

Ref #: 769670

Submission File

14 June 2021

South African Revenue Service
Private Bag X923
Pretoria
0001

BY E-MAIL: policycomments@sars.gov.za

Dear SARS

COMMENTS ON THE DRAFT INTERPRETATION NOTE 28 (ISSUE 3) – DEDUCTIONS OF HOME OFFICE EXPENSES INCURRED BY PERSONS IN EMPLOYMENT OR PERSONS HOLDING AN OFFICE

1. We herewith take an opportunity to present our comments on behalf of the South African Institute of Chartered Accountants (SAICA) on the draft Interpretation Note (IN) providing clarity on the deductibility of home office expenses incurred by persons in employment or persons holding an office.
2. We commend the authors on a document that is, in relation to the examples, well written, clear and relevant to modern day times and realities. However, it is disappointing to see that the strict requirements of section 23(b) still stand with no amendments/relaxations. We feel that given the current circumstances there should have been a certain degree of relaxation especially in relation to the requirement that the home office be “exclusively” used for the purposes of trade.
3. Furthermore, the draft IN seems to ignore that the new norm for employees is working from home, regardless of the lockdown restrictions. We do understand that legislative amendments will be needed to align with these changed circumstances and have also made suggestions for further consideration in this regard in our comments below.

COMMENTS

4.2 The general rule

4. This paragraph states that the deductibility of expenses relating to a home office is determined by reference to section 11, in particular paragraphs (a), (d) and (e), read with section 23(b) and 23(m).

- | |
|---|
| 5. <u>Submission:</u> Section 24J should also be mentioned in relation to interest on a bond that could be regarded as tax deductible if all the requirements of the section are met. |
|---|



4.4 Requirements of section 23(m)

6. The last sentence in the first paragraph reads as follows:

As far as home office expenses are concerned, the taxpayer will only be able to claim rental, repairs and expenses incurred in relation to a dwelling house or domestic premises under section 11(a) and (d), and wear-and-tear allowances under section 11(e).

7. There is no wear and tear on the premises or any permanent fixtures, it is only on the non-permanent assets used for trade purposes (in the part of the dwelling used for trade purposes).

8. Submission: The last part of the sentence in paragraph 4.4 should be amended to clarify that wear and tear will be allowed on the assets used for trade purposes (in the part of the dwelling used for trade purposes).

4.5.3 Regular and exclusive trade use

9. This paragraph provides an explanation of the terms “exclusive use” and “regular”.

10. It is, however, uncertain how strictly this interpretation should be applied as exclusive means 100% and could be interpreted quite pedantically. That is, what if one completes personal tasks/takes private calls in the space, is it no longer exclusive?

11. This could easily be ascertained by SARS through a mere questionnaire but would make the provision meaningless. As this is a current problem it may require some contextualised interpretation until the legislature can attend to the matter.

12. Submission: Further clarity on this should be provided in the draft IN, but it is our understanding that the legislation was not written with the idea of such an extreme limited application.

13. *Suggested legislative amendment needed:* We will be requesting National Treasury to clarify through legislative amendment that the provision should not have such an extremely narrow application and should be expanded to accommodate the “new normal”.

Example 1 – Regularity test

14. This example sets out to explain what circumstances would satisfy the regularity test and could qualify for a home office deduction in respect of expenditure incurred during that period.

15. Submission: An example/comment of what the minimum threshold of what would be regarded as “regular”/“frequently” is needed for taxpayers/practitioners to evaluate against each scenario. In this example Jan and Feb 2020 is clearly not regular.



Example 3 – Exclusivity test

16. In Example 3, it is stated that should kids be allowed to play in the home office during winter afternoons and on weekends, then the home office is not used exclusively as a home office and no deduction will be allowed.
17. Although the example provides some guidance on the interpretation of “exclusive use” and “regular”, it is still unclear how strictly the interpretation of these terms will be applied by SARS. That is, what if one completes personal tasks/calls in the space, is it no longer exclusive? Another example is a home office with an adjoining patio/balcony (that can only be accessed via home study) that is used as personal living space after hours or over weekends.
18. Surely the legislation was not written with the idea of such a limited application, and if so, an amendment should be considered.

19. Submission: This exclusion appears a bit harsh especially considering the current pandemic and the closure of schools for a period of time.
20. *Suggested legislative amendment needed*: Consideration needs to be given to amending the definition of “exclusively used” to “used as a home office for substantially the whole time”. This wording is also consistently used throughout the Act to convey a much stricter application than “mainly” but to allow for practicality of other uses. This would be less than 1 full day week.
21. For example, a taxpayer may have a dedicated study which is used 90-95% of the time exclusively for work, but on the odd occasion the taxpayer’s son sits next to the working taxpayer as the taxpayer has to check his maths or sometimes on a Sunday he will sit in the study...its ad-hoc use but it does happen and should not preclude the taxpayer from claiming a home office allowance.
22. Until a legislative change has been made, it is suggested that SARS should deem a taxpayer who works mainly from home to be using the home office regularly and exclusively for purposes of trade, while he/she is actually working in the home office during office hours.
23. We are afraid that without this interpretation the majority of taxpayers will unfortunately not be getting any relief as it only the privileged few that are in the fortunate situation to have huge homes that allow them the luxury of allocating a room exclusively as their own home office.
24. With regard to the cost burden to the fiscus of granting this relaxation, SARS must be aware that many businesses have terminated their corporate office leases or down scaled their office floor size hence there will be a corresponding reduction in the s11(a) deduction for rent expenses usually deducted by businesses.



Example 4 – Sharing a home office

25. The draft IN, in Example 4, explains that the where the home office is shared (for instance by spouses) to perform their duties, no home office deduction will be allowed.
26. The reality is that most people do not have a separate study/ spare room that they are now using as a dedicated home office. It is unfair to expect a single household to have more than one office space if more than one family member is working from home. It thus seems unfair to disallow the deduction for both of them.
27. Furthermore, office spaces have never catered for an office per person, especially in the more common open space environments.
28. However, we do not share SARS' views that the section deduction is in respect of a specific room (i.e. enclosed four walls) or that the prohibition in section 23(b) is in respect of such room.
29. Section 23(b) merely requires "such part" of a dwelling house or domestic premises. Therefore, if a single home office is shared and each part of the office is exclusively used by each spouse (e.g. separate desks and chairs), both can claim "their part" of the shared office, they just cannot claim the same part.

30. Submission: We believe SARS' interpretation not to reflect the law properly and that "such part" is not a specific room.
31. It is submitted that the home office should be apportioned between the persons using the same home office if they can identify the specific area they each use of such home office (or any room) they should be entitled to make the deduction. It should not be based on the room itself.
32. *Suggested legislative amendment needed:* Where the same part is exclusively used for carrying on a trade by more than one taxpayer who is related it should be allowed as a deduction for both in equal parts.

Examples 5 & 6 – Mainly used

33. Examples 5 and 6 explain the term "mainly used". The examples use the number of working days in a year of assessment to determine whether the home office is mainly occupied for trade purposes.
34. We understood this requirement was to be determined over the period one is required to work from home in respect of each expense item incurred during the tax year and for which income (salary) was earned and not determined merely in relation to the number of working days in the relevant year of assessment. The calculation used to claim any expense will be different depending on interpretation of the above.
35. To illustrate the concern, assume an employee worked for one employer for half of the tax year (50% of the working days in the year of assessment). The employee was required to work from the office during this period of employment. The employee then resigned and

started to work for a new employer for the remaining six months of the year of assessment (50% of the working days in the year of assessment). The new employer allowed the employee to work from home during this period.

36. As the employee has not worked “mainly” (**more than 50%**) of the working days in the year of assessment (only 50%), the employee would be denied any home office allowance deductions incurred during this period.

37. Submission: We submit that the deduction of the home office allowance should be based on the requirement to mainly work from home in respect of each home office expenditure item during which income was earned and not merely on the working days in a year of assessment as the above example illustrates.

4.6.1 Apportionment

38. This section attempts to clarify that when calculating an apportionment ratio, one must not only use the floor area of the main dwelling, but the floor area of all the buildings on the property must be used in calculating the apportionment ratio.

39. The application of this statement to sectional titles is unclear and requires further clarification. Furthermore, clarity is required on whether helpers quarters and unattached extensions on the property are also included in this calculation. For example, certain taxpayers have cottages on their properties or certain properties have 3 houses on one property. If these are being rented out for example, how is this situation dealt with from an apportionment perspective.

40. Submission: Clarity should be provided in the draft IN on the above concerns raised.

41. It is also suggested that the apportionment should be limited in that only the owner of a property can claim the costs, so that there are no duplicate claims. In addition, if a taxpayer does not carry any costs in relation to the cottage, it should be clarified why these should be included in the calculations – where the taxpayer can prove that he/she didn’t carry the costs.

Example 10 – Limitation of deduction when income is not derived mainly from commission

42. Example 10 provides examples of what expenditure will be allowed and disallowed in terms of section 23(m) assuming that all the requirements of section 23(b) are met.

43. Paragraph 4.4 of the draft IN states that deductions available to the taxpayer are limited under section 23(m) to the deductions listed in that section. As far as home office expenses are concerned, the taxpayer will only be able to claim rental, repairs and expenses incurred in relation to a dwelling house or domestic premises under section 11(a) and (d), and wear-and-tear allowances under section 11(e).

44. Submission: We suggest that paragraph 4.4 clarify that it is specifically section 23(m)(iv) which permits the deductions in relation to a home office.

45. The home office expenditure allowed to be deducted for salaried employees is very limited when compared to a taxpayer who mainly earns commission. It is uncertain why this is the case if similar work/tasks are being completed by each employee at home. If an expense was incurred solely for purposes of a trade, surely these must be allowed as a deduction.

46. Submission: *Proposed legislative amendment*: The ambit of section 23(b) expenses should be expanded. An example of items that should be included in the section and allowed as a deduction, would be a salaried employee meeting all the requirements of sections 23(m) and 23(b), having to incur costs such as printing paper, cartridges, stationary, fast/stable internet (such as fibre), security costs etc. to continue to work from home.

47. Regarding internet costs, taxpayers have had to upgrade their internet and telecommunications systems in order to increase bandwidth so that they can carry out their employment duties effectively, including participating in virtual meetings/video conferences, being available on their cell phones (sometimes requiring the installation of boosters etc).

48. Once-off expenses incurred specifically due to working from home e.g. a generator and internet installation costs should also be considered for a deduction or at least they should qualify for a wear and tear allowance.

49. Homeowners insurance and specific "building/structure" insurance have not been mentioned in the draft IN and although this expense would not be applicable to tenants, it would be applicable to homeowners and should be addressed in the draft IN.

50. If employers were reimbursing employees for these costs, it would be understandable that the employees would be restricted from claiming these expenses. However, many employers only covered the costs of data, but the rest of the costs of setting up a home office are not reimbursed. Many employees have thus had to validly spend a lot on office tables and chairs and phones and setting up wifi where employees did not have these. So in reality many costs are not reimbursed by employers and hence employees are left with no relief for certain expenses for which other allowances (such as section 111(e)) are available.

51. In view of the above, we submit that the interpretation of the provision "*expenses in connection with premises*" in section 23(b) should be extended to include the costs of equipping the home office with the necessary consumables (stationery, insurance etc) and running costs (e.g. monthly charges in respect of communication services).

52. *Suggested legislative amendment needed*: Should the above not be acceptable, then the legislation should be amended to accommodate the deduction of these costs considering the unprecedented times that we are living in.

53. Employers are claiming significantly reduced office expenses, i.e. tea, coffee, milk, electricity costs etc. Therefore, more expenses should be allowed as a deduction by salaried employees (earning less than 50% commission) who are covering these costs at home, not just the expenses related to the property as listed in s23(m)(iv).

Proof of expenditure

54. The draft IN does not provide any specific comments on the kind of proof that will be acceptable to SARS in order to claim the home office deduction across all requirements.
55. For example, if one looks at Example 1: How does an employee prove that from March to December that he/she was in the office 4 times a week and then January to March he/she was at home 4 times a week? Furthermore, what must the employee submit to prove these facts? Currently in practice a signed employment contract stating such expectation of mainly working from home is all that is required.
56. Example 7 also raises questions in this regard: What would be considered acceptable proof of working from home if an employer letter will not suffice? Would correspondence confirming that the office is closed suffice? Or would an update to an employment contract to state that an employee can work from home be acceptable proof?

57. <u>Submission:</u> The draft IN should provide specific examples of what kind of proof will be acceptable to SARS in respect of the above matters.
--

4.7 Capital gains tax consequences

58. It is appreciated that it is made clear in the draft IN that the primary residency exclusion of R2 million must be apportioned for non-residential use and that if more than 50% of property is used for business purposes, then it is not a primary residence.
59. However, what is not sufficiently clear or explained in the draft IN is what happens where a taxpayer is a co-owner of the property and each owner might want to claim the same home office space as a deduction in each of their tax returns. Aligned to this is what is the position where taxpayers are renting a property but incur costs in this regard. Even if the answer is that they can't claim these expenses, this needs to be addressed as not everyone owns the properties but some have home offices and have made adjustments or improvements to the properties.
60. The draft IN states the following under paragraph 4.7: *"CGT is payable on the business portion of the capital gain whether or not the taxpayer claimed, or was entitled to claim, a deduction against income in respect of home-office expenses."*
61. With COVID and everyone working from home, the above is a significant issue as it means that all employees who were forced to work from home would need to keep track of their home office expenses, whether or not they claimed the expense. If a person's home office did not meet the requirements to qualify for the home office deduction, it is not clear whether in that case one can argue that the CGT provisions would then not apply to you.

62. <u>Submission:</u> The draft IN should provide specific examples of these scenarios and how to treat them from an income tax and capital gains tax perspective.



Should you wish to clarify any of the above matters please do not hesitate to contact us.

Yours sincerely

Dr Sharon Smulders
Project Director: Tax Advocacy

Pieter Faber
Senior Executive: Tax

The South African Institute of Chartered Accountants