Tax Alert

Taxation Laws Amendment Act, 2023: Amendments to provisions dealing with preference shares

In brief

An important change to the income tax provisions dealing with preference share dividends has been implemented. Companies that have not yet considered the potential impact of this change on preference dividends received for years of assessments commencing on or after 1 January 2024 still have some time to do so.

In detail

A recent amendment of section 8EA of Income Tax Act No. 58 of 1962 will affect any dividend, including foreign dividends, received or accrued during years of assessment commencing on or after 1 January 2024.

Section 8EA is an anti-avoidance rule which deems dividend yields on third-party-backed shares to be income, unless the funds derived from the issue of the third-party-backed shares are used for a qualifying purpose (as defined).

Such dividends may now only be exempted – and therefore excluded from income – if, at the time of the receipt or accrual thereof, the person that acquired the relevant equity shares in the targeted operating company meets an ownership requirement. That means, the person must hold the equity shares in the operating company, whether directly or indirectly.

Tax consequences will therefore now arise on a dividend declared by the issuer of a preference share, which was issued for the specified qualifying purpose, after the shares in an operating company financed by the preference share funding were disposed of, unless certain requirements are met.

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Let's talk

For a deeper discussion on how this issue might affect your business, please contact:

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It is clear from this amendment that ownership of the equity shares in the operating company underpins the qualifying purpose exemption in section 8EA.

The exemption in terms of section 8EA will, however, still apply in both of the situations described below.

- The equity shares in the targeted operating company were disposed of, and the funds derived from that disposal are used by the issuer of the preference share within 90 days of that disposal for the redemption of that preference share.

- The equity shares in the operating company were listed shares that were substituted for different listed shares in terms of an arrangement that was announced and released as a corporate action as contemplated in
    - the JSE Limited Listing Requirements in the SENS (Stock Exchange News Service) (as defined in the JSE Limited Listing Requirements); or
    - the listings requirements of any other exchange licensed under the Financial Markets Act, which listings requirements are substantially the same as the requirements prescribed by the JSE Limited Listing Requirements, where that corporate action complies with the applicable requirement of that exchange.

Takeaway

Those companies with a substantial preference share book should especially be mindful of this amendment.

Companies receiving preference dividends should consider the impact of the amendments and implement processes in relation to shares that meet the qualifying purpose test to ensure they are still held directly or indirectly by that person at the time of the receipt or accrual of that dividend, or that the relevant exceptions to this rule apply.

This may necessitate a review of all preference share funding arrangements where the qualifying purpose exemption has been relied upon.