



*SOUTH AFRICAN REVENUE SERVICE*

**BINDING PRIVATE RULING: BPR 063**

Some guidance contained in this ruling is affected by new legislation.

DATE: 24 November 2009

**ACT : INCOME TAX ACT, NO. 58 OF 1962 (the Act)**  
**SECTIONS : SECTIONS 11(a), 24J AND 23(f) AND (g)**  
**SUBJECT : INTEREST INCURRED ON LOANS OBTAINED TO ACQUIRE THE SHARES OF A COMPANY AS OPPOSED TO ACQUIRING THE BUSINESS OF THE COMPANY**

**1. Summary**

This ruling deals with the deductibility of interest payable on a loan to be obtained by a company in order to acquire the entire issued share capital of another company, where such share capital is to be acquired with the intention of acquiring the business of that other company.

**2. Relevant tax laws**

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

In this ruling legislative references to sections are to sections of the Act applicable as at 1 April 2008 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This ruling has been requested under the provisions of –

- section 11(a);
- section 24J; and
- section 23(f) and (g)

**3. Parties to the proposed transaction**

The Applicant: A newly formed company

The Target company: The company whose share capital is to be acquired by the Applicant

**4. Description of the proposed transaction**

The Applicant is a new, purpose-formed company which has been constituted to acquire and hold the entire shareholding in the Target

company. The Applicant's issued share capital is of a nominal amount and the shares were issued at par.

The Applicant will acquire all the shares in the Target company. The purchase price for the shares will mainly be funded by external loans which will be raised by the Applicant from a bank with the balance being funded by loans from the shareholders of the Applicant.

The bank loans will be secured, with predetermined interest rates and maturity dates.

The loans, which will be owing to the shareholders of the Applicant, will be unsecured, subordinated to the senior bank loans, and will bear interest at rates of prime and prime plus 2%. These loans will be repayable (subject to the subordination) at the instance of the Applicant, essentially out of excess cash available and at the instance of the shareholders if there is any specified event of default.

Subsequent to the Sale of Shares agreement being implemented between the Applicant and the shareholders of the Target company, it is proposed that the Target company will immediately distribute all its assets held by it and claims against it to the Applicant in specie, on the basis that the Applicant will assume all liabilities and other obligations of the Target company, such distribution being of the type, and in the manner, contemplated in section 47.

Thereafter the Target company will be liquidated or deregistered, as the parties may decide.

## **5. Conditions and assumptions**

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

- the proposed transaction is not part of or connected to any other transaction, operation or scheme, other than as set out herein;
- the necessary steps to liquidate, wind up or deregister the Target company as envisaged in section 47 will take place within a period of eighteen (18) months after the business of the Target company has been transferred to the Applicant;
- the purchase price of the shares in the Target company represents the market value of the shares and claims purchased. If the price is overstated, the interest in relation to the inflated price will be regarded as excessive expenditure and will not be deductible for income tax purposes; and
- this ruling does not address the interest rate on the shareholders loans to purchase the shares in the Target company and no ruling is given as to whether the interest rate is excessive or not.

## **6. Ruling**

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

- The interest to be incurred on the bank and shareholder loans will be regarded as expenditure incurred in the production of income and will not be expenditure of a capital nature. The provisions of section 23(f) and (g) will not be applicable.
- The interest incurred in terms of –
  - the bank loans will be deductible under the provisions of section 24J; and
  - the loans owing to the shareholders will be deductible under the provisions of section 11(a).

Based on the facts as set out herein, and on the basis that the Applicant and the Target company duly so elect, the provisions of section 47 will be applicable to the distribution of the assets in specie by the Target company to the Applicant.

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

This binding private ruling is valid as from the date of this ruling and will remain so for the duration of the bank loans obtained in respect of the proposed transaction.

Issued by:

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