Dear Sir,

SUGGESTED AMENDMENT TO SECTION 12I(2) OF THE INCOME TAX ACT, NO 58 OF 1962

The SAICA National Tax Committee has identified an issue that requires the attention of National Treasury and/or SARS and possibly an amendment to existing legislation. Please find below the proposal for an amendment to section 12I(2) of the Income Tax Act, No 58 of 1962 (“the Act”).

1. **Current position**

   1.1 The current version of section 12I(2) of the Act which deals with additional investment and training allowances in respect of industrial policy projects provides as follows: "In addition to any other deductions allowable in terms of this Act, a company may, subject to subsection (3), deduct an amount (hereinafter referred to as an additional investment allowance) equal to –

   (a) …; or

   (b) …,

   in the year of assessment during which that asset is first brought into use by the company as owner thereof for the furtherance of the industrial policy project carried on by that company, if that asset was acquired or contracted for on or after the date of approval and was brought into use within four years from the date of approval” (our emphasis).

2. **Problem statement**

2.1 The requirement that the additional investment allowance would only be applicable to assets which were acquired or contracted for on or after the date of the approval of the industrial policy project is problematic for the following reasons:
2.1.1 Industrial companies involved in the industrial environment continuously have to consider whether or not to expand or upgrade their current facilities. Equally, these companies or companies seeking to enter the industrial market have to decide whether or not to market and/or consider economical conditions – local or global – that are conducive to the setting-up of a new industrial facility.

2.1.2 There are a number of factors which are taken into account by these companies when the timing of these expansions, upgrades or new facilities are considered. One of the major considerations is the projected after-tax return-on-investment ("ROI") of the specific investment. The sensitivity of the ROI is usually tested against the movements of various variables such as:

2.1.2.1 exchange rates in respect of:

2.1.2.1.1 the acquisition or manufacture of the various components required to erect the expanded, upgraded or new facilities; and/or

2.1.2.1.2 the export of the end products;

2.1.2.2 other costs such as transport costs in respect of the components and/or raw materials required to manufacture the products and/or the delivery of the end products to the required markets;

2.1.2.3 projected/estimated demand for the product to be produced, taking into account economic cycles;

2.1.2.4 cost to manufacture the product vs. price at which the product can be sold;

2.1.2.5 tax allowances and investment incentives.

2.1.3 All or any combination of the above and various other factors therefore could significantly impact the timing of any investments in these industrial projects.

2.2 The limitation of the application of the additional investment allowance to assets which were acquired or contracted for on or after the date of the approval of the industrial policy project is unrealistic as it ignores the practicalities surrounding the commencement of any industrial project of the nature envisaged. One of the most significant practical issues is the lead times required by suppliers of components or plant for (i.e. assets) which are required for installation. Generally, these components or plant are not of the nature where suppliers would keep stock or be able to manufacture the same on demand. Further, the time required in manufacturing these components or plant may be months and in order to ensure that the specific components or plant are available for installation at the time required in terms of the steps identified to complete the project within the specified timeframe.
2.3 The argument that, the mere fact that a company has already acquired or contracted for "assets" which would qualify for the additional investment allowance had the assets not been acquired to or contracted for on or after the date of the approval of the industrial policy project, is an indication that the company intended to invest in the assets at this time, is in our view, unfounded. Not only would these companies at the same be preparing the application for submission as required in terms of the regulations, but for the reasons noted above, these investments would, in the absence of the additional investment incentives, not produce a ROI which would meet the required hurdle rates of the company in respect of such returns.

3. **Proposed solution**

3.1 We propose that the limitation of the additional investment allowance to assets acquired or contracted for on or after the **date of the approval** be removed. Further, the additional investment allowance should be available in respect of all assets which form part of any industrial policy project which has been approved provided the assets were acquired or contracted for on or after the **effective date of the section**.

3.2 We accordingly propose that the wording of section 12I(2) of the Act be amended as follows:

"In addition to any other deductions allowable in terms of this Act, a company may, subject to subsection (3), deduct an amount (hereinafter referred to as an additional investment allowance) equal to –

(a) …; or
(b) …,

in the year of assessment during which that asset is first brought into use by the company as owner thereof for the furtherance of the industrial policy project carried on by that company, if that asset was acquired or contracted for on or after the **effective date of this section** and was brought into use within four years from the date of approval".

Please do not hesitate to contact me should you wish to discuss the above.

Yours faithfully

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