The stock exchange products

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Introduction

The Tunisian financial market now offers investors a wide range of stock exchange products, each responding to different objectives depending on the level of risk, performance or desired liquidity.

This diversity, combined with the tax benefits for some of these products tends to popularize the stock investment. This offers real opportunities for small investors and large private or institutional investors.

This document lists the stock products in Tunis and their different characteristics.

In addition to this brochure, the Tunis Stock Exchange also offers the "Investor's Guide" that presents the terms of access to the stock exchange.

I-Equity security

A-Different types of equity securities

There are three types

Ordinary shares:

- Ordinary shares
- preference non-voting share
- Investment certificate

1. Ordinary shares

Shares are title deeds of a company. Each share represents a fraction of the capital of that company.

The ownership of shares gives the right to their holder with the concerned company; the status of co-owner of the company. This right is exercised in proportion to the number of shares held.

These rights are threefold

a. **The right to information and management**: owning shares in a company gives the holder the status of partner. As such, any holder of ordinary shares of a company has a right to information and a right to vote at general assemblies. This right to vote allows the partner to express a management choice.

b. **Right to profits**: share ownership gives the right to the profits of the company in proportion to the share of capital detained. This is the right to the dividend. It varies from one year to another, arising directly from the annual profits of the company and is distributed at the end of each financial year.

c**. Right to net assets**: this right comes in case of the company's liquidation. In this situation, the assets available after payment of all debts of the company are called net assets. These net assets are distributed to shareholders in proportion to the share of capital held by each of them.

2. Preference non-voting share

Companies have the option, under certain conditions, to issue or create Preference non-voting shares. They can do this in case of a capital increase or in case of a conversion of existing ordinary shares.

Preference non-voting shares are shares without voting rights. The dividend payment is made thereon in priority to ordinary shares.

Preference non-voting shares therefore give the holder less important rights. However they are better paid: in other words, by giving up his right to vote, the preferred share holder benefits in return from a preferred dividend.

The dividend may not be lower than a level fixed at the issuance or creation of preference non-voting shares. Likewise, the dividend may not be lower than the first dividend as provided by the statutes of the company.

If the dividend cannot be paid fully due to insufficient distributable profits, the balance on the minimum level set previously is postponed to subsequent years. In the event that this situation continues for more than three years, the right to vote is reinstated and the preference non-voting share becomes an ordinary share.

However, if the distributable profits give the dividend a higher value than previously defined, it will be stored at the higher level and will be equivalent to the ordinary share dividend.

It should be noted that the preference non-voting shares cannot represent more than one third of the company's capital.

3. Investment certificate IC:

The investment certificates or IC results from a split of the ordinary share into two separate share warrants.

a. The investment certificate which includes all financial rights associated with the ordinary share includes the right to dividends. A preferred dividend may also be granted.

b. The certificate of voting right which represents the other rights attached to the ordinary share.

In other words, the certificate of investment is a non-voting share which allows the listed company to collect capital without modifying the shareholding. The issue of the certificate of investment is limited to one third of the company's capital.

B. return on equities

Whatever type of the capital held, either ordinary share, preferred share or Investment certificate, the shareholder is associated with the business results whether positive or negative. The market value of securities held in this sense is directly related to the company's profit perspectives.

The return on equities has two components

- The dividends
- Capital gain
- The capital gain and its opposite, the depreciation, occurring only during the resale of the equity.

1**. The dividend**

The dividend is the shareholder remuneration.

Specifically, at the end of each year, upon the proposal of the Board of Directors, the General Assembly decides whether or not to distribute to shareholders all or a portion of the profit. The amount to be distributed that is retained is divided by the number of shares in the company's capital: it is this product per share that we call dividend.

The distribution of dividend is made by paying the shareholder a sum of money in proportion to the number of shares held.

2. Capital gain and depreciation

The capital gain results from the profit realized between the purchase and the sale of shares. In other words, the capital gain is equal to the difference between the sale price of a share and its purchase price.

If this difference is negative, that is if the sale price is lower than the purchase price, we then speak about depreciation.

3. Taxation:

A) **The tax system on dividends:** Profits or income distributed from January 1, 2015 by resident companies in Tunisia are subject to a full withholding tax at the rate of 5% when distributed to resident and non-resident individuals in Tunisia and legal entities.

The withholding tax is deductible from the tax on annual income. It can be refundable in case the distributed income does not exceed 10,000 dinars annually.

b)Taxation of capital gains on the transfer of listed shares

The capital gain of listed shares acquired or subscribed from 1 January 2011 and sold before the end of the year following that of their acquisition or subscription is subject to tax:

- for individuals, at a 10 % rate, after deduction of the depreciation recorded during the same year and 10 000-dinar tax allowance of remainder.
- for the resident legal entities, as part of the overall profit by taking into account the depreciation

• for non-resident individuals not established in Tunisia, and subject to the exemptions provided by the double taxation agreements between Tunisia and the country of residence of sellers, by a discharge withholding tax of 10 % and with a maximum of 2,5% determined on the basis of the sale price.

Non-resident legal entities that are not established in Tunisia are subject to a withholding tax rate of 30% with a 5% ceiling calculated on the basis of the sale price.

The nonresidents can opt for a tax return to benefit from the deduction of the depreciations recorded during the same year. While individuals can opt for a 10 000-dinar allowance; following the example of the residents.

However capital gains are exempt from:

• The transfer of shares listed on Tunis Stock Exchange, acquired or subscribed:

-before 1 January 2011

-from 1 January 2011 and sold after the end of the year following that of their acquisition or subscription

• The contribution of shares and partnership shares with a capital of the parent company or of the holding company which makes a commitment to list its shares to Tunis stock exchange no later than the end of the year following that of the deduction.

• The transfer of share of unit trust and mutual funds independent of a professional asset.

• The transfer of shares of seed funds and venture capital funds subject to the terms and conditions of their assets.

Finally, it should be noted that a tax benefit is granted in the form of a 35% to 100% tax allowance on profits or taxable reserves that are reinvested in capital subscription of firms operating in certain sectors namely:

• Companies whose activity is governed by the investment incentives code

• Venture capital companies or venture capital funds placed within them, venture capital funds and seed funds.

Companies located in regional development zones or in free economic zones.

C) The tax system on depreciations

Weather the company is listed or not, the capital loss is deductible from the tax base. In addition, provisions for impairment of listed shares are deductible from corporate income tax, and in the limit of 50% of taxable income.

II. Debt securities

1. Bonds and Treasury bonds

In case of funding requirements, the stock market acts as an alternative to bank loans for private or public companies.

In this case, the company issues debt securities called bonds. The medium and long term obligations issued by the state, which can also be used in the stock exchange to raise funds, are called Treasury bonds.

Each bond represents a fraction of a loan issued by the company on the stock market. The holder of the bond becomes the company's creditor.

The bondholder runs a lower risk than the shareholder because the bond insures guarantees of remuneration and refund.

However, the bondholder does not enjoy the same rights as the shareholder: he/she does not benefit neither from the right on profits, the right of management or voting rights.

Bonds are paid according to an interest rate on the face value. This rate is set by contract upon issuance of the debt.

The interest rate can take two forms:

- The fixed interest rate remains constant throughout the duration of the loan
- The variable interest rate fluctuates based on a reference rate

The repayment of the bonds is made according to the conditions set by the contract: it can take many forms:

- Depreciation in annual installments
- A block refund from the main term to final term; it is a refund *in fine*. The bondholder thus receives interest at predetermined dates.
- A one-time refund at the final deadline including the capital lent and the bonds interests also called zero coupon bonds.

The bonds may be issued for a minimum period of 5 years, reduced to 2 years for Treasury Bonds.

2. Taxation

Interests are subject to tax as income from movable capital.

This tax system takes the form of a withholding tax.

- For legal entities, the withholding tax is 20 % on the corporate tax. However, this withholding tax is in full discharge for the legal entities exempted from the corporate tax such as unit trust.

- For individuals, the withholding tax is also 20 %. Nevertheless, interest on bonds is with other forms of savings, deductible from the income tax base within the annual limits of 1500-dinars.

III. Hybrid securities

Companies can also issue the so-called hybrid securities because they borrow some of their characteristics from bonds and other characteristics from shares.

Thus, hybrid securities combine both the benefits related to bonds and the potential gains of shares

1. Equity shares

Equity shares issued by companies are refundable after 7 years.

- The remuneration for the equity shares, counts a fixed part and a variable part according to a reference which can be the profit or the turnover of the company. This remuneration is fixed by the issuance contract.

- taxation: the remuneration of equity shares is subject to a withholding tax of 20%:
  - Attributable to income for individuals.
  - Attributable to the corporate tax for legal entities.
  - In full discharge for companies exempt from tax (unit trust).

2. The convertible bonds

These are bonds that can be converted to shares created by the issuing company at the time of the exchange.

The convertible bonds offer several advantages:

- The bearer, who is a creditor of the issuing company, benefits from a comfortable position: he enjoys a period of observation of the company before making the decision to become a shareholder and keeps the possibility of a conversion. Furthermore, he shall be guaranteed an immediate risk-free investment which performance will be improved upon conversion, as well as a favorable evolution of the issuing company.

- The issuing company benefits as well of a cash inflow in the form of loan which it will not need to pay off in case of conversion. This operation allows the company to benefit from a capital increase postponed to the due date.

IV. The securities of The Undertakings for Collective Investment in Transferable Securities, or UCITS

The Undertakings for Collective Investments in Transferable Securities, UCITS are structures that are designed to manage within securities portfolios, financial products on behalf of investors who do not wish to invest individually and directly in the stock exchange, but want to enjoy diversification and expertise of professional managers.

The main types of UCITS are open-ended investment companies or UNIT TRUST and mutual funds.

The difference between UNIT TRUST and mutual fund is essentially legal. The mutual fund has no legal personality, contrary to the UNIT TRUST. Nevertheless, for the investor, this difference is not noticeable and has no tangible consequences.

1. The shares of the unit trust

A unit trust's role is to manage a portfolio of securities. Its capital, divided into equal shares named 'unit trust shares' which represents the market value of the portfolio. Therefore, the value of the unit trust shares varies according to the evolution of the market and structure of the portfolio.

The unit trust, manager is generally a professional of the market: broker, bank or a specialized management company authorized by the Financial Market Council (CMF).

The assets of the Unit trust must be deposited in a depositary (bank), in charge of controlling the regularity of its operations.

The Unit trust, its manager, its auditor and the depositary bank are subject to the supervision and control of the Financial Market Council (CMF).

In Tunisia, the Unit trust shares are not traded in the stock exchange. They are bought through "subscription" and then resold ".This is called "repurchase" directly by the manager from banking agencies and brokers.

The value of unit trust shares, called "net asset value" is fixed periodically. It corresponds to the market value of the securities which make up the securities portfolio, divided by the number of outstanding shares.

The Unit trust must repurchase the shares of its shareholders whenever they want based on their net asset value.

The Unit trust is able to meet this obligation through the liquidity of the securities in its portfolio. This liquidity is assured by the fact that the unit trust may only hold listed securities or securities that were the subject of a public offering.

In Tunisia, there are two types of Unit trusts:

- Bond market funds: their security portfolio consists primarily of debt securities.
- Mixed Unit trust: their security portfolio consists of equity securities and debt securities. This type of Unit trust is therefore more risky: the return on listed shares may vary.

Finally, a Unit trust may be a distribution unit trust or capitalization unit trust.

- A distribution Unit trust is required to distribute all its profits under the same conditions as limited companies

- A capitalization unit trust does not distribute its profits.

2. Tax system of unit trusts

Unit trusts benefit from an advantageous tax regime in many respects:

a.The capital gains on the transfer of elements of their portfolio are exempt of taxes.

b. Products resulting from interests are subject to a full discharge rate of 20 %.

c. profits are exempt from corporate income tax.

d. dividends distributed to shareholders are exempt from corporate income tax for legal entities and income tax for individuals.

e. Capital gains from the sale of unit trust shares are exempt from tax:

o for individuals, it is a total tax exemption on income,

o for companies, capital gains are exempt from corporate income tax to the extent of the difference between the subscription price and the average net asset value of the month of December preceding the repurchase.

An equivalent plan is applicable to subscriptions as part of a professional asset of an individual.

3. Mutual funds and their tax system

The mutual fund has no legal entity. This is its main difference from the Unit trust. Similarly to unit trust, its management is entrusted to a professional and its assets to a depositary.

Just like the unit trust, the mutual Fund is subject to the supervision and control of the financial market council according to the same terms.

For tax purposes, the Mutual Fund and its unit holders receive the same benefits.

V. Share savings plan

The share savings plan is a formula of medium and long-term savings. Its advantageous tax regime makes it a very attractive financial product.

1. Elements of definition:

The share savings plan is an account where the holder deposits money. These deposits are used for the acquisition of shares of listed companies on the stock exchange, Treasury bonds or UCITS (undertaking for collective investment in transferable securities).

The deposits are allocated to listed equity securities in the limit of at least 80%; the balance is allocated to the acquisition of Treasury bond. They can also be used to acquire units of UCITS complying with the same rules of allocation.

A share savings plan can be opened with a bank or broker by an employee, a person with a commercial or non-commercial activity or a pensioner of social security funds.

It can be managed directly by its owner who decides himself the operations of purchase and sale of securities. Its management can also be entrusted to a bank or a broker. An agreement between the designated professional and a share savings plan holder will specify the management policy to be followed.

2. Taxation

The holder of a share savings plan can deduct his deposits of the income tax base within the annual limit of 50 000-dinars and a maximum of 40% of tax reduction due before deduction.

The profit of the tax benefit is subject to two conditions:

- The presentation of a certificate of deposit issued by the institution in which the share saving plan has been opened,

- Blocking sums deposited for a period of 5 years from January 1st of the year following the year of filing.

The blocking of deposits does not mean the blocking of securities. Their sale remains free. The holder must nevertheless reuse the starting amount in the acquisition of other securities.

The capital gains, dividends and interest received may in turn be withdrawn at any time.

The withdrawal of deposits before the end of the 5 year period entails the payment of the tax due and unpaid, plus penalties. However, the penalties do not take place when the withdrawal of funds deposited are made after the expiry of the third year following the year of filing or when the withdrawal comes after unpredictable events (illness, accident with personal injury, work stoppage, death of the account holder ...)

Finally, it should be noted that the death of the account holder does not involve the loss of the account of the benefits granted. The heirs retain the tax benefits subject to compliance with the blocking conditions for the remaining period.