Dear Sir/Madam

COMMENTS ON THE DRAFT INTERPRETATION NOTE: SECTION 10(1)(e)

We thank you for the opportunity to provide input on the Draft Interpretation Note on Section 10(1)(e). We set out below the SAICA National Tax Committee submission comments.

1. General comments

It is assumed that this document is not intended to have binding effect. The document contains a number of unnecessary duplications.

2. Specific comments

Relevant paragraph: Preamble

The comment regarding the duplications in the document is mostly relevant to the preamble. Most of this is again covered in specific paragraphs.

In the definition of “section” Act presumably refers to the Income Tax Act. The definition of “levy” or “levy income” in the preamble differs from the meaning given to it in paragraph 4.2. It is suggested that the meaning given to it in the relevant Acts should be used.

It is not clear why the reference in the document is to the old Companies Act, and it is suggested that this is changed to incorporate the new Companies Act. It is not clear why the preamble include the VAT Act as it is not referred to at all in the document.

Paragraph 1 – see the comment about its binding nature and the later comment about the effective date.
Paragraph 2 – the background provided adds nothing to the document and it is not clear why it is included.

Paragraph 4 - The examples given (facts 3 and 4) in Example 1 are all dealing with similar expenses. It would be useful to have an example of when such an entity would not enjoy exemption.

It is true that levy income is not defined in the Income Tax Act, but it is suggested that it must take its meaning (for purposes of items (aa) and (bb) entities) from the relevant Act. For a share-block company there may be two levies, one to the levy fund and one to the body corporate. The levies for item (cc) entities have much wider ambit. It is suggested that penalty levies may in certain circumstances be a levy as envisaged by the relevant Acts.

Paragraph 5.2 should include a reference to Form E1 and the form should be updated as it still refers to a section 10(1)(iii) entity, which would now be the item (cc) entity.

Paragraph 10.4 - The view taken in this paragraph differs from the current Practice Note 8. The relevant part is copied below:

6.2 The body will be taxable on all other income including investment income. Expenditure directly related to such other income will be allowed as a deduction in terms of the Act. A deduction of a fixed percentage of the general or total expenditure is not acceptable. A proportionate share of accounting, audit and bank charges will be allowed against the taxable income. (Taxable income in relation to total income).

This change in principle, of allowing deductions to no deduction allowed – in example 3, is a fundamental change. If this is the intention to no longer allow these expenses, it would be necessary to alert the entities to it and to apply the change not form a specific date, but rather to a specific year of assessment.

The method of apportionment used in the example is open to criticism. Why is the R50 000 deducted before the formula is applied? It must either use gross income or income to apportion. But more importantly, in the court cases that dealt with apportionment of expenses, the courts endeavoured to find a reasonable method and did not in all cases use a formula. It is suggested that the Interpretation Note should recognise that there are other methods available to apportion the expenses.

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

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PROJECT DIRECTOR: TAX

The South African Institute of Chartered Accountants