group of companies. See, however, the exceptions under section 24O(5) in **4.3.4**.

These two requirements of an "acquisition transaction" must, therefore, be met at the end of the 24-hour period of the day on which the qualifying share acquisition as mentioned above is acquired.

Example 1 – Definition of "acquisition transaction" – Section 24O(1)

Facts:

Company A's year of assessment ends on 31 December. On 31 January 2025 it acquired 70% of the equity shares in Company B, which qualified as an operating company on that date. The equity shares were acquired from Company C which did not form part of the same "group of companies" as defined in section 1(1), as Company A. All three companies are residents that have their place of effective management in South Africa.

Result:

Relationship between Company A and Company B

At the end of 31 January 2025 Company A and Company B formed part of the same "group of companies" as defined in section 41(1) and Company A was a controlling group company in relation to Company B because –

- Company A directly held shares in at least one other company (Company B);
- at least 70% of the equity shares in the controlled group company (Company B) were directly held by the controlling group company (Company A);
- the controlling group company (Company A) directly held at least 70% of the equity shares in at least one controlled group company (Company B); and

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- neither Company A nor Company B was excluded from the definition of "group of companies" in section 41(1).

Acquisition transaction

The acquisition of the equity shares by Company A in Company B qualified as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired from Company C which did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- Company B was an operating company on 31 January 2025; and
- as a result of the transaction, Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1), and that was still the position at the end of 31 January 2025.

Example 2 – Definition of "acquisition transaction" – Section 24O(1)

Facts:

Company A's year of assessment ends on 31 December. On 31 January 2025 it acquired 70% of the equity shares in Company B from Company D, which did not form part of the same "group of companies", as defined in section 1(1), as Company A. Company B held 100% of the equity shares in Company C which qualified as an operating company on that date. All the companies are residents that have their place of effective management in South Africa.

Result:

Relationship between Company B and Company C

On 31 January 2025 Company B and Company C formed part of the same "group of companies" as defined in section 41(1) and Company B was a controlling group company in relation to Company C because –

- Company B directly held shares in at least one other company (Company C);
- at least 70% of the equity shares in the controlled group company (Company C) were directly held by the controlling group company (Company B);
- the controlling group company (Company B) directly held at least 70% of the equity shares in at least one controlled group company (Company C); and
- neither Company B nor Company C was excluded from the definition of "group of companies" in section 41(1).

Relationship between Company A and Company B

At the end of 31 January 2025 Company A and Company B formed part of the same "group of companies" as defined in section 41(1) and Company A was a controlling group company in relation to Company B because –

- Company A directly held shares in at least one other company (Company B);
- at least 70% of the equity shares in the controlled group company (Company B) were directly held by the controlling group company (Company A);

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- the controlling group company (Company A) directly held at least 70% of the equity shares in at least one controlled group company (Company B); and
- neither Company A nor Company B was excluded from the definition of "group of companies" in section 41(1).

Acquisition transaction

The acquisition of the equity shares by Company A in Company B qualified as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired from Company D which did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- the equity shares were acquired in a company (Company B) which was a controlling group company in relation to an operating company (Company C) and Company B and Company C formed part of the same "group of companies" as defined in section 41(1); and
- as a result of the transaction, Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1), and that was still the position at the end of 31 January 2025.

Example 3 – Definition of "acquisition transaction" – Section 24O(1)

Facts:

Company A's year of assessment ends on 31 December. On 31 January 2025 it acquired 70% of the equity shares in Company B. Company B held 100% of the equity shares in Company C which qualified as an operating company on 31 January 2025. Company A and Company C are residents. Company B is incorporated in a foreign country and does not have its place of effective management in South Africa.

Result:

Relationship between Company B and Company C

Company B is incorporated in a foreign country and does not have its place of effective management in South Africa. Company B is therefore excluded from the definition of "group of companies" in section 41(1) under paragraph (i)(*ee*) of the proviso to the definition. As a result, Company B and Company C did not form part of the same "group of companies" as defined in section 41(1) on 31 January 2025.

Relationship between Company A and Company B

Company B is incorporated in a foreign country and does not have its place of effective management in South Africa. Company B is therefore excluded from the definition of "group of companies" in section 41(1) under paragraph (i)(*ee*) of the proviso to the definition. At the end of 31 January 2025 Company A and Company B did not form part of the same "group of companies" as defined in section 41(1) at the end of 31 January 2025.

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Acquisition transaction

The acquisition of the equity shares by Company A in Company B does not qualify as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired in a company (Company B) but Company B and Company C (the operating company) did not form part of the same "group of companies" as defined in section 41(1); and
- at the end of 31 January 2025 Company A and Company B did not form part of the same "group of companies" as defined in section 41(1).

Example 4 – Definition of "acquisition transaction" – Section 24O(1)

Facts:

Company A's year of assessment ends on 31 December. On 31 January 2025 it acquired 10% of the equity shares in Company B from Company D, which did not form part of the same "group of companies" as defined in section 1(1). Company B was an operating company on that date. Before the transaction Company A held 70% of the equity shares in Company B. All the companies are residents with the places of effective management in South Africa.

Result:

The acquisition by Company A of 10% of the equity shares in Company B on 31 January 2025 does not qualify as an "acquisition transaction" as defined in section 24O(1) because –

- Company A was already a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1) before the transaction; and
- therefore, Company A did not become a controlling group company in relation to Company B and the companies did not commence forming part of the same "group of companies" as defined in section 41(1) as a result of the share acquisition transaction entered into on that date.

Example 5 – Definition of "acquisition transaction" – Section 24O(1)

Facts:

Company A's year of assessment ends on 31 December. On 31 January 2025 it acquired 50% of the equity shares in Company B, which was an operating company on that date. All the equity shares in Company B were previously held by natural persons. On 30 June 2025 Company A acquired a further 20% of the equity shares in Company B. Both companies are residents.

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Result:

Acquisition of equity shares on 31 January 2025 (50%)

The acquisition by Company A of 50% of the equity shares in Company B on 31 January 2025 does not qualify as an "acquisition transaction" as defined in section 24O(1) because –

- Company A held only 50% of the equity shares in Company B as at the end of 31 January 2025, which is less than the required 70%; and
- therefore, Company A was not a controlling group company in relation to Company B and both companies did not form part of the same "group of companies" as defined in section 41(1) as at the end of 31 January 2025.

Acquisition of equity shares on 30 June 2025 (20%)

The acquisition by Company A of 20% of the equity shares in Company B on 30 June 2025 qualifies as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired from a natural person who did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- Company B was an operating company on 31 January and still was on 30 June 2025;
- Company A held 70% (50% + 20%) of the equity shares in Company B as at the end of 30 June 2025; and
- Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1) as at the end of 30 June 2025 as a result of this transaction.

Example 6 – Definition of "acquisition transaction" – Section 24O(1)

Facts:

Company A's year of assessment ends on 31 December. On 31 January 2025 it acquired 90% of the equity shares in Company B, which was an operating company on that date, from natural persons who held all the shares in Company B. Company A acquired these shares in consecutive transactions, namely 20% from Individual A, 40% from Individual B, 20% from Individual C and 10% from Individual D. Company A and Company B are residents.

Result:

Acquisition of equity shares from Individual A (20%) and Individual B (40%)

The consecutive acquisitions of equity shares in Company B by Company A of 20% from Individual A and 40% from Individual B on 31 January 2025 do not qualify as an "acquisition transaction" as defined in section 24O(1), because Company A held only 60% of the equity shares in Company B at the end of these two transactions, which is less than the required 70% for a controlling group company.

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Acquisition of equity shares from Individual C (20%)

The acquisition by Company A of 20% of the equity shares in Company B from Individual C on 31 January 2025 qualifies as an "acquisition transaction" as defined in section 24O(1) because –

- Company A held 80% (20% + 40% + 20%) of the equity shares in Company B as at the end of the third transaction on 31 January 2025, which is more than the required 70%;
- the equity shares were acquired from a natural person who did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- Company B was an operating company on 31 January 2025; and
- Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1) as at the end of 31 January 2025 as a result of the third transaction entered into on that date.

Acquisition of equity shares from Individual D (10%)

The acquisition by Company A of 10% of the equity shares in Company B from Individual D on 31 January 2025 does not qualify as an "acquisition transaction" as defined in section 24O(1) because –

- Company A was already a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1) before the transaction; and
- Company A did not become a controlling group company in relation to Company B and the companies did not commence forming part of the same "group of companies" as defined in section 41(1) as a result of this share acquisition transaction.

(b) Definition of "operating company"

The term "operating company" means a company of which –

- at least 80% of the aggregate amount received by or that accrued to that company during a year of assessment constitutes income [paragraph (*a*) of the definition]; and
- the income contemplated above is derived –
  - from a business carried on continuously by that company [paragraph (*b*)(i) of the definition]; and
  - in the course or furtherance of which goods or services are provided or rendered by that company for consideration [paragraph (*b*)(ii) of the definition].

At least 80% of the aggregate amount received or accrued during a year of assessment constitutes income [paragraph (a) of the definition of "operating company"]

At least 80% of the aggregate amount received by or that accrued to a potential operating company during a year of assessment must constitute income of that company. The word "income" in this context has its meaning as defined in section 1(1), namely, the amount remaining of the gross income of any person for any year or period

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of assessment after deducting any amounts exempt from normal tax under Part I[33] of Chapter II of the Act. In the context of the definition of an operating company, the "aggregate amount received by or accrued to that taxpayer", is considered to include amounts of a revenue and a capital nature.

Thus, a company deriving only exempt dividends would not qualify as an operating company, since 100% of the amounts received or accrued during a year of assessment would be exempt from normal tax and would not constitute income.

The "80%" requirement is ongoing and must be met in each year of assessment that a company seeks to claim a deduction for interest under the relevant deduction section, read with section 24O(2). Depending on the facts, under section 24O(2)(ii) (see **4.3.2**) the equity share must constitute a qualifying interest in an operating company as determined –

- in the case of an equity share held by that company at the end of that year, at the date on which that year ends; or
- if that equity share was disposed of during that year, at the date of that disposal.

Therefore, the "80%" requirement is determined with reference to the potential operating company's *latest year of assessment* which ended i) before or on the last day of the company seeking to claim the deduction's year end or, ii) if that company disposed of the equity shares acquired under the acquisition transaction during the year of assessment, the date of that disposal[34] (see **4.3.2** and **4.3.3**).

The "80%" requirement also needs to be met on the date that the company seeking to apply section 24O acquired the relevant equity shares – see **4.3.1 (a) Definition of "acquisition transaction"** which includes a requirement for the identified companies to be an operating company on the date of the transaction. It is reasonable to determine the "80%" requirement with reference to the potential operating company's latest year of assessment which ended before or on the date of acquisition.

Income derived from a business carried on continuously [paragraph (b)(i) of the definition of "operating company"]

The income referred to above must be derived by the potential operating company from a business carried on continuously.

The words "business" and "a business carried on continuously" are not defined in the Act. *CollinsDictionary.com* [35] defines "business" as –

> "**1.** a trade or profession. **2.** an industrial, commercial, or professional operation; purchase and sale of goods and services:…".

The same dictionary defines "continuous" as –

> "**1.** prolonged without interruption; unceasing:…**2.** in an unbroken series or pattern".

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33 Sections 5 to 37G are contained in Part I of Chapter II of the Act.

34 Section 24O(2)(*b*) and (3).

35 **www.collinsdictionary.com/dictionary/english/business** [Accessed 24 November 2026].

The meaning of "business" and "carrying on a business" has been considered in a number of court cases. In *CIR v Transvaal Bookmakers' Association (Co-operative) Ltd* Price J stated the following on the meaning of "business":[36]

> "The word 'business' is probably somewhat wider than the word 'trade' as ordinarily understood (*Modderfontein Deep Levels Ltd. and Another v Feinstein*, 1920 T.P.D. 288). 'Trade' must therefore be given a meaning wide enough to include 'business'. In *South African Flour Millers Mutual Association v Rutowitz Flour Mills Ltd*., 1938 C.P.D. 199, it was said that anything that occupies the time and attention of a man for profit is business, although it seems that the intention to make a profit need not be present."

All the facts and circumstances must be considered in determining whether a person carries on a business. Factors to consider include the nature and scope of the activities, the presence or absence of a profit motive and the continuity of the activities.[37]

In *Estate G v COT* Beadle CJ stated the following on the meaning of "carrying on a business":[38]

> "The sensible approach, I think, is to look at the activities concerned as a whole, and then to ask the question: Are these the sort of activities which, in commercial life, would be regarded as 'carrying on business'? The principal features of the activities which might be examined in order to determine this are their nature, their scope and magnitude, their object (whether to make a profit or not), the continuity of the activities concerned, if the acquisition of property is involved, the intention with which the property was acquired. This list of features does not purport to be exhaustive, nor are any one of these features necessarily decisive, nor is it possible to generalize and state which feature should carry most weight in determining the problem. Each case must depend on its own particular circumstances."

In *CIR v Lydenburg Platinum Ltd* Stratford JA stated the following on the element of continuity in carrying on a business:[39]

> "So that 'continuity' (as it had been called) was a necessary element in the carrying on of a business in the case of an individual but not of a company. Indeed, many cases had come before the Court where there had only been one profit-making transaction of a company, and that fact had never been relied upon as in any way decisive of the question whether the profit had been made in the carrying on of the company's business or otherwise. In the case of a company the Court had primarily to look at its objects laid down in its constitution and next at its actual operations."

A company that may in future be carrying on a business continuously but is not doing so at the time that its equity shares are acquired by another company, does not meet the above requirement.

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36 1953 (3) SA 203 (T), 19 SATC 14 at 18 and 19. See also *Smith v Anderson* (1880) 15 ChD 247 (CA); *Modderfontein Deep Levels Ltd v Feinstein* 1920 TPD 288 and *Platt v CIR* 1922 AD 42, 32 SATC 142.

37 See *Platt v CIR* 1922 AD 42, 32 SATC 142; *Stephan v CIR* 1919 WLD 1, 32 SATC 54; ITC 1501 (1989) 53 SATC 314 (C) and ITC 1529 (1991) 54 SATC 252 (C).

38 1964 (2) SA 701 (SR), 26 SATC 168 at 173. The judge drew a distinction between circumstances in which renting properties might be an investment versus the carrying on of a business.

39 1929 AD 137, 4 SATC 8 at 16 and 17. See also *Platt v CIR* 1922 AD 42, 32 SATC 142; *Yates Investments (Pty) Ltd v CIR* 1956 (1) SA 612 (A), 20 SATC 368 and *CIR v Strathmore Exploration Ltd* 1956 (1) SA 591 (A), 20 SATC 375.

In the course or furtherance of which goods or services are provided or rendered for consideration [paragraph (b)(ii) of the definition of "operating company"]

The income referred to above must be derived from a business carried on continuously in the course or furtherance of which goods or services are provided or rendered by the company concerned for consideration.

The words "goods" and "services" are not defined in the Act. Consideration must, therefore, be given to their ordinary grammatical meaning taking into account the context in which they appear and the purpose to which they are directed.

CollinsDictionary.com defines "goods" as follows:[40]

> "1. possessions and personal property …
>
> 2. commodities that are tangible, usually movable, and generally not consumed at the same time as they are produced 3. articles of commerce; merchandise."

CollinsDictionary.com defines "services" as follows:[41]

> "Services are activities such as tourism, banking, and accountancy that are part of a country's economy, but are not concerned with producing or manufacturing goods."

A company that neither provides goods nor renders services but is involved in other activities will not qualify as an operating company. For example, an investment company that derives passive income and neither provides goods nor renders any services will not qualify as an operating company, as even if it meets the 80% income requirement, that income is not derived from consideration received in providing goods or rendering services.

A company must derive consideration for providing goods or rendering services in order to qualify as an operating company.

Collinsdictionary.com defines "consideration" as follows:[42]

> "7. payment for a service; recompense; fee …
>
> 9. *Law* - the promise, object, etc, given by one party to persuade another to enter into a contract.."

In *Ogus v SIR*[43] "consideration" was held, in the context of donations tax, to mean the *quid pro quo* given under a reciprocal obligation.

The *quid pro quo* received by a person could be in the form of money or a form other than money, for example, a motor vehicle or the right of use of an asset. The principles established in *C: SARS v Brummeria Renaissance (Pty) Ltd & Others*[44] in relation to the determination of what constituted the accrual of an *amount* for the purposes of the definition of "gross income" in section 1(1) are considered relevant. Consideration in a form other than money must therefore be capable of being valued in money and

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40 **www.collinsdictionary.com/dictionary/english/goods** [Accessed 24 November 2026].

41 **www.collinsdictionary.com/dictionary/english/service** [Accessed 24 November 2026].

42 **www.collinsdictionary.com/dictionary/english/consideration** [Accessed 24 November 2026].

43 1978 (3) SA 67 (T), 40 SATC 100 at 112.

44 20 07 (6) SA 601 (SCA), 69 SATC 205. See also Interpretation Note 58 "The Brummeria case and the right to use loan capital interest free."

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although the ability to turn that consideration into money may be one of the ways to determine its value in money, it is not essential. The determination of value is an objective, not a subjective test.

Whether a company is an operating company will be determined by the facts of each case. The requirements of the definition of "operating company" must be applied strictly.

Example 7 – Definition of "operating company" – Section 24O(1)

Facts:

Company A and Company B's years of assessment end on 31 December. Both companies are residents and have their place of effective management in South Africa. On 31 January 2025 Company A acquired 70% of the equity shares in Company B, an operating company on the date of acquisition, which it still held on 31 December 2025.

Company B carried on a business continuously and derived income of R400 000 from the rendering of services during its 2025 year of assessment. It also derived dividends of R1,6 million. The aggregate amount received by or that accrued to Company B during its 2024 year of assessment amounted to R2 million (R400 000 + R1,6 million).

Result:

Under section 24O(2)(ii)(*aa*), the equity shares in Company B held by Company A must constitute a qualifying interest in an operating company at the date on which Company A's year of assessment ends, namely 31 December 2025. Section 24O(3)(*a*) provides that the equity shares in Company B will constitute a qualifying interest in an operating company at 31 December 2025 if Company B was an operating company in its latest year of assessment that ended before or on 31 December 2025. Its latest year of assessment ended on 31 December 2025.

The dividends derived by Company B of R1,6 million are included in its gross income under paragraph (*k*) of the definition of "gross income" in section 1(1). These dividends are exempt from normal tax under section 10(1)(*k*)(i) and are not included in Company B's income.

The consideration received from the rendering of services of R400 000 is included in Company B's income, since it is not exempt from normal tax. This income is derived from rendering services in the course of a business which is carried on continuously.

Although Company B derived income from the rendering of services, it is not an "operating company" as defined in section 24O(1), since only 20% [(R400 000 / R2 million) × 100%] of the aggregate amount received by or that accrued to Company B during the 2025 year of assessment constituted income, which is less than the required 80%.

Company A therefore does not have a qualifying interest in an operating company as at 31 December 2025 as required in sections 24O(2) and 24O(3).

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Example 8 – Definition of "operating company" – Section 24O(1)

Facts:

Company A and Company B's years of assessment end on 31 March and 31 December respectively. Both companies are residents and have their place of effective management in South Africa. On 31 January 2025 Company A acquired 70% of the equity shares in Company B, an operating company on the date of acquisition, which it still held on 31 March 2025.

Company B's main business constitutes investment in fixed property but it also provides administrative services. It derived R1 million from the rendering of administrative services during its 2024 year of assessment. It also derived rental income of R1,2 million from investment in fixed property and sold a fixed property which cost R2 million for R2,5 million.

Result:

Under section 24O(2)(ii)(*aa*), the equity shares in Company B held by Company A must constitute a qualifying interest in an operating company at the date on which Company A's year of assessment ends, namely 31 March 2025. Section 24O(3)(*a*) provides that the equity shares in Company B will constitute a qualifying interest in an operating company at 31 March 2025 if Company B was an operating company in its latest year of assessment that ended before or on 31 March 2025. Its latest year of assessment ended on 31 December 2024.

The consideration received for the rendering of administrative services of R1 million and the rental income of R1,2 million, in the course of a business which is carried on continuously, is included in Company B's income, since these receipts and accruals are not exempt from normal tax.

In context of the definition of "operating company" in section 24O, the aggregate amount received by or that accrued to Company B during its 2024 year of assessment amounted to R4,7 million (R1 million administration services + R1,2 million rental income + R2,5 million capital proceeds).

Although Company B derived income from the rendering of services in carrying on a business continuously, it is not an "operating company" as defined in section 24O(1), since only 21,28% [(R1 million / R4,7 million × 100%] of the aggregate amount received by or that accrued to Company B during its 2024 year of assessment was derived in the course or furtherance of providing goods or rendering of services for consideration. The rental income does not constitute income from providing goods or rendering of services. The proceeds of R2,5 million are not included in gross income or income as they are not of a revenue nature, they are however included in the aggregate amount received by or accrued to Company B during its 2024 year of assessment.

Company A therefore does not have a qualifying interest in an operating company as at 31 March 2025 as required in sections 24O(2) and 24O(3).

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4.3.2 Deductibility of interest incurred on debt relating to the acquisition of equity shares in respect of an acquisition transaction [section 24O(2)]

Section 24O(2) provides that, subject to section 24O(3), when any interest is incurred by a company on a debt issued, assumed or used by that company –

- for the purpose of financing the acquisition by that company under an acquisition transaction of an equity share; or
- in substitution for a debt issued, assumed or used as contemplated in the first bullet,

the interest incurred by that company on that debt must, to the extent to which the amount thereof relates to a period during which the company held the equity share and the equity share constituted a qualifying interest in an operating company as determined –

- in the case of an equity share held by that company at the end of that year, at the date on which that year ends; or
- if that equity share was disposed of during that year, at the date of that disposal,

be deemed to have been incurred in the production of income and laid out or expended by that company for the purposes of trade.

Since the "in the production of income" and "trade" requirements are deemed to be met, the effect of section 24O(2) is that interest so incurred becomes deductible under section 11(*a*) or 24J(2) provided all the requirements of those sections are met. For ease of reference, in the examples included throughout this Note, the deduction is generally referred to in the context of section 24J(2) only, if for some reason section 24J(2) did not apply, depending on the facts a taxpayer could potentially met the requirements of and qualify for a deduction under section 11(*a*). The interest deduction may be subject to limitation under sections 23M (see **4.5**) and 23N (see **4.4**).

Meaning of interest

The word "interest" is not defined in section 24O(1). Although "interest" is defined in section 24J(1), the term so defined applies to section 24J and to other sections that specifically refer to the definition in that section. Since section 24O does not refer to the definition of "interest" in section 24J(1), the common law meaning of "interest" must be applied for purposes of section 24O.

The *Merriam Webster Dictionary* defines "interest" as follows –[45]

> "3 a : a charge for borrowed money generally a percentage of the amount borrowed".

Dictionary.com defines "interest" as –

> "a sum paid or charged for the use of money or for borrowing money:"[46]

The term "interest" has also been considered judicially.

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45 **www.merriam-webster.com/dictionary/interest** [Accessed 24 November 2026].

46 **www.dictionary.com/browse/interest** [Accessed 24 November 2026].

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In ITC 1485 and ITC 1496 Melamet J stated the following on the meaning of interest:[47]

> " 'Interest is the return or compensation for the use or retention by one person of a sum of money belonging to or owed to another...'
>
> *Halsbury's Laws of England* 4ed Vol 32 para 106, see also Vol 33 para 524.
> *Words and Phrases Legally Defined* 3ed (D-J) s v 'Interest' at p 564.
> Lee and Honore *The South African Law of Obligations* para 174.
>
> Interest is an expense to compensate a lender for the time period during which the money is lent to a second party."

This meaning of interest was echoed in *Commissioner for Inland Revenue v Cactus Investments (Pty) Ltd*[48] when Wunsh J referred to ITC 1485[49] and stated that interest is "compensation for the receipt and retention of the money".[50]

See Interpretation Note 142 "Meaning of 'Similar Finance Charges'" for additional commentary on the meaning of interest in relation to loans for consumption.

In light of the above, it can be concluded that the amount which constitutes interest is the charge for the use of money borrowed and which a person receives for giving someone the use of the money or "compensation for the receipt and retention of money".

The meaning of "interest" as determined under common law is narrower than the definition of "interest" in section 24J(1) which has the effect that the qualifying interest contemplated in section 24O is limited.[51]

Meaning of debt

The word "debt" is not defined in sections 1(1) or 24O. Consideration must therefore be given to its ordinary grammatical meaning taking into account the context in which it appears and the purpose to which it is directed.

Collinsdictionary.com defines "debt" as follows:[52]

> "A debt is a sum of money that you owe someone."

Debt means an amount owed by one person (the debtor) to another (the creditor). Debt may include, amongst other things, a loan, advance, note, bond, debenture, bank deposit or any other claim of money requiring repayment.[53]

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47 (1990) 52 SATC 337 (T) at 342 and (1990) 53 SATC 229 (T) at 248 and 249.

48 59 SATC 1 at 27.

49 52 SATC 337.

50 The case was taken on appeal – see *Cactus Investments (Pty) Ltd v CIR* [1999] 1 All SA 345 (A); 61 SATC 43. The case dealt with a loan for consumption and the SCA noted that interest, in those circumstances, could not be compensation for the use of money, since ownership of the money changes in loans for consumption. The timing of the accrual, and not the fact that amount was interest, was in dispute. Therefore, it was not necessary for the court to provide and apply a definition tailored to loans for consumption. Subsequent to this case section 24J, which deals with the timing of the incurral, was introduced.

51 See **4.4.1 (f)** for a consideration of the meaning of "interest" as defined in section 24J(1).

52 **www.collinsdictionary.com/dictionary/english/debt** [Accessed 24 November 2026].

53 Paragraph 2.3 of the *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2012*.

Meaning of debt issued, assumed or used

The words "debt issued, assumed or used" are not defined in the Act. Consideration must therefore be given to their ordinary grammatical meaning taking into account the context in which they appear and the purpose to which they are directed.

Debt issued

Collinsdictionary.com defines "debt issue" as follows:[54]

> "any fixed corporate obligations, as bonds or debentures."

A debt issue refers to a financial obligation that allows the issuer to raise funds by promising to repay the lender at a certain point in the future and in accordance with the terms of the contract.[55] A debt may be issued by a company for, for example, the purpose of financing the acquisition by that company of an equity share under an acquisition transaction. When a debt is issued by a company, a liability to pay the debt is created.

Debt assumed

The meaning of "debt assumption" is described by the IMF[56] as follows:[57]

> "Debt assumption is a trilateral agreement between a creditor, a former debtor, and a new debtor under which the new debtor assumes the former debtor's outstanding liability to the creditor and is liable for repayment of debt."

Debt used

Utilisation of debt acquired. A company may, for example, obtain financing from a bank or other third party and apply the funds to finance the acquisition of equity shares under an acquisition transaction.

Original debt and substitution for a debt

As stated above, section 24O(2) requires that a debt be issued, assumed or used by a company for the following reasons:

- First, it may be issued, assumed or used in order to finance the acquisition by that company of an equity share under an acquisition transaction.
- Secondly, it may be issued, assumed or used to substitute the debt referred to in the first bullet. For example, this situation may occur when a company obtains funding from a person to repay the debt originally issued, assumed or used for purposes of financing the acquisition of equity shares under an acquisition transaction.

A debt issued, used or assumed by a company for purposes other than the acquisition of equity shares under an acquisition transaction or to substitute debt previously used to acquire equity shares under an acquisition transaction, falls outside the scope of section 24O.

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54 **www.collinsdictionary.com/dictionary/english/debt-issue** [Accessed 24 November 2026].

55 **www.investopedia.com/terms/d/debt-issue.asp** [Accessed 24 November 2026].

56 International Monetary Fund.

57 Sixth Edition of the IMF's Balance of Payments and International Investment Position Manual (BPM6) in Annexure 2, https://www.imf.org/external/pubs/ft/bop/2007/bopman6.htm [Accessed 24 November 2026].

To the extent to which the amount of interest relates to a period during which the company held the equity share and the equity share constituted a "qualifying interest in an operating company" as determined at the specified date

Interest incurred by a company on a debt referred to above is deemed to have been incurred in the production of income of the company and laid out or expended for the purposes of its trade to the extent to which the amount thereof relates to a period during which that company held that equity share and the equity share constituted a qualifying interest in an operating company (see **4.3.3**) as determined on the following date:

- In the case of an equity share held by the company at the end of the year of assessment, at the date on which that year of assessment ends.
- If the equity share was disposed of during the year of assessment, at the date of disposal.

4.3.3 Determination whether an equity share constitutes a qualifying interest in an operating company [section 24O(3)]

An equity share in a company constitutes a qualifying interest in an operating company, if that share is an equity share on the applicable date referred to in section 24O(2)(ii) (see **4.3.2**) in –

- a company that qualified as an operating company in its latest year of assessment that ended before or on the applicable date[58] referred to in section 24O(2)(ii) (see **4.3.2**) [section 24O(3)(*a*)]; or
- any other company to the extent the value of the equity share in that other company is derived from an equity share or equity shares held by that other company in operating companies described in section 24O(3)(*a*)[59] in relation to which that other company is (i) a controlling group company in relation to an operating company and (ii) forms part of the same "group of companies" as defined in section 41(1) as those operating companies so described [section 24O(3)(*b*)].

  For example, if 60% of the value of an equity share in Company B is derived from equity shares that Company B held in companies that qualified as operating companies in their latest year of assessment ending on the applicable date in section 24O(2)(ii) and Company B is a controlling group company in relation to each of those operating companies and forms part of the same group of companies as defined in section 41(1) as those operating companies, then the 60% of the equity share in Company B will be a qualifying interest in an operating company.

  Under the proviso to section 24O(3)(*b*) an equity share in a controlling group company holding equity shares in an operating company or companies, as described above, is treated as fully constituting a qualifying interest in an operating company if at least 90% of the value of that equity share in the controlling group company is derived from an equity share or equity shares held by that controlling group company in the operating company or operating companies referred to above. The *Explanatory Memorandum on the Taxation*

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58 In the case of an equity share held by the company at the end of the year of assessment, at the date on which that year of assessment ends. If the equity share was disposed of during the year of assessment, at the date of disposal.

59 See preceding bullet point.

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Laws Amendment Bill, 2015[60] stated that as a way to accommodate *bona fide* and non-erosive indirect acquisitions of largely productive operations, when at least 90% of the value of the equity shares of a holding company that is being acquired is derived from an equity share held by that holding company in an operating company, 100% of the interest expense will be allowed on debt used to acquire the equity shares of such a company (*subject to the requirements in section 24O(2))*.

Example 9 – Deductibility of interest incurred on debt relating to the acquisition of equity shares in terms of an acquisition transaction– Section 24O(3)(*a*)

Facts:

Company A and Company B's years of assessment end on 31 December. On 31 January 2025 Company A acquired 70% of the equity shares in Company B under an acquisition transaction which it still held on 31 December 2025. Company B qualified as an operating company for its 2025 year of assessment.

Company A incurred interest of R200 000 during its 2025 year of assessment on debt used for the purpose of financing the acquisition of the equity shares in Company B. Both companies were residents and had their place of effective management in South Africa for the duration of the 2025 year of assessment.

Result:

Under section 24O(3)(*a*) the equity shares held by Company A in Company B constituted a qualifying interest in an operating company on 31 December 2025 (last day of Company A's year of assessment), since Company B was an operating company in its latest year assessment which ended on 31 December 2025.

Under section 24O(2) the interest of R200 000 is deemed to have been incurred in the production of Company A's income and laid out or expended for the purposes of its trade, since Company A held the equity shares for the full period that the interest relates to and the equity shares constituted a qualifying interest in an operating company (Company B) on 31 December 2025. The interest is therefore deductible under section 24J(2), subject to all of its requirements being met, read with section 24O(2), but may be subject to limitation under sections 23M (see **4.5**) and 23N (see **4.4**).

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[60] In paragraph 2.1.

Example 10 – Deductibility of interest incurred on debt relating to the acquisition of equity shares in terms of an acquisition transaction – Section 24O(3)(*b*)

Facts:

On 31 January 2025 Company A acquired 70% of the equity shares in Company B which it still held on 31 December 2025. The shares were acquired from a company which did not form part of the same "group of companies" as defined in section 1(1) as Company A. On 31 January 2025 Company B held 100% of the equity shares in Company C which qualified as an operating company at that date and 10% of the equity shares in Company D, which did not qualify as an operating company. The market value of Company B's equity shares in Company C and Company D on 31 December 2025 was R3 million and R6 million respectively. Company B did not hold any other assets. Company C also qualified as an operating company for its latest year of assessment ending on 31 December 2025.

Company A incurred interest of R300 000 during its 2025 year of assessment on debt used for the purpose of financing the acquisition of the equity shares in Company B.

The years of assessment of all companies ended on 31 December. All the companies were residents and had their place of effective management in South Africa for the duration of the 2025 year of assessment.

Result:

Relationship between Company B and Company C

On 31 January 2025 and 31 December 2025 Company B and Company C formed part of the same "group of companies" as defined in section 41(1) and Company B was a controlling group company in relation to Company C because –

- Company B directly held shares in at least one other company (Company C);
- at least 70% of the equity shares in the controlled group company (Company C) were directly held by the controlling group company (Company B, held 100%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company B) directly held at least 70% of the equity shares in at least one controlled group company (Company C); and
- neither Company B nor Company C was excluded from the definition of "group of companies" in section 41(1).

Relationship between Company B and Company D

On 31 January 2025 and 31 December 2025 Company B and Company D did not form part of the same "group of companies" as defined in section 41(1) because Company B directly held 10% shares in Company D and no other controlled companies in relation to Company B held any shares in Company D.

Relationship between Company A and Company B

At the end of 31 January 2025 Company A and Company B formed part of the same "group of companies" as defined in section 41(1) and Company A was a controlling group company in relation to Company B because –

- Company A directly held shares in at least one other company (Company B);

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- at least 70% of the equity shares in the controlled group company (Company B) were directly held by the controlling group company (Company A, held 70%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company A) directly held at least 70% of the equity shares in at least one controlled group company (Company B); and
- neither Company A nor Company B was excluded from the definition of "group of companies" in section 41(1).

Acquisition transaction

The acquisition of the equity shares by Company A in Company B qualified as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired from a company which did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- the equity shares were acquired in a company (Company B) which was a controlling group company in relation to an operating company (Company C) and Company B and Company C formed part of the same "group of companies" as defined in section 41(1); and
- as a result of the transaction, Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1), and that was still the position at the end of 31 January 2025.

Under section 24O(3)(*b*), to the extent of 33⅓ %, the equity shares held by Company A in Company B constituted a qualifying interest in an operating company on 31 December 2025 (last day of Company A's year of assessment), since 33⅓ % [(R3 million / R9 million) × 100%] of the value of the equity shares acquired by Company A in Company B was derived from the value of the equity shares held by Company B in an operating company (Company C) for that operating company's latest year of assessment ending on 31 December 2025 and in relation to which Company B is a controlling group company and part of the same group of companies as defined in section 41(1).

Under section 24O(2) the interest is deemed to have been incurred in the production of income and laid out or expended for the purposes of trade *to the extent* that the interest relates to the period during which Company A held the equity shares in Company B and to the extent those shares constituted a qualifying interest in an operating company on the applicable date of 31 December 2025.

Therefore, under sections 24O(2) and 24(3)(*b*) interest of R100 000 (1 / 3 × R300 000) is deemed to have been incurred by Company A in the production of income and laid out or expended for the purposes of its trade, since the debt was used to finance the acquisition of the shares in Company B under an acquisition transaction (see above), the interest relates to a period during which Company A held the shares in Company B and to the extent ⅓ of the equity share constituted a qualifying interest in an operating company on 31 December 2025.

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Interest of R100 000 is therefore deductible under section 24J(2), subject to all of its requirements being met, read with section 24O(2) but may be subject to limitation under sections 23M (see **4.5**) and 23N (see **4.4**).

Example 11 – Deductibility of interest incurred on debt relating to the acquisition of equity shares in terms of an acquisition transaction – Section 24O(3)(*b*)

Facts:

On 31 January 2025 Company A acquired 70% of the equity shares in Company B which it disposed of on 30 June 2025. The shares were acquired from a company which did not form part of the same "group of companies" as defined in section 1(1) as Company A. On 31 January 2025 Company B held 100% of the equity shares in Company C which qualified as an operating company at that date and 10% of the equity shares in Company D, which did not qualify as an operating company. The market value of Company B's equity shares in Company C and Company D on 30 June 2025 was R3 million and R6 million respectively. Company B did not hold any other assets. Company C also qualified as an operating company on 30 June 2025.

Company A incurred interest of R300 000 during its 2025 year of assessment on debt used for the purpose of financing the acquisition of the equity shares in Company B. The full balance of the loan was outstanding at year end.

The years of assessment of all companies ended on 31 December. All the companies were residents and had their place of effective management in South Africa for the duration of the 2025 year of assessment.

Result:

Relationship between Company B and Company C

On 31 January 2025 and 30 June 2025 (date of disposal of the equity shares in Company B) Company B and Company C formed part of the same "group of companies" as defined in section 41(1) and Company B was a controlling group company in relation to Company C because –

- Company B directly held shares in at least one other company (Company C);
- at least 70% of the equity shares in the controlled group company (Company C) were directly held by the controlling group company (Company B, held 100%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company B) directly held at least 70% of the equity shares in at least one controlled group company (Company C); and
- neither Company B nor Company C was excluded from the definition of "group of companies" in section 41(1).

Relationship between Company B and Company D

On 31 January 2025 and 30 June 2025 Company B and Company D did not form part of the same "group of companies" as defined in section 41(1) because Company B directly held 10% shares in Company D and no other controlled companies in relation to Company B held any shares in Company D.

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Relationship between Company A and Company B

At the end of 31 January 2025 Company A and Company B formed part of the same "group of companies" as defined in section 41(1) and Company A was a controlling group company in relation to Company B because –

- Company A directly held shares in at least one other company (Company B);
- at least 70% of the equity shares in the controlled group company (Company B) were directly held by the controlling group company (Company A, held 70%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company A) directly held at least 70% of the equity shares in at least one controlled group company (Company B); and
- neither Company A nor Company B was excluded from the definition of "group of companies" in section 41(1).

Acquisition transaction

The acquisition of the equity shares by Company A in Company B qualified as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired from a company which did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- the equity shares were acquired in a company (Company B) which was a controlling group company in relation to an operating company (Company C) and Company B and Company C formed part of the same "group of companies" as defined in section 41(1); and
- as a result of the transaction, Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1), and that was still the position at the 30 June 2025.

Under section 24O(3)(*b*), to the extent of 33⅓ %, the equity shares held by Company A in Company B constituted a qualifying interest in an operating company on 30 June 2025 (date of disposal of the equity shares by Company A), since 33⅓ % [(R3 million / R9 million) × 100%] of the value of the equity shares acquired by Company A in Company B was derived from the value of the equity shares held by Company B in an operating company (Company C) as at 30 June 2025 and in relation to which Company B is a controlling group company and part of the same group of companies as defined in section 41(1).

Under section 24O(2) the interest is deemed to have been incurred in the production of income and laid out or expended for the purposes of trade *to the extent* that the interest relates to the period during which Company A held the equity shares in Company B ***and*** *to the extent* those shares constituted a qualifying interest in an operating company on the applicable date of disposal, 30 June 2025.

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Therefore, under section 24O(2) and (3)(*b*) interest of R44 910 [⅓ (to the extent the shares constituted a qualifying interest) x 150/ 334 (to the extent the interest relates to a period the shares were held) x R300 000] is deemed to have been incurred by Company A in the production of income and laid out or expended for the purposes of its trade, since the debt was used to finance the acquisition of the shares in Company B under an acquisition transaction (see above), the interest relates to a period during which Company A held the shares in Company B and to the extent of ⅓ that the equity share constituted a qualifying interest in an operating company on 30 June 2025.

Interest of R44 910 is therefore deductible under section 24J(2), subject to all of its requirements being met, read with section 24O(2) but may be subject to limitation under sections 23M (see **4.5**) and 23N (see **4.4**).

Example 12 – Deductibility of interest incurred on debt relating to the acquisition of equity shares in terms of an acquisition transaction– The proviso to section 24O(3)(*b*)

Facts:

On 31 January 2025 Company A acquired 70% of the equity shares in Company B which it still held on 31 December 2025. The shares were acquired from a company which did not form part of the same "group of companies" as defined in section 1(1), as Company A. On 31 January 2025 Company B held 100% of the equity shares in Company C and 10% of the equity shares in Company D. Company B held no other assets. Company C qualified as an operating company for the duration of its 2025 year of assessment, but Company D did not qualify as an operating company.

The market value of Company B's equity shares in Company C and Company D on 31 December 2025 was R9 million and R1 million respectively.

Company A incurred interest of R300 000 during its 2025 year of assessment on debt used for the purpose of financing the acquisition of the equity shares in Company B.

The years of assessments of all companies ended on 31 December. All the companies were residents for the duration of the 2025 year of assessment.

Result:

Relationship between Company B and Company C

On 31 January 2025 and 31 December 2025 Company B and Company C formed part of the same "group of companies" as defined in section 41(1) and Company B was a controlling group company in relation to Company C because –

- Company B directly held shares in at least one other company (Company C);
- at least 70% of the equity shares in the controlled group company (Company C) were directly held by the controlling group company (Company B, held 100%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company B) directly held at least 70% of the equity shares in at least one controlled group company (Company C); and
- neither Company B nor Company C was excluded from the definition of "group of companies" in section 41(1).

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Relationship between Company B and Company D

On 31 January 2025 and 31 December 2025 Company B and Company D did not form part of the same "group of companies" as defined in section 41(1) because Company B directly held 10% shares in Company D and no other controlled companies in relation to Company B held any shares in Company D.

Relationship between Company A and Company B

At the end of 31 January 2025 Company A and Company B formed part of the same "group of companies" as defined in section 41(1) and Company A was a controlling group company in relation to Company B because –

- Company A directly held shares in at least one other company (Company B);
- at least 70% of the equity shares in the controlled group company (Company B) were directly held by the controlling group company (Company A, held 70%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company A) directly held at least 70% of the equity shares in at least one controlled group company (Company B); and
- neither Company A nor Company B was excluded from the definition of "group of companies" in section 41(1).

Acquisition transaction

The acquisition of the equity shares by Company A in Company B qualified as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired from a company which did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- the equity shares were acquired in a company (Company B) which was a controlling group company in relation to an operating company (Company C) and Company B and Company C formed part of the same "group of companies" as defined in section 41(1); and
- as a result of the transaction, Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1), and that was still the position at the end of 31 January 2025.

Under the proviso to section 24O(3)(*b*) the equity shares in Company B are treated as shares in an operating company since at least 90% [(R9 million / (R9 million + R1 million)) × 100%] of the value of the equity shares acquired by Company A in Company B was derived from the value of the equity shares held by Company B in an operating company or companies (in this case, Company C) for that operating company's or companies' latest year of assessment ending on 31 December 2025 and in relation to which Company B is a controlling group company and part of the same group of companies as defined in section 41(1).

Under section 24O(3)(*a*) an equity share in an operating company in its latest year of assessment ending before or on Company A's year of assessment (31 December 2025) is a qualifying equity interest at that date.

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Under section 24O(2) the interest of R300 000 is deemed to have been incurred in the production of income and laid out or expended for the purposes of trade since the debt was used to finance the acquisition of the shares in Company B under an acquisition transaction (see above), the interest relates to a period during which Company A held the shares in Company B and the equity shares in Company B constituted a qualifying interest in an operating company on 31 December 2025.

The interest of R300 000 is therefore deductible in full under section 24J(2), subject to all of its requirements being met, read with section 24O(2) but may be subject to limitation under sections 23M (see **4.5**) and 23N (see **4.4**).

4.3.4 Acquisition of equity shares in an operating company from a controlling group company under an unbundling transaction or a liquidation distribution [section 24O(5)]

Section 24O(5) applies when a company that acquired equity shares in a controlling group company in relation to an operating company under paragraph (*b*) of the definition of "acquisition transaction" in section 24O(1), subsequently acquires the equity shares held by that controlling group company in *that* operating company under an "unbundling transaction" as defined in section 46(1)(*a*) in respect of which section 46 was applied or a "liquidation distribution" as defined in section 47(1)(*a*) in respect of which section 47 was applied [see **4.4.1(h)**].

The equity shares in the operating company so acquired from the controlling group company must for purposes of section 24O(2) be treated –

- as having been acquired under paragraph (*a*) of the definition of "acquisition transaction" in section 24O(1); and
- as constituting a qualifying interest in an operating company to the extent to which the value of the equity shares in the controlling group company from which the equity shares in the operating company were acquired was derived from the value of the equity shares in the operating company so acquired. The values at the date of the unbundling transaction are relevant.

Example 13 – Acquisition of equity shares in an operating company from a controlling group company under an unbundling transaction

Facts:

On 31 January 2025 Company A acquired 70% of the equity shares in Company B which it still held on 31 December 2025. On 31 January 2025 Company B held 100% of the equity shares in Company C which qualified as an operating company at that date. Company B held no other assets. Company C qualified as an operating company for its latest year of assessment ending on 31 December 2025.

On 30 June 2025 Company A acquired 70% of the equity shares in Company C from Company B under an "unbundling transaction" as defined in section 46(1)(*a*). Section 46 applied to the transaction.

Company A incurred interest of R300 000 during its 2025 year of assessment on debt used for the purpose of financing the acquisition of the equity shares in Company B.

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The years of assessments of all companies ended on 31 December. All the companies were residents and had their place of effective management in South Africa for the duration of the 2025 year of assessment.

Result:

Relationship between Company B and Company C

On 31 January 2025 Company B and Company C formed part of the same "group of companies" as defined in section 41(1) and Company B was a controlling group company in relation to Company C because –

- Company B directly held shares in at least one other company (Company C);
- at least 70% of the equity shares in the controlled group company (Company C) were directly held by the controlling group company (Company B, held 100%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company B) directly held at least 70% of the equity shares in at least one controlled group company (Company C); and
- neither Company B nor Company C was excluded from the definition of "group of companies" in section 41(1).

Relationship between Company A and Company B

At the end of 31 January 2025 Company A and Company B formed part of the same "group of companies" as defined in section 41(1) and Company A was a controlling group company in relation to Company B because –

- Company A directly held shares in at least one other company (Company B);
- at least 70% of the equity shares in the controlled group company (Company B) were directly held by the controlling group company (Company A, held 70%), one or more controlled group companies (not applicable) or any combination thereof;
- the controlling group company (Company A) directly held at least 70% of the equity shares in at least one controlled group company (Company B); and
- neither Company A nor Company B was excluded from the definition of "group of companies" in section 41(1).

*Acquisition transac*tion - *31 January 2025*

The acquisition of the equity shares by Company A in Company B on 31 January 2025 qualified as an "acquisition transaction" as defined in section 24O(1) because –

- the equity shares were acquired from a company which did not form part of the same "group of companies" as defined in section 1(1) as Company A;
- the equity shares were acquired in a company (Company B) which was a controlling group company in relation to an operating company (Company C) and Company B and Company C formed part of the same "group of companies" as defined in section 41(1); and

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- as a result of the transaction, Company A became a controlling group company in relation to Company B and both companies formed part of the same "group of companies" as defined in section 41(1), and that was still the position at the end of 31 January 2025.

*Acquisition transac*tion – *30 June 2025*

Under section 24O(5) the equity shares acquired by Company A in Company C on 30 June 2025 must for purposes of section 24O(2) be treated as having been acquired by Company A under paragraph (*a*) of the definition of "acquisition transaction" in section 24O(1). The equity shares so acquired in the unbundling transaction must also be treated as constituting a qualifying interest in an operating company to the extent to which the value, at the date of the unbundling transaction, of the equity shares in Company B from which the equity shares in Company C were acquired, was derived from the value, at the date of the unbundling transaction, of the equity shares in Company C. The value of the equity shares in Company B was derived in full from the value of the equity shares in Company C. Therefore, the equity shares that Company A holds in Company C are treated as a qualifying interest of 100% for purposes of section 24O(2).

Under section 24O(2) and (3) the interest of R300 000 is deemed to have been incurred in the production of Company A's income and laid out or expended for the purposes of trade *to the extent* that the interest relates to the period during which Company A held the equity shares in Company C (held for the full period) and to the extent those shares constituted a qualifying interest in an operating company on the applicable date of 31 December 2025 (100% see above). The interest of R300 000 is therefore deductible under section 24J(2), subject to all of its requirements being met, read with section 24O(2) but may be subject to limitation under sections 23M (see **4.5**) and 23N (see **4.4**).

Even though Company A still holds the shares in Company B on 31 December 2025, effectively no portion of the interest is treated as being related to those shares, since on the facts Company B has no other assets. If Company B had other assets then the equity shares held by Company A in Company C would be treated as a qualifying interest of less than 100% (the extent that it is treated as a qualifying interest would be determined according to the principles applied above, say 70%) and Company A would need to assess whether and to what extent on the facts the shares held in Company B (the 30%) meet the requirements under section 24O(2) and section 24O(3). If any of the equity shares in Company B or Company C are no longer held at year end that fact would also need to be taken into account. If Company C was no longer an operating company for its latest year of assessment ending on 31 December 2025 that would also have had an impact.

4.4 Limitation of interest deductions on reorganisation and acquisition transactions (section 23N)

Section 23N limits the deduction of interest incurred by a company on debt relating to "reorganisation transactions" and "acquisition transactions" as defined in section 23N(1). As noted above, the purpose of section 23N is to reduce the risk of the use of excessive debt to finance "reorganisation transactions" and "acquisition transactions".

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The detail in section 23N is complex but, very broadly by way of introduction, some of the principles incorporated are –

- it applies to debt used to procure, enable, facilitate or fund "reorganisation transactions" and "acquisition transactions" and debt used to redeem, refinance or settle such debt;
- the limitation applies in the year of the transaction and the 5 subsequent tax years;
- excess interest above the limitation is not carried forward to future tax years; and
- the limitation is determined according to a specified formula.

4.4.1 Definitions [section 23N(1)]

Section 23N(1) contains a number of definitions which apply for the purposes of section 23N.

(a) Definition of "acquired company"

The term "acquired company" means –

- a transferor company or a liquidating company that disposes of assets pursuant to a "reorganisation transaction", (see **4.4.1 (h)**); or
- a company in which equity shares are acquired by another company under an "acquisition transaction" as defined in section 23N(1) (see **4.4.1 (c)**).

(b) Definition of "acquiring company"

The term "acquiring company" means –

- a transferee company contemplated in the definition of "intra-group transaction" in section 45(1);
- a holding company contemplated in the definition of "liquidation distribution" in section 47(1); or
- a company that acquires an equity share in another company under an "acquisition transaction" as defined in section 23N(1).

(c) Definition of "acquisition transaction"

The term "acquisition transaction" means any transaction –

- under which an acquiring company acquires an equity share in an acquired company that is a company as contemplated in paragraph[61] (*a*) or (*b*) of the definition of "acquisition transaction" in section 24O(1), namely –
  - an operating company on the date of acquisition of the share [see **4.3.1 (b)** for the definition of "operating company" in section 24O(1)]; or
  - a controlling group company in relation to an operating company on the date of acquisition of the share and that forms part of the same "group of companies" as defined in section 41(1) as the controlling group company (see **4.3.1 (a)** for a discussion of the meaning of "group of companies" and "controlling group company"); and

[61] See section 24O(1), paragraphs *a*(i) and *b*(i) of the definition of "acquisition transaction".

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- as a result of which that acquiring company, as at the end of the day of that transaction, becomes a controlling group company in relation to that acquired company.

It is not a requirement that the acquiring and acquired companies must form part of the same "group of companies" as defined in section 41(1) as at the end of the day of the transaction. These companies must, however, form part of the same "group of companies" as defined in section 1(1) for the acquiring company to be a controlling group company in relation to the acquired company. Unlike the definition of an "acquisition transaction" in section 24O(1), there is also no restriction against the acquiring company acquiring the share from a member of the same group of companies.

A transaction that qualifies as an "acquisition transaction" under section 23N(1) will not qualify as an "acquisition transaction" under section 24O(1) should the acquiring and acquired companies not form part of the same "group of companies" as defined in section 41(1) or should the share in the acquired company be obtained from a company in the same group of companies. The result of a transaction not qualifying as an "acquisition transaction" as defined in section 24O(1) is that section 24O will not apply to interest incurred on debt relating to that transaction and the interest may therefore not be deductible under section 11(*a*) or 24J(2) because the in production of income and for purposes of trade requirements are not met [see **4.3.1 (a)**].

(d) Definition of "adjusted taxable income"

The definition of adjusted taxable income forms the basis for the determination of the maximum interest deduction that an acquiring company may be allowed relating to interest incurred on reorganisation and acquisition transactions for a specific year of assessment (see **4.4.2** and **4.4.3**).

The term "adjusted taxable income" is closely aligned to the financial term "earnings before interest, taxation, depreciation and amortisation (EBITDA)" and is calculated as follows for an acquiring company (see **Example 14** for a calculation of adjusted taxable income):

- Taxable income of an acquiring company for a specific year of assessment before applying section 23N. Taxable income could be a positive or negative figure.

  With effect from years of assessment commencing on or after 1 January 2025,[62] adjusted taxable income must also be determined before setting off any assessed loss carried forward from the preceding year of assessment. In addition, whilst taxable income could be a positive or negative figure it has been clarified that adjusted taxable income may not be less than nil.

- *Less* the following amounts included in taxable income:
  - Any amount of interest (see **(f)** below) received or accrued [paragraph (*a*)(i) of the definition].
  - Any amount included in the income of the acquiring company under section 9D(2) [paragraph (*a*)(ii) of the definition]. Under section 9D(2) a portion of the net income of a CFC is included in the income of a

[62] Clause 19(1)(*a)* and clause 19(1)(2) of the Taxation Laws Amendment Act 42 of 2024.

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resident who, together with a connected person, holds at least 10% of the participation rights and voting rights in the CFC. In summary, a foreign company is a CFC when more than 50% of its total participation rights are directly or indirectly held, or more than 50% of its voting rights are directly or indirectly exercisable, by one or more persons that are residents other than persons that are headquarter companies or when the financial results of the foreign company are reflected in the consolidated financial statements as contemplated in IFRS 10 of a resident company, other than a headquarter company.

- Any amount recovered or recouped on any allowances claimed on a "capital asset" as defined in section 19 [paragraph (*a*)(iii) of the definition]. A "capital asset" so defined means an "asset" as defined in paragraph 1 of the Eighth Schedule that is not trading stock.

- *Add* the following amounts:
  - Any amount of interest (see **(f)** below) incurred and allowed as a deduction from income [paragraph (*b*)(i) of the definition].
  - Any amount allowed as a deduction on a capital asset as defined in section 19 for purposes other than the determination of any capital gain or capital loss [paragraph (*b*)(ii) of the definition]. Examples of such deductions or allowances include those granted under sections 11(*e*), 12B, 12BA or 12C.
  - 75% of the receipts or accruals derived from the letting of immovable property [paragraph (*b*)(iii) of the definition]. Even though 100% of these receipts and accruals have already been included in taxable income, an additional 75% is also included. The *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2013*[63] stated that the formula is increased for rentals, since financial institutions are generally more willing to provide funding when immovable property is involved.
  - Any assessed loss determined in the current year of assessment or balance of assessed loss carried forward from a previous year of assessment allowed to be set off against income under section 20 [paragraph (*b*)(iv) of the definition, see footnote for date of deletion].[64]

    Section 20(1) provides that in determining the taxable income derived by any person from carrying on any trade, there shall, subject to section 20A, be set off against the income so derived by such person that is a company –

    - any balance of assessed loss incurred by a company in any previous year which has been carried forward from the preceding year of assessment to the extent that the amount of such set-off does not exceed the higher of R1 million and 80% of the amount of taxable income determined before taking into account section 20(1)(*a*) or if that company is a company carrying on mining operations as contemplated in section 15,

63 In paragraph 2.7.

64 Paragraph (*b*)(iv) of the definition of "adjusted taxable income" applies to years of assessment commencing on or after 1 January 2015. Clause 19(1)(*b)* and clause 19(3) of the Taxation Laws Amendment Act 42 of 2024 provide for the deletion of paragraph (*b)(iv)* with effect from years of assessment commencing on or after 1 January 2027.

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(special rules may apply if the company has taken steps to liquidate, wind up or deregister) [section (1)(*a*)(i)];

- any balance of assessed loss incurred by that person in any previous year which has been carried forward from the preceding year of assessment, to the extent that the amount of such set-off does not exceed the higher of R1 million and 80 per cent of the amount of taxable income determined before taking into account the application of this section and section 36 (7C), (special rules may apply if the company has taken steps to liquidate, wind up or deregister) [section (1)(*a*)(ii)];
- any assessed loss[65] incurred by the taxpayer during the same year of assessment in carrying on any other trade either alone or in partnership with others, otherwise than as a member of a company the capital whereof is divided into shares [section (1)(*b)*]; and
- any assessed loss or balance of assessed loss incurred in carrying on any trade outside South Africa cannot be set off against any amount derived by any person from a source within South Africa.[66]

The opening words of paragraph (*a*) of the definition of "adjusted taxable income" require that the taxable income be "reduced by"[67] the amounts listed in the paragraph. Having regard to the definition as a whole and its purpose, the words "reduced by" must be read as reducing a positive taxable income and increasing a negative taxable income. Adjusted taxable income is limited to nil if the overall result of the calculation is a negative amount.

(e) Definition of "average repo rate" (see footnote for date of deletion)[68]

The term "average repo rate" in relation to a year of assessment means the average of all ruling repo rates determined by using the daily repo rates during that year of assessment.

The average repo rate is applied in the formula in section 23N(4) (see **4.4.3** and **4.4.4**).

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65 The term "assessed loss" is defined in section 20(2) and means any amount by which the deductions admissible under section 11 exceeded the income in respect of which they are so admissible.

66 Paragraph (*b*) of the proviso to section 20(1).

67 Referred to above as "less the following amounts".

68 The Taxation Laws Amendment Act 42 of 2024 provides that with effect from years of assessment commencing on or after 1 January 2027 the percentage used in section 23N(3) will be a fixed amount of 0,3, that section 23N(4) will be deleted and that the definitions of "average repo rate" and "repo rate," which are used in section 23N(4), will also be deleted.

(f) Definition of "interest"

The term "interest" means "interest" as defined in section 24J. The definition in section 24J(1) is framed in wide terms and includes the following:

- The gross amount of any interest (see **4.2**) or similar[69] finance charges,[70] discount or premium payable or receivable under or in respect of a financial arrangement [paragraph (*a*) of the definition].
- The amount, or portion thereof, payable by a borrower to the lender under any lending arrangement as represents compensation for any amount to which the lender would, but for such lending arrangement, have been entitled [paragraph (*b*) of the definition].
- The absolute value of the difference between all amounts receivable and payable by a person under a sale and leaseback arrangement as contemplated in section 23G throughout the full term of such arrangement, to which such person is a party [paragraph (*c*) of the definition].

An amount qualifies as "interest" as defined in section 24J(1) irrespective of whether it is i) calculated with reference to a fixed rate of interest or a variable rate of interest, or ii) is payable or receivable as a lump sum or in unequal instalments during the term of the financial arrangement.

(g) Definition of "issue"

The term "issue" in relation to a debt, means the creation of a liability to pay or of a right to receive an amount under that debt (see **4.4.2**).

(h) Definition of "reorganisation transaction"

The term "reorganisation transaction" means any of the following transactions:

- An "intra-group transaction" as defined in section 45(1) to which section 45 applies.
- A "liquidation distribution" as defined in section 47(1) to which section 47 applies.

An "intra-group transaction" as defined in section 45(1) to which section 45 applies

A transaction will be an intra-group transaction if either of the following applies:

- An asset is disposed of by a company ("transferor company") to a company that is a resident ("transferee company"); both companies form part of the same "group of companies" as defined in section 41(1) as at the end of the day of that transaction, and the transferee company acquired that asset as a capital asset where the transferor company held it as a capital asset or as trading stock where the transferor company held it as trading stock.
- An asset, constituting an equity share held by a transferor company as a capital asset in a foreign company, is disposed of by the transferor company to a transferee company in exchange for the issue of debt or shares other than equity shares by that transferee company and that transferee company

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69 Paragraph (*a*) of the definition of "interest" was substituted by section 45 of the Taxation Laws Amendment Act 15 of 2016 with effect from 19 January 2017, to replace the word "related" with "similar".

70 See Interpretation Note 142 "Meaning of 'Similar Finance Charges'".

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acquires that asset as a capital asset. Further, immediately before and as at the end of the day of that transaction, the transferor company and the transferee company must form part of the same "group of companies" as defined in section 1(1), the transferor company must be a resident or a CFC in relation to one or more residents forming part of that group of companies (see **4.3.1 (a)** for a discussion of the meaning of "group of companies") and the transferee company must be a resident or a CFC in relation to one or more residents forming part of that group of companies.

The words "to which section 45 applies" in the definition of "reorganisation transaction" in section 23N(1) clarify that a transaction must not merely fall within the definition of "intra-group transaction" but the provisions of section 45 as a whole must apply to that transaction. Broadly stated, that means the roll-over relief provided for in the section applies to the transaction. Section 45 would not apply if one of the exclusions in section 45(6) applied. For example, section 45, and the roll-over relief it potentially provides, would not apply if the transferee company was one of the exempt persons listed in section 45(6)(*b*) such as a public benefit organisation or recreational club, or if under section 45(6)(*g*) the transferor company and transferee company agreed in writing that section 45 must not apply to the disposal.

A "liquidation distribution" as defined in section 47(1) to which section 47 applies

A transaction will be a liquidation distribution when either of the following applies:

- A company ("liquidating company"), which is a resident, disposes of all of its assets (other than assets it elects to use to settle any debts incurred by it in the ordinary course of its trade) to its shareholders in anticipation of or in the course of the liquidation, winding up or deregistration of that company and other than assets required to satisfy any reasonably anticipated liabilities to any sphere of government of any country and costs of administration relating to the liquidation or winding up, but only to the extent to which those assets are so disposed of to a company ("holding company") which is a resident and which on the date of that disposal forms part of the same "group of companies" as defined in section 41(1) as the liquidating company.
- A liquidating CFC disposes of all of its assets (other than assets it elects to use to settle any debts incurred by it in the ordinary course of its trade) to its shareholders in anticipation of or in the course of the liquidation, winding up or deregistration of that company –
    - to the extent that those assets are disposed of to a resident holding company forming part of the same "group of companies" as defined in section 1(1) as the liquidating company immediately before that distribution, or to a holding company that is a CFC in relation to any resident;
    - if, immediately before the transaction, all of the shares held by the holding company in the liquidating company, were held as capital assets; and
    - if, immediately after that transaction, in the case of a holding company that is a CFC, more than 50% of its equity shares are directly or indirectly held by a resident whether alone or together with any other resident forming part of the same "group of companies", as defined in section 41(1), as that resident.

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The words "to which section 47 applies" in the definition of "reorganisation transaction" in section 23N(1) clarify that a transaction must not merely fall within the definition of "liquidation distribution" but the provisions of section 47 as a whole must apply to that transaction. Broadly stated, that means the roll-over relief provided for in section applies to the transaction. Section 47 would not apply if one of the exclusions in section 47(6) applied. For example, section 47, and the roll-over relief it potentially provides, would not apply if the holding company was one of the exempt persons listed in section 47(6)(*a*) such as a public benefit organisation or recreational club or if under section 47(6)(*b*) the holding company and liquidating company agreed in writing that section 47 must not apply.

(i) Definition of "repo rate" (see footnote for date of deletion)[71]

The term "repo rate" means the interest rate at which the South African Reserve Bank enters into a repurchase agreement contemplated in section 10(1)(*j*) of the South African Reserve Bank Act.

4.4.2 Limitation of amounts of interest allowed to be deducted [section 23N(2)]

Section 23N(2) provides that the amount of interest incurred by an acquiring company that is allowed to be deducted by that acquiring company on the following types of debt is limited to the amount established under section 23N(3) (see **4.4.3**):

- Debt directly or indirectly assumed or applied for the purpose of procuring, enabling, facilitating or funding the acquisition by that acquiring company of any asset under a reorganisation transaction [section 23N(2)(*a*)].
- Debt used directly or indirectly for the purpose of redeeming, refinancing or settling the debt referred to in the first bullet above [section 23N(2)(*b*)].
- Debt issued, assumed or used under an acquisition transaction [section 23N(2)(*c*)].
- Debt used directly or indirectly for the purpose of redeeming, refinancing or settling the debt referred to in the third bullet above [section 23N(2)(*d*)].

Meaning of "an amount of interest that is allowed to be deducted"

The term "interest" means interest as defined in section 24J (see **4.4.1 (a)**).

An amount of interest incurred by an acquiring company is allowed to be deducted if the interest –

- qualifies for a deduction under section 11(*a*) or 24J(2);
- is incurred under an "acquisition transaction" as defined in section 24O(1) and is deemed under section 24O(2) to have been incurred in the production of income and laid out or expended for the purposes of trade and therefore deductible under section 11(*a*) or 24J(2) provided the requirements of the applicable section are met (see **4.3.2**); or

[71] The Taxation Laws Amendment Act 42 of 2024 provides that with effect from years of assessment commencing on or after 1 January 2027 the percentage used in section 23N(3) will be a fixed amount of 0,3, that section 23N(4) will be deleted and that the definitions of "average repo rate" and "repo rate," which are used in section 23N(4), will also be deleted.

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- qualifies for a deduction under another section, for example, section 24JB(2).[72]

Meaning of "debt assumed, applied, issued or used"

Section 23N(2) applies to debt either assumed, applied, issued or used. The term "issue" is defined in section 23N(1) and means in relation to a debt, the creation of a liability to pay or of a right to receive an amount under that debt.

The meaning of the words "debt issued, assumed or used" is considered in **4.3.2**. It is submitted that the words "debt applied" bear a similar meaning to the words "debt used".

Meaning of debt "directly or indirectly assumed, applied, issued or used"

Debt may be directly or indirectly assumed, applied, issued or used under a reorganisation or acquisition transaction.

Meaning of "procuring, enabling, facilitating or funding the acquisition of an asset" in section 23N(2)(a)

The words "procuring, enabling, facilitating or funding" are not defined in the Act. Consideration must therefore be given to their ordinary grammatical meaning taking into account the context in which they appear and the purpose to which they are directed.

The word "procure" is defined as follows in the *Merriam-Webster Dictionary*:[73]

> "1…. :[T]o get possession of (something) : to obtain (something) by particular care and effort procure a loan."

The word "enable" is defined in *Dictionary.com* as follows:[74]

> "1 To make able; give power, means, competence, or ability to."

The word "facilitate" is defined in *Dictionary.com* as follows:[75]

> "1. To make easier or less difficult; help forward (an action or process, etc.)."

The word "funding" is defined in *CollinsDictionary.com* as –[76]

> "…money which a government or organization provides for a particular purpose."

From the above it can be deduced that the legislature envisaged that section 23N(2)(*a*) could be applied to a wide variety of debt actions relating to the acquisition of an asset under a reorganisation transaction.

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72 Section 24JB deals with the taxation of financial assets and liabilities of covered persons. Section 24JB is not discussed for purposes of this Note.

73 **www.merriam-webster.com/dictionary/procure** [Accessed 24 November 2026].

74 **www.dictionary.com/browse/enable** [Accessed 24 November 2026].

75 **www.dictionary.com/browse/facilitate** [Accessed 24 November 2026].

76 **www.collinsdictionary.com/dictionary/english/funding** [Accessed 24 November 2026].

Meaning of "redeeming, refinancing or settling the debt" in section 23N(2)(b) and (d)

The words "redeeming, refinancing, or settling the debt" are not defined in the Act. Consideration must therefore be given to their ordinary grammatical meaning, taking into account the context in which they appear and the purpose to which they are directed.

The word "redemption" is defined in the *Cambridge English Dictionary* as follows:[77]

> 'the act of exchanging shares or bonds for cash; the act of paying back a loan."

The word "refinance" is defined in *Dictionary.com* as follows:[78]

> "1. To finance again. 2.to satisfy (a debt) by taking out another loan typically on more favourable terms, as a lower interest rate and reduced monthly payments, or a longer period of time to repay."

The word "settle" is defined in *Dictionary.com* as follows:[79]

> "3 To pay, as a bill. 4. To close (an account) by payment".

4.4.3 Calculation of the limitation of the amount of interest to be deducted [section 23N(3)]

The limitation of an amount of interest allowed to be deducted by an acquiring company for all debts owed as contemplated under section 23N(2) for any year of assessment in which the acquisition transaction or reorganisation transaction is entered into and in respect of five years of assessment immediately following that year of assessment, is determined under section 23N(3) for a specific year of assessment.

The limitation is a single limitation in the sense that the total interest incurred in a year of assessment on all debts owed as contemplated in section 23N is subject to the limitation calculated under section 23N.The amount of interest incurred by an acquiring company on the debt referred to in section 23N(2), must not exceed:

- The amount of interest received by or accrued to that company during that specific year of assessment [section 23N(3)(*a*)].
- *Add*: The amount determined by multiplying the percentage determined using the formula in section 23N(4) (see footnote for detail regarding a future change)[80] (see **4.4.4**) by the highest of adjusted taxable income determined in accordance with the definition of "adjusted taxable income" in section 23N(1) [see **4.4.1 (d)**] for each of the years of assessment –
  - in which the acquisition or reorganisation transaction is entered into [section 23N(3)(*b*)(i)];
  - in which the amount of interest is incurred by the acquiring company, namely, the specific year of assessment for which a deduction under

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77 **https://dictionary.cambridge.org/dictionary/english/redemption** [Accessed 24 November 2026].

78 **www.dictionary.com/browse/refinance** [Accessed 24 November 2026].

79 **www.dictionary.com/browse/settle** [Accessed 24 November 2026].

80 The Taxation Laws Amendment Act 42 of 2024 provides that with effective from years of assessment commencing on or after 1 January 2027 the percentage will be a fixed amount of 0,3, section 23N(4) will be deleted and definition of "average repo rate" and "repo rate" which are used in section 23N(4) will also be deleted.

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section 24J(2) or 11(*a*) read with section 23N(2) is sought [section 23N(3)(*b*)(ii)]; or

- immediately before the year of assessment in which the acquisition or reorganisation transaction is entered into [section 23N(3)(*b*)(iii)].[81]

- *Less:* Any amount of interest incurred by the acquiring company on debt other than debt relating to acquisition and reorganisation transactions.

In determining the percentage determined using the formula in section 23N(4), the following calculations must be made:

- Determine the average repo rate for the year of assessment in accordance with the definitions of "repo rate" and "average repo rate" in section 23N(1).
- Apply the average repo rate so determined in the formula in section 23N(4) (see **4.4.4**) to determine the percentage for the year of assessment.

Section 23N(2) applies only to the year of assessment in which the acquisition or reorganisation transaction is entered into and to the five subsequent years of assessment. Interest on the specific debt incurred from the sixth subsequent year of assessment onwards is not subject to limitation under section 23N(2) but may be subject to limitation under section 23M(2) (see **4.5.2**).

Amounts of interest disallowed under section 23N(2) are not carried forward to subsequent years of assessment.

4.4.4 Calculation of the percentage to be applied to adjusted taxable income [section 23N(4)]

The percentage contemplated in section 23N(3)(*b*) must be determined under section 23N(4) in accordance with the following formula referred to in section 23N(3)(*b*):[82]

$$A = B \times \frac{C}{D}$$

"A" represents the percentage to be determined.

"B" represents the number 40.

"C" represents the average repo rate plus 400 basis points.

"D" represents the number 10.

In "C" in the formula, 100 basis points equal 1% and 400 basis points therefore equal 4%.

The percentage determined under section 23N(4) for any year of assessment may not exceed 60%.

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81 Section 23N(3)(*b*)(iii) applies to years of assessment commencing on or after 1 January 2015.

82 The formula was amended by section 38(1)(*g*) of the Taxation Laws Amendment Act 43 of 2014 with effect from years of assessment commencing on or after 1 January 2015.

The following is stated in the *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2014* relating to the above formula:[83]

> "The interest deduction limitation will now be based exclusively on an adjustable formula whereby any change to the average repo rate for the year of assessment (together with a 400 basis point addition to the average repo rate) is reflected to allow for a balanced reflection of market conditions on the interest deduction limitation. A 400 basis point addition to the average repo rate will mimic the current costs of obtaining debt.
>
> As a mechanism to protect the fiscus and tax base in periods of high interest rates, a cap on the interest deduction limitation of 60 per cent is proposed. The proposed limitation implies a doubling of the current repo rate (5.5 per cent) before the cap applies. Excessive debt can also have macroeconomic implications for the economy if companies are unsustainably leveraged and the tax system should not play a role in 'encouraging' companies towards a debt financing bias."

The limitation of 60% will therefore be reached with an average repo rate of 11%. The 60% limitation is calculated as follows:

$$A = B \times \frac{C}{D}$$

$$= 40 \times (11 + 4) / 10$$

$$= 60\%.$$

The *Taxation Laws Amendment Act* 42 of 2024 provides that with effect from years of assessment commencing on or after 1 January 2027 section 23N(4) will be deleted as well as the definition of "average repo rate" and "repo rate," which are used in section 23N(4). Instead of using a variable percentage calculated under the formula discussed above, a fixed amount of 0,3 will be used in section 23N(2).

Example 14 – Calculation of the limitation determined under section 23N(3)

Facts:

Company A and Company B's years of assessment end on 31 December. On 31 January 2024 Company A acquired 70% of the equity shares in Company B, an operating company, under an "acquisition transaction" as defined in sections 23N(1) and 24O(1). Both companies were residents and had their places of effective management in South Africa for the duration of the 2024 and 2025 years of assessment.

Company A incurred interest of R100 000 and R110 000 respectively during its 2024 and 2025 years of assessment on debt used for the purpose of financing the acquisition of the equity shares in Company B. The debt was repaid on 31 December 2025. Company A incurred other interest of R350 000 and R490 000 and received interest of R25 000 and R5 000 during its 2024 and 2025 years of assessment respectively.

Assume an average repo rate of 6%, 7% and 8% for the 2023, 2024 and 2025 years of assessment respectively. The adjusted taxable income for each of the 2023, 2024 and 2025 years of assessment was R1 million, R800 000 and R1,2 million respectively.

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[83] In paragraph 2.4.

Result:

The interest of R100 000 and R110 000 incurred during the 2024 and 2025 years of assessment respectively on the debt that funded the acquisition transaction is deductible under section 24J(2), read with section 24O(2) and subject to all of its requirements being met, but subject to limitation under section 23N(2).

The limitation amounts for purposes of section 23N(2) for the 2024 and 2025 years of assessment are calculated in accordance with section 23N(3) and (4).

Calculation of the percentage under section 23N(4) to be applied to adjusted taxable income under section 23N(3)(b)

	2024	2025
Formula		
A = B × [C / D]		
B =	40	40
C = (7 + 4) / (8 + 4)	11	12
D =	10	10
A (Percentage calculated) =	44%	48%

Multiplication of the percentage by adjusted taxable income under section 23N(3)(b)

In applying section 23N(3)(*b*) in the 2024 year of assessment, the highest of the adjusted taxable income for 2023 (R1 000 000) and 2024 (R800 000) must be multiplied by the percentage determined for 2024 year of assessment (see "A" above, 44%). An amount of R440 000 (R1 000 000 X 44%) must therefore be used in section 23N(3)(*b*) to determine the amount of the limitation (see calculation below) for purposes of section 23N(2).

In applying section 23N(3)(*b*) in the 2025 year of assessment, the highest of the adjusted taxable income for 2023 (R1 000 000), 2024 (R800 000) and 2025 (R1 200 000) must be multiplied by the percentage determined for the 2025 year of assessment (see "A" above, 48%). An amount of R576 000 (R1 200 000 x 48%) must therefore be used in section 23N(3)(*b*) to determine the amount of the limitation (see calculation below) for purposes of section 23N(2).

Determination of the limitation under section 23N(3)

	2024 R	2025 R
Interest received by Company A	25 000	5 000
Add: Current percentage × highest adjusted taxable income determined under section 23N(3)(b)	440 000	576 000
Less: Interest incurred (excluding interest on debt that funded the acquisition transaction)	(350 000)	(490 000)
Limitation amounts	115 000	91 000

Determination of amounts of interest incurred on debt that funded the acquisition transaction that are disallowed under section 23N(2)

	R	R
Interest incurred on acquisition transaction	100 000	110 000
Less: Limitation determined under section 23N(3)	(115 000)	(91 000)
Interest disallowed under section 23N(2)	0	19 000

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The amounts of R100 000 and R91 000 are allowed as deductions under section 24J(2), subject to all of its requirements being met, read with sections 24O(2) and 23N(2) for the 2024 and 2025 years of assessment, respectively.

The amount of R19 000 is disallowed under section 23N(2) for the 2025 year of assessment and is not carried forward to subsequent years of assessment.

Example 15 – Application of sections 23N and 24O to an acquisition transaction

Facts:

Company A and Company B's year of assessment ends on 31 December. On 31 January 2024 Company A acquired 70% of the equity shares in Company B, an operating company, under an "acquisition transaction" as defined in section 24O(1). Both companies were residents and had their places of effective management in South Africa for the duration of the 2024 and 2025 years of assessment.

Company A incurred interest of R1 million and R1,1 million during its 2024 and 2025 years of assessment respectively on debt used for the purpose of financing the acquisition of the equity shares in Company B. The debt was repaid on 31 December 2025. Assume an average repo rate of 6%, 7% and 8% for the 2023, 2024 and 2025 years of assessment respectively.

Company A's taxable income, amounts included in taxable income and amounts deducted from income, for purposes of calculating adjusted taxable income, were as follows:

	2023 R	2024 R	2025 R
Taxable income / (Assessed loss)	(200 000)	300 000	250 000
Amounts included in taxable income			
Interest received	80 000	90 000	100 000
Recoupment of capital allowances	-	80 000	
Rental income	500 000	600 000	400 000
Amounts deducted from income			
Interest incurred on the acquisition transaction	-	1 000 000	1 100 000
Interest incurred on other debt	200 000	210 000	250 000
Capital allowances claimed	300 000	300 000	200 000
Assessed loss brought forward	-	200 000	-

Result:

The acquisition of the equity shares in Company B qualifies as an "acquisition transaction" as defined in sections 24O(1) and 23N(1).

Under section 24O(2) the interest incurred on the debt that funded the acquisition transaction is deemed to have been incurred in the production of Company A's income and laid out or expended for the purposes of its trade, since the equity shares constituted a qualifying interest in an operating company (Company B) as determined under section 24O(3)(*a*).

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The interest of R1 million and R1,1 million incurred during the 2024 and 2025 years of assessment respectively on the debt that funded the acquisition transaction is deductible under section 24J(2), subject to all of its requirements being met, read with section 24O(2) but is subject to limitation under section 23N(2).

The limitation amounts for purposes of section 23N(2) for the 2024 and 2025 years of assessment are calculated in accordance with section 23N(3) and (4) as follows:

Calculation of adjusted taxable income

	2023 R	2024 R	2025 R
Taxable income / (Assessed loss)	(200 000)	300 000	250 000
Add:			
Assessed loss / balance of assessed loss brought forward	200 000	200 000	-
	-	500 000	250 000
Less: Amounts included in taxable income:			
Interest received	(80 000)	(90 000)	(100 000)
Recoupment of capital allowances	(-)	(80 000)	(-)
	(80 000)	330 000	150 000
Add: Amounts deducted from income and 75% of rental income:			
Interest incurred on acquisition transaction	-	1 000 000	1 100 000
Interest incurred on other debt	200 000	210 000	250 000
Capital allowances claimed	300 000	300 000	200 000
75% of rental income	375 000	450 000	300 000
Adjusted taxable income	795 000	2 290 000	2 000 000

Calculation of the percentage under section 23N(4) to be multiplied by adjusted taxable income under section 23N(3)(b)

	2024	2025
Formula		
A = B × [C / D]		
B =	40	40
C = (7 + 4) / (8 + 4)	11	12
D =	10	10
A (Percentage calculated) =	44%	48%

Multiplication of the percentage by adjusted taxable income under section 23N(3)(b)

In applying section 23N(3)(*b*) in the 2024 year of assessment, the highest of the adjusted taxable income for 2023 (R795 000) and 2024 (R2 290 000) must be multiplied by the percentage determined for the 2024 year of assessment (see “A” above, 44%). An amount of R1 007 600 (R2 290 000 × 44%) must therefore be used in section 23N(3)(*b*) to determine the amount of the limitation for purposes of section 23N(2).

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In applying section 23N(3)(*b*) in the 2025 year of assessment, the highest of the adjusted taxable income for 2023 (R795 000), 2024 (R2 290 000) and 2025 (R2 000 000) years of assessment must be multiplied by the percentage determined for the 2025 year of assessment (see "A" above, 48%). An amount of R1 099 200 (R2 290 000 × 48%) must therefore be used in section 23N(3)(*b*) to determine the amount of the limitation for purposes of section 23N(2).

Determination of the limitation under section 23N(3)

	2024 R	2025 R
Interest received by Company A	90 000	100 000
Add: Current percentage × highest adjusted taxable income determined under section 23N(3)(b)	1 007 600	1 099 200
Less: Interest incurred (excluding interest on debt that funded the acquisition transaction)	(210 000)	(250 000)
Limitation amounts	887 600	949 200

Determination of amounts of interest incurred on debt that funded the acquisition transaction that are not deductible under section 23N(2)

	2024 R	2025 R
Interest incurred on acquisition transaction	1 000 000	1 100 000
Less: Limitation determined under section 23N(3)	(887 600)	(949 200)
Interest disallowed under section 23N(2)	112 400	150 800

The amounts of R887 600 and R949 200 are allowed as deductions under section 24J(2), subject to all of its requirements being met, read with sections 24O(2) and 23N(2) for the 2024 and 2025 years of assessment respectively.

The amounts of R112 400 and R150 800 are disallowed under section 23N(2) for the 2024 and 2025 years of assessment respectively. These amounts are not carried forward to subsequent years of assessment.

4.5 Limitation of interest deductions on debt owed to persons not subject to tax (section 23M)

The limitation is aimed at preventing base erosion from over-leveraging in circumstances where deductible interest is paid to persons not subject to tax on the interest income (for example, exempt persons or foreign persons subject to a reduced rate of withholding tax). Generally, section 23M provides for a limitation of an amount of interest allowed to be deducted by a debtor during a year of assessment when –

- the debt is owed to a creditor that is in a controlling relationship with the debtor or under the circumstances specified in section 23M(2)(*b*) and (*c*) if a controlling relationship with that debtor does not exist; *and*
- the amount of the interest is neither subject to tax in the hands of the person to which the interest accrues nor included in the net income of a controlled foreign company; and
- it is not disallowed under section 23N.

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The limitation is calculated according to a specified formula and excess interest above the limitation is carried forward to the next tax year.

4.5.1 Definitions [section 23M(1)]

Section 23M(1) contains a number of definitions which apply for the purposes of the section.

(a) Definition of "adjusted taxable income"

This definition forms the basis for the determination of the interest-deduction limit. That is, a debtor's adjusted taxable income is used in determining the maximum amount under section 23M(3) that may be allowed as a deduction under section 23M(2) for that debtor under specified circumstances (see **4.5.2** and **4.5.3**).

The term "adjusted taxable income" as defined in section 23M(1) is closely aligned to the financial term "earnings before interest, taxation, depreciation and amortisation (EBITDA)" and is calculated as follows:

[* - *italicised wording is an amendment effective years of assessment commencing on or after 1 January 2026*]

- Taxable income of the debtor for a specific year of assessment calculated before applying section 23M and before setting off any balance of assessed loss carried forward from the preceding year of assessment.
- *Less* the following amounts:
  - Any amount of interest *contemplated in section 24J** received or accrued that forms part of taxable income.
  - Any amount included in the income of a debtor that is a resident under section 9D(2) [see **4.4.1 (d)**] .
  - Any amount recovered or recouped on any allowances claimed on a "capital asset" as defined in section 19 [see **4.4.1 (d)**].
  - *Any amount of interest accrued,*[84] *other than amounts referred to in the first sub-bullet point above,*[85] *in respect of debt referred to in subsection (3)** (see **4.5.3**).
- *Add* the following amounts:
  - Any amount of interest *contemplated in section 24J** incurred and allowed as a deduction from income.
  - Any amount allowed as a deduction on a "capital asset" as defined in section 19 for purposes other than the determination of any capital gain or capital loss **[see 4.4.1 (d)]**.
  - Any qualifying distribution as defined in section 25BB that is deductible under subsection (2) of that section.
  - *Any amount of interest incurred,*[86] *other than amounts referred to in the first sub-bullet point above,*[87] *in respect of debt referred to in subsection (3)** (see **4.5.3**).

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84 "Interest" as defined in section 23M(1).

85 That is, interest accrued as contemplated in section 24J.

86 "Interest" as defined in section 23M(1).

87 That is, interest incurred as contemplated in section 24J.

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The amount so calculated may not be less than nil.

Example 16 – Calculation of adjusted taxable income – Definition of "adjusted taxable income" in section 23M(1)

Facts:

Individual A carried on a business and was subject to section 23M for the 2025 year of assessment. Section 23N did not apply, since that section applies only to an "acquiring company" as defined in section 23N(2).

Individual A's taxable income, amounts included in taxable income and amounts deducted from income were as follows for the 2025 year of assessment:

	2025 R
Taxable Income	450 000
Amounts included in taxable income	
Interest received	60 000
Net income of a CFC included in income under section 9D(2)	30 000
Recoupment of capital allowances	100 000
Amounts deducted from income	
Interest incurred	200 000
Capital allowances claimed	60 000
Assessed loss brought forward	380 000
Result:	
Calculation of adjusted taxable income	
Taxable Income	450 000
Add:	
Balance of assessed loss brought forward	380 000
	830 000
Less: Amounts included in taxable income	
Interest received	(60 000)
Net income of a CFC included in income under section 9D(2)	(30 000)
Recoupment of capital allowances	(100 000)
	(640 000)
Add: Amounts deducted from income	
Interest incurred	200 000
Capital allowances claimed	60 000
Adjusted taxable income	900 000

The adjusted taxable income of R900 000 is applied in section 23M(3) (see **4.5.3**) to determine the maximum amount of interest to be allowed as a deduction under section 23M(2) (see **4.5.2**) for the 2025 year of assessment.

(b) Definition of "controlling relationship"

The term "controlling relationship" means a relationship in which a person, whether alone or together with any one or more persons that are connected persons in relation to that person, directly or indirectly (for example, through another company) hold at least 50% of the equity shares in a company (see **4.3.1 (a)** for details on the meaning of "equity share") or exercise at least 50% of the voting rights or participation rights in a company.

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(c) Definition of "creditor"

The term creditor means a person to whom a "debtor" owes a "debt".

(d) Definition of "debt"

The term "debt" includes any amount on which interest is determined or incurred, and such amount must be regarded as owed, but does not include a "tax debt" as defined in section 1 of the TA Act.

"Tax debt" so defined means an amount referred to in section 169(1) of that Act, namely, an amount of tax due or payable under a tax Act.[88]

(e) Definition of "debtor"

The term "debtor" means a person that incurs an amount of interest and -

- is a resident;[89] or
- if not a resident, that owes a debt that is effectively connected with a permanent establishment of that person in South Africa. Whether a debt owed is effectively connected with a permanent establishment of a person in South Africa will depend on the facts and circumstances of the particular case.

(f) Definition of "interest"

The term "interest" means interest as defined in section 24J (see **4.4.1 (f)** for details of the meaning of this term) and includes the following:

- amounts incurred or accrued under any "interest rate agreement" as defined in section 24K(1);
- any finance cost element recognised for purposes of IFRS in respect of any lease arrangement that constitutes a finance lease as defined in IFRS16;
- amounts taken into account in determining taxable income in terms of section 24I(3) and (10A);[90] and
- any amount deemed to be interest under section 24JA,

but excludes any amount that is deemed to be a dividend *in specie* as contemplated in sections 8F and 8FA.

Under section 24JA, which deals with sharia-compliant financing arrangements, certain amounts are deemed to be interest as defined in section 24J(1). For example, the following amounts that are so deemed to be interest may be subject to the application of section 23M if the requirements of that section are met:

- The difference between the amount of consideration paid for an asset by the financier to the seller and the consideration payable to the financier by the client to acquire an asset as contemplated in paragraph (*b*)(ii) of the definition of "murabaha" that is deemed to be a premium payable contemplated in

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88 The term "tax Act" as defined in section 1(1) of the TA Act means that Act or an Act, or portion of an Act, referred to in section 4 of the South African Revenue Service Act 34 of 1997, excluding customs and excise legislation.

89 The term "resident" is defined in section 1(1).

90 Section 24I deals with gains and losses on foreign exchange transactions. See **4.5.8** – deeming of exchange gains and losses to be incurred or accrued.

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paragraph (*a*) of the definition of "interest" in section 24J(1) [section 24JA(3)(*d*)].

- A portion of an instalment paid by a client to a bank in a "diminishing mushraka", the amount of which must be determined in accordance with section 24JA(6)(*b*), that is deemed to be "interest" as defined in section 24J(1) [section 24JA(6)(*a*)].

Section 24JA is not considered for purposes of this Note.

(g) Definition of "lending institution"

The term "lending institution" means a bank or a foreign bank that is comparable to a bank, as contemplated in the Banks Act 94 of 1990. A bank is defined in that Act as a public company registered as a bank under that Act.[91]

(h) Definition of "participation rights"

The term "participating rights" means (i) the right to participate in all or part of the benefits of the rights (other than voting rights) attaching to a share, or any interest of a similar nature, in a company, or (ii) in the case where no person has any right in that company as contemplated in (i) and no such rights can be determined for any person, the right to exercise any voting rights in that company.

4.5.2 Limitation of amount of interest allowed to be deducted [section 23M(2)]

Section 23M(2) provides for a limitation, to be determined under section 23M(3), on the amount of interest allowed to be deducted by a debtor during a year of assessment, if the conditions referred to below are met, and the debtor has incurred interest *[other than interest contemplated in paragraph (c) of the definition of "interest" in section 23M(1)*[92]] on a debt owed to a creditor that is –

- in a controlling relationship with the debtor [section 23M(2)(*a*)];
- not in a controlling relationship with that debtor, if that creditor obtained the funding for the debt advanced to the debtor from a person that is in a controlling relationship with that debtor [section 23M(2)(*b*)];
- not in a controlling relationship with that debtor, if that creditor forms part of the same group of companies as that debtor if the expressions "more than 50 per cent of the equity shares or voting rights in" in the definition of "group of companies" in section 1(1) is replaced with the expression "at least 70 per cent of the equity shares in" [section 23M(2)(*c*)]; or
- in a controlling relationship with that debtor, if that creditor directly or indirectly through another creditor that is in a controlling relationship with that creditor, obtained the funding for the debt advanced to the debtor from a person that is in a controlling relationship with that creditor or that other creditor [section 23M(2)(*d*)].

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91 See section 1 of the Banks Act 94 of 1990.

92 See **4.5.1**, that is amounts taken into account in determining taxable income in terms of section 24I(3) and (10A), amendment effective years of assessment commencing on or after 1 January 2026.

Section 23M(2) will apply only when the following conditions are met:

- During that same year of assessment the amount of the interest referred to above *[other than interest contemplated in paragraph (c) of the definition of "interest" in section 23M(1)]*[93] or related interest (see below) is not subject to tax in the hands of the person, creditor or other creditor as referred to above to whom the interest or related interest accrues or is not included in the net income of a CFC in the foreign tax year of the CFC commencing or ending within that year of assessment. It is irrelevant whether the amount of the interest is subject to tax in the hands of the creditor in a subsequent year of assessment or included in the net income of a CFC in a subsequent foreign tax year.
- During that year of assessment the interest must not be disallowed under section 23N (see **4.4.2** dealing with the limitation of interest deductions under section 23N(2) relating to debt that funded acquisition and reorganisation transactions).

The amount of interest allowed to be deducted may not exceed the amount determined in accordance with subsection (3) (see **4.5.3**), provided that if any amount of interest, *other than interest contemplated in paragraph (c) of the definition of "interest" in section 23M(1),*[94] incurred or related interest is not included in the income of the person referred to above and withholding tax on interest was or will be levied on that amount of interest, on payment thereof, under the provisions of Part IVB of this Chapter[95], the amount of interest to be regarded as not subject to tax as contemplated above will be determined in accordance with the formula:

$$A = B \times \frac{(C - D)}{C}$$

in which formula—

(i) "A" represents the amount to be determined;

(ii) "B" represents the aggregate of any amount of interest incurred or paid in respect to which the provisions of Part IVB of this Chapter[96] are or will be applicable;

(iii) "C" represents the number 15; and

(iv) "D" represents the rate at which withholding tax on interest has been or will be levied on such amount of interest under the provisions of Part IVB of this Chapter,[97] multiplied by the number 100.

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93 See **4.5.1**, that is amounts taken into account in determining taxable income in terms of section 24I(3) and (10A), amendment effective years of assessment commencing on or after 1 January 2026.

94 See **4.5.1**, that is amounts taken into account in determining taxable income in terms of section 24I(3) and (10A), amendment effective years of assessment commencing on or after 1 January 2026.

95 Sections 50A to 50H of the Act.

96 Sections 50A to 50H of the Act.

97 Sections 50A to 50H of the Act.

Meaning of "an amount of interest allowed to be deducted"

An amount of interest incurred by a debtor is allowed to be deducted if the amount of interest meets the requirements of an applicable deduction section in the Act and, having met the requirement for a deduction, is not denied a deduction by another section.

An amount of interest could meet the requirements for deduction in, for example, a deduction under section 11(a), section 24J(2); or section 24JB(2).[98]

Notwithstanding having met the requirements for a deduction, an amount of interest may be denied a deduction under another section, for example, under section 23N(2).

Meaning of "related interest"

It is not only the interest that is incurred by the debtor but, also, the related interest for example, flowing from back-to-back loans, that needs to be considered. Thus, if the debtor borrows from creditor 1, and creditor 1 funded that debt by borrowing from creditor 2, then the interest income to be considered in section 23M(2) would be the interest income earned by creditor 1 (from the debtor) and the interest income earned by creditor 2 (from creditor 1).

Meaning of "subject to tax"

Section 23M applies when, amongst other requirements, the amount of the interest is neither subject to tax in the hands of the person to which the interest accrues nor included in the net income of a CFC.

The term "tax" is defined in section 1(1) and means tax or a penalty imposed under the Act. The term "tax" includes normal tax and withholding tax on interest. Interest that accrues to a person from a South African source may be subject to either normal tax or withholding tax on interest but not both.

The words "subject to tax" are not defined in the Act. These words have also not received judicial consideration in South Africa. Foreign Case Law is therefore considered.

In *Paul Weiser v The Commissioners for HM Revenue and Customs* the first-tier tribunal stated that it agrees with the following extract from HMRC's International Tax Manual on the meaning of these words:[99]

> " **'INTM332210 – DT applications and claims – Subject to tax**
>
> **Background**
>
> The expression "subject to tax" usually means that the person must actually pay tax on the income in their country of residence.
>
> However, a person is still regarded as "subject to tax" if, for example, he or she does not pay tax because their income is sufficiently small that it is covered by personal allowances that are available to set [off] against liability to tax in the other country.
>
> A person is not regarded as "subject to tax" if the income in question is exempted from tax because the law of the other country provides for a statutory exemption from tax…. ' "

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98 Section 24JB deals with the taxation of financial assets and liabilities of covered persons. Section 24JB is not considered for purposes of this Note.

99 [2012] UKFTT 501 (TC) in paragraphs 37 and 38.

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SARS accepts the above interpretation of the meaning of "subject to tax".

Subject to normal tax

Interest received by or accrued to a person that is a resident is included in that person's gross income[100]. If the person is a non-resident, the interest received or accrued must be included in gross income only if it is from a source within South Africa.

Under section 9(2)(*b*) an amount that constitutes interest as defined in section 24J will be from a source in South Africa if it –

- is attributable to an amount incurred by a person that is a resident, unless the interest is attributable to a permanent establishment which is situated outside South Africa; or
- is received or accrues in respect of the utilisation or application in South Africa by any person of any funds or credit obtained under any form of interest-bearing arrangement.

Under section 9(4)(*b*) an amount that constitutes interest as defined in section 24J(1) will be from a source outside South Africa if it is not from a source in South Africa under section 9(2)(*b*).

In line with the principles discussed above, an amount of interest that is exempt from normal tax is not subject to normal tax. Interest included in a person's gross income may be exempt from normal tax under, for example, section 10(1) when, for example, it is received by or accrues to –

- a person that is exempt from normal tax, for example, a pension fund exempt under section 10(1)(*d*)(i); or
- a person that is not a resident, unless –
  - that person is a natural person who was physically present in South Africa for a period exceeding 183 days in aggregate during the twelve-month period preceding the date on which the interest is received or accrues by or to that person; or
  - the debt from which the interest arises is effectively connected to a permanent establishment of that person in South Africa.

  (section 10(1)(*h*)).

An amount is not considered to be subject to normal tax in South Africa if it is fully relieved from taxation in South Africa under a tax treaty.[101] However, an amount subject to tax at a reduced rate exceeding 0% is still subject to tax.

Subject to withholding tax on interest

Withholding tax on interest is levied under section 50B(1)(*a*) on interest paid[102] by any person to or for the benefit of any foreign person[103] to the extent that the amount is regarded as having been received or accrued from a source within South Africa under section 9(2)(*b*) (see above). The term "interest" is defined in section 50A(1) and means

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100 See the definition of "gross income" in section 1(1).

101 See Binding Private Ruling: BPR 127 "Relief from Double Taxation of Foreign Income".

102 Section 50B applies to interest that is paid or that becomes due and payable on or after 1 March 2015.

103 The term "foreign person" is defined in section 50A(1) and means any person that is not a resident.

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interest as contemplated in paragraph (*a*) or (*b*) of the definition of "interest" in section 24J(1) [see **4.4.1 (f)** for the definition of "interest" in section 24J(1)].[104]

Certain amounts of interest paid are exempt from withholding tax on interest, for example, under section 50D and section 12Q(4). See Interpretation Note 115 "Withholding Tax on Interest" for commentary on the different exemptions. In line with the principles discussed above, an amount that is exempt from withholding tax on interest is not subject to withholding tax on interest.

Section 50E(3) provides for the reduction of the rate at which withholding tax on interest is levied if a tax treaty applies to an interest payment made to or for the benefit of a foreign person and specified requirements are met. See Interpretation Note 115 "Withholding Tax on Interest" for commentary on the reduction of the rate of withholding tax on interest. An amount is not considered to be subject to withholding tax on interest if it is fully relieved from taxation in South Africa under a tax treaty, for example, if there is no taxing right or if the rate of withholding tax is reduced to Nil. However, an amount subject to tax at a reduced rate exceeding 0% is still subject to tax.

4.5.3 Calculation of the amount of interest allowed to be deducted [section 23M(3)]

Under section 23M(3) the amount of interest allowed to be deducted on all debts owed by a debtor as contemplated in section 23M(2) for any year of assessment must not exceed the sum of the following:

- The amount of interest *contemplated in section 24J and any other amount of interest in respect of that debt*[105] received by or accrued to the debtor; and
- An amount determined by multiplying the adjusted taxable income of the debtor for that year of assessment by 0.3,

as reduced by any amount of deductible interest *contemplated in section 24J*[106] incurred by the debtor on debts other than debts contemplated in section 23M(2) (see **4.5.2**) as exceeds any amount not allowed to be deducted under section 23N (see **4.5.2**). See example 18 and 19 in **4.5.9**.

4.5.4 Excess interest determined under section 23M(3) to be carried forward to the succeeding year of assessment [section 23M(4)]

Under section 23M(4) any amount of interest as exceeds the amount determined under section 23M(3) must be carried forward to the immediately succeeding year of assessment of the debtor. The amount so carried forward must be deemed to be an amount of interest incurred in that succeeding year of assessment in respect of a debt *that qualifies for a deduction subject to the limitation in subsection (2)*.[107] This means that any brought forward interest in a particular year of assessment, together with interest incurred in that year of assessment on any debt contemplated in section 23M(2) (see **4.5.2**), that may be deducted is subject to the limitation as

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[104] The definition of "interest" in section 50A(1) was inserted by section 70(1) of the Taxation Laws Amendment Act 25 of 2015 and applies to interest that is paid or that becomes due and payable on or after 1 March 2016.

[105] Amendment effective years of assessment commencing on or after 1 January 2026.

[106] Amendment effective years of assessment commencing on or after 1 January 2026.

[107] Clarifying amendment effective years of assessment commencing on or after 1 January 2026.

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calculated in section 23M(3) (see **4.5.3**). There is no limit on the number of years that an excess amount must be carried forward to succeeding years of assessment.

Example 17 – Application of section 23M(2), (3) and (4)

Facts:

Company A's year of assessment ends on 30 June. Company A held 50% of the equity shares in Company B for the duration of Company A's 2024 and 2025 years of assessment. Company B is a foreign company and is a resident of Foreign Country B.

Company B advanced a loan of R5 million to Company A on 1 July 2023. Company A incurred interest of R500 000 on this loan for each of the 2024 and 2025 years of assessment. The interest earned by Company B is from a source within South Africa as it is attributable to an amount incurred by Company A and Company A is a resident [section 9(2)(*b*)(*i*)].

The tax treaty between South Africa and Foreign Country B provided that South Africa did not have a right to tax the interest. Accordingly, the interest income is not subject to normal tax or withholding tax on interest.

The adjusted taxable income of Company A amounted to R300 000 and R500 000 for the 2024 and 2025 years of assessment respectively.

Interest received by or accrued to Company A and interest incurred by it on other debt amounted to the following:

	2024 R	2025 R
Interest received or accrued	100 000	80 000
Interest incurred on other debt	(50 000)	(20 000)

Section 23N did not apply, since none of the interest was incurred on debt that funded acquisition or reorganisation transactions. Section 31 is not considered for purposes of this example.

Result:

Section 23M(2) applies because –

- interest was incurred by Company A on debt owed to Company B;
- Company B was in a controlling relationship with Company A, since Company A held at least 50% of the equity shares in Company B;
- during the 2024 and 2025 years of assessment, Company B was not subject to tax on the interest of R500 000 incurred by Company A in each of those years of assessment, since it was exempt from both normal tax and withholding tax on interest; and
- the interest of R500 000 incurred by Company A during each of the 2024 and 2025 years of assessment was not disallowed under section 23N.

Under section 23M(2) the amount of interest to be deducted on the debt advanced by Company B may not exceed the amount determined under section 23M(3).

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Determination of limitation under section 23M(3)

	2024 R	2025 R
Interest received by or accrued to Company A	100 000	80 000
Add: Adjusted Taxable income x 0.3 (0.3 x R300 000)/ (0.3 x R500 000)	90 000	150 000
	190 000	230 000
Less: Deductible interest incurred on other debt not contemplated in section 23M(2) that exceeds the amount disallowed under section 23N	(50 000)	(20 000)
Limitation amounts	140 000	210 000

The interest incurred by Company A of R500 000 during the 2024 year of assessment on the loan advanced by Company B that may be deducted is limited under section 23M(3) to R140 000. This means that R140 000 is allowed as a deduction under section 24J(2) assuming all the requirements of section 24J(2) are met.

Under section 23M(4) the excess of R360 000 (R500 000 – R140 000) is carried forward to the 2025 year of assessment and is deemed to be an amount of interest incurred in that year of assessment which is subject to limitation under section 23M(2).

The sum of the interest incurred by Company A of R500 000 during the 2025 year of assessment on the loan advanced by Company B and the excess of R360 000 carried forward from the 2024 year of assessment is limited under section 23M(3) to R210 000. This means that R210 000 is allowed as a deduction under section 24J(2) assuming all the requirements of section 24J(2) are met.

Under section 23M(4) the excess of R650 000 (R500 000 + R360 000 – R210 000) is carried forward to the 2026 year of assessment and is deemed to be an amount of interest incurred in that year of assessment that is subject to limitation under section 23M(2).

4.5.5 Interaction between sections 23M and 23N [section 23M(5)]

Section 23M(5) provides that when an amount of interest is to be taken into account under both sections 23M and 23N, the amount of interest shall be taken into account under section 23M only after section 23N has been applied.

An amount already disallowed in full under section 23N will therefore not be taken into account under section 23M to determine the further limitation under section 23M(2).

Example 18 – Interaction between sections 23M, 23N and 24O

Facts:

Company A and Company B's years of assessment end on 31 December. On 31 January 2024 Company A acquired 70% of the equity shares in Company B under an acquisition transaction. Company B qualified as an operating company for the duration of the 2024 and 2025 years of assessment.

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Company A incurred interest of R1 million and R1,1 million during its 2024 and 2025 years of assessment respectively on debt used for the purpose of financing the acquisition of the equity shares in Company B. The debt was advanced by Company C which was in a controlling relationship with Company A. Company C was a foreign company and a resident of Foreign Country C. The interest earned by Company C is from a source within South Africa as it is attributable to an amount incurred by Company A and Company A is a resident [section 9(2)(*b*)(*i*)].

The tax treaty between South Africa and Foreign Country C provided that South Africa did not have a right to tax the interest. Accordingly, the interest income is not subject to normal tax or withholding tax on interest.

Company A and Company B were residents for the duration of the 2024 and 2025 years of assessment. Assume an average repo rate of 6%, 7% and 8% for the 2023, 2024 and 2025 years of assessment respectively.

Section 31 is not considered for purposes of this example.

Company A's taxable income, amounts included in taxable income and amounts deducted from income, for purposes of calculating adjusted taxable income, were as follows:

	2023 R	2024 R	2025 R
Taxable income / (Assessed loss)	(200 000)	300 000	250 000
Amounts included in taxable income			
Interest received	80 000	90 000	100 000
Recoupment of capital allowances	-	80 000	-
Rental income	500 000	600 000	400 000
Amounts deducted from income			
Interest incurred on the acquisition transaction	-	1 000 000	1 100 000
Interest incurred on other debt	200 000	210 000	250 000
Capital allowances claimed	300 000	300 000	200 000
Assessed loss brought forward	-	200 000	-

Result:

The acquisition of the equity shares in Company B qualifies as an "acquisition transaction" as defined in sections 24O(1) and 23N(1). Under section 24O(2) the interest incurred on the debt that funded the acquisition transaction is deemed to have been incurred in the production of Company A's income and laid out or expended for the purposes of its trade, since the equity shares constituted a qualifying interest in an operating company (Company B) as determined under section 24O(3)(*a*).

The interest of R1 million and R1,1 million incurred during the 2024 and 2025 years of assessment respectively on the debt that funded the acquisition transaction is deductible under section 24J(2), subject to all of its requirements being met, read with section 24O(2) but is subject to limitation under sections 23N(2) and 23M(2).

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Application of section 23N

Section 23N(2) applies because interest was incurred by an acquiring company (Company A) on a debt used under an "acquisition transaction" as defined in section 23N(1).

The limitation amounts for purposes of section 23N(2) for the 2024 and 2025 years of assessment are calculated in accordance with section 23N(3) and (4) as follows:

Calculation of adjusted taxable income

	2023 R	2024 R	2025 R
Taxable income / (Assessed loss)	(200 000)	300 000	250 000
Add:			
Assessed loss / balance of assessed loss brought forward	200 000	200 000	-
	(-)	500 000	250 000
Less: Amounts included in taxable income:			
Interest received	(80 000)	(90 000)	(100 000)
Recoupment of capital allowances	(-)	(80 000)	(-)
	(80 000)	330 000	150 000
Add: Specified amounts deducted from income and 75% of rental income:			
Interest incurred on acquisition transaction	-	1 000 000	1 100 000
Interest incurred on other debt	200 000	210 000	250 000
Capital allowances claimed	300 000	300 000	200 000
75% of rental income	375 000	450 000	300 000
Adjusted taxable income	795 000	2 290 000	2 000 000

Calculation of the percentage under section 23N(4) to be applied to highest adjusted taxable income under section 23N(3)(b)

	2024	2025
Formula		
A = B × [C /D]		
B =	40	40
C = (7 + 4) / (8 + 4)	11	12
D =	10	10
A (Percentage calculated) =	44%	48%

Multiplication of the percentage by adjusted taxable income under 23N(3)(b)

In applying section 23N(3)(*b*) in the 2024 year of assessment, the highest of the adjusted taxable income for 2023 (R795 000) and 2024 (R2 290 000) must be multiplied by the percentage calculated for the 2024 year of assessment (see 'A" above, 44%). The amount of R1 007 600 (R2 290 000 x 44%) must therefore be used in section 23N(3)(*b*) to determine the amount of the limitation for purposes of section 23N(2) for the 2024 year of assessment.

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In applying section 23N(3)(*b*) to the 2025 year of assessment, the highest of the adjusted taxable income for 2023 (R795 000), 2024 (R2 290 000) and 2025 (R2 000 000) will be applicable must be multiplied by the percentage calculated for the 2025 year of assessment (see 'A" above, 48%). The amount of R1 099 200 (R2 290 000 x 48%) must therefore be used in section 23N(3)(*b*) to determine the amount of the limitation for purposes of section 23N(2) for the 2025 year of assessment.

Determination of the limitation under section 23N(3)

	2024 R	2025 R
Interest received by Company A	90 000	100 000
Add: Current percentage × highest adjusted taxable income determined under section 23N(3)(*b*)	1 007 600	1 099 200
Less: Interest incurred (excluding interest on debt that funded the acquisition transaction)	(210 000)	(250 000)
Limitation amounts	887 600	949 200

Determination of amounts of interest incurred on debt that funded the acquisition transaction that are disallowed under section 23N(2)

	2024 R	2025 R
Interest incurred on acquisition transaction	1 000 000	1 100 000
Less: Limitation determined under section 23N(3)	(887 600)	(949 200)
Interest disallowed under section 23N(2)	112 400	150 800

The amounts of R112 400 and R150 800 are disallowed under section 23N(2) for the 2024 and 2025 years of assessment respectively. These amounts are not carried forward to subsequent years of assessment.

Application of section 23M

Section 23M(2) applies because –

- interest was incurred by a debtor (Company A) on a debt owed to a creditor (Company C) that was in a controlling relationship with Company A;
- Company C was not subject to tax on the interest incurred during Company A's 2024 and 2025 years of assessment; and
- the interest incurred was not disallowed in full under section 23N.

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The limitation amounts for purposes of section 23M(2) for the 2024 and 2025 years of assessment are calculated in accordance with section 23M(3) as follows:

Calculation of adjusted taxable income

	2024 R	2025 R
Taxable income (Note)	412 400	400 800
Add:		
Balance of assessed loss brought forward (Note)	200 000	-
	612 400	400 800
Less: Amounts included in taxable income:		
Interest received	(90 000)	(100 000)
Recoupment of capital allowances	(80 000)	(-)
	442 400	300 800
Add: Amounts deducted from income:		
Interest incurred on the acquisition transaction, after applying the limitation under section 23N(2):		
2024: R1 000 000 – R112 400	887 600	
2025: R1 100 000 – R150 800		949 200
Interest incurred on other debt	210 000	250 000
Capital allowances claimed	300 000	200 000
Adjusted taxable income	1 840 000	1 700 000

Note:

Taxable income is recalculated, since interest of R112 400 and R150 800 has been disallowed under section 23N(2). Taxable income for the 2024 and 2025 years of assessment therefore amounts to R412 400 (R300 000 + R112 400) and R400 800 (R250 000 + R150 800) respectively.

In addition, any brought forward assessed loss must be excluded, therefore for 2023 the brought forward assessed loss of R200 000 must be added back.

Determination of the limitation under section 23M(3)

	2024 R	2025 R
Interest received by Company A	90 000	100 000
0.3 × adjusted taxable income (R1 840 000 x 0.3) & (R1 700 000 x 0.3)	552 000	510 000
Less: Interest incurred on debt not contemplated in section 23M(2) that exceeds the amount disallowed, if any, on that debt under section 23N (R210 000 – RNil) / (R250 000 – RNil)	(210 000)	(250 000)
Limitation amounts	432 000	360 000

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Determination of amounts of interest that are to be disallowed under section 23M(2)

	2024 R	2025 R
Interest incurred on debt owed to a creditor in a controlling relationship, allowed to be deducted (R1 000 000 – R112 400) / (R1 100 000 – R150 800)	887 600	949 200
Add: Excess carried forward from prior year under section 23M(4)	-	455 600
Less: Limitation determined under section 23M(3)	(432 000)	(360 000)
Interest disallowed under section 23M(2) and carried forward under section 23M(4) to the 2025 and 2026 years of assessment respectively	455 600	1 044 800

The amounts of interest to be disallowed under sections 23N(2) and 23M(2) are as follows:

	2024 R	2025 R
Amounts disallowed under section 23N(2) – no carry forward	112 400	150 800
Amounts disallowed under section 23M(2) – carry forward permitted	455 600	1 044 800
Total amounts to be disallowed	568 000	1 195 600

The amounts of interest to be deducted after applying the limits in sections 23N(2) and 23M(2) are as follows:

	2024 R	2025 R
Acquisition loan – current year	1 000 000	1 100 000
Section 23M(4) brought forward		455 600
Amounts disallowed under section 23N – no carry forward permitted	(112 400)	(150 800)
Amounts disallowed under section 23M – carry forward permitted	(455 600)	(1 044 800)
Other loan interest	210 000	250 000
Total amounts allowed in current year	642 000	610 000

Example 19 – Interaction between sections 23M and 23N

Facts:

Company A, a resident, was incorporated on 1 April 2024. Its 2025 year of assessment ended on 31 March.

During its 2025 year of assessment, Company A entered into an intra-group transaction under section 45(1) under which it acquired assets from another group company. The acquisition of the relevant assets by Company A was funded with debt obtained from Company B and Company C. The debt was repaid on 31 March 2025.

Company B held 51% of the equity shares in Company A and exercised 51% of the voting rights in the company. Company C held 49% of Company A's equity shares and exercised 49% of the voting rights in the company.

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Assume an average repo rate of 6% for 2025.

Company B and Company C are foreign companies that are residents of Foreign Country C. The interest earned by Company B and Company C is from a source within South Africa as it is attributable to an amount incurred by Company A and Company A is a resident [section 9(2)(*b*)(*i*)].

The tax treaty between South Africa and Foreign Country C provided that South Africa did not have a right to tax the interest. Accordingly, the interest income is not subject to normal tax or withholding tax on interest. Section 31 is not considered for purposes of this example.

Company A's taxable income before applying sections 23M and 23N as well as interest incurred and interest received by or accrued to it during the 2025 year of assessment was as follows:

	R
Taxable income	100 000
Interest received	200 000
Interest incurred on debt payable to Company B	(3 000 000)
Interest incurred on debt payable to Company C	(2 000 000)
Interest incurred on other debt	(100 000)

Assume an average repo rate of 6% for the 2025 year of assessment.

Result:

Application of section 23N

Section 23N(2) applies, since interest was incurred by an acquiring company (Company A) on debt directly used for the purpose of funding the acquisition of assets under an intra-group transaction under section 45(1) that qualifies as a reorganisation transaction under the definition of "reorganisation transaction" in section 23N(1).

The interest incurred by Company A under the reorganisation transaction of R5 million (R3 million + R2 million) must not exceed the amount determined as follows under section 23N(3):

	R
Calculation of adjusted taxable income	
Taxable income	100 000
Less: Amounts included in taxable income	
Interest received	(200 000)
	(100 000)
Add: Amounts deducted from income:	
Interest incurred on debt payable to Company B	3 000 000
Interest incurred on debt payable to Company C	2 000 000
Interest incurred on other debt	100 000
Adjusted taxable income	5 000 000

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Calculation of the percentage under section 23N(4) to be applied to adjusted taxable income under section 23N(3)(b)

Formula	2025
A = B × [C /D]	
B =	40
C = (6 + 4)	10
D =	10
A (Percentage calculated) =	40%

Determination of the limitation under section 23N(3)

	R
Interest received	200 000
Add: Percentage × adjusted taxable income (see above)	
(40% × R5 000 000)	2 000 000
Less: Interest incurred on other debt	(100 000)
Limitation amount	2 100 000

The interest of R5 million incurred on the debt that funded the reorganisation transaction is therefore limited to R2,1 million under section 23N(2). The excess of R2,9 million (R5 million – R2,1 million) is disallowed and is not carried forward to Company A's 2026 year of assessment.

The R2,9 million disallowed under section 23N must be allocated between the debt payable to Company B and the debt payable to Company C – this will be required when applying section 23M (see below). Allocated pro-rata based on the interest expense as a fair and reasonable approach:

i) Not allowed on debt payable to Company B = R2 900 000 disallowed x R3 000 000 / R5 000 00 = R1 740 000.
ii) Not allowed on debt payable to Company C = R2 900 000 disallowed x R2 000 000 / R5 000 00 = R1 160 000.

Application of section 23M

Section 23M(2) applies because –

- interest was incurred by a debtor (Company A) on a debt owed to a creditor (Company B) that was in a controlling relationship with the debtor;
- a controlling relationship existed between Company A and Company B, since Company B held at least 50% of Company A's equity shares and exercised at least 50% of its voting rights (Note 1);
- during Company A's 2025 year of assessment, Company B was not subject to tax on the interest incurred by Company A of R3 million on the debt owed to Company B; and
- the interest incurred of R3 million was not disallowed in full under section 23N.

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The limitation amount for purposes of section 23M(2) for the 2025 year of assessment is calculated under section 23M(3) as follows:

Calculation of adjusted taxable income

	R	R
Taxable income before applying sections 23M and 23N		100 000
Add: Interest disallowed under section 23N		2 900 000
Taxable income before applying section 23M		3 000 000
Less: Amounts included in taxable income		
Interest received		(200 000)
		2 800 000
Add: Amounts deducted from income		
Interest incurred on debt payable to Company B	3 000 000	
Interest incurred on debt payable to Company C	2 000 000	
Less: Interest disallowed under section 23N(2) (Note 2)	(2 900 000)	
Interest incurred that has been allowed as a deduction after section 23N		2 100 000
Interest incurred on other debt		100 000
Adjusted taxable income		5 000 000

Determination of the limitation under section 23M(3)

Interest received	200 000
Add: 0.3 × adjusted taxable income (0.3 × R5 000 000)	1 500 000
Less: Interest incurred on debt not contemplated in section 23M(2) as exceeds an amount disallowed on that debt under section 23N	
- Interest on debt payable to Company C [R2 000 000 interest – R1 160 000 disallowed under section 23N (see above)]	(840 000)
- Interest on other debt [R100 000 interest – Rnil disallowed under section 23N]	(100 000)
Limitation amount	760 000

The interest of R5 million (R3 million + R2 million) was limited to R2,1 million under section 23N(2). The portion of that limitation (that is, what was allowed to be deducted) allocated to the debt to Company B (the debt subject to section 23M), based on pro-rata relative interest expenditure, was R1 260 000 (R2,1 million x 3/5). The limitation amount of R760 000 determined under section 23M(2) is lower than the limitation amount of R1 260 000 determined under section 23N(2). An amount of R500 000 (R1 260 000 – R760 000) is therefore disallowed under section 23M(2), but may be carried forward.

The amounts of interest to be disallowed under sections 23N(2) and 23M(2) are as follows:

	R
Amount disallowed under section 23N(2)	2 900 000
Amount disallowed under section 23M(2) (carry forward)	500 000
Total amount to be disallowed	3 400 000

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The amount of interest to be deducted after applying the limits in sections 23N(2) and 23M(2) are as follows:

	R
Debt payable to Company B	3 000 000
Debt payable to Company C	2 000 000
Section 23M(4) brought forward	-
Amounts disallowed under section 23N – no carry forward permitted	(2 900 000)
Amounts disallowed under section 23M – carry forward permitted	(500 000)
Other loan interest	100 000
Total amounts allowed in current year	1 700 000

Note:

(1) A controlling relationship did not exist between Company A and Company C, since Company C neither held at least 50% of Company A's equity shares nor did it exercise at least 50% of its voting rights.

(2) Interest of R2 900 000 is added back to adjusted taxable income, since it was disallowed under section 23N(2).

4.5.6 Non-application of section 23M [section 23M(6)]

Section 23M does not apply under the circumstances provided for in section 23M(6)(*a*) (interest on back-to-back loans originally sourced from third-party lending institutions subject to certain requirements) and, prior to 1 January 2027, (*b*) (interest incurred by a debtor in respect of any linked unit held by a creditor, where that creditor is either a long-term insurer, a pension fund or provident fund subject to certain requirements).

(a) Funding granted by a lending institution that is not in a controlling relationship with the debtor [section 23M(6)(*a*)]

Section 23M does not apply to a debt owed to a creditor as contemplated in section 23M(2) *in respect of which interest contemplated in section 24J is incurred*[108] when both the following requirements are met:

- The creditor *directly or indirectly*[109] funded the debt amount advanced to the debtor with funding granted by a lending institution[110] that is not in a controlling relationship with the debtor [section 23M(6)(*a*)(i)].
- The interest incurred by the debtor on the debt owing to the creditor is determined with reference to a rate of interest that does not exceed the official rate of interest as defined in section 1(1) plus 100 basis points (1%) [section 23M(6)(*a*)(ii)]. The official rate of interest as defined is linked to the South African repurchase rate plus 1%. If the official rate of interest is, for example, 8,75%, the maximum interest rate envisaged in section 23M(6)(*a*)(ii) would be 9,75% (8,75% plus 1%).[111]

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[108] Amendment effective years of assessment commencing on or after 1 January 2026.

[109] Amendment effective years of assessment commencing on or after 1 January 2026.

[110] As defined in section 23M(1) [see **4.5.1 (g)**].

[111] A list of the official rates of interest is available on the SARS website under Legal Counsel ⇨ Legal Counsel Publications ⇨ Tables of Interest Rates ⇨ Table 3.

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Example 20 – Application of section 23M(6)(*a*)

Facts:

Company A's year of assessment ends on 30 November. Company A held 50% of the equity shares in Company B for the duration of Company A's 2025 year of assessment. Company B is a foreign company and resident of Foreign Country B. Company B advanced a loan of R1 million to Company A on 1 December 2024.

These funds were obtained from Foreign Bank B, which is a "lending institution" as defined in section 23M(1). Company A and Foreign Bank B are not in a controlling relationship with each other.

Company A incurred interest of R80 000 at the rate of 8% a year on this loan for the 2025 year of assessment. Company B was exempt from normal tax on the interest that accrued to it during the 2025 year of assessment under section 10(1)(*h*). The tax treaty between South Africa and Foreign Country B provided that South Africa did not have a right to tax the interest. Accordingly, the interest income is not subject to normal tax or withholding tax on interest.

The official rate of interest was 8,75% for the period 1 December 2024 to 31 January 2025, 8,5% for the period 1 February 2025 to 31 May 2025, 8,25% for the period 1 June 2025 to 31 August 2025 and 8% for the period 1 September 2025 to 30 November 2025.

Section 23N did not apply, since the interest was not incurred on debt that funded an acquisition or reorganisation transaction. Section 31 is not considered for purposes of this example.

Result:

Section 23M(2) potentially applies, since –

- interest was incurred by Company A on debt owed to a creditor (Company B) that was in a controlling relationship with Company A, since Company A held at least 50% of the equity shares in Company B;
- Company B was not subject to tax on the interest of R80 000 incurred by Company A during Company A's 2025 year of assessment, since the tax treaty between South Africa and Foreign Country B provided that South Africa did not have a right to tax the interest; and
- the interest of R80 000 incurred by Company A during the 2025 year of assessment was not disallowed under section 23N.

However, the requirements of section 23M(6)(*a*) were met because –

- the funding was obtained by Company B from a lending institution that is not in a controlling relationship with Company A; and
- the interest incurred by Company A was determined at a rate of 8% a year, which does not exceed the prescribed rate of interest for the relevant periods (the official rate of interest (see above) plus 1%.

The limitation rules under section 23M(2) therefore do not apply.

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Example 21 – Application of section 23M(6)(*a*)

Facts:

Company A's year of assessment ends on 30 November. Company A held 50% of the equity shares in Company B for the duration of Company A's 2025 year of assessment. Company B is a foreign company and resident of Foreign Country B.

Company B advanced a loan of R1 million to Company A on 1 December 2024. These funds were obtained from Foreign Bank B, which is a "lending institution" as defined in section 23M(1). Company A and Foreign Bank B are not in a controlling relationship with each other.

Company A incurred interest of R100 000 at the rate of 10% a year on this loan for the 2025 year of assessment. The tax treaty between South Africa and Foreign Country B provided that South Africa did not have a right to tax the interest. Accordingly, the interest income is not subject to normal tax or withholding tax on interest.

Section 23N did not apply, since the interest was not incurred on debt that funded an acquisition or reorganisation transaction.

The official rate of interest was 8,75%% for the period 1 December 2024 to 31 January 2025, 8,5% for the period 1 February 2025 to 31 May 2025, 8,25% for the period 1 June 2025 to 31 August 2025 and 8% for the period 1 September 2025 to 30 November 2025.

Section 31 was not considered for purposes of this example.

Result:

Section 23M(2) applies because –

- interest was incurred by Company A on debt owed to a creditor (Company B) that was in a controlling relationship with Company A, since Company A held at least 50% of the equity shares in Company B;
- Company B was not subject to tax on the interest of R100 000 incurred by Company A during Company A's 2025 year of assessment, since it was exempt from both normal tax and withholding tax on interest; and
- the interest of R100 000 incurred by Company A during the 2025 year of assessment was not disallowed under section 23N.

Even though the funding was obtained by Company B from a lending institution that is not in a controlling relationship with Company A, the requirement in section 23M(6)(*a*)(ii) has not been met, since the interest incurred by Company A was determined at a rate of 10% a year which exceeds the prescribed rates of interest for the relevant period (the official rate of interest (see above) plus 1%).

Section 23M(6)(*a*) therefore does not apply with the result that section 23M(2) remains applicable. Under section 23M(2) the amount of interest allowed to be deducted on the debt advanced by Company B may not exceed the amount determined under section 23M(3).

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(b) Interest incurred by a debtor on certain linked units [section 23M(6)(*b*)]

Before 1 January 2027, section 23M does not apply to any interest incurred by a debtor on any linked unit that is held by a creditor as contemplated in section 23M(2) when the creditor was a long-term insurer as defined in the Long-term Insurance Act 52 of 1998, a pension fund or a provident fund, if –

- the long-term insurer, pension fund or provident fund held at least 20% of the linked units in that debtor;
- the long-term insurer, pension fund or provident fund had acquired the linked units before 1 January 2013; and
- at the end of the previous year of assessment 80% or more of the value of the assets of that debtor, reflected in the annual financial statements prepared in accordance with the Companies Act for the previous year of assessment, was directly or indirectly attributable to immovable property.

Section 23M(6)(*b*) will be repealed with effect from 1 January 2027 meaning that section 23M applies under the above circumstances to interest incurred on or after that date.

4.5.7 Interest on loan used for mining purposes [section 23M(6A)]

Section 23M(6A) provides that interest incurred on a loan used for mining purposes during pre-production or non-production periods, as contemplated in paragraph (*b*) of "capital development expenditure" in section 36(11), is not subject to the limitations of section 23M. This interest remains fully deductible as part of the capital expenditure of the mining operations under section 36(11).

4.5.8 Exchange gains and losses [section 23M(7)]

Section 23M(7) provides that any exchange difference deducted from the income of a person contemplated under sections 24I(3) or 10A is deemed to have been incurred by that person. Similarly, any exchange difference included in the income of a person contemplated under sections 24I(3) or 10A is deemed to have accrued to that person.

Exchange gains and losses taken into account under section 24I(3) and 24I(10A) are included in interest for purposes of section 23M (see **4.5.1(f)**).

4.5.9 Interaction between sections 23M, 23N and 31

Section 31[112] determines the taxation of international transactions between connected persons or associated enterprises, not dealing at arm's length if any person that is a party to that transaction, operation, scheme, agreement or understanding derives a tax benefit from it.

Section 31 requires taxpayers to –

- determine whether the actual terms and conditions of any transaction, operation, scheme, agreement or understanding meeting paragraph (*a*) of the definition of "affected transaction"[113] differ from the terms and conditions that

[112] See Interpretation Note 127 "Determination of the Taxable Income of Certain Persons from International Transactions: Intra-group Loans," for a detailed consideration of section 31 in the context of the pricing of intra-group loans.

[113] See the definition of "affected transaction" in section 31(1).

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would have existed if the parties had been independent persons dealing at arm's length; and

- to calculate their taxable income or tax payable based on the arm's length terms and conditions of the affected transaction if there is a difference that results or will result in a tax benefit for the taxpayer that is a party to the affected transaction.

The interaction between sections 23M, 23N and 31 is explained as follows in the *Draft Response Document from National Treasury and SARS on the Draft Taxation Laws Amendment Bill, 2014 and Tax Administration Laws Amendment Bill, 2014* to the Standing Committee on Finance:[114]

> "The purpose of section 31 is to ensure that if cross-border transactions, such as debt financing, are entered into by connected persons, they must be treated (for tax purposes) as if the amount lent and the interest rate charged between the parties are equivalent to that between two independent parties, i.e. the arm's length principle. In essence, section 31 seeks to correct mispricing due to the terms and conditions of the transaction.
>
> The excessive interest limitation has a broader objective. By limiting the amount of interest deductible, it discourages companies from excessive leveraging, which is often done because the tax system inherently encourages debt over equity financing. Interest limitation rules based on profitability and the ability to fund the finance charges is (sic) closer aligned with commercial practice and is (sic) more effective at protecting the South Africa[n] economy than a simple debt to equity ratio.
>
> A cap on the amount of interest deductible thus assists in both how much debt (in relation to equity) a company takes on, as well as the price thereof. Transfer pricing always applies first by determining the correct pricing, the draft legislation will be changed to provide that section 23N applies first and then section 23M and that interest expenses disallowed under section 23N are not covered by 23M as well."

Section 31 applies prior to considering the impact, if any, of section 23M and section 23N. This is apparent from the wording in section 31, section 23M and section 23N. If the requirements of section 31 are met, section 31(2) requires that taxable income must be calculated as if the affected transaction had been entered into on arms' length terms and conditions.

The term "adjusted taxable income", as defined in section 23M and section 23N, is a key component in determining the amount of interest that is allowed to be deducted under these sections. By definition, the starting point in determining "adjusted taxable income" is taxable income calculated before applying section 23M or section 23N and the definition also refers to, amongst others, the amount of interest received or accrued that forms part of taxable income and the amount of interest incurred that has been allowed as a deduction from income.

In calculating taxable income, and therefore the amount that is *prima facie* deductible, section 31(2) requires the application of the arm's length principle. Since section 31 is applied in calculating taxable income and, if applicable, would have an impact of the amount received or accrued that is part of taxable income, and that is incurred and has been allowed as a deduction, it is clear that section 31 applies before section 23M or section 23N.

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[114] In paragraph 3.2.

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Section 23M and section 23N are sections which potentially place a limitation on the amount of interest that would otherwise be deductible, that is the arm's length amount that is initially included in calculating taxable income after applying the arm's length principle under section 31 (if applicable) but before applying section 23N and section 23M (as noted previously section 23N is applied first and then section 23M). It is not a case of that if one provision (section 23M or section 23N) applies then the other (section 31) does not apply. Depending on the facts section 31, section 23M and section 23N could all apply.

Accordingly, when section 23M and section 23N refer to taxable income in the definition of "adjusted taxable income" and to the amount of interest which is included as part of taxable income or which is allowed to be deducted in section 23M(3) and section 23N(2), the reference is to the amount of taxable income and the amount of interest, after section 31 has been applied.

5. Conclusion

Special rules apply to interest incurred on debt that financed the acquisition of equity shares under an "acquisition transaction" as defined in section 24O(1). Under section 24O(2) any interest incurred by a company on such debt must, to the extent to which the amount thereof relates to a period during which the company held the equity shares and the equity shares constituted a qualifying interest in an operating company as determined at the dates referred to in section 24O(2)(ii), be deemed to have been incurred in the production of income and laid out or expended for the purposes of trade.

Section 23N(2) provides that an amount of interest incurred by an acquiring company allowed to be deducted on the following debt must not exceed an amount determined under section 23N(3):

- Debt directly or indirectly assumed or applied for the purpose of procuring, enabling, facilitating or funding the acquisition by that acquiring company of any asset under a reorganisation transaction.
- Debt used directly or indirectly for the purpose of redeeming, refinancing or settling the debt referred to in the first bullet, relating to a reorganisation transaction.
- Debt issued, assumed or used under an acquisition transaction.
- Debt used directly or indirectly for the purpose of redeeming, refinancing or settling the debt referred to in the third bullet, relating to an acquisition transaction.

A transaction that qualifies as an "acquisition transaction" as defined under section 23N(1) will not qualify as an "acquisition transaction" as defined under section 24O(1) should the acquiring and acquired companies not form part of the same "group of companies" as defined in section 41(1).

Amounts of interest disallowed under section 23N(2) are not carried forward to subsequent years of assessment. Under section 23N(3), a limitation must be calculated for the year of assessment that the acquisition or reorganisation transaction is entered into and for the five subsequent years of assessment. Interest on the specific debt incurred from the sixth subsequent year of assessment onwards is not subject to limitation under section 23N(2).

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Section 23M(2) provides for a limitation, to be determined under section 23M(3), of a deduction for interest incurred by a debtor during a year of assessment and the debtor incurred interest (other than interest contemplated in paragraph (c) of the definition of "interest" in section 23M(1), that is amounts taken into account in determining taxable income in terms of section 24I (3) and (10A))[115] on a debt owed to a creditor that is –

- in a controlling relationship with the debtor; or
- not in a controlling relationship with the debtor, if that creditor obtained the funding for the debt advanced to the debtor from a person that is in a controlling relationship with that debtor.
- not in a controlling relationship with that debtor, if that creditor forms part of the same group of companies as that debtor if the expression "more than 50 per cent of the equity shares or voting rights in" in the definition of "group of companies in section 1(1) is replaced with the expression "at least 70 per cent of the equity shares in"; or
- in a controlling relationship with that debtor, if that creditor directly or indirectly through another creditor that is in a controlling relationship with that creditor, obtained the funding for the debt advanced to the debtor from a person that is in a controlling relationship with that creditor or that other creditor

Section 23M(2) will apply only when the following requirements are met and a controlling relationship has been established:

- The amount of the interest referred to above (that is, other than interest contemplated in paragraph (c) of the definition of "interest" in section 23M(1)[116] or related interest is not during that same year of assessment subject to tax in the hands of the person to which the interest or related interest accrues or is not included in the net income of a CFC in the foreign tax year of the CFC commencing or ending within that year of assessment.
- The interest is not during that year of assessment disallowed in full under section 23N.

In addition, before 1 January 2027, section 23M(2) does not apply to any interest incurred by a debtor on any linked unit that is held by a creditor as contemplated in section 23M(2) when the creditor was a long-term insurer as defined in the Long-term Insurance Act 52 of 1998, a pension fund or a provident fund, if certain conditions are met.

Under section 23M(4) any amount of interest that exceeds the amount determined under section 23M(3) must be carried forward to the immediately succeeding year of assessment of the debtor. The amount so carried forward must be deemed to be an amount of interest incurred in that succeeding year of assessment in respect of a debt that qualifies for deduction in that succeeding year of assessment subjection to the limitation in section 23M(2).

Section 23M(5) provides that when an amount of interest is to be taken into account under both sections 23M and 23N, the amount of interest shall be taken into account under section 23M only after section 23N has been applied.

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[115] Amendment effective years of assessment commencing on or after 1 January 2026.

[116] Amendment effective years of assessment commencing on or after 1 January 2026.

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Section 23M does not apply to a debt owed to a creditor as contemplated in section 23M(2) in respect of which interest contemplated in section 24J is incurred when –

- the creditor directly or indirectly funded the debt amount advanced to the debtor with funding granted by a lending institution that is not in a controlling relationship with the debtor; and
- the interest is determined with reference to a rate of interest that does not exceed the "official rate of interest" as defined in section 1(1) plus 100 basis points (1%).

Under section 23M(6A) interest incurred on a loan used for mining purposes during pre-production or non-production periods is not subject to the limitations of section 23M. This interest remains fully deductible as part of the capital expenditure of the mining operations.

Any exchange difference deducted from the income of a person under sections 24I(3) or 10A is deemed to have been incurred by that person. Similarly, any exchange difference included in the income of a person under sections 24I(3) or 10A is deemed to have accrued to that person (section 23M(7)).

Section 31 applies before considering the impact, if any, of sections 23M and 23N. Accordingly, when these sections refer to taxable income in the definition of "adjusted taxable income" in sections 23M(1) and 23N(1) and to the amount of interest that is allowed to be deducted under sections 23M(2) and 23N(2), they do so after first applying section 31. If all three sections are applicable, section31 is applied first, then section 23N and lastly section 23M.

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Annexure – The law

Section 1(1) – Definition of "controlled foreign company"

"controlled foreign company" means a controlled foreign company as defined in section 9D;

Section 1(1) – Definition of "controlled group company"

"controlled group company" means a controlled group company contemplated in the definition of "group of companies";

Section 1(1) – Definition of "controlling group company"

"controlling group company" means a controlling group company contemplated in the definition of "group of companies";

Section 1(1) – Definition of "equity share"

"equity share" means any share in a company, excluding any share that, neither as respects dividends or foreign dividends, nor as respects returns of capital or foreign returns of capital, carries any right to participate beyond a specified amount in a distribution;

Section 1(1) – Definition of "group of companies"

"group of companies" means two or more companies in which one company (hereinafter referred to as the **"controlling group company"**) directly or indirectly holds shares in at least one other company (hereinafter referred to as the **"controlled group company"**), to the extent that—

(*a*) at least 70 percent of the equity shares in each controlled group company are directly held by the controlling group company, one or more other controlled group companies or any combination thereof; and

(*b*) the controlling group company directly holds at least 70 per cent of the equity shares in at least one controlled group company;

Section 1(1) – Definition of "official rate of interest"

"official rate of interest" means—

(*a*) in the case of a debt which is denominated in the currency of the Republic, a rate of interest equal to the South African repurchase rate plus 100 basis points; or

(*b*) in the case of a debt which is denominated in any other currency, a rate of interest that is the equivalent of the South African repurchase rate applicable in that currency plus 100 basis points:

Provided that where a new repurchase rate or equivalent rate is determined, the new rate of interest applies for the purposes of this definition from the first day of the month following the date on which that new repurchase rate or equivalent rate came into operation;

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Section 9(2)(*b*)

(2) An amount is received by or accrues to a person from a source within the Republic if that amount—

(*b*) constitutes interest as defined in section 24J where that interest—

(i) is attributable to an amount incurred by a person that is a resident, unless the interest is attributable to a permanent establishment which is situated outside the Republic; or

(ii) is received or accrues in respect of the utilisation or application in the Republic by any person of any funds or credit obtained in terms of any form of interest-bearing arrangement;

Section 9D(1) – Definition of "controlled foreign company"

"controlled foreign company" means—

(*a*) any foreign company where more than 50 per cent of the total participation rights in that foreign company are directly or indirectly held, or more than 50 per cent of the voting rights in that foreign company are directly or indirectly exercisable, by one or more persons that are residents other than persons that are headquarter companies: Provided that—

(i) no regard must be had to any voting rights in any foreign company—

(*aa*) which is a listed company; or

(*bb*) if the voting rights in that foreign company are exercisable indirectly through a listed company;

(ii) any voting rights in a foreign company which can be exercised directly by any other controlled foreign company in which that resident (together with any connected person in relation to that resident) can directly or indirectly exercise more than 50 per cent of the voting rights are deemed for purposes of this definition to be exercisable directly by that resident; and

(iii) a person is deemed not to be a resident for purposes of determining whether residents directly or indirectly hold more than 50 per cent of the participation rights or voting rights in a foreign company, if—

(*aa*) in the case of a listed company or a foreign company the participation rights of which are held by that person indirectly through a listed company, that person holds less than five per cent of the participation rights of that listed company; or

(*bb*) in the case of a scheme or arrangement contemplated in paragraph (*e*)(ii) of the definition of "company" in section 1 or a foreign company the participation rights of which are held and the voting rights of which may be exercised by that person indirectly through such a scheme or arrangement, that person—

(A) holds less than five per cent of the participation rights of that scheme or arrangement; and

(B) may not exercise at least five per cent of the voting rights in that scheme or arrangement,

unless more than 50 per cent of the participation rights or voting rights of that foreign company or other foreign company are held by persons who are connected persons in relation to each other; or

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(*b*) any foreign company where the financial results of that foreign company are reflected in the consolidated financial statements, as contemplated in IFRS 10, of any company that is a resident, other than a headquarter company;

Section 10(1)(*h*)

10. Exemptions.—(1) There shall be exempt from normal tax—

(*h*) any amount of interest which is received or accrues by or to any person that is not a resident, unless—

(i) that person is a natural person who was physically present in the Republic for a period exceeding 183 days in aggregate during the twelve-month period preceding the date on which the interest is received by or accrues to that person; or

(ii) the debt from which the interest arises is effectively connected to a permanent establishment of that person in the Republic;

Section 11(*a*)

11. General deductions allowed in determination of taxable income.—For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived—

(*a*) expenditure and losses actually incurred in the production of the income, provided such expenditure and losses are not of a capital nature;

Section 23(*f*)

23. Deductions not allowed in determination of taxable income.—No deductions shall in any case be made in respect of the following matters, namely—

(*f*) any expenses incurred in respect of any amounts received or accrued which do not constitute income as defined in section *one*;

Section 23(*q*)

23. Deductions not allowed in determination of taxable income.—No deductions shall in any case be made in respect of the following matters, namely—

(*q*) any expenditure incurred in the production of income in the form of foreign dividends; or

Section 23M (* - *amendment effective years of assessment commencing on or after 1 January 2026*)

23M. Limitation of interest deductions in respect of debts owed to persons not subject to tax.—(1) For the purposes of this section—

"adjusted taxable income" means taxable income calculated before applying this section and before setting off any balance of assessed loss that has been carried forward from the preceding year of assessment—

(*a*) reduced by—

(i) any amount of interest *contemplated in section 24J** received or accrued that forms part of taxable income;

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(ii) any amount included in the income of a person as contemplated in section 9D(2);

(iii) any amount recovered or recouped in respect of an allowance contemplated in this Act in respect of a capital asset as defined in section 19;

(iv) any amount of interest accrued, other than amounts referred to in subparagraph (i), in respect of debt referred to in subsection (3);* and

(*b*) with the addition of—

(i) any amount of interest *contemplated in section 24J** incurred that has been allowed as a deduction from income;

(ii) any amount allowed as a deduction in terms of this Act in respect of a capital asset as defined in section 19 for purposes other than the determination of any capital gain or capital loss;

(iii) …

(iv) any qualifying distribution as defined in section 25BB that is deductible under subsection (2) of that section:

(v) any amount of interest incurred, other than amounts referred to in subparagraph (i), in respect of debt referred to in subsection (3);*

Provided that the result of the calculation may not be less than zero;

"average repo rate" …

"controlling relationship" means a relationship where a person, whether alone or together with any one or more persons that are connected persons in relation to that person directly or indirectly hold at least 50 per cent of the equity shares or can exercise at least 50 per cent of the voting rights or participation rights, in a company;

"creditor" means a person to whom a "debtor" owes a "debt";

"debt" includes any amount in respect of which interest is determined or incurred, and such amount must be regarded as owed, but does not include a tax debt as defined in section (1)1 of the Tax Administration Act;

"debtor" means a person that incurs an amount of interest and—

(*a*) is a resident; or

(*b*) in the case of a person that is not a resident, owes a debt that is effectively connected with a permanent establishment of that person in the Republic;

"interest" means interest as defined in section 24J, and includes—

(*a*) amounts incurred or accrued under any "interest rate agreement" as defined in section 24K(1);

(*b*) any finance cost element recognised for purposes of IFRS in respect of any lease arrangement that constitutes a finance lease as defined in IFRS16;

(*c*) amounts taken into account in determining taxable income in terms of section 24I(3) and (10A); and

(*d*) any amount deemed to be interest under section 24JA,

but excludes any amount that is deemed to be a dividend *in specie* as contemplated in sections 8F and 8FA;

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"issue" …

"lending institution" means—

(*a*) a bank; or

(*b*) a foreign bank that is comparable to a bank,

contemplated in the Banks Act;

"participation rights" means—

(*a*) the right to participate in all or part of the benefits of the rights (other than voting rights) attaching to a share, or any interest of a similar nature, in a company; or

(*b*) in the case where no person has any right in that company as contemplated in paragraph (a) or no such rights can be determined for any person, the right to exercise any voting rights in that company;

"repo rate" …

(2) Where an amount of interest*, other than interest contemplated in paragraph (c) of the definition of 'interest' in subsection (1),** is incurred by a debtor during a year of assessment in respect of a debt owed to—

(*a*) a creditor that is in a controlling relationship with that debtor; or

(*b*) a creditor that is not in a controlling relationship with that debtor, if that creditor obtained the funding for the debt advanced to the debtor from a person that is in a controlling relationship with that debtor,

(*c*) a creditor that is not in a controlling relationship with that debtor, if that creditor forms part of the same group of companies as that debtor if the expression "at least 70 per cent of the equity shares in" in paragraphs (*a*) and (*b*) of the definition of "group of companies" in section 1 were replaced by the expression "more than 50% of the equity shares or voting rights in"; or

(*d*) a creditor that is in a controlling relationship with that debtor, if that creditor, directly or indirectly through another creditor that is in a controlling relationship with that creditor, obtained the funding for the debt advanced to the debtor from a person that is in a controlling relationship with that creditor or that other creditor

and the amount of interest so incurred or related interest is not during that year of assessment—

(i) (*aa*) subject to tax in the hands of the person, creditor or other creditor referred to in paragraphs (*a*), (*b*), (*c*), or (*d*) to which the interest*, other than interest contemplated in paragraph (c) of the definition of 'interest' in subsection (1),** or related interest accrues; or

(*bb*) included in the net income of a controlled foreign company as contemplated in section 9D in the foreign tax year of the controlled foreign company commencing or ending within that year of assessment; and

(ii) disallowed under section 23N,

the amount of interest allowed to be deducted may not exceed the amount determined in accordance with subsection (3): Provided that where any amount of interest*, other than interest contemplated in paragraph (c) of the definition of 'interest' in subsection (1),** incurred or related interest is not included in the income of the person referred to in paragraph (i)(*aa*), and withholding tax on interest was or will be levied on the amount of interest, on payment thereof, under the provisions of Part IVB of this Chapter, the amount of interest to be regarded as not subject to tax as contemplated in paragraph (i)(aa) will be determined in accordance with the formula:

$$A = B \times \frac{(C - D)}{C}$$

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in which formula—

(*i*) "A" represents the amount to be determined;

(*ii*) "B" represents the aggregate of any amount of interest incurred or paid in respect to which the provisions of Part IVB of this Chapter are or will be applicable;

(iii) "C" represents the number 15; and

(iv) "D" represents the rate at which withholding tax on interest has been or will be levied on such amount of interest under the provisions of Part IVB of this Chapter, multiplied by the number 100.

(3) The amount of interest allowed to be deducted in respect of all debts owed as contemplated in subsection (2), in respect of any year of assessment must not exceed the sum of—

(*a*) the amount of interest *contemplated in section 24J and any other amount of interest in respect of that debt,** received by or accrued to the debtor; and

(*b*) an amount determined by multiplying the adjusted taxable income of that debtor for that year of assessment by 0.3,

reduced by so much of any amount of deductible interest *contemplated in section 24J** incurred by the debtor in respect of debts other than debts contemplated in subsection (2) as exceeds any amount not allowed to be deducted in terms of section 23N.

(4) So much of any amount of interest as exceeds the amount determined in terms of subsection (3) *must** be carried forward to the immediately succeeding year of assessment and must be deemed to be an amount of interest incurred in that succeeding year of assessment in respect of a debt *that qualifies for a deduction subject to the limitation in subsection (2)*.*

(5) Where an amount of interest is to be taken into account in terms of this section and in terms of section 23N, that amount of interest shall only be taken into account in terms of this section after section 23N has been applied.

(6) This section does not apply—

(*a*) to a debt owed to a creditor as contemplated in subsection (2) *in respect of which interest contemplated in section 24J is incurred,** where—

(i) that creditor *directly or indirectly** funded that debt amount advanced to that debtor with funding granted by a lending institution that is not in a controlling relationship with that debtor; and

(ii) that interest is determined with reference to a rate of interest that does not exceed the official rate of interest plus 100 basis points.

(*b*)[117] to any interest incurred by a debtor in respect of any linked unit that is held by a creditor as contemplated in subsection (2) where that creditor is a long-term insurer as defined in the Long-term Insurance Act, a pension fund or a provident fund, if—

(i) the long-term insurer, pension fund or provident fund holds at least 20 per cent of the linked units in that debtor;

(ii) the long-term insurer, pension fund or provident fund acquired those linked units before 1 January 2013; and

(iii) at the end of the previous year of assessment 80 per cent or more of the value of the assets of that debtor, reflected in the annual financial statements prepared in accordance with the Companies Act for the previous year of assessment, is directly or indirectly attributable to immovable property.

[117] Repealed with effect from 1 January 2027.

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(6A) This section does not apply to interest incurred on a loan utilised for mining purposes during any period prior to the commencement of production or during any period of non-production, as contemplated in paragraph (*b*) of the definition of "capital expenditure" in section 36(11).

(7) For purposes of this section any exchange difference--

(*a*) deducted from the income of a person as contemplated in section 24I(3) or 10A is deemed to have been incurred by the person; or

(*b*) included in income of a person as contemplated in section 24I(3) or 10A is deemed to have accrued to that person

Section 23N

23N. Limitation of interest deductions in respect of reorganisation and acquisition transactions.—(1) For the purposes of this section—

"acquired company" means—

(*a*) a transferor company or a liquidating company that disposes of assets pursuant to a reorganisation transaction; or

(*b*) a company in which equity shares are acquired by another company in terms of an acquisition transaction;

"acquiring company" means—

(*a*) a transferee company contemplated in the definition of "intra-group transaction" in section 45(1);

(*b*) a holding company contemplated in the definition of "liquidation distribution" in section 47(1); or

(*c*) a company that acquires an equity share in another company in terms of an acquisition transaction;

"acquisition transaction" means any transaction—

(*a*) in terms of which an acquiring company acquires an equity share in an acquired company that is a company as contemplated in paragraph (*a*) or (*b*) of the definition of "acquisition transaction" in section 24O(1); and

(*b*) as a result of which that acquiring company, as at the end of the day of that transaction, becomes a controlling group company in relation to that acquired company;

"adjusted taxable income" means taxable income calculated before applying this section and before setting off any balance of assessed loss that has been carried forward from the preceding year of assessment: Provided that the result of this calculation may not be less than zero—

(*a*) reduced by—

(i) any amount of interest received or accrued that forms part of taxable income;

(ii) any amount included in the income of a person as contemplated in section 9D(2);

(iii) any amount recovered or recouped in respect of an allowance contemplated in this Act in respect of a capital asset as defined in section 19; and

(*b*) with the addition of—

(i) any amount of interest incurred that has been allowed as a deduction from income;

(ii) any amount allowed as a deduction in terms of this Act in respect of a capital asset as defined in section 19 for purposes other than the determination of any capital gain or capital loss;

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(iii) 75 per cent of the receipts or accruals derived from the letting of any immovable property; and

(iv)[118] any assessed loss or balance of assessed loss allowed to be set off against income in terms of section 20;

"average repo rate"[119] in relation to a year of assessment means the average of all ruling repo rates determined by using the daily repo rates during that year of assessment;

"interest" means interest as defined in section 24J;

"issue" in relation to a debt, means the creation of a liability to pay or of a right to receive an amount in terms of that debt;

"reorganisation transaction" means—

(*a*) an intra-group transaction as defined in section 45(1) to which section 45 applies; or

(*b*) a liquidation distribution as defined in section 47(1) to which section 47 applies;

"repo rate"[120] means the interest rate at which the South African Reserve Bank enters into a repurchase agreement contemplated in section 10(1)(*j*) of the South African Reserve Bank Act.

(2) Where an amount of interest is incurred by an acquiring company in terms of a debt—

(*a*) directly or indirectly assumed or applied for the purpose of procuring, enabling, facilitating or funding the acquisition by that acquiring company of any asset in terms of a reorganisation transaction;

(*b*) used directly or indirectly for the purpose of redeeming, refinancing or settling the debt contemplated in paragraph (*a*);

(*c*) issued, assumed or used in terms of an acquisition transaction; or

(*d*) used directly or indirectly for the purpose of redeeming, refinancing or settling the debt contemplated in paragraph (*c*),

the amount of interest allowed to be deducted must not exceed the amount determined in terms of subsection (3).

(3)[121] The amount of interest allowed to be deducted in terms of all debts owed as contemplated in subsection (2), in respect of any year of assessment in which the acquisition transaction or reorganisation transaction is entered into and in respect of five years of assessment immediately following that year of assessment, must not exceed the sum of—

(*a*) the amount of interest received by or accrued to the acquiring company; and

(*b*) the highest of the amounts determined by multiplying the percentage determined under subsection (4) by the adjusted taxable income of the acquiring company for each of the years of assessment—

(i) in which the acquisition transaction or reorganisation transaction is entered into;

(ii) in which the amount of interest is incurred by that acquiring company; or

(iii) immediately prior to the year of assessment contemplated in subparagraph (i),

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[118] Pending amendment – to be deleted by section 19(1)(*b*) of Act No. 42 of 2024 with effect from 1 January 2027 and applicable in respect of years of assessment on or after that date.

[119] Pending amendment – to be deleted by section 19(1)(*c*) of Act No. 42 of 2024 with effect from 1 January 2027 and applicable in respect of years of assessment on or after that date.

[120] Pending amendment – to be deleted by section 19(1)(*d*) of Act No. 42 of 2024 with effect from 1 January 2027 and applicable in respect of years of assessment on or after that date.

[121] Pending amendment – wording to be amended by section 19(1)(*e*) of Act No. 42 of 2024 with effect from 1 January 2027 and applicable in respect of years of assessment on or after that date.

reduced by any amount of interest incurred by the acquiring company in respect of debts other than debts contemplated in subsection (2).

(4)[122] The percentage contemplated in subsection (3)(*b*) must be determined in accordance with the formula—

$$A = B \times \frac{C}{D}$$

in which formula—

(*a*) "A" represents the percentage to be determined;

(*b*) "B" represents the number 40;

(*c*) "C" represents the average repo rate plus 400 basis points; and

(*d*) "D" represents the number 10,

but not exceeding 60 per cent of the adjusted taxable income of that acquiring company.

Section 24J(1) – Definition of "interest"

"interest" includes the—

(*a*) gross amount of any interest or similar finance charges, discount or premium payable or receivable in terms of or in respect of a financial arrangement;

(*b*) amount (or portion thereof) payable by a borrower to the lender in terms of any lending arrangement as represents compensation for any amount to which the lender would, but for such lending arrangement, have been entitled; and

(*c*) absolute value of the difference between all amounts receivable and payable by a person in terms of a sale and leaseback arrangement as contemplated in section 23G throughout the full term of such arrangement, to which such person is a party,

irrespective of whether such amount is—

(i) calculated with reference to a fixed rate of interest or a variable rate of interest; or

(ii) payable or receivable as a lump sum or in unequal instalments during the term of the financial arrangement;

Section 24J(2)

(2) Where any person is the issuer in relation to an instrument during any year of assessment, such person shall for the purposes of this Act be deemed to have incurred an amount of interest during such year of assessment, which is equal to—

(*a*) the sum of all accrual amounts in relation to all accrual periods falling, whether in whole or in part, within such year of assessment in respect of such instrument; or

(*b*) an amount determined in accordance with an alternative method in relation to such year of assessment in respect of such instrument,

[122] Pending amendment – to be deleted by section 19(1)(*f*) of Act No. 42 of 2024 with effect from 1 January 2027 and applicable in respect of years of assessment on or after that date.

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which must be deducted from the income of that person derived from carrying on any trade, if that amount is incurred in the production of the income.

Section 24J(12)

(12) This section must not apply to an instrument if—

(*a*) the holder of that instrument has, throughout any period during a year of assessment during which that holder holds that instrument, a right to require the redemption of that instrument at any time during that period; and

(*b*) that instrument does not provide for the payment of any deferred interest.

Section 24O

24O. Incurral of interest in respect of certain debts deemed to be in the production of income.—(1) For the purposes of this section—

"acquisition transaction" means any transaction in terms of which a company acquires an equity share in another company from a person that does not form part of the same group of companies as that company, if—

(*a*) that other company is—

(i) an operating company on the date of acquisition of that share; and

(ii) as a result of which, at the end of the day of that transaction—

(*aa*) that company is a controlling group company in relation to that other company; and

(*bb*) that company and that other company form part of the same group of companies as defined in section 41(1); or

(*b*) that other company is—

(i) a controlling group company in relation to a company that is an operating company on the date of acquisition of that share and that forms part of the same group of companies, as defined in section 41(1), as that controlling group company; and

(ii) as a result of which, at the end of the day of that transaction—

(*aa*) that company is a controlling group company in relation to that other controlling group company; and

(*bb*) that company and that other controlling group company form part of the same group of companies as defined in section 41(1);

"operating company" means a company of which—

(*a*) at least 80 per cent of the aggregate amount received by or that accrued to that company during a year of assessment constitutes income in the hands of that company; and

(*b*) the income contemplated in paragraph (*a*) is derived—

(i) from a business carried on continuously by that company; and

(ii) in the course or furtherance of which goods or services are provided or rendered by that company for consideration.

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(2) Subject to subsection (3), where during any year of assessment any interest is incurred by a company in respect of a debt issued, assumed or used by that company—

(*a*) for the purpose of financing the acquisition by that company, in terms of an acquisition transaction, of an equity share; or

(*b*) in substitution for a debt issued, assumed or used as contemplated in paragraph (*a*),

the interest incurred by that company in respect of that debt must, to the extent to which the amount thereof relates to a period during which—

(i) that company held that equity share; and

(ii) that equity share constituted a qualifying interest in an operating company, as determined—

(*aa*) in the case of an equity share held by that company at the end of that year, at the date on which that year ends; or

(*bb*) if that equity share was disposed of by that company during that year, at the date of that disposal,

be deemed to have been so incurred in the production of the income of that company and laid out or expended by that company for the purposes of trade.

(3) An equity share in a company constitutes a qualifying interest in an operating company if that equity share is an equity share on the date referred to in subsection (2) in—

(*a*) a company that qualified as an operating company in its latest year of assessment that ended prior to or on the date referred to in subsection (2); or

(*b*) any other company, to the extent that the value of that equity share is derived from an equity share or equity shares held by that company in a company or companies described in paragraph (*a*)—

(i) in relation to which that company is a controlling group company; and

(ii) that form part, with that company, of a group of companies, as defined in section 41(1):

Provided that if at least 90 per cent of the value of that equity share is so derived, that equity share must be treated as an equity share in an operating company.

(4) ……

(5) Where a company that acquired equity shares in a controlling group company in relation to an operating company as contemplated in paragraph (*b*) of the definition of "acquisition transaction" acquires the equity shares held by that controlling group company in that operating company in terms of—

(*a*) an unbundling transaction as defined in section 46(1)(*a*) in respect of which section 46 was applied; or

(*b*) a liquidation distribution as defined in section 47(1)(*a*) in respect of which section 47 was applied,

those equity shares must for purposes of subsection (2) be treated—

(i) as having been acquired by that company in terms of paragraph (*a*) of the definition of "acquisition transaction"; and

(ii) as constituting a qualifying interest in an operating company to the extent to which the value of the equity shares in the controlling group company from which the equity shares in the operating company were acquired was derived from the value of the equity shares in the operating company so acquired.

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Section 31(1) and (2)

31. Tax payable in respect of international transactions to be based on arm's length principle.—(1) For the purposes of this section—

"affected transaction" means any transaction, operation, scheme, agreement or understanding where—

(*a*) that transaction, operation, scheme, agreement or understanding has been directly or indirectly entered into or effected between or for the benefit of either or both—

(i) (*aa*) a person that is a resident; and

(*bb*) any other person that is not a resident;

(ii) (*aa*) a person that is not a resident; and

(*bb*) any other person that is not a resident that has a permanent establishment in the Republic to which the transaction, operation, scheme, agreement or understanding relates;

(iii) (*aa*) a person that is a resident; and

(*bb*) any other person that is a resident that has a permanent establishment outside the Republic to which the transaction, operation, scheme, agreement or understanding relates; or

(iv) (*aa*) a person that is not a resident; and

(*bb*) any other person that is a controlled foreign company in relation to any resident,

and those persons are connected persons or associated enterprises in relation to one another; and

(*b*) any term or condition of that transaction, operation, scheme, agreement or understanding is different from any term or condition that would have existed had those persons been independent persons dealing at arm's length;

"associated enterprise" means an associated enterprise as contemplated in Article 9 of the Model Tax Convention on Income and on Capital of the Organisation for Economic Co-operation and Development;"

"financial assistance" includes any—

(*a*) debt; or

(*b*) security or guarantee.

(2) Where—

(*a*) any transaction, operation, scheme, agreement or understanding constitutes an affected transaction; and

(*b*) any term or condition of that transaction, operation, scheme, agreement or understanding—

(i) is a term or condition contemplated in paragraph (*b*) of the definition of "affected transaction"; and

(ii) results or will result in any tax benefit being derived by a person that is a party to that transaction, operation, scheme, agreement or understanding or by any resident in relation to a controlled foreign company contemplated in subparagraph (iv) of the definition of "affected transaction",

the taxable income or tax payable by any person contemplated in paragraph (*b*)(ii) that derives a tax benefit contemplated in that paragraph must be calculated as if that transaction, operation, scheme, agreement or understanding had been entered into on the terms and conditions that would have existed had those persons been independent persons dealing at arm's length.

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Section 41(1) – Definition of "group of companies"

"group of companies" means a group of companies as defined in section 1: Provided that for the purposes of this definition—

(i) any company that would, but for the provisions of this definition, form part of a group of companies shall not form part of that group of companies if—

(*aa*) that company is a company contemplated in paragraph (*c*), (*d*) or (*e*) of the definition of "company";

(*bb*) that company is a non-profit company as defined in section 1 of the Companies Act;

(*cc*) any amount constituting gross income of whatever nature would be exempt from tax in terms of section 10 were it to be received by or to accrue to that company;

(*dd*) that company is a public benefit organisation or recreational club that has been approved by the Commissioner in terms of section 30 or 30A;

(*ee*) that company is a company contemplated in paragraph (*b*) of the definition of "company", unless that company has its place of effective management in the Republic; or

(*ff*) that company has its place of effective management outside the Republic; and

(ii) any share that would, but for the provisions of this definition, be an equity share shall be deemed not to be an equity share if—

(*aa*) that share is held as trading stock; or

(*bb*) any person is under a contractual obligation to sell or purchase that share, or has an option to sell or purchase that share unless that obligation or option provides for the sale or purchase of that share at its market value at the time of that sale or purchase;

Section 45(1) – Definition of "intra-group transaction"

"intra-group transaction" means any transaction—

(*a*) (i) in terms of which any asset is disposed of by one company (hereinafter referred to as the "transferor company") to another company that is a resident (hereinafter referred to as the "transferee company") and both companies form part of the same group of companies as at the end of the day of that transaction; and

(ii) as a result of which that transferee company acquires that asset from that transferor company—

(*aa*) as a capital asset, where that transferor company holds it as a capital asset; or

(*bb*) as trading stock, where that transferor company holds it as trading stock; or

(*b*) (i) in terms of which any asset that constitutes an equity share held by a transferor company as a capital asset in a foreign company is disposed of by that transferor company to a transferee company in exchange for the issue of debt or shares other than equity shares by that transferee company;

(ii) as a result of which that transferee company acquires that asset from that transferor company as a capital asset; and

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(iii) if, immediately before and as at the end of the day of that transaction—

(*aa*) that transferor company and that transferee company form part of the same group of companies (as defined in section 1);

(*bb*) that transferor company is a resident or is a controlled foreign company in relation to one or more residents that form part of that group of companies; and

(*cc*) that transferee company is a resident or is a controlled foreign company in relation to one or more residents that form part of that group of companies.

Section 46(1)(*a*) – Definition of "unbundling transaction"

46. Unbundling transactions.—(1) For the purposes of this section, **"unbundling transaction"** means any transaction—

(*a*) (i) in terms of which the equity shares in a company (hereinafter referred to as the "unbundled company"), which is a resident that are held by a company (hereinafter referred to as the "unbundling company"), which is a resident, are all distributed by that unbundling company to any shareholder of that unbundling company in accordance with the effective interest of the shareholders in the shares of that unbundling company, and if—

(*aa*) all of the equity shares of the unbundled company are listed shares or will become listed shares within 12 months after that distribution;

(*bb*) that shareholder to which that distribution is made by that unbundling company forms part of the same group of companies as that unbundling company; or

(*cc*) that distribution is made pursuant to an order in terms of the Competition Act, 1998 (Act No. 89 of 1998), made by the Competition Tribunal or the Competition Appeal Court; and

(ii) if the equity shares distributed as contemplated in subparagraph (i) constitute—

(*aa*) where that unbundled company is a listed company immediately before that distribution—

(A) and no shareholder of the unbundled company other than the unbundling company holds the same number of equity shares as or more equity shares than the unbundling company of that unbundled company, more than 25 per cent of the equity shares of the unbundled company; or

(B) and any shareholder of the unbundled company other than the unbundling company holds the same number of equity shares as or more equity shares than the unbundling company of that unbundled company, at least 35 per cent of the equity shares of that unbundled company; or

(*bb*) where that unbundled company is an unlisted company immediately before that distribution, more than 50 per cent of the equity shares of that unbundled company; or

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Section 47(1) – Definition of "liquidation distribution"

(1) For the purposes of this section **"liquidation distribution"** means any transaction—

(*a*) in terms of which any company (hereinafter referred to as the "liquidating company") which is a resident disposes of all of its assets (other than assets it elects to use to settle any debts incurred by it in the ordinary course of its trade) to its shareholders in anticipation of or in the course of the liquidation, winding up or deregistration of that company and other than assets required to satisfy any reasonably anticipated liabilities to any sphere of government of any country and costs of administration relating to the liquidation or winding up, but only to the extent to which those assets are so disposed of to another company (hereinafter referred to as the "holding company") which is a resident and which on the date of that disposal forms part of the same group of companies as the liquidating company; or

(*b*) in terms of which a liquidating company which is a controlled foreign company in relation to any resident disposes of all of its assets (other than assets it elects to use to settle any debts incurred by it in the ordinary course of its trade) to its shareholders in anticipation of or in the course of the liquidation, winding up or deregistration of that company—

(i) to the extent that those assets are so disposed of to a holding company which—

(*aa*) is a resident and which forms part of the same group of companies (as defined in section 1) as the liquidating company immediately before that distribution; or

(*bb*) is a controlled foreign company in relation to any resident;

(ii) if, immediately before that transaction, each of the shares held by the holding company in the liquidating company is held as a capital asset; and

(iii) if, immediately after that transaction, where that holding company is a controlled foreign company as contemplated in subparagraph (i)(*bb*), more than 50 per cent of the equity shares in the holding company are directly or indirectly held by a resident (whether alone or together with any other resident that forms part of the same group of companies as that resident).

Section 50B(1)(*a*)

50B. Levy of withholding tax on interest.—(1)(*a*) There must be levied for the benefit of the National Revenue Fund a tax, to be known as the withholding tax on interest, calculated—

(i) at the rate of 15 per cent; or

(ii) at such rate as the Minister may announce in the national annual budget contemplated in section 27(1) of the Public Finance Management Act, with effect from a date mentioned in that Announcement,

of the amount of any interest that is paid by any person to or for the benefit of any foreign person to the extent that the amount is regarded as having been received or accrued from a source within the Republic in terms of section 9(2)(*b*).

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Section 50D(3)

(3) A foreign person is exempt from the withholding tax on interest if—

(*a*) that foreign person is a natural person who was physically present in the Republic for a period exceeding 183 days in aggregate during the twelve-month period preceding the date on which the interest is paid; or

(*b*) the debt claim in respect of which that interest is paid is effectively connected with a permanent establishment of that foreign person in the Republic if that foreign person is registered as a taxpayer in terms of Chapter 3 of the Tax Administration Act.

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