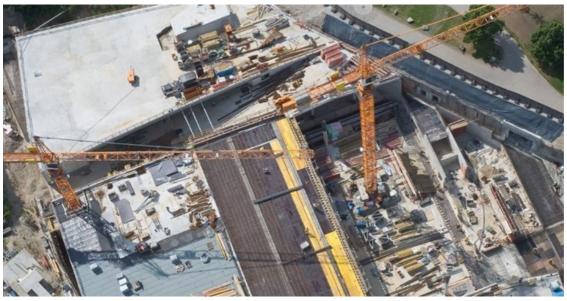
BIZCOMMUNITY

Urban Development Zone allowance under the Income Tax Act

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In line with international models, South Africa has attempted to incentivise investment into the development and renewal of certain urban areas. One of these incentives is the accelerated tax depreciation allowance, introduced in 2003 by section 13quat of the Income Tax Act, 1962, and is commonly referred to as the Urban Development Zone (UDZ) allowance.



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The UDZ allowance is available in respect of the "cost" (as defined in 13quat) of erection, extension, addition to 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.

This allowance was originally available only until 31 March 2014, but has been extended for a further six years until 31 March 2020.

There are five main requirements that must be met in order for a taxpayer to claim the UDZ allowance. These are:

1. The building in question must be a commercial or residential building;

2. Which is owned by the taxpayer;

- 3. Situated within a UDZ;
- 4. Which has been brought into use on or before March 31 2020; and

5. Is used solely for the purposes of that taxpayer's trade.

The UDZ allowance is not limited to the taxable income of a taxpayer and may create an assessed loss. The allowance is restricted to the cost of erection, extension, addition to or improvement of the specific building.

The cost of the land on which the building is located is specifically excluded. Therefore, should the "purchase price" (as defined) of the building include the purchase price of the land, an apportionment will have to be made to determine the portion of the price attributable to only the building.

There are a number of important documents that need to be completed and retained by the taxpayer in order to validly claim the UDZ allowance. These forms are readily available on the South African Revenue Service's (SARS) website.

Further, should a "developer" be involved in a property development project, special reporting requirements are mandated by section 13quat(10A). Reporting to SARS in this context includes, among other things, details of estimated costs of the building that the developer intends to sell, the estimated selling price of the building that the developer intends to sell, and, following the sale of the building, actual costs incurred and the actual selling price of the building.

Section 13quat defines a "developer" as "a person who erects, extends, adds to or improves a building or part of a building -

(a) With the purpose of disposing of that building or part thereof immediately after completion of that erection, extension, addition or improvement; and

(b) Disposes of the building or part of a building within three years after completion of that erection, extension, addition or improvement".

From 10 January 2012, the amended definition of "developer" allows a developer, for a period of three years, to use or let the constructed or improved property. This has resulted in the allowance being available to both the initial developer and the subsequent purchaser, provided the developer has not claimed the UDZ allowance within the period in which the property was used or let.

Rates of the allowance

The amount of the allowance in relation to "cost" (as defined) varies according to the following distinctions.

The erection of any new building, or the extension of or addition to any building, is equal to:

- 20% of the "cost" to the taxpayer during the year of assessment in which the building is brought into use by the taxpayer; and
- 8% of the "cost" to the taxpayer in each of the 10 succeeding years of assessment.

The improvement of any existing building or part of a building (including any extension or addition which is incidental to that improvement) where the existing structural or exterior framework thereof is preserved is equal to:

- 20% of the "cost" to the taxpayer during which the part of the building so improved is brought into use by the taxpayer solely for the purposes of that taxpayer's trade; and
- 20% of that "cost" in each of the four succeeding years of assessment.

Where the taxpayer purchased a building or part of a building from a developer, the below will be deemed to be the cost incurred by that taxpayer in respect of the erection, extension, addition to or improvement of that building or part of a building:

- 55% of the purchase price of that building or part of a building, in the case of a new building erected, extended or added to by that developer; or
- 30% of the purchase price of that building or part of a building, in the case of a building improved by that developer.

13sex

Since October 21 2008, section 13sex has provided a comprehensive consolidation of allowances available to taxpayers for certain residential units. Generally, this results in an allowance of 5% per annum over a 20-year period of the cost of erection, improvement or acquisition of any new and unused residential units, or any new and unused improvement to a residential unit, owned by the taxpayer.

Should the residential units qualify as "low-cost residential units" (as defined), the taxpayer may be eligible for an additional 5% allowance (ie the allowance would be increased to 10% of allowed costs per annum over a 10-year period).

The following four requirements may be distilled from section 13sex:

1. The units or improvements must be owned by the taxpayer;

2. The units must be situated in South Africa;

3. The taxpayer must own five (or more) residential units in South Africa, which units must also be used solely for the purposes of the taxpayer's trade; and

4. The unit or improvement must be used solely for purposes of the taxpayer's trade.

It is pertinent to note that this allowance is limited to new and unused units or improvements thereto. The allowance is therefore not available to costs associated with second-hand residential units.

The interaction between 13quat AND 13sex

To the extent that a taxpayer qualifies for the UDZ allowance in respect of a particular development, it would be unlikely to qualify for a deduction in terms of section 13sex in respect of that same development, as section 13sex expressly applies only in instances where no other deduction is available in terms of any part of the "cost" of the unit(s). This is so, as the concept of the "cost" of a unit, as defined under 13sex, largely overlaps with the concepts of "cost" and "purchase price" in terms of section 13quat.

Generally, therefore, should the development have already qualified for the UDZ allowance, part of the "cost" under 13sex would likely have already qualified for a deduction, rendering 13sex unavailable on the facts. The exact interaction between the two deductions, however, needs to be considered specifically on the facts of each case.

It is to the benefit of property developers and investors to consider these and other allowances, as well as the interaction between respective allowances, provided for under the Income Tax Act.

Source: The Times

ABOUT THE AUTHOR

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