

REPUBLIC OF SOUTH AFRICA

SOUTH AFRICAN REVENUE SERVICE: INLAND REVENUE

OFFICE OF THE COMMISSIONER FOR INLAND REVENUE

PRACTICE NOTE: NO 1 DATE: 4 APRIL 1996

INCOME TAX: PROVISION FOR SHIP REPAIRS IN TERMS OF SECTION (1)(c) OF THE INCOME TAX ACT

1. Section 14(1)(c) of the Income Tax Act (the Act) provides for a deduction from the income of a person referred to in section 9(1)(c) of the Act in respect of any expenditure which such person can satisfy the Commissioner for Inland Revenue he is likely to incur within five years from the end of the year of assessment in question on repairs to any ship used by him for the purpose of his trade. The allowance is additional to the normal annual expenditure incurred in keeping the ship in running repair and is designed to cover the cost of heavy repairs in overhauling and refitting which at the time the allowance was introduced was understood normally to be effected about once in every five years.
2. Practice Note No. 26 dated 18 August 1994 was issued with a view of clarifying the Commissioner's practice regarding the provision for ship repairs in terms of section 14(1)(c) of the Act. It has come to the attention of this office that the practice note is being interpreted in a manner which results in an allowance being claimed which exceeds that which was intended. Practice Note No.26 is, therefore, hereby withdrawn and replaced by this practice note with effect from 4 April 1996.
3. It is evident that the allowance contemplated in section 14(1)(c) of the Act cannot be compartmentalised into fixed cycles of five years. In the determination of the allowance at the end of any particular year of assessment regard must be had to the expenditure likely to be incurred during the next five years. In other words, the allowance must be recalculated at the end of each year of assessment in relation to the expenditure likely to be incurred during the next five years, the estimation being subject to revision from year to year.
4. The accepted method for the calculation of the expenditure to be allowed as a deduction from income is the following:

4.1 In the current year of assessment the expenditure likely to be incurred on heavy (extraordinary) repairs in each of the next five years must be estimated. The total amount to be allowed in the current year of assessment (year 0) of the estimated expenditure will be:

- 100% of the estimated expenditure to be incurred in year one
- 50% of the estimated expenditure to be incurred in year two
- 33.3% of the estimated expenditure to be incurred in year three
- 25% of the estimated expenditure to be incurred in year four
- 20% of the estimated expenditure to be incurred in year five

5. The following examples illustrate the calculation of the allowance:

5.1 Year 0: Estimated expenditure likely to be incurred on heavy (extraordinary) repairs during the period ending five years after the current year (year 0).

Vessel	Y1	Y2	Y3	Y4	Y5
No 1 (Estimated expenditure)	R25 000		R300 000		R50 000
No 2 (Estimated expenditure)		R150 000	R72 000		
No 3 (Estimated expenditure)	R75 000		R28 000	R150 000	
Total estimated expenditure	R100 000	R150 000	R400 000	R150 000	R50 000
Percentage to be allowed	100%	50%	33.3%	25%	20%
Allowance	R100 000	R75 000	R133 200	R37 500	R10 000

5.1.1 The allowance deductible in year 0 amounts to R355 700 (R100 000 + R75 000 + R133 200 + R37 500 + R10 000).

5.2. Year 1: Estimated expenditure likely to be incurred on heavy (extraordinary) repairs during the period ending five years after the current year (year 1)

Vessel	Y2	Y3	Y4	Y5	Y6
No 1 (Estimated expenditure)		R300 000		R50 000	R10 000
No 2 (Estimated expenditure)		R150 000	R20 000		R70 000
No 3 (Estimated expenditure)	R28 000		R15 000		R20 000
Total estimated expenditure	R28 000	R450 000	R35 000	R50 000	R100 000
Percentage to be allowed	100%	50%	33.3%	25%	20%
Allowance	R28 000	R225 000	R11 656	R12 500	R20 000

5.2.1 The allowance deductible in the current year (year 1) amounts to R297 156 (R28 000 + R225 000 + R11 656 + R12 500 + R20 000). The allowance of R355 700 (see par 5.1.1) deducted in the preceding year (year 0) must be included in the income of the taxpayer in the current year (year 1).

6. As the quantum of the allowance is at the discretion of the Commissioner, the taxpayer, if he wishes to claim it, will have to furnish the necessary information to the relevant Receiver of Revenue to enable him to calculate the allowance.

7. Since it is difficult to define "heavy repairs" (as the conditions relevant to, or the extent of, the repairs will vary from ship to ship), a useful guideline would be to distinguish between "ordinary running repairs", which are normally incurred every year, and "extraordinary repairs", which are expected to occur at intervals of more than a year.

COMMISSIONER FOR INLAND REVENUE

PRETORIA