

18 March 2016

The South African Revenue Service

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**PRETORIA**

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**RE:     DRAFT INTERPRETATION NOTE ON THE DEDUCTION FOR ENERGY-EFFICIENCY SAVINGS  
SECTION 12L OF THE INCOME TAX ACT**

Provided below are SAIT's comments relating to the Draft Interpretation Note on the Deduction for energy-efficiency savings.

The comments are presented in the order of the paragraphs used in the Draft Interpretation Note. When reference is made to the 'Draft Interpretation Note' we used the abbreviation 'Draft IN'. When reference is made to 'Regulations' it is to the Regulations published under section 12L(5) by the Minister of Finance. References to section 12L will of course be to section 12L of the Income Tax Act.

### **Paragraph 2 – background**

*The comment in footnote 2 relating to section 20A*

Footnote 2 on page 2 of the Draft IN states that "in case of a natural person claiming a deduction under section 12L, the provisions of section 20A which relates to the ring-fencing of assessed losses must, however, be taken into consideration."

The comment is not relevant to the section 12L deduction.

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Section 20A applies to an individual when the individual is engaged in a suspect trade or suffered losses in a number of years. Section 12L provides that the deduction is available to any person who derived income from carrying on any trade. Even where section 20A applies, the taxpayer meets the trade requirement. In addition section 20A limits the loss, which consists of all the allowable expenditure and not only a specific expense – such as for instance the section 12L deduction.

The comment relating to section 20A should therefore be removed.

**Paragraph 4.1 – Introduction; paragraph 4.3.1 - Activities that may qualify and paragraph 4.3.2 Activities that may not qualify**

In the first sentence in paragraph 4.1 reference is made to “a project which is registered with SANEDI”. Both paragraphs 4.3.1 and 4.3.2 also refer to a project. It does say that it “encompass the planned undertaking by a business to reduce its energy usage.”

Section 12L makes no reference of the word “project” or that it must be “registered”. It is paragraph 2(a) of the Regulations that requires that a “person that claims the allowance must, in respect of each year of assessment for which the allowance is claimed ... register with SANEDI in the form and manner and at the place that SANEDI may determine...”

It is only in paragraph 5(1) of the regulations that reference is made to a project and it is to a “greenfields project”. The Regulation then doesn’t require that the ‘greenfields project’ be registered. In terms of the Regulation a “greenfield project” is a “wholly new project which does not utilise any assets other than wholly new and unused assets”.

We submit that the section 12L deduction is not a project driven incentive, but an all-inclusive energy savings incentive.

In the preamble to the Carbon Tax Act, 2017 (still a Bill) it is stated that “government believes that imposing a tax on greenhouse gas emissions and concomitant measures such as providing tax incentives for rewarding the efficient use of energy will provide appropriate price signals to help nudge the economy towards a more sustainable growth path.”

Section 12L is clearly a tax incentive for rewarding the efficient use of energy. If the taxpayer uses carbon energy in a more efficient the taxpayer gets an incentive (the section 12 deduction), irrespective of how the taxpayer achieved this. It doesn't require a project.

It is also clear that the intention of section 12L is not to “fund” projects. It is to incentivise all efficiency, independent of how it was achieved.

The section 12I (Additional investment and training allowances in respect of industrial policy projects) is a project driven allowance and the word “project” is mentioned 52 times in the section.

Except for greenfields projects the word project is never mentioned in the section 12L. Section 12L(3) does not require that SANEDI must review projects, but it states that SANEDI must review the energy savings. If SANEDI is satisfied with respect to the energy efficiency savings for which a deduction is claimed in respect of that year of assessment it issues the certificate regarding efficiency savings.

It is therefore clear that the references in the Draft IN to a project and projects (other than a greenhouse project) are not in line with the Regulations. If the resulting SARS interpretation regarding “project” is allowed, it would mean that any good energy deed, not described in the original project, will not receive any incentive. Clearly this could not have been the intent of section 12L as its purpose is to incentivise all efficiency initiatives.

It further means that only new projects approved by SANEDI can be incentivised under section 12L. This implies that projects already implemented will not qualify. In practice, on the basis of the following time line: 6 – 9 months project design; 3 months to obtain SANEDI approval and 12 months to implement the incentive

therefore only “kicks” in in 2018. There are thus only 2018 and 2019 (two years) available for 12L. This could also not have been the purpose of section 12L.

The Draft IN must therefore be amended and the references to project (other than a greenhouse project) must be removed. As SANEDI’s uses the term “project” to refer to a specific section 12L claim it is suggested that the term “project” in the Draft IN be replaced with the term “claim application”.

#### **Paragraph 4.4 - Steps to be undertaken before claiming the allowance**

In the third bullet of the paragraph it is stated that the taxpayer must “present the measurement and verification plan and project details to a SANEDI panel which will inform the taxpayer and the measurement and verification body whether the baseline has been approved.” The fourth bullet it states that the taxpayer must “implement the project if written confirmation is received from SANEDI.”

Neither of the above requirements is a requirement of either section 12L(3) or paragraph 2 of the Regulation.

It is therefore submitted that the two bullet points mentioned above should be deleted from the Draft IN. As it is a requirement that the taxpayer must obtain a certificate from SANEDI, it is suggested that this be added as a bullet point in paragraph 4.4 of the Draft IN.

#### **Paragraph 4.5 - Registration of projects**

The comments regarding to projects and the requirement that they be registered made earlier in our submission are also relevant to the paragraph.

As suggested, the use of the word project is not appropriate and should be replaced.

## Paragraph 4.8.1 - The “trade” requirement and exempt income

### *The commencement date of the section 12L deduction*

The Draft IN states that “as section 12L came into effect on 1 November 2013, a person carrying on a trade and generating energy-efficiency savings between the period of 1 November 2013 and the year of assessment ending before 1 January 2020, could be eligible to claim a deduction under section 12L. A taxpayer that generates energy-efficiency savings from a date preceding the effective date may claim only the portion relating to savings from 1 November 2013...”

Section 12L, as it was amended by Act 22 of 2012, was to come into operation on a date determined by the Minister of Finance by notice in the Gazette. The Minister of Finance notice gave notice that section 12L of the Income Tax Act, 1962, as inserted by section 27 of the Taxation Laws Amendment Act, 2009 (Act No. 17 of 2009), amended by section 27 of the Taxation Laws Amendment Act, 2010 (Act No.7 of 2010), and substituted by section 29 of the Taxation Laws Amendment Act, 2012 (Act No. 22 of 2012), comes into operation on 1 November 2013.

Section 12L provides that, for the purpose of determining the taxable income derived by any person from carrying on any trade in respect of any year of assessment ending before 1 January 2020, there must be allowed as a deduction from the income of that person an amount in respect of energy efficiency savings by that person in respect of that year of assessment. The allowance itself is determined in accordance with subsection (2), subject to subsection (3) of section 12L.

SAIT’s interpretation of the above is that a taxpayer will only be entitled to make the deduction in respect of energy efficiency savings if the year of assessment of the taxpayer ends on or after 1 November 2013. With regard to the words “any year of assessment ending before 1 January 2020” used in section 12L it is our view that the deduction would be available in respect of that year. In other words, if the year of assessment commenced before 1 November 2013, but ends thereafter, the deduction would be available. No such

deduction can be made in respect of a year of assessment that ended before 1 November as section 12L, whilst in the law, was not effective in that year of assessment.

The effect of the notice by the Minister was therefore to enable taxpayers to make the deduction. It does not require that the baseline be determined on 1 November 2013. In terms of section 12L(3) all that is required is that the taxpayer "must obtain a certificate issued by an institution, board or body prescribed by the regulations (contemplated in 12Lsection (5)) in respect of the energy efficiency savings for which a deduction is claimed in respect of that year of assessment. This certificate must, amongst others, contain "the baseline at the beginning of the year of assessment."

This interpretation implies that a taxpayer (a company) with a financial year starting in January and ending in December can construct a baseline period of 12 months prior to January 2013. Any measureable and verifiable savings during 2013 will qualify for the tax allowance.

It is therefore suggested that the Draft IN be amended to accommodate the above view.

#### *Exempt income*

We agree with the principle in the Draft IN that an entity that only derives amounts exempt from normal tax (section 10) will not have "income" as defined against and that the section 12L deduction is not available. This in a sense, whilst in terms of section 12L, is similar to the prohibition found in section 23(f). It is then stated in the Draft IN that if an "entity implement(s) a project in a trade from which it also earns "income" as defined, a deduction may be possible in certain instances."

We disagree with the following comment:

"If a person implements a project which spans an entire building but operates two trades, namely, a trade from which exempt income is earned and another from which taxable income is earned, an apportionment must be made to limit any deduction for energy-efficiency savings to the portion of savings relating to the portion of the amount that constitutes income."

It has been held that an apportionment is necessary where section 23(f) or possibly more relevant section 23(g) applies. Section 23(f) refers to 'expenses incurred' and 23(g) refers to 'moneys were not laid out or expended'. It would therefore limit the expenses incurred, but as section 12L is not based on expenses (it is based on energy saved) the sections will not apply and no apportionment of the section 12L deduction is required.

Please do not hesitate to contact us if you need to discuss or require further clarification with regard to any of the above comments.

Sincerely

**PJ Nel**

**cc: National Treasury**