Ref#: 426242
Submission File

25 March 2013

South African Revenue Service
Private Bag X923
PRETORIA
0001

BY E-MAIL: policycomments@sars.gov.za

SUBMISSION: COMMENTS ON THE DRAFT INTERPRETATION NOTE:
DEDUCTION OF EXPENDITURE INCURRED ON REPAIRS

Dear Sir/Madam

The South African Revenue Service’s draft interpretation note on the deduction of expenditure incurred on repairs issued in February 2013 refers. Please find SAICA’s response to the request for comments on the draft interpretation note.

General comment

The draft interpretation note, once issued, will be an “official publication” (as defined in section 1 of the Tax Administration Act) and will therefore create “practice generally prevailing” – section 5. It will therefore be relevant when section 99 of the same Act (the “period of limitations for issuance of assessments”) or section 99 of the same Act (“objection against assessment or decision”) apply. Our comments will take this fact into account.

Our comments are presented in the order of and under the headings used in the note. When reference is made to the draft interpretation note itself the abbreviation “draft IN” will be used. Our comments are presented in the order of the rules.
Point 1 – Purpose

The draft IN states the purpose of the note is to provide “guidance on the interpretation and application of section 11(d) which allows a deduction for expenditure incurred on repairs for the purposes of trade.”

It is suggested that the words “for the purposes of trade” be deleted from the sentence.

Point 2 – Background

The discussion about the capital nature of expenditure on repairs is inappropriate. Section 11(d) does not contain any reference to the capital nature or not of the expenditure incurred. The reference to section 11(a) is also not appropriate as section 23B would apply and a deduction in respect of “expenditure incurred on repairs” cannot be made in terms of section 11(a).

We agree that Judge Joubert (in the Flemming case) indicated that the difference between “a repair” and “an improvement” is relevant when section 11(d) is considered. The judge confirmed that our courts have not provided guidelines to assist in this determination. It may be appropriate for SARS to provide some guidance on when they will consider that it will in fact be an improvement. The guidance provided by judge Joubert was that distinction must be made by taking in the ordinary grammatical meaning of the word “repair” and by applying that to the facts of the case. In essence one can say that if it is a repair it will not be an improvement. Judge Joubert held that the expenditure incurred by Mrs Flemming was to improve the water supply and as such it was not a repair (the exact words used are: “Sy het dit bestee vir die verbetering van watervoorsiening wat niks met "repairs of property" te doen het nie en derhalwe volkome irrelevant vir doeleindes van art 11 (d) is.”
The above comments are also relevant to the discussion in paragraph 4.1.5 of the draft IN (the Distinction between repairs and improvements).

Point 4 – Application of the law

The following sentence “No deduction for expenditure incurred on repairs will be permissible if the expenditure is recoverable” is based on section 23(c). Our comment relates to the use of the words “no deduction.” Section 23(c) qualifies the word recoverable by stating that the prohibition would apply to any “any loss or expense, the deduction of which would otherwise be allowable, to the extent to which it is recoverable under any contract of insurance, guarantee, security or indemnity.”

It is suggested that the wording should be changed to read “No deduction for expenditure incurred on repairs will be permissible if the expenditure is recoverable as envisaged in section 23(c). The footnote can then be deleted.

Point 4.1.1 – The meaning of “repairs”

It is assumed that the following paragraph is SARS’s summary of the dictionary meaning of the word repair and the principles used by the courts:

“It is immaterial whether repairs occur as a result of some fortuitous act, such as a storm or fire, or as a result of the wearing out, damage or deterioration of an asset by use. Restoration involves a renewal or replacement of subsidiary parts of the structure and the expenditure incurred will be deductible. However, if the damage is of such an extent that the asset is partially destroyed, one would then have to look at whether the repair or renovation is a reconstruction of the entire asset, in which case the expenditure will not be deductible. To the extent that the cost of repairs is recoverable under a policy of insurance the deduction will be prohibited by section 23(c)”.

We agree that the only relevant consideration is as was stated earlier in this paragraph (It is necessary in each case to determine whether or not what has been done actually constitutes
“repairs” in the ordinary meaning of the word, and the extent to which it falls under that heading). It is also accepted that an improvement may well not be a repair.

The discussion in the paragraph should refer to paragraph 8.37.6.4 Replacement of part of an asset comprising a repair of the SARS guide on capital gains and its discussion of paragraph 33(3)(d) of the Eighth Schedule.

The reference to section 23(c) is superfluous as it is already covered earlier in the draft IN and not relevant to the meaning of the word repair.

**Paragraph 4.1.2 - The meaning of “maintenance” and paragraph 4.1.3 - Maintenance deductible as repairs under section 11(d)**

It is not clear why the discussion of the meaning of maintenance forms part of the draft IN. It is submitted that where expenditure were incurred to maintain the property or the asset it is done to before it is necessary to repair the property or asset. The deduction of the expenditure must then be considered in terms of section 11(a). On the other hand, if the “maintenance” is done to repair the property or asset concerned the deduction is to be made in terms of section 11(d).

We agree that maintenance “requires keeping the asset in good working order and condition”, but submit that it does not necessarily imply “that it has become defaced or worn out or worn down by use or possibly by wear-and-tear...”

**Paragraph 4.1.9 - Limitation of section 11(d)**

The following statement in the draft IN is wrong:

“An example will be where a taxpayer purchases replacement parts for a delivery vehicle in need of repair and pays in advance for the goods, but only half of the goods are delivered by year-end”.

Clearly the replacement parts will be trading stock (as explained in paragraph 4.1.7 of the draft IN) and should be treated as such. Section 23H specifically states that it excludes “expenditure incurred in respect of the acquisition of any trading stock.” The expenditure relating to the undelivered parts must be dealt with in terms of section 23F.

**Paragraph 5 - Conclusion**

We agree with the following statement:

“Because there are no set criteria as to what constitutes a repair and only principles derived from case law, each case will have to be determined on its merits.”

Please do not hesitate to contact us, should you have any questions regarding the above.

Yours faithfully

Piet Nel CA(SA)

**PROJECT DIRECTOR: TAX**

*The South African Institute of Chartered Accountants*