

# SELLING property holding entities?

Christine du Toit of CAP Chartered Accountants



The introduction of section 9C into the Income Tax Act, effective since 1 October 2007, was smooth and silent. However, there have been repercussions for transactions in which properties change hands by a mere selling of shares in a property entity. One just has to plan accordingly.

Unaware of the changes in the Income Tax Act, a certain Mr Gold decided to purchase a property. He had a dormant company of which he was the registered shareholder for five years. Mr Gold approached a financial institution, which granted him a loan provided that he stood surety for the debt. He purchased property and six months later was approached by a potential buyer. Mr Gold decided to sell but structured the transaction so that he only transferred his shares to the buyer. Being under the impression that he had been the shareholder for more than five years, he wanted to elect the proceeds of the sale of shares to be capital in nature.

As this transaction happened after 1 October 2007, the rules of the game had changed. Section 9B, which had the 'safe harbour' rule of five years, had been replaced by section 9C. This section now governs all 'qualifying shares'. A qualifying share can be one of the following: shares in a company listed on the JSE; shares in a private company; members' interest in a closed corporation; as well as collective investment schemes in securities.

What, then, is excluded? Shares in a share block company, shares in an unlisted foreign company and section 8E hybrid equity instruments are not included. Where a 'qualifying' share is disposed of after a three-year period of ownership, it will be deemed capital in nature. It does not matter if you are making a gain or loss, it will be a capital gain or loss.

Some may think, "Great! If we set up a company and buy a property, we can dispose of the shares after three years and only pay capital gains tax on the profit."

If only it were that easy. Section 9C has an anti-avoidance provision in subsection 3, particularly with regard to shares in property-holding companies. This provision prevents the three-year capital rule from applying where shareholders have a meaningful level of shares and are able to influence the decision of the company that acquired the property. Meaningful levels of shares could be as little as twenty per cent of shareholding.

Where you have a shareholding of twenty per cent or more, and more than fifty per cent of the total value of the company shares can be directly or indirectly linked to the value of immovable property acquired within three years of selling your shares, the sale will not (by default) be deemed as capital. This also applies to any other asset that the company



acquired within the last three years before selling the shares, where the asset has been encumbered by a lease or license and the payments have been received by someone other than the company.

Therefore, what happens when Mr Gold has sold his shares that he held for five years, but the property was only acquired

six months ago? It will not, by default, be deemed capital as the property had not been acquired at least three years prior. Mr Gold will have to prove what his intention was with the property so the tax authorities can determine if it was a speculative transaction subject to income tax, or part of his capital assets and subject to capital gains tax.

	<p><b>Our Services Include:</b></p> <ul style="list-style-type: none"> <li>• Financial management</li> <li>• Accounting &amp; payroll</li> <li>• Trust formation</li> <li>• Company formation</li> <li>• Taxation</li> <li>• Auditing</li> </ul>	
	<p>Continuity and Communication where it really matters</p>	
<p>CAP Chartered Accountants Tel: (021) 914-7738 Fax: (021) 914-7789 www.chartered.co.za cap@chartered.co.za</p>		