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# Doubtful debt allowances - Commissioner's discretion revoked

The latest set of proposed changes to section 11(j) of the Income Tax Act seeks to remove SARS' discretion in order to provide a level playing field and reduce the South African Revenue Service's ("SARS") administrative burden. The question is, at what cost to the taxpayer?

## Doubtful debt allowances based on the Commissioner's discretion and rulings made for specific taxpayers.

Based on current legislation and prior to the proposed amendments below, the Commissioner has the authority to grant an allowance of so much of any debt due to the taxpayer it considers doubtful. In practice, SARS allows 25% of doubtful debt provisions as a deduction based on a specific list and determined with reference to a debtors' listing.

Some taxpayers were able to negotiate a more favourable allowance through rulings. In particular SARS' directive to the Banking Association of South Africa ("BASA") provided for much more favourable terms to its members.
In certain instances, certain taxpayers considering themselves moneylenders, often applied the BASA directive, albeit not members of BASA and without special dispensation provided by the Commissioner.

## Enter IFRS 9

The introduction of IFRS 9 rendered the BASA directive and most other specific rulings unusable. The terminology and concepts used in said directive were aligned with IAS 39 and are no longer used in IFRS 9.
National Treasury, after extensive lobbying by the banks, introduced section 11(jA), effective from years of assessment commencing on or after 1 January 2018, to govern the treatment of doubtful debt allowances for covered persons as defined (mostly banks).

Broadly speaking, banks are allowed a deduction of 85 percent of stage 3, 40 percent of stage 2 and 25% of stage 1 expected credit losses as determined in terms of IFRS 9. There are some intricacies, considering that section 11(jA) does not specifically refer to the three stages.

Importantly, section 11(jA) is only available to banks and not any other moneylenders, so what about everyone else?

## Proposed changes

With the following amendments being proposed in the 2018 Taxation Laws Amendment Bill (to which comments are due by 16 August 2018):

Section 11(j) will be repealed and replaced in its entirety to read as follows:

*(i) an allowance equal to 25 per cent of the loss allowance relating to impairment, as contemplated in IFRS 9, in respect of debt other than in respect of lease receivables as defined in IFRS 9, if IFRS 9 is applied to that debt by that person for financial reporting purposes; or*

*(ii) an allowance equal to 25 per cent of so much of any debt, other than a debt contemplated in subparagraph (i), due to the taxpayer, that would have been allowed as a deduction under any other provision of this Part had that debt become bad if that debt is 90 days or more in arrears:*

*Provided that an allowance under this paragraph must be included in the income of the taxpayer in the following year of assessment.*

Effectively, the proposal revokes all of the Commissioners' discretion and provides for an allowance of 25% of so-called IFRS 9 loss allowances or 25% of other debt older than 90 days before considering specific provisos.

## Equality versus equity

The question for consideration: Is 25% acceptable? Most non money-lender taxpayers stand to benefit from the proposed amendment, owing to the 25% to be allowed on all IFRS 9 impairments, not limited to specific impairments as previously. On face of it, all taxpayers are treated equally and had it not been for the special dispensation the banks are enjoying under section 11(jA), this question might not have been as protruding.

However, the mere fact that a class of taxpayers is treated differently from its direct competitors resulting in a competitive advantage should accentuate a clear answer of "No it is not acceptable".
As example, a company providing vehicle finance to the general public should be treated similarly to a bank providing vehicle finance.

We are not advocating that banks should also be subject to an allowance of 25%. The nature of their business and the specific financial risks that comes with lending necessitates specific dispensation and could impact the cost of lending for the man on the street if not available.

The nature of a taxpayer's business should dictate to what extent an allowance is available for debt considered doubtful. Also, to provide an equitable solution, taxpayers with similar businesses/activities should be treated equally.
In this regard, banks with the special dispensation as included in section 11(jA) and moneylenders subject to the new section 11(j) comes to mind.

Non-bank moneylenders are at a distinct disadvantage.

**For more information, contact:**

**Vian Strydom**
Partner, Tax Management Services
**T:** +27 82 564 9118
**E:** vian.strydom@kpmg.co.za

**Carl Nel**
Associate Director, Tax Management Services
**T:** +27 82 719 5611
**E:** carl.nel@kpmg.co.za

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