



Legal & Policy

Income Tax

Guide to Building Allowances



South African Revenue Service

Guide to Building Allowances

Preface

This guide provides general guidance on building allowances available to owners and lessees of buildings. It does not go into the precise technical and legal detail that is often associated with tax, and should not, therefore, be used as a legal reference. It is not an “official publication” as defined in section 1 of the Tax Administration Act 28 of 2011 and accordingly does not create a practice generally prevailing under section 5 of that Act. It is also not a binding general ruling under section 89 of Chapter 7 of the Tax Administration Act. Should an advance tax ruling be required, visit the SARS website for details of the application procedure.

This guide is based on legislation as at the date of issue.

For more information you may –

- visit the SARS website at **www.sars.gov.za**;
- visit your nearest SARS branch;
- contact your own tax advisor or tax practitioner;
- contact the SARS National Contact Centre –
 - if calling locally, on 0800 00 7277; or
 - if calling from abroad, on +27 11 602 2093 (only between 8am and 4pm South African time).

Comments on this guide may be sent to **policycomments@sars.gov.za**.

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Glossary

In this guide unless the context indicates otherwise –

- “**First Schedule**” means the First Schedule to the Act;
- “**section**” means a section of the Act;
- “**the Act**” means the Income Tax Act 58 of 1962; and
- any word or expression bears the meaning ascribed to it in the Act.

1. Introduction

This guide provides guidance on the application and interpretation of the various building allowance provisions available to owners and lessees of buildings under the Act for the erection of buildings or the effecting of improvements to buildings.

2. Building allowances under the Act

2.1 The meaning of certain concepts

2.1.1 “Building”

The word “building” is not defined in the Act but has been considered in a number of court cases from which several general principles have emerged.

Normally a building is a substantial structure, more or less of a permanent nature, consisting of walls, a roof and the necessary appurtenances (accessories).¹ The question whether accessories or attachments to a building are of a permanent nature is dependent upon the facts of each case. Factors to be considered in this regard are, for example, the intention with which the accessory is attached, the nature of the accessory and the manner in which it has been attached to the building.² Anything attached to the building of a permanent nature will be considered part of it if it is structurally integrated or otherwise permanently physically integrated into the building in such a manner that it has lost its own separate identity and character.³ The word building does not include the land upon which the structure stands.⁴

Since a building can sometimes be a movable or temporary structure, the relevant provision of the Act will have to be considered in order to determine whether a building of a movable or immovable nature qualifies for the allowance.

2.1.2 “Wholly or mainly used”

The determination whether a building is wholly or mainly used for a particular purpose tends to be a question of fact. It is unnecessary that the building be used *wholly* for the required purpose, as long as the building is used *mainly* for that purpose. In practice SARS requires that more than 50% of a building, measured by floor space or volume, be used for the qualifying purpose.⁵

¹ *CIR v Le Sueur* 1960 (2) SA 708 (A), 23 SATC 261.

² *Konstanz Properties (Pty) Ltd v WM Spilhaus and Co (WP) Ltd* 1996 (3) SA 273 (A).

³ *SIR v Charkay Properties (Pty) Ltd* 1976 (4) SA 872 (A), 38 SATC 159.

⁴ ITC 1619 (1996) 59 SATC 309 (C) at 314.

⁵ A P de Koker & R C Williams *Silke on South African Income Tax* [online] (August 2013) in § 8.17A.

2.1.3 “Process of manufacture”

A process of manufacture covers those cases in which raw materials are converted into a product suitable for use. According to case law, it must be a complete process and it must produce an object or thing “essentially different” from the materials which went into its making. See Practice Note 42 dated 27 November 1995⁶ for a list of processes of manufacture and processes similar to a process of manufacture. This is not a closed list.

2.1.4 “Erection of which was commenced”

The courts have held that the date when erection of a building or improvements commences is the date when the laying of the foundation begins. Levelling of the site and excavations for the foundation have been held not to form part of the erection phase.⁷

2.1.5 “Improvements”

The word “improvement” is not defined in the Act and must be given its ordinary grammatical meaning. It is described in the New Oxford Thesaurus of English,⁸ as –

“[d]evelopment, upgrade, change for the better, refinement, enhancement, furtherance, advancement, forwarding; boost, augmentation, raising; correction, rectification, rectifying, upgrading, amelioration, rally, recovery, upswing, breakthrough”.

Reference must be made to the facts of each case. An improvement must, however, be distinguished from repairs.⁹

For the purpose of section 13¹⁰ only, “improvements” is defined in section 13(9) as follows:

“**[I]mprovements**”, in relation to any improvements commenced on or after the first day of April, 1971, means any extension, addition or improvements (other than repairs) to a building which is or are effected for the purpose of increasing or improving the industrial capacity of the building;

The expression “extension, addition or improvements” has been held in a number of court cases to mean physically attached to, connected or integrated with the building. For example, some years after a factory building was built, concrete aprons were added around the building. The aprons were held not to form part of the building as they were separate structures and not physically attached to the building and accordingly did not qualify as an improvement.¹¹

2.1.6 “Cost”

The court in *SIR v Eaton Hall (Pty) Ltd* considered the meaning of “cost to the taxpayer of the building” as ordinarily meaning the “price or consideration given or paid by him for the erection of the building... it does not, therefore, include expenses, incurred by the taxpayer in connection with the erection of the building unless, of course, they are part of the price or consideration paid for the erection.”¹² It does not include the cost of the land on which the

⁶ “Process of Manufacture and Processes Not Regarded as Processes of Manufacture or Processes Similar to a Process of Manufacture”.

⁷ ITC 1137 (1969) 32 SATC 1 (C).

⁸ P Hanks, first published (2000) Oxford University Press Inc, New York.

⁹ Interpretation Note No. 74 dated 6 August 2013 “Deduction and Recoupment of Expenditure on Repairs” for the distinction between repairs and improvements.

¹⁰ See the discussions below for section specific reference to “improvements”.

¹¹ *African Detinning Works (Pty) Ltd v SIR* 1982 (1) SA 797 (A), 44 SATC 1.

¹² 1975 (4) SA (A), 37 SATC 343 at 347 to 348.

building is erected nor the preparation of the land for the erection¹³ nor additional costs such as transfer duties or interest incurred on any financial instrument used for the erection or effecting improvements. Costs that are directly and closely connected with the erection of the building such as architect and civil engineering fees are included.

2.1.7 “Shipbuilding structure”

For the purpose of the allowance under section 13 a “shipbuilding structure” is defined in section 13(9) as follows:

“**[S]hipbuilding structure**” means any launching way, fitting-out quay or craneway which is not part of a building.

2.1.8 “Hotel keeper”

A “hotel keeper” is defined in section 1(1) as follows:

“**[H]otel keeper**” means any person carrying on the business of hotel keeper or boarding or lodging house keeper where meals and sleeping accommodation are supplied to others for money or its equivalent;

2.2 Allowance on buildings or improvements to buildings used in a process of manufacture, research and development or similar process (section 13)

2.2.1 Requirements to be met before the allowance may be claimed

Depending on the date of commencement of the erection of the building or improvements to the building, the building has to be wholly or mainly used by the taxpayer or the lessee during the year of assessment for the purpose of carrying on in the building any process of manufacture, research and development or any process which in the opinion of the Commissioner is of a similar nature in the course of the taxpayer’s or lessee’s trade, but specifically excluding mining or farming. The reference to “research and development” comes into operation on 1 April 2012 and is applicable to buildings in which research and development is carried on or after 1 April 2012.

It is a question of fact which must be determined on its merits on a case-by-case basis whether a building or improvements to a building meet this requirement, . For example, a taxpayer, as owner of a building used in a process of manufacture which includes offices, change rooms or a cafeteria, would be eligible for the allowance, but no allowance would be granted for any improvements made to the offices, change rooms or cafeteria as these improvements are not considered to improve the industrial capacity of the building.

The cost of erection of separate buildings created at the same time as the factory building but erected to house the administration staff, or as storerooms, change rooms or cafeterias, but on the same factory site, must be taken into account for the purpose of determining the allowance.¹⁴

In a year of assessment where a building is no longer used wholly or mainly in a process of manufacture, research and development or similar process, for the entire year, for example

¹³ See **2.1.4**. Levelling of the site and excavations for the foundation have been held not to form part of the erection phase.

¹⁴ SARS Circular Minute 27 of 5 July 1960.

the taxpayer uses it mainly for another trade, the taxpayer will no longer qualify for the allowance and may not claim.

2.2.2 Date when erection commenced and amount of allowance

(a) The erection of buildings commenced on or after 25 March 1959 and ending on 14 March 1961¹⁵

The taxpayer may deduct an allowance of 2% on the cost of any building, the erection of which was commenced by the taxpayer during this period and which was used during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture.

A taxpayer who purchases any building, the erection of which commenced during this period, from another person who was entitled to the 2% allowance, may continue to claim the 2% allowance as long as the taxpayer used the building during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture.

(b) The erection of buildings commenced on or after 15 March 1961

The taxpayer may deduct an allowance of 2% on the cost of any building the erection of which commenced on or after 15 March 1961 and which was used by the taxpayer during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture, research and development¹⁶ or any other process which, in the opinion of the Commissioner, is of a similar nature, or which is let by the taxpayer and is wholly or mainly used by a tenant or subtenant for the above purpose.¹⁷

A taxpayer who purchases any building the erection of which commenced on or after 15 March 1961, from another person who was entitled to the 2% allowance may continue to claim the 2% allowance as long as the taxpayer or his tenant or sub-tenant used the building during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture, research and development or any other process which, in the opinion of the Commissioner, is of a similar nature.¹⁸

The taxpayer may deduct an allowance of 2% on the cost of any building that has never been used if it was acquired by the taxpayer from another person and was during the year of assessment wholly or mainly used by the taxpayer for the purpose of carrying on a process of manufacture, research and development or any other process which, in the opinion of the Commissioner, is of a similar nature, or which is let by the taxpayer and is during the year of assessment wholly or mainly used by a tenant or subtenant for that process.¹⁹

(c) The erection of buildings commenced on or after 1 July 1985 and ending on 31 December 1988

The taxpayer may deduct an "initial" allowance of 17,5% on the cost of any building [under the now repealed section 13(7)] the erection of which was commenced during this period. The taxpayer may deduct an "annual" allowance of 2% on the cost (reduced by the "initial" allowance) of any building the erection of which was commenced during this period and

¹⁵ Section 13(1)(a) and (c) deleted by the Taxation Laws Amendment Act 31 of 2013 with effect from years of assessment commencing on or after 1 January 2014.

¹⁶ Research and development carried on for the period on or after 1 April 2012 but before 1 April 2022.

¹⁷ Section 13(1)(b).

¹⁸ Section 13(1)(d).

¹⁹ Section 13(1)(dA).

which was used during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture, research and development or any other process which, in the opinion of the Commissioner, is of a similar nature, or which is let by the taxpayer and is wholly or mainly used by a tenant or subtenant for that purpose. The cost of the building refers to the cost of the building less any recoupment referred to in **2.2.6**.

(d) The erection of buildings commenced on or after 1 January 1989

The taxpayer may deduct an allowance of 5% on the cost of any building (other than any building referred to in **(e)** below) the erection of which was commenced on or after 1 January 1989 and which was used during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture, research and development or any other process which, in the opinion of the Commissioner, is of a similar nature, or which is let by the taxpayer and is wholly or mainly used by a tenant or subtenant for that purpose. The cost of the building refers to the cost of the building less any recoupment referred to in **2.2.6**.²⁰

(e) The erection of buildings commenced on or after 1 July 1996 and ending on 30 September 1999²¹

The taxpayer may deduct an allowance of 10% on the cost of a building the erection of which was commenced during this period and which was brought into use during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture, research and development or any other process which, in the opinion of the Commissioner, is of a similar nature, or which is let by the taxpayer and is wholly or mainly used by a tenant or subtenant for that purpose. The cost of the building refers to the cost of the building less any recoupment referred to in **2.2.6**.

The allowance of 10% is deductible provided the building in question was brought into use on or before 31 March 2000. In the event that the building is brought into use after 31 March 2000, the allowance of 10% will be reduced to 5%.

2.2.3 Date when improvements commenced and amount of allowance

(a) Improvements commenced not later than 31 March 1971

The taxpayer may deduct an allowance of 2% on the cost of any improvements to any building referred to above, which was used as provided for in that paragraph during the year of assessment, if the improvements commenced not later than 31 March 1971.²²

(b) Improvements commenced on or after 1 April 1971

The taxpayer may deduct an allowance of 2% on the cost of improvements to any building if the improvements commenced on or after 1 April 1971 and that building was wholly or mainly used by the taxpayer, tenant or sub-tenant during the year of assessment for the purpose of carrying on any process of manufacture or any other process which, in the opinion of the Commissioner, is of a similar nature. This will apply irrespective of whether the building was erected or purchased, and if purchased, whether the seller was entitled to the allowance or not.²³

²⁰ Paragraph (b) of the proviso to section 13(1)(f).

²¹ Paragraph (c) of the proviso to section 13(1)(f). Deleted by the Taxation Laws Amendment Act 31 of 2013 with effect from years of assessment commencing on or after 1 January 2014.

²² Section 13(1)(e).

²³ Section 13(1)(f).

(c) Improvements commenced on or after 1 January 1989

The taxpayer may deduct an allowance of 5% on the cost of any improvements which have commenced on or after 1 January 1989 (other than any improvements referred to in **(d)** below) to any building which was used during the year of assessment wholly or mainly for the purpose of carrying on any process of manufacture or any other process which, in the opinion of the Commissioner, is of a similar nature, or which is let by the taxpayer and is wholly or mainly used by a tenant or subtenant for that purpose. The cost of the improvements to the building refers to the cost of the improvements less any recoupment referred to in **2.2.6**.²⁴

(d) Improvements commenced on or after 1 July 1996 and ending on 30 September 1999

The taxpayer may deduct an allowance of 10% on the cost of the improvements which have commenced after 1 July 1996 provided the building was brought into use on or before 31 March 2000. In the event that the improved building is brought into use after 31 March 2000, the allowance of 10% is reduced to 5%. The cost of the improvements to the building refers to the cost of the improvements less any recoupment referred to in **2.2.6**.²⁵

(e) Improvements on land or to buildings on leased property

A lessee, who has erected a building on, or effected improvements to a building on, leased property under a lease agreement, may not claim the allowance on that portion of the cost for erecting the building or effecting the improvements commenced on or after 1 July 1961 if an allowance was claimed under section 11(g) (the leasehold improvement allowance) for the same costs.

A lessee who undertakes obligatory improvements on a leased property as envisaged under section 12N will be deemed to be the owner of such improvements. Therefore, the allowance on the improvements is to be calculated as if the lessee owns the underlying property directly and the expenditure incurred by the lessee to complete the improvements is deemed to be the cost to the lessee for the purposes of the section 13 allowance.²⁶

2.2.4 Calculation of the allowance

The rate of the allowance varies and will depend on when the erection of the building or qualifying improvements commenced. The allowance is calculated annually on the cost to the taxpayer of the erection of a building or of effecting improvements to the building or the purchase price of the building. The building or improvements to the building need not be used for the full year of assessment in order for the allowance to be granted. The allowance on a building that is used for a portion of a year of assessment is allowed in full and not prorated for the number of months used during the year of assessment.

Date on which the erection of the building or improvements commenced	Rate of allowance
(a) Before 1 July 1985	2% × cost
(b) On or after 1 July 1985 but not later than 31 December 1988	2% × [cost – (17,5% × cost)*]

²⁴ Paragraph (b) of the proviso to section 13(1)(f).

²⁵ Paragraph (c) of the proviso to section 13(1)(f).

²⁶ Paragraph (d) of the proviso to section 13(1)(f).

	* Initial allowance
(c) On or after 1 January 1989 but not later than 30 June 1996	5% × cost
(d) On or after 1 July 1996 but not later than 30 September 1999 and brought into use on or before 31 March 2000	10% × cost
(e) On or after 1 July 1996 but not later than 30 September 1999 and brought into use after 31 March 2000	5% × cost
(f) On or after 1 October 1999	5% × cost

* The initial allowance (which was 17,5% of the cost of qualifying buildings and improvements the erection of which commenced between 1 July 1985 and 31 December 1988, if completed and brought into use by 31 December 1989) was available under the now repealed section 13(7).

The rate of the allowance is calculated on the cost of the building or improvements less any –

- recovery or recoupment of the allowance that is set off against the cost of the building or improvements; and
- costs of any building or any improvements as had been taken into account in the calculation for the allowance of leasehold improvements.

A taxpayer who acquires a building without paying any consideration, for example, by donation or inheritance, is not entitled to the allowance, since the taxpayer has not incurred any cost.²⁷

Example 1 – Improvements to buildings

Facts:

Company A, a manufacturer, commenced improvements to a building during September 2011 at a cost of R80 000 of which R60 000 was used to enlarge the existing storage rooms used for manufactured goods and the balance of R20 000 to improve the facilities for staff, such as new offices and a canteen. These improvements were brought into use on 1 November 2011.

Result:

The improvements must have been effected for the purpose of increasing or improving the industrial capacity of the building in order to qualify for the allowance. The allowance will only be allowed on the enlargement of the existing storage rooms at 5% of cost, that is, R3 000 (5% of R60 000). The new offices and the canteen will not qualify for the allowance.

²⁷ Silke on South African Income Tax in § 8.17.

Example 2 – Sale of a building that qualifies for an allowance

Facts:

Company B, a manufacturer with a year-end of 28 February, erected a factory building at a cost of R400 000. Erection commenced on 1 April 1988 and the building was completed and brought into use on 1 December 1988. Company B commenced improvements to the building on 1 June 1996 at a cost of R200 000 which were completed and brought into use on 1 August 1996.

Company B sold the building on 1 March 2010 to Company C for R800 000. Company C uses the building for the purpose of manufacture and has a year-end of 28 February.

Result:

The allowances that Company B and Company C are entitled to claim on buildings for the years of assessment ended 28 February 1996 to 28 February 2014 are as follows:

Company B

	R
Cost of factory building	400 000
Less: Initial allowance (17,5% × R400 000)	<u>(70 000)</u>
	<u>330 000</u>

The allowance on the factory building for each year of assessment (28 February 1996 to 28 February 2010) must be based on the cost less the initial allowance, that is, R330 000.

The allowance is calculated as follows:

$$2\% \times R330\,000 = R6\,600$$

The allowance on the improvements to the factory building for each year of assessment (28 February 1997 to 28 February 2010) is calculated as follows:

$$5\% \times R200\,000 = R10\,000$$

Company C

As the rate of the allowance for a building that is purchased follows the date on which the erection of the building commenced, both the building (which qualified for 2% on the original construction cost) and the improvements to the building (which qualified for 5% on the cost of improvements) will only qualify for the allowance of 2% on cost of purchase once acquired by Company C.

For the 2011 to 2014 years of assessment Company C may claim an annual allowance calculated as follows:

$$2\% \times R800\,000 = R16\,000.$$

2.2.5 Limit on the allowance

The aggregate of the allowance allowed may not exceed the cost of the building or improvements less the sum of any recoupment (see **2.2.6**) and the aggregate of the leasehold improvement allowance under section 11(g) of the Act or any previous legislation.²⁸

²⁸ Section 13(2).

2.2.6 Recoupment

The allowance is subject to recoupment under section 8(4)(a) on disposal of the building. The taxpayer does, however, have an option under section 13(3) to prevent the recoupment from being included in the taxpayer's income. The recoupment will not be included in the taxpayer's income but will be set off against the cost of a further building, provided the taxpayer purchases or erects the further building within 12 months or any longer period which the Commissioner may allow from the date on which the event giving rise to the recovery or recoupment occurred. The further building purchased or erected must itself qualify for the allowance in order for this option to be exercised. Should the taxpayer not erect or purchase any other building, the amount of the recoupment will be taxed in the year of accrual.

2.3 Allowance on any permanent shipbuilding structure [section 13(8)]

The provisions of the Act governing the building allowance and its recoupment as discussed in 2.2 are extended to any permanent shipbuilding structure that was wholly or mainly used during the year of assessment for the purposes of the shipbuilding trade.

2.4 Allowance on buildings used by hotel keepers (section 13bis)

2.4.1 Requirements to be met before the allowance may be claimed

Section 13bis provides for an allowance on the erection of hotel buildings or improvements to such buildings. The allowance is calculated on the cost of erecting the buildings and improvements (other than repairs) which meet the following criteria:

- The erection of the building or improvements was commenced on or after 2 March 1960.
- The building was used during the year of assessment by the taxpayer for the purpose of trade as hotel keeper or was let by the taxpayer and so used by the lessee.
- In the case of improvements, the building (or portion of it) to which the improvements are effected was registered as a hotel under the Hotels Act 70 of 1965 during the year of assessment irrespective of when it was erected.

There is no requirement that the building be used as a hotel for the entire year of assessment and the allowance is not apportioned for periods of less than a full year. The use of only a part of the building as a hotel will result in the cost of erection of that part being ascertained for the purpose of calculating the allowance.

No allowance is granted on the cost of a hotel building that has been purchased; only the cost for the erection of the building by the taxpayer or improvement to such building will qualify for the allowance. The cost of the building excludes the cost of the land on which it is erected.

A lessee who undertakes obligatory improvements on a leased property as envisaged under section 12N will be deemed to be the owner of such improvements. Therefore, the allowance on the improvements is to be calculated as if the lessee owns the underlying property directly.

2.4.2 Calculation of the allowance

The rate of the allowance on buildings used by hotel keepers varies and will depend on when the erection of the building or qualifying improvements commenced.

Date on which the erection of buildings or improvements commenced	Rate of allowance
(a) On or after 2 March 1960 but later than 31 December 1963 used by taxpayer or lessee ²⁹	2% x cost
(b) On or after 1 January 1964 (any building) and not later than 13 June 1965 (any improvements thereto) and such building was brought into use not later than 30 June 1965 by the taxpayer or the lessee	2% x cost
(c) On or after 1 January 1964 [such portion of any building] or improvements to buildings in this paragraph or (a) above or any improvements to buildings in (b) above if the improvements were commenced on or after 1 July 1965 and used by the taxpayer or lessee	2% x cost
(d) On or after 1 January 1964 any building improvements	2% x cost
(e) On or after 4 June 1988 any building or improvements	5% x cost
(f) On or after 17 March 1993 (only improvements that do not extend the existing exterior framework of the building)	20% x cost

The rate of the allowance is calculated on the cost of the building or improvements less any recovery or recoupment of the allowance that is set off against the cost of the building or improvements and excludes any costs as had been taken into account in the calculation for the allowance of leasehold improvements.

Example 3 – Allowance claimed on a hotel building erected by the taxpayer

Facts:

Company A, with a year-end of 28 February, commenced the erection of a hotel building during 1986 which was completed on 1 March 1988 at a cost of R4 000 000 and brought into use in its trade as hotel keeper on the same day. Company A commenced with improvements on 30 June 1994 which substantially increased the size of the hotel. The improvements to the hotel were completed on 1 March 1995 at a cost of R3 000 000 and brought into use on the same day.

²⁹ Section 13bis(1)(a) and (b) deleted by the Taxation Laws Amendment Act 31 of 2013 with effect from years of assessment commencing on or after 1 January 2014.

Result:

Company A may claim an allowance of R80 000 (2% of R4 000 000) for the year of assessment ended 28 February 1989 and each subsequent year of assessment until the year of assessment ending on 28 February 2038. Company A may also claim an allowance of R150 000 (5% of R3 000 000) on the cost of the improvements for the year of assessment ended 28 February 1996 and every subsequent year of assessment until the year of assessment ending on 28 February 2015.

Company A may not claim 20% on the cost of the improvements because they extended the existing exterior framework of the building.

2.4.3 The hotel building grading allowance

Section 13*bis*(2) provided for an additional hotel building grading allowance for qualifying hotel buildings and improvements to qualifying hotel buildings. The hotel building grading allowance was based on the erection of a building or improvements to the building which commenced on or after 2 March 1960 and before 4 June 1988 and applied only to buildings erected and improvements commenced during this period. The allowance could be claimed for a maximum period of 25 years and is therefore not available from the 2015 year of assessment.

The hotel building allowance and the hotel building grading allowance may not in the aggregate exceed the cost of the building or improvements taken into account for the calculation of these allowances, which excludes any amount for leasehold improvements and the amount of any recovery or recoupment not included in income.³⁰

2.4.4 Recoupment

The allowance on buildings and improvements is subject to recoupment (see **3**). The taxpayer may, however, opt to delay including the recoupment in income but must then erect within 12 months or such further period as the Commissioner may allow, a further building which must itself qualify for the allowance. This set-off is limited to the amount of the cost of the building less any leasehold improvements.³¹

2.5 Allowance on commercial buildings (section 13*quin*)

Section 13*quin* provides for an allowance on any new and unused buildings or improvements that are used by the taxpayer wholly or mainly in the production of income in the course of a trade, other than the provision of residential accommodation. The allowance is not apportioned if the building is brought into use for part of the year of assessment.

2.5.1 Requirements to be met before the allowance may be claimed

The allowance applies to buildings contracted for on or after 1 April 2007 (the effective date) and of which the construction, erection or installation commenced on or after the effective date. It applies to new and unused buildings and improvements effected to existing commercial buildings. Buildings that have been used by the taxpayer before the effective date do not qualify for the allowance. A building purchased by the taxpayer from a seller who used the building before the sale does not qualify for the allowance.³²

³⁰ Section 13*bis*(3).

³¹ Section 13*bis*(6).

³² Explanatory Memorandum on the Revenue Laws Amendment Bill, 2007 at pages 45 to 46.

The taxpayer does not have to erect the building to claim the allowance. The building may be acquired by the taxpayer from a third party, such as a property developer, provided the building is new and unused.³³

A lessee who undertakes obligatory improvements on a leased property as envisaged under section 12N will be deemed to be the owner of such improvements.

Section 12N allows for the depreciation allowances on the improvements to be calculated as if the lessee owns the underlying property directly, provided the lessee uses the property for purposes of earning income. The expenditure incurred by the lessee to complete the improvements is deemed to be the cost to the lessee of any new and unused building or of any new and unused improvements to a building undertaken for the purposes of the section 13quin allowance.³⁴

The allowance is granted at a rate of 5% a year on the cost of the building.³⁵ The building and improvements are written off over a period of 20 years. The cost is the lesser of the cost to the taxpayer or the arm's length price of the building at the time of acquisition.³⁶

A special deeming rule³⁷ applies to a taxpayer who –

- claimed a deduction under section 13quin on a building or improvement in the year under review;
- during a previous financial year brought that building or improvement into use for the first time for the purposes of the taxpayer's trade; and
- during that previous year did not include the receipts and accruals from that trade in income.

Any deduction which could have been allowed under section 13quin during that year or any subsequent year in which the building or improvement was used by the taxpayer is, for the purposes of section 13quin, deemed to have been allowed during that previous year or years as if the receipts and accruals of that trade had been included in the taxpayer's income.

Once a building has been disposed of in a year of assessment, no allowance under section 13quin can be claimed for the building in a subsequent year of assessment.³⁸ This prevents the taxpayer from claiming the allowance for a building for 15 years, disposing of it and then later reacquiring it and claiming an allowance under the section for the building.³⁹

No deduction is allowable under section 13quin for the cost of a building or improvement if any of that cost has qualified or will qualify for deduction from the taxpayer's income as a deduction of expenditure or an allowance for expenditure under any other section of the Act.⁴⁰

³³ D Davis, L Olivier and G Urquhart *Juta's Income Tax* [online] under Legislation and Commentary, Section 13quin.

³⁴ Section 13quin(1A).

³⁵ Section 13quin(1).

³⁶ Section 13quin(2).

³⁷ Section 13quin(3).

³⁸ Section 13quin(4).

³⁹ *Juta's Income Tax* in the commentary on section 13quin.

⁴⁰ Section 13quin(5).

The aggregate allowance may not exceed the cost to the taxpayer of the building upon which the allowance is calculated.⁴¹ For subsequent owners of the building, the building will not qualify for the allowance as it will not then be unused or new, but improvements effected by them to the building could, subject to the provisions of the section, qualify for the allowance.

Example 4 – Allowance claimed on erection of a commercial building

Facts:

Individual A contracted to have a four-storey building erected on 1 May 2007. Construction commenced and the building was completed on 31 May 2008 at a cost of R4 million. The first three floors of the building were designed as office space while the top floor comprised a number of penthouse apartments. By the end of the 2009 year of assessment the taxpayer had let all the office space and apartments.

Result:

Three-fourths of the building is used to produce income in the course of the taxpayer's trade other than the provision of residential accommodation. The building is accordingly "wholly or mainly", that is, more than 50%, used for that purpose. The building is also new (recently constructed) and unused (the taxpayer is the first person to use the building).

Individual A therefore qualifies for the section 13quin allowance and will be entitled to an annual allowance of $R4\ 000\ 000 \times 5\% = R200\ 000$.

2.5.2 Part-acquisition

The cost of acquiring part of a building (or improvement) on or after 21 October 2008, without erecting or constructing it, is deemed to be –

- 55% of the acquisition price, in the case of the part being acquired;⁴² and
- 30% of the acquisition price, in the case of an improvement being acquired.⁴³

The reference to "a part of a building being acquired" would include, for example, the acquisition of a sectional title unit in a building from a developer. The purpose of the limitation of the allowance to 55% of the cost of such a unit is to ensure that the allowance is not allowed on the cost of the land which would be included in the purchase price of the unit. The acquisition of an improvement could include additions to the common property such as the addition of parking garages or the upgrading of the reception area on the ground floor.

2.5.3 Recoupment

See 3 for the general recoupment provision.

2.6 Allowance on the erection or improvement of buildings in urban development zones (section 13quat)

Section 13quat provides for an allowance on the cost of erection, extension, addition or improvement of any commercial or residential building or part of that building within an urban development zone which is owned by the taxpayer and is used solely for purposes of that taxpayer's trade.

⁴¹ Section 13quin(6).

⁴² Section 13quin(7)(a).

⁴³ Section 13quin(7)(b).

For more information on the allowance under section 13*quat* please refer to the *Guide to the Urban Development Zone Tax Incentive* available on the SARS website www.sars.gov.za.

2.7 Allowance on residential buildings

2.7.1 Housing for employees or the households of employees [section 11(f)]

A deduction was allowed under section 11(f) to taxpayers who erected or financed the cost of erection of housing for employees or the households of employees. This section was deleted from the Act by the Revenue Laws Amendment Act 60 of 2008 and only applies to housing, the erection of which commenced before 21 October 2008.

(a) Requirements to be met before the allowance may be claimed

A deduction was allowed to taxpayers who erected or financed the cost of erection (whether by loan or donation) of housing for employees during the year of assessment in which the expenditure was incurred or the loan or donation was made. The dwelling had to be occupied exclusively by persons or the households of the persons who were employed by the taxpayer for purposes of the taxpayer's trade (excluding mining and farming). The allowance was equal to 50% of the expenditure incurred or of the amount financed by advance or donation. The aggregate of all the allowances under section 11(f) on any one dwelling could not exceed R6 000.⁴⁴

If a company is mainly engaged in the provision of housing facilities for the employees of its sole or principal shareholder, or for the employees of any other company, the shares of which are held wholly by the sole or principal shareholder, the employees of the shareholder or that other company are deemed to be the employees of the company providing the facility.⁴⁵

For purposes of section 11(f), an "employee" in relation to a taxpayer does not include –

- any person who is a relative of the taxpayer; or
- if the taxpayer is a company, any person who is a shareholder (or a relative of a shareholder) in that company or in any company which is associated with that company by virtue of shareholding, excluding a shareholder who holds shares in that company solely because the shareholder is employed by that company and who will, in terms of the articles of association of that company, not be entitled to continue to hold those shares after the shareholder ceases to be so employed.

(b) Recoupment

Should a dwelling on which an allowance has been allowed no longer be occupied by a person or by the household of any person who is not an employee of the taxpayer, the deduction less an amount equal to one-tenth of that deduction of each completed year (not exceeding 10 years) during which the dwelling was occupied by an employee or the household of an employee of the taxpayer, is included in the taxpayer's income.⁴⁶

A recoupment under section 8(4)(a) on the sale of the dwelling will be reduced by any amount previously included under the recoupment mentioned above.

⁴⁴ Section 11(f)(ii).

⁴⁵ Section 11(f)(i).

⁴⁶ Section 11(f)(iii).

The allowance under section 11(t), when a dwelling is sold and the selling price is payable in instalments, is recouped as and when the employer recovers the selling price. Each instalment will therefore include an element of recoupment which is determined as follows:

$$\frac{\text{Capital repayment in each year}}{\text{Selling price}} \times \text{Amount of allowance under section 11(t)}$$

An employer who has been granted an allowance under section 11(t), on a loan advanced to an employee for the erection of a dwelling, must be taxed under section 8(4)(a) on any recoupment of the allowance by way of repayment of the loan to the employer.

Example 5 – Allowance on housing erected for employees

Facts:

Company A erected a dwelling at a total cost of R60 000. It is occupied by one of its employees from 1 June 2002 to 31 August 2007. The dwelling was sold by Company A on 15 March 2013 for R60 000. Company A's year of assessment ends on the last day of February.

Result:

Year of assessment ended 28 February 2003

Company A will be allowed a deduction of R6 000 (50% of R60 000 = R30 000 limited to R6 000).

Year of assessment ended 29 February 2008

Company A must include R3 000 in its income as a recoupment, that is, R6 000 – (1 / 10 × R6 000 × 5 completed years).

Year of assessment ended 28 February 2014

Company A must recoup a further R3 000 under section 8(4)(a):

	R
Cost	60 000
Less: Section 11(t) allowance allowed in 2003	<u>(6 000)</u>
	54 000
Section 11(t)(iii) recoupment subject to tax in 2008	<u> 3 000</u>
Income tax value of dwelling on 15 March 2013	<u>57 000</u>
Selling price on 15 March 2013	60 000
Less: Income tax value of dwelling	<u>(57 000)</u>
Recoupment under section 8(4)(a)	<u> 3 000</u>

2.7.2 Residential units under a housing project (section 13ter)

A residential building annual allowance and a residential building initial allowance were available to a taxpayer who erected residential units under a housing project under section 13ter. This section applied to units that were erected on or after 1 April 1982 and before 21 October 2008.⁴⁷

⁴⁷ Section 13ter(1). After this date the allowance will be governed by section 13sex.

For the purpose of section 13*ter*(1) the term “housing project” is defined as follows:

“**[H]ousing project**” means any project for the erection of a building or buildings in the Republic consisting of or including at least five residential units;

For the purpose of section 13*ter*(1) the term “residential unit” is defined as follows:

“**[R]esidential unit**” means any self-contained residential accommodation consisting of more than one room (but excluding any hostel, hotel or similar accommodation), the erection of which was commenced by the taxpayer on or after 1 April 1982 and before 21 October 2008 and which was erected under a housing project of the taxpayer—

- (a) in order to be let to a tenant for the purpose of deriving a profit for the taxpayer; or
- (b) in order to be occupied by a *bona fide* full-time employee of the taxpayer.

(a) The residential building initial allowance

A residential building initial allowance of 10% of the cost is available in the year in which the residential unit is for the first time let or occupied by a tenant or full-time employee of the taxpayer provided that at least five units in the housing project have been let or occupied. If less than five units are let or occupied, the allowance is delayed and made available in the year in which at least five of those units are let or occupied.⁴⁸

(b) The residential building annual allowance

A residential building annual allowance is available at a rate of 2% of the cost of the residential unit for the period in which it so qualifies. This allowance is first granted in the year of assessment in which the residential building initial allowance is granted on the residential unit concerned.⁴⁹

A special deeming rule⁵⁰ applies to a taxpayer who –

- claimed a deduction under section 13*ter* on a building in the year under review; and
- during a previous financial year or years used the building for the purposes of carrying on any trade from which the receipts and accruals were not included in income.

Any deduction which could have been allowed under section 13*ter* during that year or any subsequent year in which the building was used by the taxpayer is, for the purposes of section 13*ter*,⁵¹ deemed to have been allowed during that previous year or years as if the receipts and accruals of that trade had been included in the taxpayer’s income. The deemed deduction is not subject to recoupment under section 8(4)(a).⁵²

⁴⁸ Section 13*ter*(5)

⁴⁹ Section 13*ter*(6).

⁵⁰ Section 13*ter*(6A).

⁵¹ Excluding section 13*ter*(7)(a) which provides for a recoupment of the residential building initial allowance when the building ceases to be available for letting or occupation by an employee.

⁵² Section 8(4A).

Example 6 – Allowances on residential units erected under a housing project

Facts:

Company D erected a block of flats consisting of 10 units at a cost of R12 000 000. Four units were completed and let during the year of assessment ended on 28 February 2006. The remaining 6 units were completed and occupied by permanent employees of Company D during the year of assessment ended 28 February 2007.

Result:

2006 Year of assessment

Company D may not claim the residential building initial allowance or the residential building annual allowance since less than 5 units were let to tenants during the 2006 year of assessment.

2007 Year of assessment

A residential building initial allowance of R1 200 000 (10% of R12 000 000) may be claimed.

A residential building annual allowance of R240 000 (2% of R12 000 000) may be claimed.

(c) Requirements to be met before the allowance may be claimed

A taxpayer who does not own the premises on which the taxpayer erects the residential units, cannot claim any allowance unless the taxpayer is entitled to occupation of those premises for at least 10 years after the date of commencement of the erection of those units or if the provisions of section 12N are applicable.⁵³

Section 12N allows for the depreciation allowances on the improvements to be calculated as if the lessee owned the underlying property directly, provided the lessee uses the property for purposes of earning income. The expenditure incurred by the lessee to complete the improvements shall be deemed to be the cost to the lessee of a residential unit for the purposes of the section 13*ter* allowance.⁵⁴

The cost of the residential unit (for purposes of calculating these two allowances) will exclude any costs allowed as a deduction under any other provisions of the Act, whether in the current or any previous year of assessment.

Example 7 – Claiming an allowance under another provision of the Act

Facts:

Taxpayer A erects 5 residential units for R10 000 each under a housing project for occupation by employees. An allowance of R6 000 per unit has been allowed as a deduction under section 11(*t*).

⁵³ Section 13*ter*(4). Section 12N will apply if a lessee undertakes obligatory improvements on leased property under a public private partnership, or to leased property owned by the government in the national, provincial or local sphere or any entity exempt under section 10(1)(cA) or (*t*).

⁵⁴ Section 13*ter*(2A).

Result:

The following costs will qualify for the allowance under section 13*ter*:

	R
Cost of units (R10 000 × 5)	50 000
Less: Allowance under section 11(<i>t</i>) (R6 000 × 5)	(30 000)
Costs that qualify for allowance purposes under section 13 <i>ter</i>	<u>20 000</u>

The aggregate allowance on both the residential building initial allowance and the residential building annual allowance cannot exceed the cost on which these allowances are calculated.⁵⁵

Costs may only include the cost of erecting the building and do not include amounts such as the purchase price of the land, transfer costs and furniture.

(d) Recoupment

A recoupment will occur when the residential unit is no longer let to a tenant or is no longer occupied by a full-time employee.⁵⁶ The amount of the residential building initial allowance is included in the income of the taxpayer less one-tenth of that amount for each completed period of one year, but not exceeding 10 years, from the date the unit qualified to the date on which it ceased to qualify.⁵⁷ In addition, the residential building annual allowance may not be claimed until the unit is once again occupied for the specified purpose.

The taxpayer is thus permitted to retain the benefit of one-tenth of the residential building initial allowance for every completed year, up to a maximum of 10 years, during any unbroken period in which the unit was first let or occupied for the specified purpose for a full year of assessment.

The general recoupment provisions of section 8(4)(a) and the balancing allowance under section 11(o) do not apply to the amount of the residential building initial allowance which is included in income as mentioned above, whether it be in the current or any previous year of assessment.⁵⁸

Example 8 – Recoupment when section 13*ter* requirements are not met

Facts:

Taxpayer A erected a residential building, consisting of 8 units, at a cost of R500 000 each. All units were completed on 1 March 2007 and all were let as from that date. On 1 June 2013 two of the units were occupied by family members at no cost.

Result:

An amount must be included in Taxpayer A's income for the year of assessment ended 28 February 2014 under section 13*ter*.

⁵⁵ Section 13*ter*(10).

⁵⁶ Section 13*ter*(7).

⁵⁷ Section 13*ter*(7)(b).

⁵⁸ Section 13*ter*(8).

The residential building initial allowance claimed for the year of assessment ended 28 February 2008 on the 2 units is calculated as follows:

$$= (500\,000 \times 2) \times 10\%$$

$$= R1\,000\,000 \times 10\%$$

$$= R100\,000$$

Year of assessment ended 28 February 2014

	R
Residential building initial allowance claimed for 2 units during 2008	100 000
Less: $1 / 10 \times 100\,000 \times 6$ completed years	<u>(60 000)</u>
Amount to be included in income	<u>40 000</u>

2.7.3 Allowance for certain residential units (on or after 21 October 2008) (section 13sex)

The provisions for residential housing were contained in various sections of the Act. As from 21 October 2008 the existing allowances for residential units (as mentioned in the aforementioned paragraphs) have been replaced with a new allowance for low-cost housing which has been brought into one simplified and comprehensive provision, namely, section 13sex.

This allowance only applies to those residential units or improvements which were acquired or the erection of which commenced, on or after 21 October 2008 and is subject to section 36, which provides for an allowance on disposal of low-cost residential units to employees by an employer undertaking mining operations.

A “residential unit” is defined in section 1(1) as follows:

“**[R]esidential unit**” means a building or self-contained apartment mainly used for residential accommodation, unless the building or apartment is used by a person in carrying on a trade as an hotel keeper;

A “low-cost residential unit” is defined in section 1(1) as follows:

“**[L]ow-cost residential unit**” means—

- (a) an apartment qualifying as a residential unit in a building located within the Republic, where—
 - (i) the cost of the apartment does not exceed R350 000; and
 - (ii) the owner of the apartment does not charge a monthly rental in respect of that apartment that exceeds one per cent of the cost; or
- (b) a building qualifying as a residential unit located within the Republic, where—
 - (i) the cost of the building does not exceed R300 000; and
 - (ii) the owner of the building does not charge a monthly rental in respect of that building that exceeds one per cent of the cost contemplated in subparagraph (i) plus a proportionate share of the cost of the land and the bulk infrastructure:

Provided that for the purposes of paragraphs (a)(ii) and (b)(ii), the cost is deemed to be increased by 10 per cent in each year succeeding the year in which the apartment or building is first brought into use;

(a) Requirements

A taxpayer may deduct an allowance of 5% of the cost of the erection, improvement or acquisition of any new and unused⁵⁹ residential unit (or any new and unused improvement to a residential unit) owned by the taxpayer if –

- the unit or improvement is used by the taxpayer solely for the purposes of a trade carried on by the taxpayer;⁶⁰
- the unit is situated in South Africa;⁶¹ and
- the taxpayer owns at least five residential units within South Africa, which are used by the taxpayer for the purposes of a trade carried on by the taxpayer.⁶²

A taxpayer that completes an improvement provided for in section 12N⁶³ is allowed to calculate the depreciation allowances on the improvements as if the lessee owned the underlying property directly, provided the lessee uses the property for purposes of earning income. The expenditure incurred by the lessee to complete the improvements shall be deemed to be the cost to the lessee of any new and unused residential unit or of any new and unused improvement to a residential unit undertaken for the purposes of the section 13sex allowance.⁶⁴

The taxpayer may claim an additional 5% allowance should the residential units qualify as low-cost residential units, bringing the allowance to 10% in total.⁶⁵

The cost of a building (or improvement) is the lesser of the cost of the building to the taxpayer or its arm's length price at the time of acquisition.⁶⁶ "Arm's length" suggests that each party is independent of the other and in their dealings will each strive to get the utmost possible advantage out of the transaction. The allowance will not be granted if the cost of the residential unit (or improvement) qualifies for any other allowance under any other section of the Act.⁶⁷

No allowance may be claimed on the cost of any residential unit or improvement if that residential unit has been disposed of by the taxpayer during any previous year of assessment.⁶⁸

The periods during which a residential unit or improvement was used by a taxpayer who was not previously subject to tax will be taken into account in determining the remaining extent of the allowance. For example, if the unit was erected and then rented for three years before the taxpayer became taxable for the first time, the allowance would be granted from the fourth year at 5% (10% in the case of a low-cost residential unit) for 17 years.

⁵⁹ In ITC 672 (1948) 16 SATC 227 (U), the word "new" was regarded as meaning in the sense of not having been used before by that particular taxpayer and in the sense of not having been acquired from somebody else and so second-hand.

⁶⁰ Section 13sex(1)(a).

⁶¹ Section 13sex(1)(b).

⁶² Section 13sex(1)(c).

⁶³ Section 12N will apply if the taxpayer as a lessee undertakes obligatory improvements on leased property under a public private partnership, or to leased property owned by the government in the national, provincial or local sphere or any entity exempt under section 10(1)(cA) or (t).

⁶⁴ Section 13sex(1).

⁶⁵ Section 13sex(2).

⁶⁶ Section 13sex(3).

⁶⁷ Section 13sex(6).

⁶⁸ Section 13sex(5).

The allowance is claimed in full and is not apportioned even if the residential unit is brought into use for only a portion of the year of assessment.

(b) Part-acquisition of a building

The cost of acquiring a residential unit (or improvement to a residential unit) which represents only a part of a building without erecting or constructing that unit, is deemed to be –

- 55% of the acquisition price, in the case of the unit acquired,⁶⁹ and
- 30% of the acquisition price, in the case of the improvement acquired.⁷⁰

The reference to “a residential unit forming part of a building” would apply, for example, to a flat forming part of a block of flats. The intention in limiting the qualifying cost in such instances is to prevent the allowance being allowed on the cost of the land on which the building is situated and which would form part of the cost of the flat. An improvement acquired by a taxpayer could include, for example, the taxpayer’s share of extending the servant’s quarters on the common property in the case of a unit held under sectional title.

Example 9 – Allowance on residential units acquired in a building

Facts:

On 1 March 2013 Taxpayer A bought 8 new and unused apartments directly from a developer in a building at a cost of R500 000 each. On 1 October 2013 the taxpayer rented out 3 units to family members and 5 units to the public.

Result:

Each of the 5 units let to the public comprises a “residential unit” as defined in section 1(1) and accordingly qualifies for the section 13sex allowance which is calculated as follows:

$$R500\ 000 \times 5 \text{ units} = R2\ 500\ 000$$

Since these 5 units form part of a building, only 55% of their cost will qualify for the allowance under section 13sex(8)(a).

$$R2\ 500\ 000 \times 55\% = R1\ 375\ 000$$

$$R1\ 375\ 000 \times 5\% = R68\ 750 \text{ (section 13sex allowance)}$$

The full allowance will be granted even though the 5 units were used for only a part of the 2014 year of assessment.

(c) Recoupment

See the general recoupment provision in 3. See 2.7.4(c) for the recoupment provision in the case of the sale of low-cost residential units.

⁶⁹ Section 13sex(8)(a).

⁷⁰ Section 13sex(8)(b).

2.7.4 Allowance on the sale of low-cost residential buildings on loan account (section 13sept)

An allowance under section 13sept was introduced to offer relief to employers wishing to transfer ownership of low-cost residential housing to their employees by making use of interest-free loan financing. The section came into operation on 21 October 2008 and applies to a unit disposed of on or after that date and is subject to section 36.

(a) The allowance

The allowance claimed is an amount equal to 10% of any amount owing to the taxpayer by the employee on the unit at the end of the taxpayer's year of assessment over a period of 10 years.⁷¹

(b) Requirements to be met before the allowance may be claimed

An employer will qualify for the allowance provided all the following requirements are met:

- There must be a disposal of a "low-cost residential unit" as defined in section 1(1)⁷² to the taxpayer's employees or the employees of an "associated institution" as defined in the Seventh Schedule to the Act.⁷³
- The sale must not be subject to any conditions other than that upon termination of employment or failure to repay the loan amount for a period of three months, the employee must dispose of the residential unit to the taxpayer (or an associated institution in relation to the taxpayer) for an amount equal to the actual cost (other than borrowing or finance costs) to the employee.⁷⁴
- The employee must not pay interest to the taxpayer on the amount owing to the taxpayer.⁷⁵
- The taxpayer must sell the residential unit at a consideration that is not greater than the actual cost to the taxpayer of that residential unit (including the land on which it is erected). In determining the taxpayer's actual cost for this purpose no account must be taken of borrowing and finance charges.⁷⁶

Example 10 – Allowance on the sale of a low-cost residential building

Facts:

An employer erects a house for R100 000 on land costing R20 000. In year 1 the employer disposes of the house to an employee for R120 000 on a non-interest bearing loan account provided by the employer, repayable over 20 years. The amount of the outstanding loan was R120 000 at the end of year 1 and R114 000 at the end of year 2.

Result:

The employer is entitled to the following allowances under section 13sept:

Year 1

The employer may claim a deduction calculated at 10% of R120 000 = R12 000.

⁷¹ Section 13sept(2).

⁷² See 2.7.3 for the definition.

⁷³ Section 13sept(1).

⁷⁴ Section 13sept(3)(a).

⁷⁵ Section 13sept(3)(b).

⁷⁶ Section 13sept(3)(c).

Year 2

The employer may claim a deduction calculated at 10% of R114 000* = R11 400.

* R120 000 – R6 000

(c) Recoupment

The deduction will be recouped every time the loan capital is repaid by the employee. The recoupment will be limited to the lesser of –

- the amount so paid;⁷⁷ or
- the amount allowed as a deduction in the current year and any previous year of assessment.⁷⁸

The excess not allowed in any year of assessment will be recouped in any following year of assessment when another amount of the loan capital is repaid by the employee.

Example 11 – Recoupment of the deduction for the sale of a low-cost residential building

Facts:

An employer erects a house for R100 000 on land costing R20 000. In year 1 the employer disposes of the house to an employee for R120 000 on a non-interest bearing loan account provided by the employer, repayable over 20 years. In year 2 the employee repays R25 000 of the loan. No further repayments are made by the employee in year 3

Result:

The employer will have the following tax consequences for years 1 to 3:

Year 1

The employer may claim a deduction calculated at 10% of R120 000 = R12 000.

Year 2

The employer may claim an deduction calculated at 10% × (R120 000 – R25 000) = R9 500. However, of the R25 000 repaid only an amount of R21 500 is recouped in year 2 (R12 000 allowed in year 1 + R9 500 allowed in year 2). The balance of R3 500 on the repayment of R25 000 is carried forward to the following year.

Year 3

The employer may claim an allowance of 10% of R95 000 = R9 500.

R3 500 is recouped and added to the employer's taxable income.

⁷⁷ Section 13sept(4)(a).

⁷⁸ Section 13sept(4)(b).

2.8 Allowance on farm buildings

2.8.1 Farm buildings used in farming operations

Under paragraph 12(1)(f) of the First Schedule a taxpayer who incurs expenditure on the erection of, or extensions, additions or improvements to, buildings used in connection with the taxpayer's farming operations, other than those used for domestic purposes, may qualify for a deduction of that expenditure. The term "farming operations" is not defined in the Act. The question whether a person is carrying on farming operations is one of fact and is determined on a case-by-case basis.

The building so erected must be brought into use directly in connection with the farming operations. No deduction is allowable on expenditure incurred on converting or reconstructing a building to serve farming needs if it was not used in connection with the farming operations before the conversion or reconstruction.

There is no limit on the qualifying amount of the expenditure claimed on any one building. However, buildings erected for the domestic use of employees will not qualify. The deduction may be claimed against farming income in the year in which the expenditure was incurred and not necessarily in the year in which the building is brought into use.

2.8.2 Housing for farm employees

An allowance was granted under paragraph 12(5) of the First Schedule to a farmer for the erection of, or extensions, additions or improvements (other than repairs) to, any buildings used for the domestic purposes of any one of the farmer's employees. It was limited to R6 000 per any one employee or the employee's family occupying a dwelling.

This provision was deleted from the Act by the Revenue Laws Amendment Act. 60 of 2008 and is thus only applicable to housing the erection of which commenced before 21 October 2008. As from 21 October 2008 farmers can claim a deduction under section 13sex (see **2.7.3**).

For the purposes of this provision "employees" are defined in paragraph 12(4)(a) of the First Schedule as follows:

"[E]mployees", in relation to any farmer, means persons employed by that farmer in connection with his or her farming operations, but does not include his or her relatives or, where the farmer is a company, the holders of shares (or the relatives of holders of shares) in that company or in any company which is associated with it by virtue of the holding of shares.

Example 12 – Allowance on the erection of farm buildings occupied by employees

Facts:

A farmer erects two buildings on a farm for R20 000 each. Building A is occupied by one employee and building B is occupied by two employees. None of the employees are related to the farmer.

Result:

The farmer may claim an allowance on building A to a maximum of R6 000 and on building B to a maximum of R12 000(2 × R6 000).

Note: If the two employees are related to each other, SARS will not allow the deduction for each employee. The two employees are treated as one family unit and only one deduction of R6 000 will be allowed.

2.8.3 Recoupment

Should a dwelling, on which an allowance has been allowed, no longer be occupied by a taxpayer's employee (or the employee's household), the deduction less an amount equal to one-tenth of that deduction for each completed year (not exceeding 10 years) during which the dwelling was occupied by the employee, is included in the taxpayer's income.

Except for the above recoupment, deductions allowed to a farmer under paragraph 12(1)(f) of the First Schedule are not subject to taxation if recovered or recouped.

2.9 Allowance on buildings in special economic zones

Section 12S provides for an allowance of 10% of the cost of any new and unused building owned by the taxpayer, or any new and unused improvement to any building owned by the taxpayer, if that building or improvement is wholly or mainly used by the taxpayer for purposes of producing income within a special economic zone in the course of its trade, excluding the provision of residential accommodation.

For more information on the allowance under section 12S refer to the *Guide to Special Economic Zones* which will be available on the SARS website.

3. General recoupment provision

A recoupment means that what was once allowed as a deduction is added back to the taxpayer's income. Under section 8(4)(a) there must be included in a taxpayer's income (subject to certain exceptions) all amounts allowed to be deducted or set off in the current or any previous year of assessment that have been recovered or recouped during the current year of assessment.

Section 8(4)(a) will apply upon the sale or disposal of the building concerned in excess of its income tax value. This general recoupment provision is in addition to any recoupment provision specifically provided for within a particular deduction or allowance section. For commentary on the specific recoupment provisions see the commentary on the specific deductions or allowances in this guide.

Section 8(4)(a) does not apply to farming expenditure that was allowed as a deduction under paragraph 12(1) of the First Schedule.

Any disposal of assets on which a deduction has been allowed under paragraph 12(1) or (1A) and which has become a movable asset is recouped under the provisions of paragraph 12(1B) or (1C).

4. Capital gains tax

The sale of a building could trigger capital gains tax. For a more in-depth discussion of capital gains tax and its implications, see the *Comprehensive Guide to Capital Gains Tax* (Issue 4) available on the SARS website.

5. Objection and appeal

A taxpayer who has claimed a deduction or allowance discussed in this guide and who is not satisfied with an assessment issued by SARS, for example, when an adjustment has been made by SARS to the allowance claimed in the taxpayer's return of income, may object to the assessment.⁷⁹

The objection must –

- be lodged using the prescribed form;
- state the grounds on which the objection is lodged; and
- reach the Commissioner within 30 business days after the date of issue of the assessment.

The Commissioner will either –

- allow the objection;
- disallow the objection; or
- allow the objection in part and disallow the other part.

A taxpayer has a right to appeal against the disallowance of an objection that is disallowed in full or in part. The appeal must be delivered to the Commissioner within 30 business days from the date of the disallowance of the objection.

Further information on the objection and appeal procedures is set out in the *Guide on Tax Dispute Resolution* and is available on the SARS website or from a SARS branch.

6. Retention of records

Section 29(1) of the Tax Administration Act 28 of 2011 provides that a person must keep the records, books of account or documents that –

- enable the person to observe the requirements of a tax Act;
- are specifically required under a tax Act; and
- enable SARS to be satisfied that the person has observed these requirements.

The records should be retained by the person for a period of five years from the date of submission of the return.⁸⁰ Section 30(1) of the Tax Administration Act provides that the records referred to in section 29 must be kept or retained in –

- their original form in an orderly fashion and in a safe place;
- the form, including electronic form, as may be prescribed by the Commissioner in a public notice;⁸¹ or
- a form specifically authorised by a senior SARS official.

⁷⁹ Section 104 of the Tax Administration Act.

⁸⁰ Section 29(3)(a) of the Tax Administration Act.

⁸¹ See GN 787 in GG 35733 of 1 October 2012.

These records should be available for inspection purposes by a SARS official to verify compliance with the requirements as explained above, or for purposes of an inspection, audit or investigation.⁸²

Records which are relevant to an audit or investigation or an objection or appeal must be retained until the audit or investigation is concluded or until the assessment or the decision becomes final in the case of an objection or appeal (in case the five year retention period is exceeded).⁸³

7. Conclusion

The Act currently makes provision for the following building allowances:

- Section 13 – Buildings used in a process of manufacture, research and development or a similar process
- Section 13*bis* – Buildings used by hotel keepers
- Section 13*quin* – Commercial buildings
- Section 13*quat* – Buildings in urban development zones
- Section 13*sex* – Residential units
- Section 13*sept* – Deduction for loans to employees to acquire low-cost housing from employers
- Paragraph 12(1)(f) of the First Schedule – Buildings used in farming operations

A number of other building allowances discussed in this guide have been discontinued but will be relevant to taxpayers still claiming such allowances on buildings acquired before the relevant provisions were discontinued.

Some of the sections which make provision for building allowances or deductions contain their own recoupment provisions. The general recoupment provisions of section 8(4)(a) will also apply in most cases unless excluded, as in the case of farm buildings.

Since building allowances tend to be claimed over extended periods of up to 50 years taxpayers must retain proper records of the cost of buildings and the allowances claimed.

⁸² Section 31 of the Tax Administration Act.

⁸³ Section 32 of the Tax Administration Act.