

Beware the interest free shareholder loan



By [Graeme Palmer](#)

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Companies often lend funds to their shareholders, for a variety of reasons, and are often referred to as debit loans. However, if a loan is made to a shareholder at a low interest rate or interest free, it may trigger dividends tax.



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Dividends tax applies at a rate of 15% on dividends paid on or after 1 April 2012. However, it is not only a cash dividend or the distribution of assets in specie that triggers the tax, there are provisions in the Income Tax Act that deem certain low interest or interest free debit loans to be dividends.

Section 64E(4) of the Act applies where any amount is owing to a company, by virtue of any share held in that company, by a person that is:

- not a company;
- a resident; and
- either a connected person to the company or a connected person to that person

If all of these elements are present, the company is deemed to have paid a dividend in specie.

The dividend amount will be equal to the greater of the market related interest in respect of the debt, less the amount of interest payable to the company in respect of the debt for that year of assessment, or nil. Therefore, the dividend is determined by applying an interest rate to the debit balance on the loan account during the year. The interest rate that is

used is the difference between the 'market-related interest' (ie the 'official interest', as defined in the 7th Schedule of the Act, currently 7.75%) and the actual interest rate charged on the loan.

The dividend will be deemed to have been paid on the last day of the year of assessment. As the dividend is deemed to consist of a distribution of an asset in specie, it is the company, and not the shareholder that becomes liable for dividends tax under section 64EA(b).

For example, Company ABC (Pty) Ltd advances a loan of R1 million on 1 March 2016 to shareholder X at an interest rate of 4%. In year one the amount of the dividend deemed to have been paid will be R37,500 [R1 million x 3.75% (7.75% - 4%)]. The dividends tax payable in year one by ABC (Pty) Ltd will be R5 625 (R37,500 x 15%).

ABOUT GRAEME PALMER

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