

https://dspace.org/

Capital allowances in terms of South African tax law

Coetzee, Hendrik Andries

2015-02-09
http://hdl.handle.net/10539/16942

Downloaded from a DSpace repository. https://dspace.org/

CAPITAL ALLOWANCES IN TERMS OF SOUTH AFRICAN TAX LAW

Hendrik Andries Oosthuizen

A dissertation Submitted to the Faculty of Commerce
University of the Witwatersrand, Johannesburg
for the Degree of Master of Commerce

June 1984

DECLARATION

I declare that this dissertation is my own, unaided work. It is being submitted for the degree of Master of Commerce in the University of the Witwatersrand Johannesburg. It has not yet been submitted before for any degree or examination in any other University.

HENDRIK ANDRIES COETZEE

22 June 1984

CONTENTS

		Page
ABSTRACT		xvi
TABLE OF CASES	Supreme Court and others	xix
	Special court for hearing income tax appeals	xxx
	PART I	
	PRIVILEGED CLASSES OF TAXPAYERS	1
Chapter 1	MANUFACTURERS	
	Machinery or plant - initial allowance	3
	Investment allowance	7
	Machinery or plant - investment allowance	11
	Buildings	12
	Building annual allowance	12
	Building investment allowance	18
Chapter 2	INDUSTRIALISTS IN REGIONAL DEVELOPMENT AREAS	21
	Regional development incentives	25
	Development regions	31
	The incentives	33
	Incentives in Metropolitan areas	33
	Who qualifies for incentive allowances	33
	Capital allowances	35
	Rail rebate on outgoing goods	35
	Rail Rebate on incoming goods	35
	Road transportation - own vehicles	36
	Rebate on private road transportation	36
	Rebate on harbour services	36
	Electricity subsidy	36

		Page
	Subsidy on housing for key personnel	37
	Training rebate in cash	37
	Special tender preferences	38
	Labour incentive	38
	Interest subsidy	38
	Rental subsidy	39
	Relocation costs	39
Chapter 3	HOTELKEEPERS	41
	The nature of an hotel	42
	Hotel equipment - initial allowance	46
	Hotel equipment - investment allowance	47
	Hotel buildings	48
Chapter 4	PROCESS OF MANUFACTURE	53
	Meaning of "process of manufacture"	53
	Manufacture v alterations	55
	Manufacture v assembly	56
	Manufacture v preparation	57
	Manufacture v repair	58
	Use of labour and machines with skill and experience	59
	Change in Utility	60
	Process as one in a series	62
	Difference in nature of product	64
	Change in immovable property	66
	Volume of production	67
	Process of manufacture - summary of judicial interpretation	69
	Commencement of the process	69
	Directly in a process of manufacture	74
	New machinery	76

		Page
	Qualification - who must carry on process	79
	Cost of buildings or improvements	80
	Pre-production interest	84
	Trade and income from trade	86
	Location of trade	88
	Interpretation	89
	Privileged classes of taxpayers	91
	Undistributed profits tax	91
	Recoupment - UPT	94
	Recoupment of initial allowance	96
	Recoupment of investment allowance	97
	Scrapping allowance	97
	Tax implications of leasing instead of purchasing	98
	The element of time - illustration	99
	The availability of a tax base	102
	Cost of machinery or plant	106
	Departmental practice	110
	Practical application	110
Chapter 5	TAXPAYERS ERECTING RESIDENTIAL UNITS	119
	Nature of a residential unit	120
	Locality of residential unit	122
	Capital allowances	122
	Residential building annual and initial allowances	123
	Recoupment	123
	Scrapping	126
Chapter 6	SHIPBUILDERS AND OWNERS OF SHIPS	127
	The nature and meaning of a "ship"	127
	The nature and meaning of a "ship" under English law	131

		Page
	Nature and meaning of "ship" - conclusion	138
	Ship and its appurtenances	139
	Movable property	141
	Machinery or plant	141
	Capital allowances	142
	Annual allowance	142
	Special initial allowance	144
	Allowance in respect of future repairs	146
	Adjustable cost	147
	Recoupment of allowance	147
	Scrapping allowance	149
	Subsidiary companies	157
Chapter 7	OWNERS OF AIRCRAFT	160
	Brief history of flight	160
	Nature of an aircraft	161
	Capital allowances	162
	Annual allowance	162
	Initial allowance	163
	Adjustable cost	165
	Recoupment	174
	Scrapping allowance	177
Chapter 8	EXPORTERS CARRYING ON A BENEFICIATION PROCESS	178
	The nature of the beneficiation allowance	180
	Beneficiation process v process of manufacture	184
	The amount of the beneficiation allowance	185
	Recoupment of the beneficiation allowance	185
	Scrapping allowance	186
	Machinery or plant	186

		Page
Chapter 9	MINERS	187
	The meaning of "mining operations"	188
	Mining operations v process of manufacture	191
	Mining v processing - common law	193
	Mining v processing - foreign countries	195
	Summary of decisions under common law and in foreign cases	199
	Mining operations - uranium and natural oil	199
	Mining operations v process of manufacture - conclusion	203
	"Minerals" - under common law	204
	"Minerals" - under tax law	205
	"Minerals" under foreign tax law	207
	"Minerals" - conclusion	209
	Capital expenditure incurred by a miner	209
	The nature of capital expenditure	214
	Capital expenditure - multiple mining operations	218
	Capital expenditure - locality of assets created	219
	Special capital allowance	221
	Recoupment of capital allowances	224
	Prospecting expenditure	227
	Capital expenditure on change of ownership	229
Chapter 10	FARMERS	234
	Farming operations	234
	Summary of judicial interpretations - "farming operations"	240
	Income derived from farming operations	241
	Speculation in livestock	244
	Horse racing	245

		Page
	Donation and inheritance	246
	Fructus	247
	Summary of South African interpretations - "derived from farming operations"	249
	Farming operations v process of manufacture	249
	Summary of judicial decisions	254
	Capital expenditure	254
	Expenditure must be incurred by the farmer	264
	Expenditure incurred "in respect of"	266
	Buildings used in connection with farming operations	269
	In connection with farming activities	276
	Other buildings	279
	Machinery, implements, utensils and articles	279
	Recoupment of capital expenditure	283
	Plantation farmers - capital expenditure	290
	Plantation farmers - recoupment of capital allowances	291
Chapter 11	CO-OPERATIVES	292
	Co-operatives v companies	293
	Types of co-operatives	295
	Primary agricultural co-operatives	296
	Primary special farmers' co-operatives	297
	Primary trading co-operatives	298
	Central and federal agricultural co-operatives	298
	Central and federal special farmers' co-operatives	299
	Central and federal trading co-operatives	299
	Membership	300
	Capital allowances	300

		Page
	Storage building	302
	Agricultural products	303
	Primary process	305
	Structures of a permanent nature	309
	Annual allowance	310
	Investment allowance	314
	Cost of building	315
	Machinery initial allowance	316
	Machinery investment allowance	317
	Cost of machinery or plant	319
	Loan repayment allowance	320
	Recoupment	326
	Scrapping	327
	Amalgamations of co-operatives	327
	Location of qualifying assets	331
	Machinery or plant	332
Chapter 12	OWNERS OF NATIONAL KEY POINTS	334
	Expenditure incurred	335
	"Place or area"	336
	"Directly"	337
	The owner of a national key point	340
	Recoupment of security expenses	341

INTELLECTUAL PROPERTY

Chapter 13	PATENTS	345
	Brief history	345
	Nature of patents	346
	Inventive steps	349
	"Capable of being used"	349
	Categories of excluded matter	350
	Assignment	351

		Page
	PART II	
Chapter 14	DESIGNS	352
	Nature of a design	352
	Duration of design protection	354
Chapter 15	TRADE MARKS	355
	Brief history	355
	The nature of trade marks	358
	Validity of a trade mar	360
	Distinctiveness of a t: le mark	362
	Duration or "life" of a trade mark	363
	Registered users of trade marks (Section 48 of the Trade Marks Act)	363
	Assignment of a trade mark (Section 49 of the Trade Marks Act)	365
	Deemed trade mark	366
	Defensive trade marks (Section 53 of the Trade Marks Act)	367
Chapter 16	COPYRIGHTS	368
	Brief history	368
	Works eligible for copyright	370
	Copyright of computer programs	372
	Nature of copyright	373
	Duration of copyright protection	374
Chapter 17	SIMILAR PROPERTY AND OTHER PROVISIONS	377
	Similar property	377
	Acquisition of intellectual property	380
	Royalty payment	381
	Lump sum payment	381
	Capital payment	381
	Character of outright assignment	381

		Page
	Premium or consideration in the nature of a premium	383
	Capital allowance - outright purchase	384
	The amount of the allowance	385
	Exporters	387

PART III

KNOWLEDGE

Chapter 18	"KNOW-HOW"	391
	Nature of "know-how"	391
	Secret processes	395
	Secret processes and "similar property"	395
	Premium or consideration in the nature of a premium	397
	Impa.ting knowledge	398
	Directly or indirectly connected	399
	Active and passive elements	400
	Amount of the allowance in respect of premiums	400
	Acquisition of "know-how"	401
	"Connected with"	402
	Used in the production of income	403
	Amount of the allowance	403
	Recoupment of allowances	404
	Scrapping allowance	406
	Relief to lessors	406
Chapter 19	SCIENTIFIC RESEARCH	407
	Nature of scientific research	407
	Scientific activities	408
	Research and development	408

		Page
	Distinction between development and implementation	411
	Research - related scientific activities	412
	Non-research related scientific activities	413
	Research fields	414
	Capital allowances	414
	Expenditure of a capital nature	419
	Certificates by the Council for Scientific and Industrial Research (CSIR)	424
	Recoupment of scientific research expenditure	424
	Recoupment	426
	Scrapping allowance	427
	Conclusion	427
Chapter 20	POST-GRADUATE STUDIES	430
	Expenditure incurred	433
	Travelling	434
	Living and subsistence	435
	Departmental practice	435
	1983 Amendment	439
	PART IV	
Chapter 21	WEAR AND TEAR	442
	Commissioner's discretion	443
	Basis used in the calculation of wear and tear	445
	Value of any machinery, implements, utensils and articles	447
	Machinery, implements, utensils and articles	452
	Buildings	455
	Plant or machinery	456
	Structures	467

		Page
	Articles	468
	Movables attached to immovables	469
	Weirs	473
	Railway lines	473
	Other structures	475
	Carports	477
	Subject matter attached or affixed to buildings or structures of a permanent nature	478
	Improvements	486
	Used by the taxpayer for the purposes of his trade	487
	"By reason of wear and tear"	488
	"During the year of assessment"	491
	Recoupment of wear and tear	492
	How recoupments take place	493
	Date on which recoupment takes place	494
	Amount of recoupment	495
	Privileged classes of taxpayers	497
	Capital nature of recoupment	500
	"Lock stock and barrel" transactions	502
	Incidence of inflation	502
	Departmental practice	504

PART V

Chapter 22	SCRAPPING	506
	Special features	506
	The meaning of "scrapping"	510
	Physical deterioration - during the course of carrying on a trade	512
	Decision to scrap and cessation of use	516
	Owner of assets	518
	For the purposes of trade	518
	During the year of assessment	519

		Page
	PART VI	
Chapter 23	LEASEHOLD IMPROVEMENTS	522
	Limitations	523
	Leveraged leasing	527
	Lease agreement	529
	Period of lease	530
	The amount of the allowance	530
	Obligation	533
	Implied obligation	534
	Variations to lease agreements	536
	Proportionment	537
	The tax treatment of the lessor	538
	Relief granted to the lessor	540
	Recoupment	543
	Scrapping allowance	547
	PART VII	
Chapter 24	REPAIRS	551
	Meaning of "repairs"	551
	Actually incurred	553
	Occupied for the purposes of trade	554
	In respect of which income is receivable	554
	Beetles	555
	For the purpose of trade	556
	Repairs v reconstruction and improvements	557
	Intention	570
	Notional cost of repairs	571
	Conclusion	573

Page

PART VIII

Chapter 25	LEASE PREMIUMS	576
	Meaning of "lease premiums"	576
	The tax treatment of the lessor	579
	Relief granted to lessor	580
	Recoupment	580
	Tax exempt entities	580
Annexure A	Industrial development points	583
Annexure B	Minimum requirements for hotels	589
Annexure C	Minimum differencial grading requirements for hotels	601
Annexure D	Hotel grading factors and points	613
Annexure E	Research fields	630
Annexure F	Departmental practice - wear and tear	659
BIBLIOGRAPHY		668
INDEX		673

ABSTRACT

As a general rule, expenditure of a capital nature does not rank for deduction in the determination of taxable income.

Section 11(a) of the Income Tax Act, 1962, as amended (the Act) provides:

"For the purpose of determining the taxable income derived by any person from carrying on any trade within the Republic, there shall be allowed as deductions from the income of such person so derived -

(a) expenditure and losses actually incurred in the Republic in the production of the income, provided such expenditure and losses are not of a capital nature".

The Act does, however, provide in specific cases for the deduction of capital expenditure.

To a large extent, therefore, this dissertation is concerned with the nature and the extent of the special capital allowances with emphasis on the approach by the Courts, and practice adopted by the Revenue Department. The distinction blurred, as it often is, between expenditure of a capital nature and revenue expenditure falls outside the scope of this study.

Part I covers the incentives which are available to specific classes of taxpayers. Certain taxpayers are allowed to deduct capital expenditure from their income in the determination of taxable income. To this extent these taxpayers are placed in a privileged position. Various expressions relating to these taxpayers are not defined in the Act. One such expression is a "process of manufacture". An analysis of the decided cases has

revealed twelve different factors which the courts have considered in the interpretation of the expression. One of the main difficulties with "process of manufacture" seems to be the point at which process of manufacture commences, especially in relation to miners and farmers. Should a wine farmer, for instance be classed as a farmer or an industrialist? If the making of wine is a process of manufacture then the farmer is also an industrialist who would qualify for other incentives not normally available to farmers. However, the Act is not clear on what constitutes "process of manufacture".

Part II covers capital allowances available under the Act for intellectual property. Intellectual property consists of patents, designs, trade marks and copyrights. The Act refers to such intellectual property "or any other property which in the opinion of the Commissioner is of a similar nature". A detailed examination of each branch of intellectual property is made to identify "similar property".

Part III covers the deduction of expenses incurred in respect of knowledge. Knowledge is dealt with under three headings - know-how, scientific research and post-graduate studies. The deduction of capital allowances in respect of scientific research relates to the field of natural or applied science. The field of natural science is very wide and includes engineering, architecture and quantity surveying. It would therefore seem possible that the professions engaged in those fields, for instance, could benefit by the tax allowances available in respect of scientific research.

Parts IV to VIII covers capital allowances available to most, and not only specific classes of taxpayers . Allowances for wear and tear, scrapping, leasehold improvements, lease premiums and repairs are discussed. The main issue in respect of the wear and tear allowance is the judicial interpretation of the expression "machinery or plant". One problem is that wear and tear is not allowed "buildings or other structures or works of a permanent nature". This leads to the question of machinery or plant re "machinery or plant" or whether they manner as to loo : their identity to become "building". The court cases have laid down a number of tests in this regard, such as intention, and these are discussed and related to the judicial interpretation of "machinery or plant" under common law.

The author wishes to express his thanks to the following persons for their advice, encouragement and assistance towards the preparation of this dissertation:

- The Department of Inland Revenue for permission to make use of the A F Corbett Library.
- Professor E B Broomberg for his advice and encouragement and many valuable suggestions.
- The partners of Alex. Aiken & Carter for their assistance in the production of the manuscript, and the permission to make use of their word processor and stationery.
- A L H Mayne for his proof-reading of the manuscript.
- Miss G Smith for her patient and painstaking typing and retyping of the manuscript.
- Cynthia, my wife, for her extreme patience and tolerance.

TABLE OF CASES

SUPREME COURT AND OTHER	Page
A v Cot 1954(1) SA 38(SR), 19 SATC 29	533
African Detinning Works (Pty) Ltd, SIR v, 1982(1) SA 797(AD), 42 SATC 134	486
African Products Manufacturing Co Ltd, CIR v, 1944 TPD 248, 13 SATC 164	558 569
Afrikaanse Verbond Begrafnis Onderneming Beperk v CIR 1950 (3) SA 209 (A), 16 SATC 401	252 260
Ambleside Tobacco Grading Company (Pvt) Ltd v Abrahamson No 1959 (1) SA 295 (R)	236 251
Anglo American Corporation of SA Ltd v COT (1) SA 973 (RAD), 37 SATC 45	260
B v COT 19 SATC 353	572 573
Bacher Aron & Co (Rhodesia) Ltd, Minister of Finance v, 1956(1) SA 63 (SR), 20 SATC 321	53 55 56
Badenhorst & Others v CIR 1955 (.) SA 207 (N), 20 SATC 39	2 291
Barclay, Curle & Co Ltd, CIR v, (1969) IWLR 675, 45 TC 221	81 461
Barron and Others v Sachar 1947 (2) SA 1049	243
Bells Trust v CIR 1948 (3) SA 480 (A), 15 SATC 255	275
Bellville-Inry Edms Bpk v Continental China (Pty) Ltd 1976 (3) SA 583 (C)	182
Beneke & Another, R v, 1957(1) SA 594, 21 SATC 183	59 251
Benson v Yard Arm Club Ltd (1979) STC 266, (1979) 2 All ER 336	463
Berg, Rex v, 6 SATC 320	488
Berold, Rex v, 1943 CPD 344	253
Blom and Another, Rex v, 1951 (1) SA 708(T)	194
Blumberg & Sulski v Brown & Freitas 1922 TPD 130	242

TABLE OF CASES

SUPREME COURT AND OTHER (Cont) Page

Boksburg Brick and Fire Clay Co Ltd v CIR 1941 TPD 232 12 SATC 225, 189 190 191 206
Booysen's Estates, COT v 1918 AD 576, 32 SATC 10 430
Broken Hill (Proprietary) Limited v FCT 1969 1 ATR 40 82 197 230 454 464
Brown v Burnley Football and Athletic Co Ltd (1980) STC 424 463
Bryant v Minister of Labour and Minister of Justice 1943 TPD 205 217 250
Buglers Post (Pty) Ltd v SIR 1974 (3) SA 28 (A), 36 SATC 71 2 234 268
Butcher Bros (Pty) Ltd, CIR v, 1945 AD 301, 13 SATC 21 538 576 578
C v COT 1981 (2) SA 298(ZA), 43 SATC 9 469 485
Cadac Engineering Works (Pty) Ltd, SIR v, 1965 (2) SA 511 A, 27 SATC 61 420
Caladonian Railway Co v Banks 1880, 18 SLR 85, 1 TC 487 489
Californian Copper Syndicate v Inland Revenue 1904, 41 SCLR 691 246
Caltex (Africa) Ltd v Director of Valuations 1961 (1) SA 525 (C) 288
Cape Brandy Syndicate 1921 1 KB 64 89 90
Cape Explosives Works v South African Oil and Fat Industries Ltd 1921 CPD 244 272
Cape Lime Company Ltd, SIR v, 1967 (4) SA 226(A) 29 SATC 131 70 72 192

TABLE OF CASES

SUPREME COURT AND OTHER (Cont) — Page

Cape Truck Co, Commissioner of Customs v, 15 SATC 474 459
Carfax Waste Paper Co Ltd v Minister of Labour (1968) 1 All ER 1041 63 308
Carlis v Oldfield, 4 HC 385 141
Carltonville Motors (Pty) Ltd, CIR v, 1964(3) SA 581 AD, 26 SATC 195 535
Cate v Devon and Exeter Constitutional Newspaper Co (1889) 40 Ch D 500 374
Champions Ltd v van Staden Bros and Another, 1929 CPD 330 287 471
Charkay Properties (Pty) Ltd, SIR v, 1976 (4) SA 872 (AD), 38 SATC 159 468 477 483 387
City Deep Limited, CIR v, 1924 AD 298, 1 SATC 18 377 395 433
Clayton v COT 1923, SR 105 553
Cole Bros Ltd v Phillips (1980) STC 518 464
Coltman v Chamberlain (1890) 25 QB 328 140
Consolidated Citrus Estates Ltd, SIR v, 1976 (4) SA 500, 38 SATC 126 339
Cook v Beach Station Caravans (1974) STC 402 (1974) 3 All ER 159 463
Corelli v Gray 1912 29 TLR 570 1913, 30 TLR 116 373
Crown Mines Ltd, CIR v, 1923 AD 121 267
CTC Bazaars (SA) Ltd, Rex v, 1943 CPD 334 253
Daphne v Shaw (1927) 11 TC 256 460 461
D'Arcy v Allen 11 Co (Rep 846)
Dawson v Counsell (H M Irspector of Taxes) 1922 TC 149 245
Delfos, CIR v, 1933 AD 242 89
Dibowitz v CIR 1952 (1) SA 55 (AD) 90
Die Olifantsrivierse Ko-operatiewe Wynkelders Bpk, SBI v 1976(3) SA 261 (AD), 38 SATC 79 87

TABLE OF CASES

SUPREME COURT AND OTHER (Cont) Page

Dixon v Fitch's Garage Ltd (1975) STC 480, (1975) 3 All ER 455 463
Dryburgh v The Lord Advocate 1926 Scots Law Times, p99 217
Dun & Bradstreet (Pty) Ltd v SA Merchants Combined Credit Bureau (Cape) (Pty) Ltd 1968 (1) SALR 209 396
du Preez v Steenkamp 1926 TPD 362 242
E S & A Robinson (Rhodesia) (Pvt) Ltd v Macintyre No 1962(2) SA 638, 24 SATC 767 59
Earl of Derby v Aylmer 6 TC 665 457
Eaton Hall (Pty) Limited, SIR v, 1975 (4) SA 954(AD), 37 SATC 343 83 84 338
Eaton v Registrar of Deeds 1890 7 SC 249 342 451
Edwards v Barberton Mines 1961 (1) SA 187(T) 288 471
EJ Bowman (London) Ltd and Others, T Oertli AG v, (1957) RPC 388 358
Ernst v CIR 1954 (1) SA 318 (A), 19 SATC 1 2 265 267 271 272
Evans Medical Supplies Ltd v Moriarty (H.M. Inspector of Taxes) 37 TC 540 392 396
Ex Parte Beal 1867 3 QB 387 374
Ex Parte Erasmus 1968 (4) SA 788 (T) 205
Ex Parte Ferguson and Hutchinson (1870) 6 QB 280 137
Falcon Investments Ltd v Birnam (Suburban) (Pty) Ltd 1973 (4) SA 384 (A) 182 204 205 207
Fisher's Executrix, Union Government v, 1921 TPD 328 342
Francis Day and Hunter v Bron (Trading as Delmar Publishing CO) 1963 2 All ER 16 24 373 374
Franz Hanfstaengl v H R Baines & Co Ltd and E J Mansfield 1895 AC 20 374

TABLE OF CASES

SUPREME COURT AND OTHER (Cont) Page

Gale v Laurie and Others 5 B & C 156 139
Gault v Behrmann 1936 TPD 38 287 471
George Forest Timber Co Ltd, CIR v, 1924 AD 516, 1 SATC 20 209 342 415
Giesken and Giesken, Rex v, 1947 (4) SA 561 (AD) 235 251
Glen Anil Development Corporation Limited v SIR 1975(4) SA 715 (AD), 37 SATC 319 90
Gordon's Hotel Ltd, LCC v, 114 LT 1126 276
Gray No v Assistant Master & Another 1979(3) SA 427, (High Court of Zimbabwe), 41 SATC 117 66
Great Western Railway v Carpalla United China Clay Company 1909 1 Ch 218 207
Grootvlei Proprietary Mines Ltd v CIR 1952 (4) SA 440 (A), 18 SATC 231 224 225
Guardian Assurance Holdings (SA) Ltd, SIR v, 1976 (4) SA 522 (A), 38 SATC 111 433
Guernsey & Foreign Investment Trust Ltd v CIR 1938 CPD 158, 9 SATC 390 188
H v COT 1981 (2) SA (ZA), 43 SATC 22 238
Hampton v Forte Autogrille Ltd (1980) STC 80 463
Handley Page v Butterworth 19 TC 328 392
Hanfstaengl v Newnes 1894 3 Ch 109 374
Hastings v Cogavin 1904 2 Ir R 529 267
Hatrick & Co Ltd v The King 128 LT 430 276
Hayne and Co v Kaffrarian Steam Mill Co Ltd 1914 AD 363 229 282 335
Henderson, FCT v 1969 1 ATR 133 189
Herbert Morris Ltd v Saxelby 1916 1 AC 688 392
Hersamer (Pty) Ltd, SIR v, 1967(3) SA 177(AD), 29 SATC 53 53 55 61 62 63 68

TABLE OF CASES

SUPREME COURT AND OTHER (Cont) Page

Highland Railway Co v Balderston 1889, 16 R 950, 2 TC 425 555
Hobday v Nicol 1944(1) AER 302 467
Hogg v Parochial Board of Auchtermuchty 7 Rettie 986 2 271
ICI Australia Ltd, COT v, 1972 3 ATR 321 198
Imperial Chemical Industries of Australia and New Zealand v FCT 1 ATR 450 466
J Lyons and Co Ltd v Attorney General (1944) Ch 281 460
Jarrold v John Good & Sons Ltd (1963) 1 All ER 141, 40 TC 681 CA 463
Jones & Co v CIR 1926 CPD 1, 2 SATC 7 188
Joseph Crisfield & Sons Ltd Appn (1909) 26 RPC 837 362
Kantor v Macintyre No & Another 1958(1) SA 45 (FC), 21 SATC 407 54 59 66 251
Kerguelen Sealing and Whaling Co Ltd v CIR 1939 AD 487, 10 SATC 363 272
Knight v COT (Ratcliffe and McGrath Income Tax Decisions 1928 - 30 p 330) 245
Kramer, Rex v, 1929 TPD 173 253
KWV v Industrial Council for the Building Industry & Others 1949 (2) SA 614 (AD) 236 250 253 303 467
Koffyfontein Estates Ltd v COT 1917 TPD 259 473
Le Sueur, CIR v, 1960 (2) SA 709 (AD), 23 SATC 261 279 333 475 478 481 486
Lewis v Fothergill 5 Ch 106 194
Lombard, R v, 1948 (2) SA 31 128 235
Lurcott v Wakely and Wheeler 1911 1 KB 905 551 561 563
Macdonald Ltd v Radin NO 1915 AD 467 287 470 474 479
MacGregor TM RPC 36 364
Maden & Ireland Ltd, Hinton (H M Inspector of Taxes) v, (1959) 3 All ER 356 458 460

TABLE OF CASES

SUPREME COURT AND OTHER (Cont)	Page
Margrett v Lowestoft Water and Gas Co (1935) 19 TC 481	567
Mashaoane v Mashaoane 1962 (1) SA 628 (D & CLD)	336
Masonite Africa Ltd v Estcort Municipality 1955 (3) SA 88	302 455
McNicol v Pinch 1906 2KB 352	56
McVeigh v Arthur Sanderson & Sons Ltd (1969) 1 WLR 1143, 45 TC 273	461
Melluish v LCC 111 LT 539	276
Merchant's Marine Insurance Co Ltd v North of England Protecting & Indemnity Association (1926) 25 Lloyd LR 446	133 136
Millin v CIR 1928 AD 207, 3 SATC 170	430
Modderfontein Deep Levels Ltd & Another v Feinstein 1920 TPD 288	87
Mooi v SIR 1972 (1) SA 675 (A), 34 SATC 1	421 579
Moorreesburg Produce Co Ltd v CIR 1945, CPD 289, 13 SATC 245	493
Moreton Central Sugar Mill Co Ltd v FCT Commissioner of Taxation 1967 10 AITR 420 73 464	
Morris Motors v Lilley 9, 3 All ER 737	77
Mount Isa Mines v FCT 1955, 6 AITR 346	227
Munby v Furlong (1976) STC 72, 50 TC 491	461
Murchison Exploration and Mining Co Ltd v CIR (TPD) June 1938, 10 SATC 143	190
Murray v Imperial Chemical Industries Limited 1967 2 All ER 980	381
Musker v English Electric Co 41 TC 556	393
Mutual Life Insurance Co of New York v Ingle 1910 TPD 540	189
Myerson, CIR v, 1947 (2) SA 1243 (AD), 14 SATC 300	576
Natal Estates v SIR 1975 (4) SA 177 (A), 37 SATC 193	246

TABLE OF CASES

SUPREME COURT AND OTHER (Cont) Page

New South Wales Associated Blue Metal Quarries Ltd v FCT 1955 6 AITR 239 207
New State Areas Ltd v CIR 1945 AD 610, 14 SATC 155 415 421
Newcastle Collieries v Borough of Newcastle, 1916 AD 561 332 473
Nicholson v Chapman (1793) 2 Hy Bl 254 132
Niko, CIR v, 1940 AD 416, 11 SATC 124 502
Nlhovo, R v, 1921 AD 485 70
Northern Office Micro Computers (Pty) Ltd and Others v Rosenstein 1981 (4) SA 123 (C) 372
Nourse Mines Ltd, Union Government v, 1912 TPD 24 193 215 216
Nyasaland Quarries and Mining Co, COT v, February 1961, 24 SATC 579 189 208
Olivier v Haarhof TS 1906 471
Oosterhuizen v Oosthuizen 1903 TS 688 241 242
Overseas Trust Corporation Limited v CIR 1926 AD 444, 2 SATC 71 246
Palabora Mining Company Ltd v SIR 1973 (3) SA 819 (A) 35 SATC 159 220 420
Partington v The Attorney-General 21 LT 370 89
Pearl Assurance Co Ltd v O'Callaghan (1943) 1 All ER 624, 25 TC 211 CA 464
Polpen Shipping Co Ltd v Commercial Union Assurance Co Ltd (1942) 1 KB 162 135
Port Alfred Landing and Shipping Co v Bonnievale 3 EDC 146 141
Porterville Ko-op Landbou Maatskappy Bpk, Rex v, 195?) SA 44 (C) 236 251
Powell v The Birmingham Vinegar Brewery CO Ltd (1897) 14 RPC 720 358
Prance v LCC 122 LT 820 276

TABLE OF CASES

SUPREME COURT AND OTHER (Cont) Page

Princess Estate and Gold Mining Co v Registrar of Mining Titles 1911 TPD 1066 332

Processing Enterprises (Pvt) Ltd, COT v, 1975 (2) SA ?, (RAD) 37 SATC 109 55 62 65 306

Professional Suites Ltd v COT (High Court of Northern Rhodesia (December 1960), 24 SATC 573 536 537

Purefoy Engineering Co Ltd v Sykes Boxall & Co Ltd (1955) 72 RPC (CA) 89 373 374

Pyott Limited v CIR, 1945 AD 128, 13 SATC 121 451

Queen Slide Fasteners of SA (Pty) Ltd v Commissioner of Customs 1953(3) SA 195 (W), 19 SATC 73 53 56

Rabinowitz & Another v de Beers Consolidated Mines Ltd 1958 (3) SA 619 (AD) 268

Rand Refinery Ltd v Town Council of Germiston 1929 WLD 63 193

Raphaely, R v, 1957 (3) SA 41 465

Real Estate Land Company v United States 309 US 13, 160 ALR 1248 511

Rees v Melville (1914) 1911-1016 Mac CC 168 373

Rees v Robbins 1914 Times 6 February and 4 July 373

Reinhardt v Ricker and David 1905 TS 179 342

Reliant Tool Co, Lord Advocate v, 1968 1 All ER 162 63

Rex Tearoom Cinema v CIR 1946 TPD 338, 14 SATC 76 534 535

Rhodesian Railways Limited and Others v COT 1925 AD 438, 1 SATC 133 473 474 571

Ridgeway Hotel Ltd, COT v (Federal Supreme Court) (November 1961), 24 SATC 616 531 537

Rolls-Royce Ltd v Jeffrey (1962) 1 WLR 425 393 394 401

Rose & Company v Campbell (1968) All ER 405 459

S v Clearwater Tea Manufacturers (Pvt) Ltd 1975 (3) SA 65(AD), 37 SATC 279 65 250

Sacks v CIR 1946 AD 31, 13 SATC 343 421

TABLE OF CASES

SUPREME COURT AND OTHER (Cont)	Page
Safranmark (Pty) Ltd, SIR v, 1982(1) SA 113(AD), 43 SATC 235	53 67
Salmon & Woods, Ex Parte Gould 2 Mor Bkcy Cas 137	140
Samuel McCausland Ltd v Ministry of Commerce (1956) N1 36	307 309
Schofield v R and H Hale Ltd 1975 STC 353	303 463
Schoombie, R v, 1945 AD 541	70
Seligan, Rex v, 1926 TPD 27	253
Sharpe, R v, 1903 TS 871	70
Sidersky, R v, 1928 TPD 109	217 253
South Metropolitan Gas Company v Dodd, 13 TC 211	510
South Wales Aluminium Co Ltd v Assessment Committee for the Neath Assessment Area (1943 (2) AER 587	467
St John's School (Mountford and Knibbs) v Ward (1975) STC 7 CA	463
Standard Vacuum Refining Co v Durban City Council 1961 (2) SA 669 (A)	201 288 471
Stott, CIR v, 1928 AD 252, 3 SATC 253	246
Sub Nigel Ltd v CIR 1948 (4) SA 580 (A) 15 SATC 381	213 451
Swaziland Ranches Ltd, COT v, (Swaziland Court of Appeal, July 1978, 1978, 40 SATC 232	277 278 310
TA v COT 1960 (4) SA 917 (High Court of Zimbabwe) 24 SATC 47	57 306
The Gas Float Whitton, No 2 1896 P42	131
The Mayor of Southport v Morris (1893) 1 QB 359	136
Theatre Investments (Pty) Ltd v Butcher Brothers Ltd 1978 (3) SA 682 (AD)	201 332 333 471
Torf's Est. v Minister of Finance 1948 (2) SALR 283, 293 NPD	342

TABLE OF CASES

SUPREME COURT AND OTHER (Cont)	Page
Trego v Hunt (1896) AC 7	392
Turnbull v CIR 1953 (2) SA 573 (A), 18 SATC 336	383 398 422 576
United Aircraft Corporation, FCT v, 68 CLR 525	396
Vacu-lug (Pvt) Ltd v COT 1963 (2) SA 694 (SR) 25 SATC 201	382
Van Wezel v Van Wezel's Trustees 1924 AD 409	287 332 469 471
Victoria Falls and Transvaal Power Co Ltd, Commissioner of Customs v, 6 SATC 131	459
Wangaratta Woollen Mills Ltd v FCT (1969), 1 ATR 329	63 308 454
Watson v RCA Victor Co Incorporated (1934) 50 Lloyd LR 77	134
Western Clock Co v Oris Watch Co Ltd (1931) Ex CR 64	362
Whitwick Colliery Co Ltd, Boyce (Inspector of Taxes) v, 1934 All ER 706	220
Wolf, CIR v, 1928 AD 177, 3 SATC 153	224
Yarmouth v France (1887) 19 QBD 647	458 460 466
Yorkshire Copper Works' Appn (1954) 71 RPC 150	362
Zaaiplaats Tin Mining Co Ltd v Union Government 1944 TPD 42	182 183

TABLE OF CASES

SPECIAL COURT FOR HEARING INCOME TAX APPEALS		Page
ITC 12, 1 SATC 117		529
ITC 50, 2 SATC 123		489
ITC 91, 3 SATC 235		491
ITC 122, 4 SATC 115		553
ITC 135, 4 SATC 201		430
ITC 141, 4 SATC 218		560
ITC 146, 4 SATC 278	490	573
ITC 150, 4 SATC 294		489
ITC 152, 4 SATC 299		430
ITC 162, 5 SATC 76		555
ITC 163, 5 SATC 77		567
ITC 164, 5 SATC 79	445	490
ITC 166, 5 SATC 85	241	242
ITC 180, 5 SATC 256		469
ITC 200, 5 SATC 389	512	514
ITC 203, 6 SATC 34		568
ITC 205, 6 SATC 42		518
ITC 208, 6 SATC 55	237	240
ITC 212, 6 SATC 63		469
ITC 213, 6 SATC 66		443
ITC 215, 6 SATC 133	489	492
ITC 225, 6 SATC 158		476
ITC 238, 6 SATC 353		571
ITC 240, 6 SATC 363	444	488
ITC 243, 6 SATC 370		554
ITC 247, 6 SATC 379		491
ITC 251, 7 SATC 47	444	476
ITC 261, 7 SATC 139	270	271
ITC 271, 7 SATC 170		473
ITC 280, 7 SATC 251		264

TABLE OF CASES

SPECIAL COURT FOR HEARING INCOME TAX APPEALS (Cont)					Page
ITC 295, 7 SATC 350		443	488	492	
ITC 311, 8 SATC 152			492	502	
ITC 322, 8 SATC 243				518	
ITC 358, 9 SATC 179				519	
ITC 361, 9 SATC 189			559	569	
ITC 370, 9 SATC 313				475	
ITC 410, 10 SATC 232				478	
ITC 442, 11 SATC 78				572	
ITC 450, 11 SATC 101				264	
ITC 456, 11 SATC 171				530	
ITC 458, 11 SATC 178				246	
ITC 460, 11 SATC 186			444	502	
ITC 469, 11 SATC 261				475	
ITC 481, 11 SATC 345				553	
ITC 491, 12 SATC 77				567	
ITC 512, 12 SATC 246				86	
ITC 519, 12 SATC 271				530	
ITC 520, 12 SATC 404			558	559	
ITC 559, 13 SATC 308				500	
ITC 561, 13 SATC 313				554	
ITC 565, 13 SATC 330				502	
ITC 568, 13 SATC 443				444	
ITC 577, 13 SATC 486				444	
ITC 586, 14 SATC 123			235	244	
ITC 589, 14 SATC 132				456	
ITC 605, 14 SATC 361				554	
ITC 615, 14 SATC 399				86	
ITC 617, 14 SATC 474	551	558	564	570	
ITC 623, 14 SATC 510				443	
ITC 626, 14 SATC 530				564	

TABLE OF CASES

SPECIAL COURT FOR HEARING INCOME TAX APPEALS (Cont)					Page
ITC 295, 7 SATC 350		443	488		492
ITC 311, 8 SATC 152			492		502
ITC 322, 8 SATC 243					518
ITC 358, 9 SATC 179					519
ITC 361, 9 SATC 189			559		569
ITC 370, 9 SATC 313					475
ITC 410, 10 SATC 232					478
ITC 442, 11 SATC 78					572
ITC 450, 11 SATC 101					264
ITC 456, 11 SATC 171					530
ITC 458, 11 SATC 178					246
ITC 460, 11 SATC 186			444		502
ITC 469, 11 SATC 261					475
ITC 481, 11 SATC 345					553
ITC 491, 12 SATC 77					567
ITC 512, 12 SATC 246					86
ITC 519, 12 SATC 271					530
ITC 520, 12 SATC 404			558		559
ITC 559, 13 SATC 308					500
ITC 561, 13 SATC 313					554
ITC 565, 13 SATC 330					502
ITC 568, 13 SATC 443					444
ITC 577, 13 SATC 486					444
ITC 586, 14 SATC 123			235		244
ITC 589, 14 SATC 132					456
ITC 605, 14 SATC 361					554
ITC 615, 14 SATC 399					86
ITC 617, 14 SATC 474	551	558	564		570
ITC 623, 14 SATC 510					443
ITC 626, 14 SATC 530					564

TABLE OF CASES

SPECIAL COURT FOR HEARING INCOME TAX APPEALS (Cont)					Page
ITC 631, 15 SATC 100			516	517	520
ITC 637, 15 SATC 126				565	573
ITC 639, 15 SATC 226			245	246	247
ITC 641, 15 SATC 233		246	443	450	457
ITC 643, 15 SATC 243					556
ITC 651, 15 SATC 369					562
ITC 657, 15 SATC 495		511	513	514	516
ITC 663, 16 SATC 121					445
ITC 665, 16 SATC 127					556
ITC 666, 16 SATC 130					419
ITC 672, 16 SATC 227					76
ITC 681, 16 SATC 357					500
ITC 685, 16 SATC 372					534
ITC 693, 16 SATC 510				469	490
ITC 699, 17 SATC 99					501
ITC 709, 17 SATC 227				562	573
ITC 720, 17 SATC 474					430
ITC 722, 17 SATC 490					476
ITC 732, 18 SATC 108					242
ITC 740, 18 SATC 219					247
ITC 741, 18 SATC 222					270
ITC 754, 18 SATC 424			513	514	515
ITC 767, 19 SATC 206					539
ITC 769, 19 SATC 214		452	457	509	514
ITC 770, 19 SATC 216					86
ITC 773, 19 SATC 308					478
ITC 774, 19 SATC 311			94	106	452
ITC 780, 19 SATC 328					450
ITC 782, 19 SATC 410					246
ITC 785, 19 SATC 419					530
ITC 795, 20 SATC 107					514

TABLE OF CASES

SPECIAL COURT FOR HEARING INCOME TAX APPEALS (Cont)						Page
ITC 800, 20 SATC 226						434
ITC 811, 20 SATC 465					422	447
ITC 821, 21 SATC 75						553
ITC 838, 21 SATC 419						447
ITC 840, 21 SATC 424						488
ITC 844, 22 SATC 70						559
ITC 849, 22 SATC 8[illegible]						556
ITC 852, 22 SATC 187					511	515
ITC 853, 22 SATC 191					267	268
ITC 855, 22 SATC 195	436	474	561	566		569
ITC 859, 22 SATC 292						267
ITC 865, 22 SATC 393						573
ITC 866, 22 SATC 397					480	481
ITC 885, 23 SATC 336			276	278		310
ITC 898, 23 SATC 491						532
ITC 900, 23 SATC 501						515
ITC 905, 24 SATC 87				474		509
ITC 906, 24 SATC 90						563
ITC 915, 24 SATC 219						568
ITC 923, 24 SATC 246	268	282	291			336
ITC 925, 24 SATC 252						563
ITC 937, 24 SATC 274						237
ITC 940, 24 SATC 380						533
ITC 955, 24 SATC [illegible]31				515		516
ITC 957, 24 SATC 637						86
ITC 964, 24 SATC 709				533		534
ITC 971, 24 SATC 791						537
ITC 997, 25 SATC 177						63
ITC 1006, 25 SATC 248				54	60	62
ITC 1007, 25 SATC 251				456		486
ITC 1011, 25 SATC 283						476

TABLE OF CASES

SPECIAL COURT FOR HEARING INCOME TAX APPEALS (Cont)	Page
ITC 1031, 26 SATC 63	516
ITC 1034, 26 SATC 78	535
ITC 1036, 26 SATC 84	531
ITC 1047, 26 SATC 223	476
ITC 1052, 26 SATC 253	63
ITC 1061, 26 SATC 317	54 73 74 337
ITC 1066, 27 SATC 114	389 436
ITC 1097, 27 SATC 290	265
ITC 1101, 29 SATC 23	54 66
ITC 1110, 29 SATC 169	214
ITC 1114, 30 SATC 14	72 76 78
ITC 1135, 31 SATC 228	235 239 240
ITC 1137, 32 SATC 1	80 82
ITC 1145, 33 SATC 26	389 430
ITC 1149, 33 SATC 98	279 481 482
ITC 1159, 33 SATC 190	517
ITC 1177, 34 SATC 147	240
ITC 1186, 35 SATC 129	536
ITC 1188, 35 SATC 150	522
ITC 1190, 35 SATC 188	391
ITC 1213, 36 SATC 113	566
ITC 1228, 37 SATC 64	62
ITC 1234, 37 SATC 188	458
ITC 1245, 38 SATC 13	517 520
ITC 1246, 38 SATC 21	58
ITC 1247, 38 SATC 27	66 68 73 94
ITC 1248, 38 SATC 35	482
ITC 1249, 38 SATC 74	195 196 208 253
ITC 1257, 39 SATC 55	422
ITC 1258, 39 SATC 8	235
ITC 1258, 39 SATC 58	239

TABLE OF CASES

SPECIAL COURT FOR HEARING INCOME TAX APPEALS (Cont)				Page
ITC 1263, 39 SATC 120				570
ITC 1264, 39 SATC 133				560
ITC 1266, 39 SATC 142	76	79		192
ITC 1285, 41 SATC 73				246
ITC 1286, 41 SATC 98				456
ITC 1297, 42 SATC 36			72	76
ITC 1313, 42 SATC 197				477
ITC 1319, 42 SATC 263		235		237
ITC 1323, 42 SATC 287				485
ITC 1324, 42 SATC 288				238
ITC 1339, 43 SATC 178				196

PART I

South Africa is becoming more industrialised and technology is developing rapidly. More and better machines are needed in order to -

- meet the quality and quantity of products demanded by world markets; and to
- manufacture products timeously for export markets.

In an effort to meet these objectives and also to stimulate development growth, certain privileged classes of taxpayers are provided with tax concessions and incentives. These concessions and incentives take various forms but normally amount to accelerated wear and tear allowances. In addition, certain taxpayers qualify for investment allowances, which result in deductions from their income of amounts which exceed the actual cost of qualifying items. The privileged classes of taxpayers are -

- manufacturers;
- industrialists in regional development areas;
- hotelkeepers;
- taxpayers erecting residential units;
- shipbuilders and owners of ships;
- owners of aircraft;
- exporters carrying on a beneficiation process;
- miners;
- farmers;
- co-operatives; and
- owners of national keypoints.

It is important to note that where doubt arises as regards the interpretation of the Act in relation to the deduction of capital expenditure by a privileged class, the interpretation must be applied restrictively against

the class privilege: "The general rule is that expenditure of a capital nature cannot be deducted for the purpose of de.ermining the taxable income of a taxpayer. See section 11(2)(a) of the Act. In para 17 of the Third Schedule an exception is made in the case of farmers who are allowed to deduct the capital expenditure therein specified. To this extent farmers are, as a class, placed in a favourable position but there is no justification in the paragraph for extending this exception. Craies on Statute Law, p 109 says: 'The Courts, in dealing with taxing Acts, will not presume in favour of any special priviledge of exemption from taxation. Said Lord Young in Hogg v Parochial Board of Auchtermuchty, 7 Rettie 986: "I think it proper to say that, in dubio, I should deem it the duty of the Court to reject any construction of a modern statute which implied the extension of a class privilege of exemption from taxation, provided the language reasonably admitted of another interpretation"'" [per Centlivres CJ held in Ernst v CIR [1954 (1) SA 318 (A), 19 SATC 1 at 8]. This approach was confirmed in Badenhorst & Others v CIR [1955(2) SA 207 (N), 20 SATC 39]; and Buglers Post (Pty) Ltd v SIR [1974 (3) SA 28 (A), 36 SATC 71].

Machinery or plant

Deductions may be claimed in the form of initial and investment allowances in respect of machinery or plan. used directly in a process of manufacture (Sections 12(1) and 12(2)). Although these allowances are available to hotelkeepers, they are not available in respect of mining and farming operations. The words "machinery or plant" are not defined in the Act (see C.21.7 infra).

CHAPTER 1

MANUFACTURERS

In the determination of their taxable income, manufacturers are allowed to deduct from their income, two types of allowances. These are an initial and an investment allowance calculated by reference to the cost of the qualifying item. The conditions under which these allowances may be claimed and the rates of the allowances are different in relation to the type of asset which would qualify. The qualifying assets are machinery or plant and buildings. In the case of buildings an annual allowance instead of an initial allowance may be claimed by industrialists.

1.1 Machinery or plant - initial allowance

The initial allowance relating to machinery or plant was introduced into the Act in 1954 at a rate of 10% calculated on the cost of new or unused machinery or plant. The rate of the allowances was increased over the years to its present level of 25%. Originally the allowance was restricted to machinery or plant used in a process of manufacture. In 1961, however, the allowance was extended to machinery or plant used in a process, which in the Commisisoner's opinion was of a similar nature.

An important concession was made in 1966. The allowance could from then onwards also be claimed by a lessor on the condition that the lessee uses the machinery or plant for the lessee's trade and is used by the lessee directly in a process of manufacture carried on by him or in any other process carried on by him which in the opinion of the Commissioner is of a similar nature.

Another important concession was made in 1978. The term "new or unused machinery" was extended to include used machines.

The effect of the initial allowance is to accelerate the writing off for tax purposes of the cost of machinery or plant. Unlike the wear and tear allowance which is calculated on the value (C21.4 *infra*) after certain adjustments, the initial allowance is calculated on the cost price of machinery or plant. Any donated asset, for instance would therefore not qualify for the initial allowance. However, there could be an argument that the initial allowance may well be calculated on the value of machinery or plant (C4.31 *infra*).

Example

A taxpayer purchases a machine on 1 January 1983 at a cost of R20 000. The machine is brought into use in a process of manufacture on 1 February 1983. The Commissioner allows 10% wear and tear on a "straight-line basis" and the taxpayer's year end is on 28 February 1983. Calculate the initial allowance.

Solution

	R
Cost of machine	20 000
Initial allowance - 25%	5 000
	15 000
Wear and tear allowance (10% x 15 000) x 1/12	125
Tax value at 28 February 1983	14 875

The special features of the initial allowance, are as follows:

- The machinery or plant may be new or used (second hand) but must be used by the taxpayer for the purposes of his trade, and used by him directly in a process of manufacture carried on by him, or in any other process carried on by him which in the opinion of the Commissioner is of a similar nature.
- The allowance is available to a lessor if the machinery or plant are used by the lessee for the purposes of the lessee's trade, directly in a process of manufacture carried on by him or any other process carried on by him which in the opinion of the Commissioner is of a similar nature [Section 12(1)(b) and (d)]. Sections 12(1)(b) and (d) provides that the machinery or plant must be used by a lessee for the purposes of the lessee's trade. A sub-lessee would therefore not qualify. The only section which specifically mentions a sub tenant is section 13(1) which deals with the annual allowance on buildings. It is further provided in sections 12(1)(b) and (d) that the lessor would not qualify for the allowance if the lessee does not derive amounts constituting "income" for the purposes of the Act.
- The cost of new or unused machinery or plant for the purposes of calculating the intial allowance is deemed to be the cost which, in the opinion of the Commissioner, is the cash price under a transaction concluded at *arms* length plus the direct cost of installation [Section 17(3A)]. This cost must be reduced by any untaxed recoupment in respect of machinery or plant damaged or destroyed.
- The cost of "used machinery, plant, implements, utensils or articles", for the purposes of calculating the allowance is "deemed to be the actual cost thereof (as established to the satisfaction of the Commissioner) less the aggregate of the amounts allowed to be deducted in respect thereof under

section 11(e)". The reason why the term "machinery, plant, implements, utensils or articles" is used in section 12(4) instead of "machinery or plant", is that the section applies also to hotelkeepers. A deduction of untaxed recoupments is not made from the cost of used machinery or plant as the concession under section 8(4)(e) is available only in respect of new machinery or plant in relation to a process of manufacture or in any other process which in the opinion of the Commissioner is of a similar nature.

- It should be noted that the term "cost" would include the cost of foundations and supporting structures [Section 11(e) (iiA)].
- The initial allowance is not available to a lessor unless the lease is for a period of at least five years, or such shorter period as the Commissioner may approve [Section 12(5)(a)]. Any allowances which have been granted are included in income should the lessor dispose of his interest or portion of his interest within this period [Section 12(5)(b)].
- The recoupment of the allowance is subject to tax [Section 8(4)].
- The initial allowance is not available in respect of mining and farming operations.

The following recommendations by the Standing Commission on Taxation Policy was accepted in 1983 by the Minister of Finance:

"i) The initial allowance, which is currently granted at the rate of 25 per cent, should be increased in so far as machinery and plant used in a process of manufacture are concerned as from 1 July 1985 to at least 55 per cent (ie the existing 25 per cent plus 30 per cent to compensate for the abolition of the investment allowance) but to not more than 100 per cent.

(ii) Depending on the percentage at which the enhanced allowance is to be set any balance of the cost of the asset be written off over a limited period in order to ensure that taxpayer will not be in a worse position than at present.

(iii) The figure of 55 per cent should not be regarded as sacrosanct and could be decreased in future years.

(iv) Adequate warning of a proposed change in the rate should be given by the Minister.

(v) The initial allowance of 25% be retained for the time being in respect of machinery and plant used in a process similar to a process of manufacture and that the Commission examine at the earliest opportunity the desirability or otherwise of extending the enhanced allowance referred to in recommendation - (i) above to equipment used in such similar processes".

1.2 Investment allowances

The investment allowances were introduced into the Act in 1960 with the purpose of giving a further incentive to the manufacturing and hotel industries. The Minister of Finance, at the time of introduction pointed out that these allowances were not be to regarded as a permanent feature of our tax system. The investment allowances were therefore granted for a limited period, were abolished a few years later (except in certain cases), and were re-introduced in 1970. The latest expiry dates are 30 June 1985 and 30 June 1986 in respect of machinery or plant and buildings respectively.

What the Minister said in 1970:

"My next concession is specifically designed to encourage fixed investment in manufacturing industry, which, as I

explained earlier, has for some time been lower than I should like to see.

Honourable Members will recall that a system of investment allowances was introduced by my predecessor in the early 1960s when investment was extremely sluggish, and was abolished (except in certain special cases) a few years ago when conditions had changed and inflationary pressures were building up.

Although, as I have explained, the danger of excessive pressure of demand on our limited resources has by no means disappeared, I think that a temporary encouragement to investment in manufacturing industry is again justified. (per 1970 ITR at p151)

In addition to mere encouragement, the Minister in 1973 revealed another purpose for the investment allowance. (per 1983 ITR at p62).

"With a view to encouraging industrial investment and also to allow to some extent for rising prices and consequential increased replacement cost of industrial buildings and machinery, an increase in the investment allowance is, to my mind, justified".

What the Minister said in 1975:

"I come to some important concessions designed to encourage investment, which is so essential for our economic future.

There has been much discussion lately of the effects of inflation under traditional accounting methods on business profits and in particular on the ability of business to set aside sufficient funds to replace capital assets. It is argued that depreciation allowances based on historical costs are insufficient at a time of rapid

inflation, to make adequate provision for such replacement and in effect result in the over-statement of business profits". (per 1975 ITR at p69)

In 1976 and 1977 the purposes of the allowances were seen to compensate for the effects of inflation on the value of productive assets, and in 1979 inflation and increased replacement costs were again linked together as justification for the investment allowances.

During 1980 the Minister added yet another purpose for the investment allowance:

"These allowances today fulfil a dual function: firstly, they reduce the effective rate of taxation payable by companies and, secondly they bring relief in cases where depreciation and the write-off assets (are) based on historical costs. The view is held in some quarters that these allowances, by encouraging investments, tend to increase industrial capacity, a development which should normally not be curbed but that it may in certain circumstances be advantageous to pay these allowances in cash especially in decentralised areas because of the more difficult location problems experienced there.

Others, again, express concern about the large amounts foregone in revenue, especially when the allowances are not limited to their original purpose, and feel that it would be better to provide the desired incentive in the form of an appropriation of expenditure.

It is also argued that the possible encouragement of capital-intensive industries in this way is not conductive to the provision of adequate employment opportunities and that a better balance should be sought between incentives for capital and labour-intensive enterprises, also in the mining and agricultural sectors.

The matter has many facets and I feel that we should be cautious before changing the status quo. 'Opinions have vested interests just as men have', said Samuel Butler, and he could be right. I have thus deemed it fit to direct the Standing Commissioner on Taxation to investigate this whole issue and to submit recommendations to me". (per 1980 ITR at p76)

Considering the various statements by the Minister, the question arises as to whether these allowances have become a permanent feature of our tax law. The answer was given in 1981.

What the Minister said in 1981:
"The machinery investment allowance, which is granted to manufacturers in terms of the Income Tax Act has been in operation for many years. It is, however, not a permanent feature of tax law, but has been renewed from time to time for the purpose of encouraging continuing investment in modern industrial machinery and plant. In recent years the allowance has also served as a buffer against the steadily rising replacement costs of new equipment". (per 1981 ITR at p5).

The investment allowances are in addition to the initial and wear and tear allowances. They have the effect of allowing a manufacturer or a hotelkeeper to claim as a deduction an amount which is in excess of the cost of a qualifying asset.

Initially the investment allowances were meant for owners of assets only. In 1962 and 1966 the building and machinery or plant investment allowances respectively, were extended to the effect that lessees would as from those dates also qualify for the allowances.

The extension of the dates to which the investment allowances are claimable by taxpayers has become a regular feature since they were introduced into the Act. In a speech delivered on 13 November 1980 the Minister referred to an investigation into the desirability or otherwise of incentive allowances which was being carried out by the Standing Commission on Taxation Policy. The Commission recommended that:

"The investment allowance on machinery and plant, which is due to expire on 30 June 1985, should not be extended for a further period but should be abolished". (per Report By The Standing Commission 1983 at p19).

The Minister of Finance accepted this recommendation in 1983.

1.3 Machinery or plant - investment allowance

The special features of the investment allowance, the rate of which is at present 30% of the cost of new machinery or plant, are as follows:

- The machinery or plant must be new or unused [Section 12(2)].
- The machinery or plant must be used by the taxpayer for the purposes of his trade directly in a process of manufacture carried on by him [Section 12(2)]. Prior to 1 July 1979 processes similar to a process of manufacture also qualified.
- The allowance is available to a lessor if the machinery or plant are used by the lessee for the purposes of his trade directly in a process of manufacture carried on by him. It is specifically provided that the allowance is not available if the lessee does not in carrying on his trade, derive income as defined in the Act. In other words, if the lessee is, say, a pension fund which is exempt from tax, the allowance would not be available [Section 12(2)(d)].

- The allowance is calculated on the cost, which is deemed to be the cost which in the opinion of the Commissioner is the cash price, under a transaction concluded at arm's length, plus the direct cost of installation [Section 12(3A)]. The term "cost" includes the cost of foundations and supporting structures [Section 11(e)(iiA)].
- The allowance is not available to a lessor unless the lease is for a period of at least five years, or such shorter period as the Commissioner may approve [Section 12(5)].
- The recoupment of the investment allowance is subject to tax only in the instance where a lessor has within five years disposed of the whole or portion of his interest or his right to receive rent under the lease [Section 12(5)(b)].
- The allowance may be increased by the Minister of Finance if such machinery or plant are brought into use in an economic development area [Section 12(2A)].
- The investment allowance is not available in respect of mining or farming operations.

1.4 Buildings

Deductions may be claimed in the form of annual and investment allowances in respect of buildings used in a process of manufacture [Sections 13(1), 13(5)]. The allowances are not available in respect of mining or farming operations. The word "building" is not defined in the Act (C21.6 infra).

1.5 Building annual allowance

The annual allowance of 2% on the cost of new factory buildings was introduced into the Act in 1959. Initially the allowance was only available on new buildings, but

has subsequently been extended to include improvements to existing buildings. The allowance is available on a "straight-line" basis and is not reduced proportionally if not used as specified for the full year of assessment.

Example

A factory is erected by a taxpayer and is occupied on 27 February 1983 for the purposes of a process of manufacture. The taxpayer's year end is 28 February 1983 and the cost of the building was R200 000.

Solution

	R
Allowance at 28 February 1983	
Annual allowance of 2%	4 000
Investment allowance - 20% (Cl.6 *infra*)	40 000
	44 000

It is interesting to note that the annual allowance is specifically available to a lessor even if the occupier of the premises is a sub-tenant. Section 13(1) uses the phrase "tenant or subtenant" and not "lessee" as in the case of section 12(1) and 12(2) which deal with capital allowances in respect of machinery or plant.

The special features of the annual allowance which has remained unchanged at 2% [Section 13(1)] per annum of the cost of buildings are:

. The allowance is available to a taxpayer who incurs the cost of the building or improvements. In other words, a non-owner of the assets concerned such as a lessee will also qualify for the allowance.

- The buildings must be used during the year of assessment by the taxpayer in the course of his trade, or by his tenant or subtenant, wholly or mainly for the purposes of carrying on therein any process of manufacture or any other process which in the opinion of the Commissioner is of a similar nature [Section 13(1)(b)].
- A taxpayer who purchases a building will be allowed the annual allowance only if the seller was entitled to the allowance and the building was wholly or mainly used during the year of assessment by the taxpayer, his tenant or subtenant for the purpose of carrying on therein a process of manufacture or any other process which in the opinion of the Commissioner is of a similar nature [Section 13(1)(d)].
- Improvements to buildings will qualify for the allowance. The buildings must be used during the year of assessment by the taxpayer, his tenant or subtenant in the manner outlined above [Section 13(1)(f)].
- Buildings or improvements thereto to the extent to which an allowance has been granted in terms of section 11(g) ("leasehold improvements" Chapter 23), are specifically excluded for the purpose of the annual allowance. The aggregate of the annual and leasehold improvements allowances are limited to the cost of the buildings or improvements thereto [Section 13(2)]. The reference to cost of the buildings or improvements is the cost after the deduction of untaxed recoupments under section 8(4)(e).

Example

A taxpayer carries on a process of manufacture, and:

a) in terms of an obligation under a lease for twenty years erects a factory at a cost of R200 000; or

b) erects a factory on his own property at a cost of R200 000.

Two years subsequent to occupying the factory, it was destroyed by fire. An insurance claim of R200 000 was received and the taxpayer replaces the factory in the same year at a cost of R250 000.

Solution (a)

Should the taxpayer claim an allowance under section 11(g), he would not be allowed a deduction under section 13(1) viz the annual allowance.

	R
Cost of improvements	200 000
Allowances under section 11(g) for 2 years, ie 2 x R10 000	20 000
Tax value at date of fire	180 000
Insurance receipt	200 000
Recoupment of section 11(g) allowances	20 000

The taxpayer has an option to set off this recoupment "against so much of the cost to him of such further building purchased or erected by him as remains after the deduction of any portion of such cost in respect of which an allowance has been granted to the taxpayer under section 11(g), whether in the current or any previous year of assessment". [Section 13(3). See below for conditions].

Should such an election be made:

	R
Cost of replacement building	250 000
Less: Recoupment	20 000
	230 000
Less: Aggregate allowances under section 11(g) (will be spread over 18 years but is limited to the amount stipulated in the lease)	200 000
Portion of cost subject to annual allowance of 2%)	30 000

Solution (b)

Cost of factory	200 000
Annual allowance - 2% for 2 years	8 000
Tax value at date of fire	192 000

The receipt of R200 000 from the insurance company will render R8 000 subject to inclusion into income of the taxpayer as a recoupment [section 8(4)(a)]. The recoupment of the investment allowance is exempt from tax. In terms of section 13(3) the recoupment of the annual allowance can at the option of the taxpayer be set off against the cost of a replacement and not be included in the taxpayer's income in the year of recoupment. There are however, certain conditions -

. the taxpayer must notify the Commissioner in writing of the exercise of the option when submittng his return of income for the year during which the recoupment occurred; and

- another qualifying building must be purchased or erected within twelve months or such further period as the Commissioner may allow from the date on which the event giving rise to the recovery or recoupment occurred.

	R
Cost of replacement building	250 000
Less untaxed recoupment	8 000
Amount subject to annual allowance to be claimed at the rate of 2% p.a.	242 000

- Any untaxed recoupment in terms of section 8(4)(e) must be deducted from the cost of the building or improvements thereto replacing those which have been damaged or destroyed, for the purposes of calculating the annual allowance [Section 13(3)].
- A regular feature of this allowance is that the buildings must be used during the year of assessment by the taxpayer, his tenant or subtenant in the manner outlined above. It follows therefore that a lessee will qualify for the allowance if he has incurred the cost irrespective of the period of the lease. In other words if the lessee is still in occupation after the expiry of the lease he would still qualify for the allowance. Should the lessee cease occupation, the allowance will likewise cease. The lessee could under the latter circumstances qualify for a scrapping allowance.
- The 1983 Report By The Standing Commission of Enquiry recommended (at p20) as regards factory buildings that "where the erection of such buildings is commenced after 30 June 1985 a building initial allowance equal to 20 per cent of the cost to the taxpayer of the building be granted in the year in which the building is brought into use". This incentive is to substitute the present annual and investment allowances on the cost of industrial buildings.

- another qualifying building must be purchased or erected within twelve months or such further period as the Commissioner may allow from the date on which the event giving rise to the recovery or recoupment occurred.

	R
Cost of replacement building	250 000
Less untaxed recoupment	8 000
Amount subject to annual allowance to be claimed at the rate of 2% p.a.	242 000

- Any untaxed recoupment in terms of section 8(4)(e) must be deducted from the cost of the building or improvements thereto replacing those which have been damaged or destroyed, for the purposes of calculating the annual allowance [Section 13(3)].
- A regular feature of this allowance is that the buildings must be used during the year of assessment by the taxpayer, his tenant or subtenant in the manner outlined above. It follows therefore that a lessee will qualify for the allowance if he has incurred the cost irrespective of the period of the lease. In other words if the lessee is still in occupation after the expiry of the lease he would still qualify for the allowance. Should the lessee cease occupation, the allowance will likewise cease. The lessee could under the latter circumstances qualify for a scrapping allowance.
- The 1983 Report By The Standing Commission of Enquiry recommended (at p20) as regards factory buildings that "where the erection of such buildings is commenced after 30 June 1985 a building initial allowance equal to 20 per cent of the cost to the taxpayer of the building be granted in the year in which the building is brought into use". This incentive is to substitute the present annual and investment allowances on the cost of industrial buildings.

Author Coetzee H A
Name of thesis Capital allowances in terms of South African Tax law 1984

PUBLISHER:
University of the Witwatersrand, Johannesburg
©2013

LEGAL NOTICES:

Copyright Notice: All materials on the University of the Witwatersrand, Johannesburg Library website are protected by South African copyright law and may not be distributed, transmitted, displayed, or otherwise published in any format, without the prior written permission of the copyright owner.

Disclaimer and Terms of Use: Provided that you maintain all copyright and other notices contained therein, you may download material (one machine readable copy and one print copy per page) for your personal and/or educational non-commercial use only.

The University of the Witwatersrand, Johannesburg, is not responsible for any errors or omissions and excludes any and all liability for any errors in or omissions from the information on the Library website.