Cross issue of shares

DLA Cliffe Dekker HofmeyrAndrew LewisSouth Africa

Section 24B of the Act was initially introduced to deal with the acquisition of assets through the issue of shares. Pursuant to the judgment of ***CIR v Labat Africa Limited 72 SATC 75*** a company would ordinarily not incur expenditure in connection with the issue of its own shares and thus the need for s24B. Section 24B of the Income Tax Act was recently amended to only deal with the issue of shares in exchange to the issue of shares (ie the cross-issue of shares), being an "anti-avoidance" provision.

Section 24B(2) of the Income Tax Act provides that if a company acquires shares that are issued to that company "*directly or indirectly in exchange for shares issued by that company*", that company incurs no expenditure for the acquisition of the shares issued to it. As a result, the subsequent disposal of the shares by the company may trigger a significant tax liability (ie the tax liability being determined with no tax base).

Treasury have recognised that this anti-avoidance rule is impractical in South Africa, because cross-issues are a common feature of many commercially driven share schemes (especially involving black economic empowerment (BEE) parties). For instance, many BEE transactions were implemented on the basis that the empowerment company (BEE CO) would issue preference shares in the empowered company (OPCO) and use the subscription price thereof to subscribe for ordinary shares in OPCO. Section 24B(2) of the Income Tax Act had the effect that the shares in OPCO would have no base cost, triggering significant adverse tax implications for BEE CO on the disposal thereof.

It will be a welcome relief to taxpayers and advisers alike

that the proposal by National Treasury is for these anti-avoidance rules to be reworked. The zero base cost rule will either be eliminated or narrowed. In addition, cross-issues (and share-for-share-transactions) acting as a mechanism to indirectly shift value into tax exempt hands will trigger immediate taxation.