Tax benefits of public-private partnerships

By Graeme Palmer

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It is becoming commonplace for government to enter into arrangements with a private party where the government provides land for the construction or improvements to buildings by the private party without parting with ownership of the land. This is referred to as a public-private partnership (PPP).

PPP transactions are dealt with in s12N of the Income Tax Act, 1962, which treats the private party making the improvements to government land as if it was the owner of the land. If the private party complies with s12N, it can claim capital allowances for the improvements.
In order to qualify, the private party must:

- hold a right of use or occupation of land or building;
- effect an improvement in terms of a PPP;
- incur expenditure to effect the improvement; and
- use or occupy the land or building for the production of income or derive income from it.

However, some PPP agreements are not meeting these requirements because the right of use or occupation is not given to the private party. For example, a serviced office accommodation project, where the private party finances, constructs, operates and maintains a government-owned building.

Here, government is effectively buying a serviced office which it will occupy to carry out its work. Conversely the private party is constructing an asset to provide a service, and fails to meet the s12N requirements as it only has service access to the building.

Amendment to Act

A recent amendment to the Act in the form of s12NA was introduced to address this problem. It allows a private party to a PPP, where government will use or occupy the land or building, to claim a capital allowance for expenditure incurred to make improvements on government land.

In order to qualify for a capital allowance the private party must be a party to a PPP agreement with government and must incur expenditure of a capital nature. In addition to claiming capital allowances, the private party can deduct all maintenance and operating expenses which are ordinarily allowed under the general deduction formula in s11(a).

This recent amendment to the Act operates retrospectively and applies to expenditure incurred to effect improvements during any year of assessment commencing on or after 1 January 2013. Both sections 12N and 12NA do not apply where the person effecting the improvements is in the business of banking, financial services or insurance.

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