If an expense has to be claimed in year 1, and, by mistake, it is not claimed, it cannot be claimed in later years (Sub-Nigel Ltd v CIR, 15 SATC 381, 1948 (4) SA 580 (A)).

4. The provisions of the section do not apply in any of the following cases-

Proviso (aa)
where all the goods or services to which the expenditure relates (which would be subject to the section) are supplied within six months of the year end or the benefits are enjoyed within the same period;

- This 6-month rule does not apply to section 11D(1) research and development expenditure. Such expenditure must always be spread over the period to which it relates (if it is prepaid).
- A question arises as to whether the 6-month rule should apply separately to each prepaid expense, or whether it applies to all the prepaid expenses taken together. The act is not clear. In such a case it is submitted that the section should be interpreted in favour of the taxpayer (contra fiscum), and that the 6-month rule should be applied separately to each prepaid expense.

Proviso (bb)
where the aggregate of all amounts of expenditure incurred by the person, which would otherwise be limited by this section (except for the 6-month rule, it is submitted) does not exceed R100 000; or

Proviso (cc)
to any expenditure to which the provisions of section 24K (interest-rate agreements) or 24L (option contracts) apply; or

Proviso (dd)
to expenditure actually paid in respect of any liability imposed by legislation.

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Example – Prepaid expenditure

A taxpayer with a February year end incurs a tax-deductible expense of R180 000 on 15 February 2014 for services to be rendered to him for the period 1 February 2014 to 31 July 2014. Also, on 1 January 2014 he paid his business insurance premium of R24 000 for the 2014 calendar year. In addition, on 25 February 2014 he paid R60 000 rental in advance for the 12 months from 1 March 2014 to 28 February 2015, for equipment storage. The section 11(a) deductions which he may claim in respect of these payments for the year of assessment ended 28 February 2014 are as follows:

<table>
<thead>
<tr>
<th>28 February 2014</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Services cost (R180 000)</td>
<td>R180 000</td>
<td></td>
</tr>
<tr>
<td>(As this expense relates to a period ending within 6 months of the year end, the full amount is deductible)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Other prepaid expenses (where the 6-month rule is not applicable) | Portion relating | Portion relating |
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Insurance premiums (R24 000 x 2/12 &amp; 10/12)</td>
<td>R4 000</td>
<td>20 000</td>
</tr>
<tr>
<td>Rental for storage space (all for the following year)</td>
<td>0</td>
<td>60 000</td>
</tr>
</tbody>
</table>

As this does not exceed R100 000 it is all deductible in the 2014 year | R4 000 | R80 000 |

Total deductions for the 2014 year | R264 000 |

If the rental for storage had been R85 000 for the period from 1 March 2014 to 28 February 2015, the position would be as follows:

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Services cost (R180 000)</td>
<td>R180 000</td>
</tr>
<tr>
<td>(As this expense relates to a period ending within 6 months of the year end, the full amount is deductible.)</td>
<td></td>
</tr>
</tbody>
</table>

Other prepaid expenses (where the 6-month rule is not applicable) | Portion relating | Portion relating |
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Insurance premiums</td>
<td>R4 000</td>
<td>20 000</td>
</tr>
<tr>
<td>Rental for storage space (all for the following year)</td>
<td>0</td>
<td>60 000</td>
</tr>
</tbody>
</table>

As this does not exceed R100 000 it is all deductible in the 2014 year | R4 000 | R80 000 |

Total deductions for the 2014 year | R264 000 |
Insurance premiums (R24 000 x 2/12 & 10/12) | R4 000 | 20 000
Rental for storage space (all for the following year) | 0 | 85 000

As this exceeds R100 000, it is only deductible in the 2015 year, even though it has been paid in the 2014 year.

Total deductions for the 2014 year | 0 | 105 000

Total deductions for the 2014 year | 0 | 180 000

Where a taxpayer shows, during a year of assessment that the goods will not be received, or the service will not be rendered in the future, or that the benefit will not be enjoyed in the future, the expenditure already paid will be allowed as a deduction in that year of assessment to the extent that it has not already been deducted.

5.5.21 PROHIBITION OF DEDUCTIONS IN RESPECT OF INTELLECTUAL PROPERTY – SECTION 23I

Section 23I(2) prohibits the deduction of an expense incurred for the use, right of use, or permission to use tainted intellectual property. Such an expense is a ‘royalty’ in ordinary terms. The section also prohibits the deduction of expenditure determined directly or indirectly with reference to the aforementioned expenditure.

The prohibition only applies to the extent that the payment does not constitute income of the recipient (or part of the ‘net income’ of a controlled foreign company).

If the royalty is subject to the section 35 withholding tax, and the withholding tax is at least 10% of the royalty, then section 23I(3) allows a deduction of 1/3 of the royalty. Section 35 is repealed from 1 July 2013, and replaced with a 12% withholding tax in terms of section 49B. When the royalty withholding tax is 15%, then ½ of the royalty may be deducted under section 11(a).

‘Tainted intellectual property’ is discussed in the discussion of royalties paid to non-residents, in Chapter 19.

5.5.22 LIMITATION OF DEDUCTIONS IN RESPECT OF REORGANISATION AND ACQUISITION TRANSACTION – SECTION 23K

Section 23K limits the deduction of an interest expense if the interest arises out of a reorganisation or acquisition transaction (as contemplated in sections 45, 47, or 24O). In order to deduct the interest expense, application has to be made to the Commissioner for a directive.

This is discussed in detail in Chapter 18.

5.6 SPECIFIC EXPENSES AND LOSSES

The application of the s 11(a) general deduction formula to specific types of expenditure and losses is dealt with below.

5.6.1 ADVANCE PAYMENTS

When an amount is paid in advance, two problems arise for tax purposes. The first is whether it is an expense actually incurred, and the second is whether an enduring benefit is created. (capital). It is important to note that s 11(a) refers to expenditure "actually incurred" and makes no mention of expenditure actually paid.

In ITC 542 (1942) it was held that "incurred" means "paid" or "becoming liable for". In Caltex Oil (SA) Ltd v SIR (1975 AD), Botha JA said:

“It is in the tax year in which the liability for the expenditure is incurred, and not in the tax year in which it is actually paid (if paid in a subsequent year), that the expenditure is actually incurred for the purposes of s 11(a).” (emphasis added)

In the Caltex case, where the liability arose and was paid in the same year, the court looked to the payment to determine the expense "actually incurred". It is only where payment takes place in a later year, that the liability represents the expense.

Once an amount has been paid an expense has been incurred if the amount paid is not refundable. Where an amount is paid and the recipient of the payment is placed under an obligation to deliver goods or services at a