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TAXATION | BASIC/INTERMEDIATE

# Video Transcription: How to Use the Income Tax Act



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Hi, my name is Riley Carpenter and, in this video, we will be looking at the Income Tax Act, both the structure and how to use the act as part of your studies. We will also be looking at how to understand some of the key legal terminology in the act, as well as what these specific terms mean.

The information required to be able to calculate income tax consists of the original 1962 Income Tax Act as well as a number of amendments (changes to the act that periodically occur). So what does this mean? Each year if we need to calculate income tax, we need to make sure we have all of this information, i.e the 1962 act, existing amendments and any new amendments that have just been released.

How is this information generally packaged for students and tax practitioners? A number of publishers offer a resource referred to as “The Income Tax Act”. Let’s look at how one of these resources, namely the LexisNexis Income Tax Act is structured and how best to use it in your studies. This LexisNexis Income Tax Act consists of sections, schedules, tax rates, regulations and notices, and interpretation notes.

Remember that any of these parts of the act could have been amended. Before you use the relevant part, check whether there have been any amendments and whether these amendments have been incorporated into the act you are using. You will find the list of amendments at the beginning of the act. So, what are each of the parts of the act?

The sections each deal with the rules necessary to calculate the income tax amount owed. How do we read each section? Each section is numbered and deals with a new topic. For example, section 10 deals with exempt income. A section may be broken up into subsections. For example, subsection (1) of section 10 deals with types of income that are exempt. Subsection (2) of section 10 then deals with types of instance when income will not be exempt. Subsections are broken up into paragraphs, each with their own letter. For example, paragraph (i) of section 10(1) deals with the interest exemption for natural persons.

Paragraphs can be divided into sub-paragraphs and are given a Roman numeral, such as sub-paragraphs (i) and (ii) in section 10(1)(i). Sub-paragraph (i) deals with the interest exemption for people 65 years and older and sub-paragraph (ii) deals with the interest exemption for people younger than 65. So, how do sections, subsections, paragraphs and sub-paragraphs relate to one another? Whatever is said in a section applies to all of the subsections, paragraphs and sub-paragraphs in that section. Whatever is said in a subsection applies to all of the paragraphs and sub-paragraphs in that subsection, but not to any of the other subsections in the same section. And anything in a paragraph applies only to that paragraph.

So, what are the schedules? Schedules contain rules on how to treat specific items mentioned in the sections. For example, fringe benefits are included in gross income through the special inclusion in the gross income definition paragraph (i). Paragraph (i) refers us to the Seventh Schedule and to use those rules to calculate the value of the fringe benefit to include in the tax calculation.



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What are the Tax Rates and Regulations and Notices? These are annual rates that apply and help calculate the income tax owed to SARS. The tax rates generally change each year, and while the Regulations and Notices also change, they do not normally change each year. The final part is the Interpretation Notes and Practice Notes. The Notes provide additional guidance on how to deal with certain sections in the Income Tax Act. For example, Interpretation Note 47 gives guidance on how to apply the wear and tear allowance in section 11(e). While these Interpretation Notes are drafted by SARS, the same body that collects income tax, they are not part of the income tax legislation. So technically, they are not law, but it is important to understand what SARS considers to be the correct understanding of these issues.

Useful navigation tools through what is a very long Act, include the contents page and the index. These can save you in a test or exam. So remember to turn to the index, where topics are listed in alphabetical order. How should you use this Act as part of your studies? Once you've been introduced to a topic in a lecture, you must go read that part of the Act. When you read the sections, you will need to realise that, until you have spent time completing tutorials and other questions, it is unlikely that you will understand the Act. Once you actually understand the work, i.e. can correctly complete questions, you should go back to the sections in the Act and highlight the key words that are important in those sections. Highlight only the key words that you may need to find quickly, to refresh your memory.

You want to go into the assessment knowing your way around the Act. You don't want to be reading a section for the first time in the test or exam. Even if you are not allowed to use the Act in your assessments, knowing the specific wording in the Act will help your understanding of taxation. Now, what's with all this the legal terminology? At first the Act is very intimidating and difficult to read because it's drawn up by lawyers. These lawyers make sure that the intention of the legislation is being captured correctly in words that will hold up in court. So the Act uses specific terms that have specific meanings. Section 1 is the definitions, which indicate what terms mean.

Sometimes sections use terms that are specific to that section and will have definitions at the beginning of the section. Let's look at some frequently-used terms that are not defined in the Act, but which are important to understand. "Mainly" means more than 50%. For example, for the industrial building allowance in section 13 to apply, the building must be used wholly or mainly for the purposes of a process of manufacture. This means that more than 50% of the building must be used in a process of manufacture. "Exceed" means greater than. For example in section 1 in the definition of "low cost residential unit" the cost of an apartment must not exceed R350 000. This means the cost cannot be greater than R350 000, or else the definition will not apply.

"Provided that" introduces some additional rules to a section that may result in a change in outcome of the application of that section. We refer to this part of the section as a "proviso". Provisos normally come near the end of a section. For example, towards the end of the definition of resident in section 1, the Act reads, "Provided that where any person that is a resident ceases to be a resident during a year of assessment, that person must be regarded as not being a resident from the day on which that person ceases to be a resident."



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This means that the person is no longer a resident from the day that person no longer meets the definition of resident.

“Notwithstanding” means that even though the Act might say something elsewhere on this topic, you must apply the principles of the section you are reading. For example, in section 13(1), the Act reads, “Notwithstanding anything to the contrary contained in paragraph (ii) of the proviso to section 11(e)” This means that even though section 11(e) may say something that might seem to be relevant, you must ignore that section for the moment and apply what section 13(1) is saying. “Subject to” means that if the other section referred to applies, you must first apply the other section. If the other section doesn’t apply, then apply the current section. For example, section 6 deals with rebates and reads in section 6(2), “In the case of a natural person there shall, subject to the provisions of subsection (4), be allowed by way of— (a) a primary rebate, an amount of...” This means that subsection (4) must be applied first. In this circumstance subsection (4) tells us when the rebates must be apportioned for parts of a year where the period of assessment is less than 12 months.

The way the Act uses “and” and “or”. Often there are lists of requirements to be met in order for a section to apply. Sometimes the whole list of requirements must be met for the section to apply. In this circumstance, “and” is used at the end of the second last requirement. For example, in section 11(o), the disposal allowance, the depreciable asset being disposed of must (i) have qualified for deductions under specific sections, AND (ii) not have a useful life exceeding 10 years. Both of these requirements must be met before section 11(o) could apply.

Sometimes only one item on the list needs to be met for the section to apply. Here, “or” is used at the end of the second last requirement. For example, section 23 lists circumstances in which a deduction is disallowed. In the list, after section 23(q) the Act reads, “or” before section 23(r). This means that if one of the paragraphs (a) to (r) apply, the deduction is disallowed.

So use the Act systematically, make sure you have read the relevant sections and understood the terminology, and you should be better prepared for tests and exams.

I hope you enjoyed watching the video.