

Dear Taxpayer

AUDIT FINDINGS

The South African Revenue Service (SARS) has completed the corporate income tax (CIT) audit for the period(s) 2023; 2024. This letter informs you of the proposed adjustment(s) to your assessment based on the audit findings.

Summary of Findings			
Tax Period(s)	Provisions of the Income Tax Act No. 58 of 1962 (IT Act)	Brief description of proposed adjustment	Adjustment Amount
2023	Income Tax Act No. 58 of 1962, Section 11(a), Tax Administration Act no. 28 of 2011, Section 92, Section 221 "definition", "understatement", sub-paragraph (c), Section 221(1) & (2), Section 222(3)(c) and Section 223(1)	Finance Cost Disallowed	R58 701.72
2023	Income Tax Act no. 58 of 1962, Section 11 (e), Tax Administration Act no. 28 of 2011, Section 92, Section 221 (c), Section 222(1) & (2), Section 222(3)(c), Section 223(1)	Depreciation Overstated	R4 828 850.82
2024	Income Tax Act No. 58 of 1962, Section 11(a), Tax Administration Act no. 28 of 2011, Section 92, Section 221 "definition", "understatement", sub-paragraph (c), Section 221(1) & (2), Section 222(3)(c) and Section 223(1)	Finance Cost Disallowed	R14 408.55
2024	Income Tax Act no. 58 of 1962, Section 11 (e), Tax Administration Act no. 28 of 2011, Section 92, Section 221 (c), Section 222(1) & (2), Section 222(3)(c), Section 223(1)	Depreciation Overstated	R5 245 961.49
Total			R10 147 922.58

Explanation of proposed adjustment(s):

1. Finance Cost Disallowed - 2023

1.1 The facts (audit findings):

During the audit it was noted that the taxpayer claimed finance cost on their original income tax return. The taxpayer was requested to provide supporting information relating to the amount claimed and the taxpayer responded by indicating that the finance cost should not have claimed as a deduction. The adjustment will be made to disallow the finance cost claimed because they were not supposed to be claimed as a deduction.

1.2 The law:

Income Tax Act No. 58 of 1962

Section 11. General deductions allowed in determination of taxable income. - "For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived-

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

Tax Administration Act no. 28 of 2011

Section 92. Additional assessments. - "If at any time SARS is satisfied that an assessment does not reflect the correct application of a tax Act to the prejudice of SARS or the fiscus, SARS must make an additional assessment to correct the prejudice."

Section 221. Definitions. -

'understatement' means any prejudice to SARS or the fiscus as a result of -

(c) An incorrect statement in a return."

Section 222 - Understatement penalty. -

"(1) In the event of an 'understatement' by a taxpayer, the taxpayer must pay, in addition to the 'tax' payable for the relevant tax period, the understatement penalty determined under subsection (2) unless the 'understatement' results from a bona fide inadvertent error.

(2) The understatement penalty is the amount resulting from applying the highest applicable understatement penalty percentage in accordance with the table in section 223 to each shortfall determined under subsection (3) and (4) in relation to each 'understatement'

(3) The shortfall is the sum of -

(c) the difference between the amount of an assessed loss or any other benefit to the taxpayer properly carried forward from the tax period to a succeeding tax period and the amount that would have been carried forward if the 'understatement' were accepted, multiplied by the tax rate determined under subsection (5).

Section 223 (1). Understatement penalty percentage table. - "The understatement penalty percentage table provides a guideline on how the percentages are levied and the behaviour of the taxpayer." Refer to annexure B for the table.

1.3 Application of the law:

The taxpayer claimed finance cost expenses during the year of assessments and indicated that they were not supposed to be claimed as a deduction, therefore the amount claimed will be reversed because they were not incurred in the production of income in terms of section 11(a).

The assessment resulting from the above-mentioned transgression will be made in terms of section 92 of the TAA, as the taxpayer claimed finance cost that were not supposed to be claimed as a deduction.

Understatement Penalty

In addition, SARS may impose an understatement penalty in terms of the Tax Administration Act based on the circumstances of the case.

In terms of the definition of an understatement in Section 221 paragraph (c) of the TAA, an understatement has occurred as the taxpayer claimed finance cost that were not supposed to be claimed. This has resulted to prejudice to SARS.

According to section 222(1) of the TAA in a case of understatement, SARS must levy an understatement penalty. Therefore, an understatement penalty being the amount resulting from applying the highest applicable penalty percentage in accordance with the table in section 223(1) of the TAA, to the sum of the difference between the amount of the assessed loss properly carried forward from the tax period to the succeeding tax period and the assessed loss that would have been carried forward if the understatement were accepted in terms of section 222(3)(c) of the TAA for the tax period under audit should be levied in line with Section 222(1) and Section 222(2) of the TAA.

In this regard SARS is of the view that the behaviour applicable is of gross negligence as the taxpayer claimed finance cost that were not supposed to be claimed as a deduction. The taxpayer's conduct is regarded to be of a standard case as the taxpayer partially cooperated during the audit. Therefore 100% understatement penalty may be levied on the shortfall for this period.

Note that this is just a proposal by SARS, and the taxpayer is invited to propose with reasons the applicable USP percentage. The proposal will then be presented to the committee which will make the final determination of the applicable behaviour and conduct.

2. Depreciation Overstated - 2023

2.1 The facts (audit findings):

During the audit it was noted that the taxpayer claimed depreciation expenses on their original income tax return. The taxpayer was requested to provide invoices of the assets purchase as reflected in the asset register and the taxpayer responded by providing limited invoices. Depreciation that will be allowed as a deduction will be limited to the assets reflected in the assets register and supported by invoices.

2.2 The law:

Income Tax Act no. 58 of 1962.

"Section 11. General deductions allowed in determination of taxable income.-For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived- (e) save as provided in paragraph 12 (2) of the First Schedule, such sum as the Commissioner may think just and reasonable as representing the amount by which the value of any machinery, plant, implements, utensils and articles (other than machinery, plant, implements, utensils and articles in respect of which a deduction may be granted under section 12B, 12BA, 12C, 12DA, 12E (1), 12U or 37B) owned by the taxpayer or acquired by the taxpayer as purchaser in terms of an agreement contemplated in paragraph (a) of the definition of "instalment credit agreement" in section 1 of the Value-Added Tax Act and used by the taxpayer for the purpose of his or her trade has been diminished by reason of wear and tear or depreciation during the year of assessment."

Tax Administration Act no. 28 of 2011

Section 92. Additional assessments. -"If at any time SARS is satisfied that an assessment does not reflect the correct application of a tax

Act to the prejudice of SARS or the fiscus, SARS must make an additional assessment to correct the prejudice."

Section 221. Definitions. -

'understatement' means any prejudice to SARS or the fiscus as a result of -

(c) An incorrect statement in a return."

Section 222 - Understatement penalty. -

"(1) In the event of an 'understatement' by a taxpayer, the taxpayer must pay, in addition to the 'tax' payable for the relevant tax period, the understatement penalty determined under subsection (2) unless the 'understatement' results from a bona fide inadvertent error.

(2) The understatement penalty is the amount resulting from applying the highest applicable understatement penalty percentage in accordance with the table in

section 223 to each shortfall determined under subsection (3) and (4) in relation to each 'understatement'

(3) The shortfall is the sum of -

(c) the difference between the amount of an assessed loss or any other benefit to the taxpayer properly carried forward from the tax period to a succeeding tax period and the amount that would have been carried forward if the 'understatement' were accepted, multiplied by the tax rate determined under subsection (5).

Section 223 (1). Understatement penalty percentage table. - "The understatement penalty percentage table provides a guideline on how the percentages are levied and the behaviour of the taxpayer." Refer to annexure B for the table.

2.3 Application of the law:

The invoices and assets register submitted by the taxpayer during the audit revealed that the assets were used for the purposes of the taxpayer's trade in line with section 11(e) of the Income Tax Act, therefore depreciation recalculated based on the invoices submitted will be allowed as a deduction. Depreciation claimed as a deduction which could not be substantiated by documentary proof will not be allowed because there is not proof that it was incurred for the purpose of the taxpayer's trade in terms of section 11(e) of the Income Tax Act.

The assessment resulting from the above-mentioned transgression will be made in terms of section 92 of the TAA to correct the prejudice as the taxpayer claimed depreciation expense without supporting documents.

Understatement Penalty

In addition, SARS may impose an understatement penalty in terms of the Tax Administration Act based on the circumstances of the case.

In terms of the definition of an understatement in Section 221 paragraph (c) of the TAA, an understatement has occurred as the taxpayer claimed depreciation without providing supporting information e.g invoices. This has resulted to prejudice to SARS.

According to section 222(1) of the TAA in a case of understatement, SARS must levy an understatement penalty. Therefore, an understatement penalty being the amount resulting from applying the highest applicable penalty percentage in accordance with the table in Section 223(1) of the TAA, to the sum of the of the difference between the amount of the assessed loss properly carried forward from the tax period to the succeeding tax period and the assessed loss that would have been carried forward if the understatement were accepted in terms of section 222(3)(c) of the TAA for the tax period under audit should be levied in line with Section 222(1) and Section 222(2) of the TAA.

In this regard SARS is of the view that the behaviour applicable is of gross negligence as the taxpayer claimed depreciation which could not be substantiated by documentary proof. The taxpayer's conduct is regarded to be of a standard case as the taxpayer partially cooperated during the audit. Therefore 100% understatement penalty maybe levied on the shortfall for this period.

Note that this is just a proposal by SARS, and the taxpayer is invited to propose with reasons the applicable USP percentage. The proposal will then be presented to the committee which will make the final determination of the applicable behaviour and conduct.

3. Finance Cost Disallowed - 2024

3.1 The facts (audit findings):

During the audit it was noted that the taxpayer claimed finance cost on their original income tax return. The taxpayer was requested to provide supporting information relating to the amount claimed and the taxpayer responded by indicating that the finance cost should not have claimed as a deduction. The adjustment will be made to disallow the finance cost claimed because they were not supposed to be claimed as a deduction.

3.2 The law:

Income Tax Act No. 58 of 1962

Section 11. General deductions allowed in determination of taxable income. - "For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived-

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

Tax Administration Act no. 28 of 2011

Section 92. Additional assessments. - "If at any time SARS is satisfied that an assessment does not reflect the correct application of a tax Act to the prejudice of SARS or the fiscus, SARS must make an additional assessment to correct the prejudice."

Section 221. Definitions. -

'understatement' means any prejudice to SARS or the fiscus as a result of -

(c) An incorrect statement in a return."

Section 222 - Understatement penalty. -

"(1) In the event of an 'understatement' by a taxpayer, the taxpayer must pay, in addition to the 'tax' payable for the relevant tax period, the understatement penalty determined under subsection (2) unless the 'understatement' results from a bona fide inadvertent error.

(2) The understatement penalty is the amount resulting from applying the highest applicable understatement penalty percentage in accordance with the table in section 223 to each shortfall determined under subsection (3) and (4) in relation to each 'understatement'

(3) The shortfall is the sum of -

(c) the difference between the amount of an assessed loss or any other benefit to the taxpayer properly carried forward from the tax period to a succeeding tax period and the amount that would have been carried forward if the 'understatement' were accepted, multiplied by the tax rate determined under subsection (5).

Section 223 (1). Understatement penalty percentage table. - "The understatement penalty percentage table provides a guideline on how the percentages are levied and the behaviour of the taxpayer." Refer to annexure B for the table.

3.3 Application of the law:

The taxpayer claimed finance cost expenses during the year of assessments and indicated that they were not supposed to be claimed as a deduction, therefore the amount claimed will be reversed because they were not incurred in the production of income in terms of section 11(a).

The assessment resulting from the above-mentioned transgression will be made in terms of section 92 of the TAA, as the taxpayer claimed finance cost that were not supposed to be claimed as a deduction.

Understatement Penalty

In addition, SARS may impose an understatement penalty in terms of the Tax Administration Act based on the circumstances of the case.

In terms of the definition of an understatement in Section 221 paragraph (c) of the TAA, an understatement has occurred as the taxpayer claimed finance cost that were not supposed to be claimed. This has resulted to prejudice to SARS.

According to section 222(1) of the TAA in a case of understatement, SARS must levy an understatement penalty. Therefore, an understatement penalty being the amount resulting from applying the highest applicable penalty percentage in accordance with the table in section 223(1) of the TAA, to the sum of the difference between the amount of the assessed loss properly carried forward from the tax period to the succeeding tax period and the assessed loss that would have been carried forward if the understatement were accepted in terms of section 222(3)(c) of the TAA for the tax period under audit should be levied in line with Section 222(1) and Section 222(2) of the TAA.

In this regard SARS is of the view that the behaviour applicable is of gross negligence as the taxpayer claimed finance cost that were not supposed to be claimed as a deduction. The taxpayer's conduct is regarded to be of a standard case as the taxpayer partially cooperated during the audit. Therefore 100% understatement penalty may be levied on the shortfall for this period.

Note that this is just a proposal by SARS, and the taxpayer is invited to propose with reasons the applicable USP percentage. The proposal will then be presented to the committee which will make the final determination of the applicable behaviour and conduct.

4. Depreciation Overstated - 2024

4.1 The facts (audit findings):

During the audit it was noted that the taxpayer claimed depreciation expense on their original income tax return. The taxpayer indicated that there was no trading during the year of assessment, in addition to that bank statements reflected no business receipts during the year of assessment as such depreciation claimed will be disallowed as a deduction.

4.2 The law:

Income Tax Act no. 58 of 1962.

"Section 11. General deductions allowed in determination of taxable income.-For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived-

(e) save as provided in paragraph 12 (2) of the First Schedule, such sum as the Commissioner may think just and reasonable as representing the amount by which the value of any machinery, plant, implements, utensils and articles (other than machinery, plant, implements, utensils and articles in respect of which a deduction may be granted under section 12B, 12BA, 12C, 12DA, 12E (1), 12U or 37B) owned by the taxpayer or acquired by the taxpayer as purchaser in terms of an agreement contemplated in paragraph (a) of the definition of "instalment credit agreement" in section 1 of the Value-Added Tax Act and

used by the taxpayer for the purpose of his or her

trade has been diminished by reason of wear and tear or depreciation during the year of assessment."

Tax Administration Act no. 28 of 2011

Section 92. Additional assessments. - "If at any time SARS is satisfied that an assessment does not reflect the correct application of a tax Act to the prejudice of SARS or the fiscus, SARS must make an additional assessment to correct the prejudice."

Section 221. Definitions. -

'understatement' means any prejudice to SARS or the fiscus as a result of -

(c) An incorrect statement in a return."

Section 222 - Understatement penalty. -

"(1) In the event of an 'understatement' by a taxpayer, the taxpayer must pay, in addition to the 'tax' payable for the relevant tax period, the understatement penalty determined under subsection (2) unless the 'understatement' results from a bona fide inadvertent error.

(2) The understatement penalty is the amount resulting from applying the highest applicable understatement penalty percentage in accordance with the table in section 223 to each shortfall determined under subsection (3) and (4) in relation to each 'understatement'

(3) The shortfall is the sum of -

(c) the difference between the amount of an assessed loss or any other benefit to the taxpayer properly carried forward from the tax period to a succeeding tax period and the amount that would have been carried forward if the 'understatement' were accepted, multiplied by the tax rate determined under subsection (5).

Section 223 (1). Understatement penalty percentage table. - "The understatement penalty percentage table provides a guideline on how the percentages are levied and the behaviour of the taxpayer." Refer to annexure B for the table.

4.3 Application of the law:

The taxpayer indicated that they were not trading during the 2024 year of assessment and bank statements confirmed that the taxpayer did not trade during this year of assessment, therefore depreciation claimed will be disallowed as a deduction because the assets were not used in the production of income of the taxpayer in line with section 11 (e) of the Income Tax Act.

The assessment resulting from the above-mentioned transgression will be made in terms of section 92 of the TAA to correct the prejudice as the taxpayer claimed depreciation expense on the assets that were not used in the production of income.

Understatement Penalty

In addition, SARS may impose an understatement penalty in terms of the Tax Administration Act based on the circumstances of the case.

In terms of the definition of an understatement in Section 221 paragraph (c) of the TAA, an understatement has occurred as the taxpayer claimed depreciation expense on the assets that were not used in the production of income of the taxpayer. This has resulted to prejudice to SARS.

According to section 222(1) of the TAA in a case of understatement, SARS must levy an understatement penalty. Therefore, an understatement penalty being the amount resulting from applying the highest applicable penalty percentage in accordance with the table in Section 223(1) of the TAA, to the sum of the difference between the amount of the assessed loss properly carried forward from the tax period to the succeeding tax period and the assessed loss that would have been carried forward if the understatement were accepted in terms of section 222(3)(c) of the TAA for the tax period under audit should be levied in line with Section 222(1) and Section 222(2) of the TAA.

In this regard SARS is of the view that the behaviour applicable is of intentional tax evasion as the taxpayer claimed the depreciation expense on the assets that were not used in the production of income of the taxpayer. The taxpayer's conduct is regarded to be of a standard case as the taxpayer partially cooperated during the audit. Therefore 150% understatement penalty may be levied on the shortfall for this period.

Note that this is just a proposal by SARS, and the taxpayer is invited to propose with reasons the applicable USP percentage. The proposal will then be presented to the committee which will make the final determination of the applicable behaviour and conduct.

Interest

In terms of the Tax Administration Act interest is to be charged on the underpayment of provisional tax that arises as a result of the above proposed adjustments. The Commissioner has the discretion to review the interest charged and, if appropriate, remit or reduce the charge. In order to do so, the Commissioner of SARS needs to be satisfied that:

In respect of omitted or understated income adjustments, that the taxpayer has on reasonable grounds contended that such amounts should not have been included in taxable income

- In respect of overstated or non-deductible expenditure or allowances, that the taxpayer has on reasonable grounds contended that such amounts should have been allowed.

Finalisation of Audit

SARS reserves the right to amend the above-mentioned proposed understatement penalty percentage(s) depending on the circumstances of the case. The final decision regarding understatement penalties will reflect in the Finalisation of Audit Letter and the Notice of Assessment once the audit is finalised. If you are not in agreement with any of the proposed adjustments, kindly respond in writing furnishing reasons and/or supplying any relevant material on or before 2025-12-23. Also provide reasons in writing as to why understatement penalty and interest should not be imposed.

When submitting your relevant material, enclose this original letter as it contains a unique bar-coded reference which links it to your income tax account with SARS. A photocopy of this letter will not be accepted by SARS. You may make a copy of this letter for your records.

Note that SARS only accepts relevant material in A4 format and no other formats will be accepted. Electronically stored data can be submitted by arrangement with the SARS official.

Relevant material can be submitted through the following channels:

- At your nearest SARS branch
- By post to the address above
- Electronically via eFiling (if you are registered as an eFiler)

Should you have any queries relating to the audit, please contact the SARS official as per the contact details above.

Should you have any other queries please call the SARS Contact Centre on 0800 00 SARS (7277). Remember to have your income tax reference number at hand when you call to enable us to assist you promptly.

Sincerely

ISSUED ON BEHALF OF THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE