TANZANIA REVENUE AUTHORITY

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THE INCOME TAX ACT, CAP.332

PRACTICE NOTE

DEPRECIATION ALLOWANCE FOR DEPRECIABLE ASSETS.

PRACTICE NOTE NO. 08/2013.
DATE OF ISSUE 1ST NOVEMBER , 2013

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1.0 TAX LAW

This Practice Note applies in respect of depreciation allowance for depreciable asset (initial and annual allowance) under section 17 read with the Third Schedule to the Income Tax Act, Cap. 332.

2.0 INTERPRETATION

1.1 In this Practice Note, unless the context requires otherwise-
"Act" means the Income Tax Act, Cap. 332
"beneficial owner" means the person who has actually incurred the qualifying expenditure on or who has paid for, the depreciable asset and is liable to prove such a claim by documentary or other evidence;
"legal owner" means the person in whose name the depreciable assets is registered or otherwise recorded [example: a certificate of registration for motor vehicle; warranty certificate for a machine; title deeds etc.

1.2 Definitions and expressions used in this Practice Note that are used in the Act have, unless the context requires otherwise, the same meaning in this Note as they have in the Act.

2.0 THE PURPOSE OF THIS PRACTICE NOTE

Depreciation allowances are allowed in respect of assets owned and employed by the person wholly and exclusively in the production of income from a business, and which is likely to lose value because of wear and tear, obsolescence or the passing of time.

This Practice Note considers the ownership and use of a depreciable asset in a person's business and its effect on whether the person qualifies to claim depreciation allowances under section 17 of the Act in respect of that asset in calculating the person's income from the business.

4.0 HOW THE TAX LAW APPLIES

4.1 Depreciation Allowance

Depreciation allowance shall be granted to a person's pool of depreciable assets equal to the depreciation for the year of income for each pool. The allowance for each of a person's pools of depreciable assets shall be calculated as follows:-

(a) In the case of Class 1, 2 and 3 pools, according to diminishing value method; and

(b) In the case of Class 4,5,6 and 7 pools, according to the straight line method.

4.2 Depreciation Basis

4.2.1 Calculation of Depreciable basis

The depreciation basis of depreciable assets of a person at the end of each year of income is calculated as follows:-

(i) In the case of class 1,2,3 or 8 pool of depreciable assets:-

- the depreciation basis of the pool at the end of the previous year of income, if any, after deducting depreciation for that pool for that year of income; and
- amounts added to the depreciation basis of the pool during the year income in respect of additions to the cost of assets (expenditures) in or added to the pool;

  reduced but not below zero, by incomings for the assets in the pool that have been derived during the year of income.

(ii) in the case of Class 4,5,6 or 7 pool of depreciable assets.

- the deprecation basis of the pool at the end of the provisions year of income, and

- amounts added to the depreciation basis of the pool during the year of income in respect of additions to the of assets in or added to the pool;

  reduced by but not below zero, by incomings for the assets in the pool derived during the year of income.

(iii) In the case of a movable tangible asset used by a person who conducts a business of land, sea or air transport operator or charterer to carry passengers, mail, livestock or other movable tangible assets between different countries (international transport) of the depreciation basis of each such asset is calculated separately from other assets of any other class.

If the depreciation basis of a pool at the end of a year of income reduced by depreciation allowance produces an amount that is less than Shs. 1,000,000 additional depreciation of the pool shall be calculated as equal to that amount. The additional allowance will be granted during the year and bring down the depreciations basis to zero.

4.2.1 Calculation of depreciation basis of a pool

For the purpose of calculating the depreciation basis of a pool of depreciable assets –

i) amounts to be added in respect of an asset when the asset is added to the pool shall be reduced by an initial allowance available in respect of the asset (the second portion and the remaining half of the cost) irrespective of the year of income in which the initial allowance is available; and

ii) expenditure incurred in acquiring a road vehicle other than a commercial vehicle to the extent that the expenditure exceeds Shs. 15,000,000 the excess of the expenditure shall not be recognised. For this purpose "commercial vehicle" means:-

   (a) a road vehicle designed to carry loads of more than half a tonne or more than thirteen passengers; or

   (b) a vehicle used in transportation or vehicle rental business

4.3 Deduction for depreciation allowance

In calculating the income from a business, depreciation allowances under the Third Schedule to the Act [*hereinafter referred to as depreciation allowances*] are deductible. When a person acquires and starts using a depreciable asset in a year of income, the person cannot normally deduct the full amount of the expenditure in the first year except for the plant and machinery used in agriculture or mining business and Electronic Fiscal Devices (For Non-VAT registered persons), but can deduct portions of the expenditure for a number of years until the full expenditure amount has been exhausted. The depreciation allowance deduction system can be either straight-line or reducing balance method depending on the class of the asset. Depreciable Assets are grouped in 8 Classes whereby each Class is entitled to a specified rate of depreciation allowance as indicated in the classification table below.

4.4 Classification of Depreciable Assets, Depreciation Rates and Methods

Depreciable assets are classified as follows –

Classification Of Depreciable Assets.

Class number	Depreciable assets	Depreciation rate and method
1	Computers and data handling equipment together with peripheral devices; automobiles, buses and minibuses with a seating capacity of less than 30 passengers, goods vehicles with a load capacity of less than 7 tonnes; construction and earth-moving equipment	37.5% Reducing Balance
2	Buses with a seating capacity of 30 or more passengers, heavy general purpose or specialised trucks, trailers and trailer-mounted containers; railroad cars, locomotives, and equipment; vessels, barges, tugs, and similar water transportation equipment; aircraft; other self-propelling vehicles; plant and machinery used in manufacturing or mining operations; specialised public utility	25% Reducing Balance

	plant, equipment, and machinery; irrigation installations and equipment	
3	Office furniture, fixtures and equipment; any asset not included in another Class	12.5% Reducing Balance
4	Natural resource exploration and production rights and assets in respect of natural resources prospecting, exploration and development expenditure	20% Straight line
5	Buildings, structures and similar works of a permanent nature used in agriculture, livestock farming or fish farming	20% Straight line
6	Buildings, structures and similar works of a permanent nature other than those mentioned in Class 5	5% Straight line
7	Intangible assets other than those in Class 4	1 divided by the asset's useful life Straight line
8	Plant and machinery (including windmills, electric generators and distribution equipment) used in agriculture, Electronic Fiscal Devices (For non VAT registered persons)	100%

A pooling system is used, so that instead of calculating depreciation for each asset separately Depreciation allowance for assets in a Class is calculated with all other assets in that Class. However, for Class 7 assets, each asset is considered separately as a distinct pool. In the case of a movable tangible asset used in a business of land, sea or ait transport or charterer to carry-passengers, mail, livestock or other movable tangible assets between different countries of its own separately from assets of any other Class.

4.5 Conditions for Deduction.

Section 17 of the Act, provides the following general conditions that are to be satisfied for a person to qualify for deduction of depreciation allowance in calculating the person's income for the year of income:

(i) the asset must be owned by the person during the year of income; and

(ii) the asset must be employed wholly and exclusively in the production of the person's income from the business.

While it is normal for an asset to be owned and used by the same person in his business, in some circumstances a depreciable asset may be owned by one person and used by a different person as shown in the following scenarios. For each scenario there will be specific conditions to be satisfied for the person using the asset to qualify for depreciation allowance.

A The asset is registered in the name of one person (the legal owner) although the qualifying expenditure has been incurred by another person (the beneficial owner)

B The asset is registered in the name of one person (the legal owner) although the qualifying expenditure has been incurred jointly by the legal owner and another person.

C The asset is used for the purpose of the business of the legal owner or the business of the beneficial owner.

Asset used for the purpose of the business of one person but registered in the name of another person

Where a person has:

(i) incurred the qualifying expenditure on the asset; and

(ii) the asset is used for the purpose of the business of the person during the year of income; and

(iii) the asset was still in use at the end of the year of income;

that beneficial owner is entitled to claim the depreciation allowance in respect of that asset, even though he is not the registered owner of the asset.

Example

Mambo Safi purchases a lorry in year 2013 and registers it in the name of Mambo Poa. The lorry is used by Mambo Safi in carrying on his transportation business.

Mambo Poa is not entitled to claim depreciation allowance as he has not incurred the qualifying expenditure.

Asset registered in the name of a person and used for the purpose of the business of more than one beneficial owners

Where:

(i) more than one person have incurred qualifying expenditure on a depreciable asset;

(ii) that asset is used for the purpose of a business of each of them during the year of income;

(iii) the asset was still in use at the end of the year of income, and

(iv) the asset is registered in the name of only one of the beneficial owners or in the name of some other person;

each of the beneficial owners of the asset is entitled to claim the depreciation allowances in respect of that asset in the appropriate proportion as determined by his respective share of the qualifying expenditure incurred.

[In such a situation, a statement to the effect that more than one person is claiming the depreciation allowance in respect of the same asset together with details of the apportionment must be made in their respective tax computations.]

***Note*: The requirement to make a statement above does not apply to a situation, which involves a partnership to which each of the persons owns a membership interest.**

Example

Brothers Jua and Kali, each operating his own restaurant business, together purchase a van costing shs. 26,000,000 on 01.09.2013. Jua pays shs.16.0m and Kali pays shs. 10,000,000. The van is registered in

Jua's name. The van is used in both Jua's and Kali's businesses in the year of income. The accounts of both businesses are closed on 31 December.

Depreciation allowance shall be computed as follows:

Year of income 2013	**Jua**	**Kali**
Qualifying expenditure	Shs. 16,000,000	Shs. 10,000,000
Initial allowance [cost due]	NIL	NIL
Balance	Shs. 16,000,000	Shs. 10,000,000
Annual Allowance (37.5%)	Shs. 6,000,000	Shs. 3,750,000
Written Down Value	Shs. 10,000,000	Shs. 6,250,000

For year of income 2013, Juais entitled to depreciation allowance amounting to shs. 6,000,000 and Kali can claim shs. 3,750,000 in respect of the van.

Asset registered in the name and used for the purpose of the business of the legal owner but the qualifying expenditure incurred by another person

Where the qualifying expenditure in respect of a depreciable asset is incurred by a person (the beneficial owner) but the asset is registered and used for the purpose of the business of another person (the legal owner), neither the beneficial nor the legal owner is entitled to claim the depreciation allowances since neither has fulfilled all the prescribed conditions of incurring the expenditure of and employing the asset in the person's business.

Example

Mazao Bora Ltd. Purchases a lorry and registers it in the name of its subsidiary company, Ndizi Safi Ltd. The lorry is used by NdiziSafi Ltd. in conducting its business.

Neither company qualifies for the depreciation allowances in respect of the lorry, since:

i. although it has incurred capital expenditure, Mazao Bora Ltd. did not incur it for the purpose of its business, nor did it use the asset for the purpose of its business; and
ii. although it used the asset for the purpose of its business, Ndizi Safi Ltd. has not incurred the qualifying expenditure.

Note:

Where a depreciable asset is the under a finance lease, the lesser shall be treated as transferring the ownership of the asset to the lessee. In such a case, the lessee has satisfied the condition of ownership of depreciable asset and upon satisfaction of other condition of using the asset he will be entitled to depreciation allowance.

4.6 Initial allowance

Certain depreciable assets are allowed 50% initial allowance. The allowance is available in two portions. The first portion is available in the first year the asset is put into use and second portion is available twelve month after the asset is acquired and put into use.

Note:

50 per cent remaining expenditure of the depreciable assets should not form part of the depreciation basis in the first year in which the first portion of the initial allowance is available but added in the pool with the remaining portion of the initial allowance twelve (12) months after the asset is put to use or the expenditure is incurred whichever is later.

4.6.1 Condition for Granting Initial Allowance.

Initial allowance is granted to items of plant and machinery under the following conditions:

a) Either the item is -
   (i) used in manufacturing processes and fixed in a factory; or
   (ii) used in fish farming; or
   (iii) used for providing services to tourists and fixed in a hotel; and
b) added to the person's Class 2 or 3 pool of depreciable asset.

4.6.2 Calculation of Initial Allowance

Initial allowance is granted in two portions; the first portion 25 percent is available in the year the asset is first put to use and the remaining 25 percent (second portion) is available 12 months after the first portion was available.

4.6.3 Calculation of depreciation allowance

Depreciation allowance shall be granted to a person for a year of income of each pool calculated in accordance with subparagraph (2), (7) and (8) of paragraph 3 of the Third Schedule to the Act.

Illustration.

Calculation of depreciation allowance is illustrated bellow:

During the year of income 2011, Big Limited Company, a manufacturing company had the following balances for each class of depreciable assets. The company also purchased and fixed plant and machinery and disposed some assets as stated below:

Class	1	2	3	4
Dep. Basis as at 1/1/2011	37,500,000	75,000,000	20,000,000	85,000,000
Additions		5,000,000	15,000,000	
Realization proceeds	8,500,000	7,500,000	0	10,000,000

At the end of the year calculation of depreciation allowance will be made in the following manner:

Depreciation Allowance for year of income 2011

Class	**1**	**2**	**3**	**4**
Dep. Basis as at 1/1/2011	37,500,000	75,000,000	20,000,000	85,000,000
Additions		**	**	
Less disposal proceeds	8,500,000	7,500,000	0	10,000,000
Dep. Basis as at 31/12/2011	29,000,000	67,500,000	20,000,000	75,000,000
Depreciation	(10,875,000)	(16,875,000)	(2,500,000)	(15,000,000)
	18,125,000	50,625,000	17,500,000	60,000,000

**- Additions in Class 2 TZS 5,000,000 and Class 3 TZS 15,000,000 are subject to initial allowance in 2011.

Summary of Depreciation allowance year of income 2011

Class	1	2	3	4

First portion of 50% Initial Allowance	0	1,250,000	3,750,000	0
Depreciation	10,875,000	16,875,000	2,500,000	15,000,000
Total allowance	10,875,000	18,125,000	6,250,000	15,000,000

Depreciation for year of income 2012

Class	1	2	3	4
Dep. Basis as at 1/1/2012	18,125,000	50,625,000	17,500,000	60,000,000
Additions (50% of cost)	0	2,500,000	7,500,000	0
Realization proceeds.	0	0	0	0
Dep. Basis as at 31/12/2012	18,125,000	53,125,000	25,000,000	60,000,000
Depreciation	6,796,875	13,281,250	3,125,000	15,000,000
	11,328,125	39,843,750	21,875,000	45,000,000
Second portion of initial allowance	0	1,250,000	3,750,000	0

Summary of Depreciation allowance year of income 2012

Class	1	2	3	4
Second portion of 50% Initial Allowance	0	1,250,000	3,750,000	0
Depreciation	6,796,875	13,281,250	3,125,000	15,000,000
Total allowance	6,796,875	14,531,250	6,875,000	15,000,000

Illustration 2.

Refer Illustration 1 above and assume that Big Company sold the class 3 asset (purchased in 2011) for TZS 12,000,000 in October 2012.

Note:

For the year of income 2012, there is an initial allowance outstanding in respect of class 3 pool of depreciable assets.
Depreciation allowance computation will be as follows:

Depreciation for year of income 2012

Class	1	2	3	4
Dep. Basis as at 1/1/2012	18,125,000	50,625,000	17,500,000	60,000,000
Additions (50% of Initial Allowance)	0	2,500,000	7,500,000	0
Realization proceeds.	0	0	12,000,000	0
Dep. Basis as at 31/12/2012	18,125,000	53,125,000	13,000,000	60,000,000
Depreciation	6,796,875	13,281,250	1,625,000	15,000,000

Summary of Depreciation allowance year of income 2012

Class	1	2	3	4
Second portion of 50% Initial Allowance	0	1,250,000	3,750,000	0
Depreciation	6,796,875	13,281,250	1,625,000	15,000,000
Total allowance	6,796,875	14,531,250	5,375,003	15,000,000

4.7 Realization of Depreciable Assets

4.7.1 Realisation in accordance with Section 39

A person who owns a depreciation asset shall be treated as realizing the asset -

(i) subject to item (ii) below, when the person parts with ownership of the asset including when the asset is sold, exchanged, transferred, distributed, cancelled, redeemed, destroyed, lost, expired or surrendered;

(ii) in the case of an asset of a person who ceases to exist, excluding a deceased individual, immediately before the person ceases to exist;

(iii) in the case of an asset other than a Class 1, 2, 3, 4, 5, 6 or 8 pool of depreciable assets, where the sum of the incomings for the asset exceeds the cost of the asset;

(iv) a depreciable asset, is treated as realised investment asset or trading stock, immediately before the person begins to employ the asset in such a way that it ceases to be a depreciable asset;

Where the asset is realised under any of the circumstances stated above the person realizing the asset is required to calculate the amount to be included in calculating the income of the person for the year of income as required under paragraph 3 of The Third Schedule to the Act.

The excess of –

(a) incomings derived by a person during a year of income for any assets that are or have been in a Class 1, 2, 3, 4, 5, 6 or 8 pool of depreciable assets of the person during the year of income; over;

(b) (i) or (ii), as appropriate –

(ii) in the case of a Class 1, 2, 3 or 8 pool, the depreciation basis of the pool at the end of the year of income

(iii) in the case of a Class 4, 5 or 6 pool, the written down value of the pool at the end of the year of income.

4.7.2 Amount derived from realization of depreciable assets required to be included in the person's income for the year of income:

Gain on realization of a depreciable asset will be included in calculating a person's income from a business, calculated in accordance with the provisions of Section 8(2)(d) read with paragraph 4 of the Third Schedule to the Act as follows:

(a) Realisation of assets in a pool without dissolving the pool

In calculating a person's income for a year of income from the business in which the depreciable assets are or wee employed the excess of incomings over the depreciation basis or the written down value of the pool, as appropriate, shall be included. The excess is calculated as follows:

(i) Class 1.2.3 or 8 pool of depreciable assets

The excess of –

(a) Incomings derived by a person during a year of income for any of the assets during the year of income; over

(b) The depreciation basis of the pool at the end of the year of income calculated under paragraph 3(3) but disregarding these incomings.

(ii) Class 4,5 or 6 pool of depreciable assets

The excess of –

(a) incomings derived a person during the year of income;

or

(b) the written down value of the pool at the end of the year of income disregarding those incomings.

Example

An entity D Corp Limited's balance of depreciable basis of its Class 2 pool of depreciable assets at the end of the year 2011 was Shs. 7,599,999/=. The entity transferred in year 2012 one of its assets in the pool to its resident subsidiary for Shs. 8,000,000 being the market value calculated in consistence with the Act.

The amount to be included in calculating the entity's income the business for year 2012 from the realisation is the excess of the incomings over the depreciation basis of the pool, calculated as follows:

Incomings		Shs.	8,000,000
Less:			
- Depreciation basis 2011 -	7,500,000		
- Depreciation for year 2012	1,875,000		
Depreciation basis end of 2012	Shs.	5,625,000	
The excess to be included	Shs.	2,375,000	

Note

Where the asset was realised for a value (incomings) of less than the deprecation basis of the pool at the end of the year, in this case shs. 5,625,000 the entity would have incurred a loss. The loss is not deductible in calculating the entity's income since section 18 allows only deduction of loss from realisation of a business asset of the business.

(b) Dissolution of a pool of depreciable assets

Where the assets in a pool of depreciable assets of a person are all realised by the person before the end of a year of income the pool shall be dissolved and –

(aa) an amount is included in calculating the person'sincome for the year of income calculated in accordance with the following formula –

$$A – B$$

(bb) an allowance shall be granted to the person for the year of income calculated in accordance with the following formula –

$$B – A$$

Where;

A is the person's incomings derived during the year of income or to be derived for the assets; and

B an allowance shall be granted to the person for the year of income calculated in accordance with the following formula –

Where;

A is the person's incomings derived during the yer of income or to be derived for the assets; and

B is the sum of –

(i) the written down value of the pool at the end of the previous year of income; and

(ii) any initial allowance otherwise available in respect of the pool for the following year of income under Paragraph 2; and

(iii) expenditure added to the depreciation basis of the pool during the year of income or to be added during the following year of income under paragraph 3(5).

5.0 REVOCATION

Pursuant to the provisions of Section 130(2) the Practice Note Number 07/2004 issued on 15th December, 2004 is hereby revoked.

Signed……………….

Commissioner

1st November, 2013.