Dear Sir/Madam

CALL FOR COMMENT: DRAFT INTERPRETATION NOTE ON SECTION 24; INSTALMENT CREDIT AGREEMENTS AND DEBTORS ALLOWANCE

We refer to the call for comment on the above-mentioned document. Set out below please find the SAICA National Tax Committee’s submission. The purpose of this submission is to highlight practical difficulties which could arise if the Draft Interpretation Note is adopted in its current format.

General comment

It is our belief that it is not the Interpretation Note that needs revision, but that Section 24 should be amended. The wording of the section is problematic for the following reasons:

- The section refers to credit agreements in the heading and then continues to specify that the agreements are those that postpone transfer.
- The National Credit Act refers to those credit agreements as “instalment agreement” and applies to movable property only.

Section 24 does not distinguish between a suspensive condition and a resolutive condition. It should do so as the rules of accrual differ for each. It is our opinion that where transfer of ownership is delayed due to a suspensive condition, that section 24 should not apply and that the principle established in Paragraph 13 (of the Eighth Schedule) should apply.

The tax consequences for a credit agreement where the transfer of ownership is postponed should then be treated in the same manner as the ‘time of disposal’ rules for capital gains tax purposes. An alternative would be to include only the actual amount received in each year of assessment in “gross income”.
It is noted that in terms of the sections that grants allowances in respect of depreciable assets, the seller of the property may now not claim and wear and tear in respect of movable assets sold in terms of a credit agreement as mentioned above.

Specific comments:

1. There is no indication of whether or not this Interpretation Note is a binding general ruling or merely a non-binding opinion.

2. In 4.1 we believe that the reference to “whole of that amount” in section 24 is interpreted wrongly in the Interpretation Note.

   The total transaction amount will consist of the following:
   - The cash value of the property subject to the credit agreement;
   - An initial fee (in terms of the National Credit Act). We believe the administration fee levied throughout the contract should not form part of the Section 24 amount;
   - The finance charges (or interest);
   - The output tax.

   The principal debt is the amount deferred and where an initial payment is made on the signing of the credit agreement, it is deducted from the transaction amount referred to above to arrive at the deferred amount. The 25% test in section 24(2) should then be done with reference to the principal debt (the deferred amount) and the Interpretation Note is incorrect to base it on the total transaction amount or as it is put in 4.1 “the whole of that amount”.

3. In point 4.4 it is agreed that if the “the whole of that amount” is deemed to accrue to the taxpayer, that an allowance is necessary.

4. We find no support in Section 24 for the statement that the debtors allowance may not create a loss. It is agreed that the allowance must be limited to the amount included in gross income, and in subsequent years to the allowance of the previous year.

5. The fact that SARS will take the section 11(i) allowance (refer to 4.5) into account is accepted, but is not based on section 24, which only refers to section 11(j).

6. In point 4.6, the second paragraph reads as follows:

   "The debtors' allowance is not automatically granted and taxpayers must apply to the Commissioner for its invocation."

   It will be helpful if the Interpretation Note describes the process for making such an application.

7. In point 4.8, the second paragraph, last sentence reads as follows:

   "The gross profit should include other forms of “income” such as delivery charges, fees for maintenance contracts and insurance premiums."
It is our opinion that the related costs should also be included in determining the gross profit?

**Recommendation**

We find it problematic that the debtors allowance is not granted automatically. The purpose of the Interpretation Note should be to provide guidelines for taxpayers to calculate the allowance. It now is clear that they must first apply for the allowance without clarifying whether or not this is by way of an advanced tax ruling or not.

To have to apply each year for the Commissioner's discretion is not practical. It can lead to provisional tax estimate problems, delays in finalising Annual Financial Statements due to uncertainty in regard to tax provisions, delays at SARS etc.

SARS has always had the right to call for information from the taxpayer and to adjust the taxable income accordingly. There appears to be no reason in obtaining SARS’s consent in advance. It is our recommendation that this requirement should be removed from the Draft Interpretation Note.

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

Yours faithfully

M Hassan CA(SA)

**PROJECT DIRECTOR: TAX**

*The South African Institute of Chartered Accountants*