DEDUCTIBILITY OF ROYALTIES: A RECENT CASE THAT RUFFLED FEATHERS
[DISCUSSION OF THE JUDGMENT OF WAGLAY J IN CASE NUMBER 11454 IN THE TAX COURT]*

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1 Introduction

The Tax Court, sitting in Cape Town, recently had occasion to consider the deductibility of royalty payments.[1] In general it may be said that royalties are payments for the use of another's intellectual property, such as patents or trade marks. As such, royalty payments are made on a daily basis in the commercial world. It has always been widely accepted that royalty payments are deductible from income in terms of the general deduction formula[2] and taxpayers have for years claimed this deduction without objection from the South African Revenue Service. In the case under discussion, the Commissioner for the South African Revenue Service (the "Commissioner") successfully challenged this accepted view regarding the deductibility of royalties, the court finding that the payments were of a capital nature and therefore not deductible.

2 The Facts

The taxpayer manufactures supplies and markets certain products in South Africa. Together with a number of other companies, the taxpayer dominates the market in South Africa. Each of these companies conducts its operations under a brand name, which it either owns or is licensed to use. In terms of the taxpayer's memorandum it is obliged to use a certain corporate name by permission of its holding company with the stipulation that on withdrawal of such permission, it would cease to use this name or trade mark.

The taxpayer's holding company, which is incorporated in England and Wales, is the owner of the trade mark and other licensed marking *indicia* (collectively referred to as the trade mark) used by the taxpayer. Until 1997, the taxpayer used this trade mark free of charge. In 1997 an agreement was entered into between the taxpayer and its holding company in terms of which the taxpayer obtained the non-exclusive and non-assignable authorisation to use this trade mark, whilst the holding

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[1] Case no 11454.
[2] Emslie, Davis, Hutton & Oliver *Cases and Materials* 350; De Koker *Silke on South African Income Tax* (2005) par 7.25.

company remained the owner of the trade marks. The agreement would subsist for a period of two years, whereafter it would be renewed automatically for succeeding twelve-month periods, unless either of the parties terminated the agreement by giving six months' notice to the other, or by reason of some breach, as set out in the agreement. If the agreement were to be terminated, the taxpayer would no longer be able use the trade mark. In return for the use of the trade mark, the taxpayer was to pay an annual royalty fee to the holding company. The fee was calculated as a rate per measure of product sold. During the 1997, 1998 and 1999 years of assessment, the taxpayer sought to deduct these royalty payments in terms of section 11(a) of the Income Tax Act ("the Act") in calculating its taxable income. After the Commissioner refused the deduction, the taxpayer appealed to the Tax court.

3 The Law

Section 11(a), read with section 23(g) of the Act, allows the deduction of expenditure or losses actually incurred in the production of income, provided that the expenditure or losses are not of a capital nature. The deduction will be allowed only to the extent to which moneys are laid out or expended for the purposes of trade. In issue in the present case was whether the expenditure in question, that is, the payment of royalties, was of a capital nature. If found to be of a capital nature, these expenses would not be deductible in terms of the relevant section.

In order to determine whether expenditure is of a capital nature or not, the true nature of each transaction must be examined. If the expenditure incurred should properly be regarded as part of the cost of performing the income-earning operations of the taxpayer, it is of a revenue nature. If, on the other hand, the expenditure incurred should properly be regarded as part of the cost of establishing or improving or adding to the income-earning plant or machinery, it is of a capital nature.[3] Put differently, money spent on creating or acquiring a source of profit is capital expenditure, whilst money spent working that source is of a revenue nature.[4]

Two subsidiary tests have been developed by the courts to assist in determining whether expenditure is of a capital or revenue nature.[5] The first is the so-called "enduring benefit test" which Lord Cave, in *British Insulated Helsby Cables v Atherton*,[6] formulated as follows:

> "But where an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

[3] *New State Areas Ltd v CIR* 1946 AD 621.
[4] *CIR v George Forest Timber* 1924 AD 526.
[5] According to Emslie et al *Income Tax Cases and Materials* 350, if the test set forth in the *New State Areas* case provides a clear answer, there is no need to apply the other two tests. It is only when the first-mentioned test is equivocal that the subsidiary tests are applied.
[6] 1926 AC 205.

This test has been applied by our courts many times.[7] It has been pointed out that the word "enduring" does not mean "interminable or even for the whole of the duration of the business of the company". Depending on the nature of the enterprise and of the benefit, a lesser degree of permanence is sufficient.[8] Criticism against the enduring benefit test is that no certainty exists as to the length of the time which is needed in respect of each asset or advantage, in order for it to be regarded as "enduring".[9] It may therefore be difficult to apply the enduring benefit test, as one would never be sure when a court will regard an asset or benefit as enduring.

The second of the subsidiary tests is the "once-and-for-all test". According to this test, if a payment is made once and for all, it is a capital expenditure, whilst recurrent expenditure is of a revenue nature. This test has, however, been described as:

> "[O]f little value in those cases where capital expenditure is given the appearance of revenue expenditure because it is paid in instalments and where revenue expenditure is given the appearance of capital expenditure because it is commuted and paid in one lump sum."[10]

This test is therefore also of limited practical value because of the fact that the frequency of payments may be controlled or even manipulated by the parties to the transaction.

4 The Judgment

4 1 The taxpayer's arguments

On behalf of the taxpayer it was argued that the holding company, and not the taxpayer, was the owner of the trade mark, that the taxpayer obtained no enduring benefit, as the contract could be terminated on six months' notice and that the royalty payments were recurrent annually. For these reasons, the taxpayer argued, the royalty fees were not of a capital nature and therefore deductible.

In order to support the point that the payment was of a revenue nature, counsel for the taxpayer drew an analogy between the royalty payments made by the taxpayer and rental payable by a tenant to a landlord. Like the rental, the royalty was payment for the use of another's asset. The court rejected this analogy on the basis that the nature and effect of the asset, the use of which was being paid for, differed on two material points. First, so the court reasoned, the taxpayer would be unable to trade without the trade mark. The court rejected the notion that the trade mark was comparable with a good trade location in the context of the landlord and tenant analogy, on the basis that a single location is not necessary for the success of a business. Secondly, a characteristic of a

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[7] Eg *Palabora Mining Co Ltd v SIR* 1973 3 SA 819 (A); *CIR v African Oxygen Ltd* 1963 1 SA 681 (A).
[8] *CIR v African Oxygen Ltd supra* 689.
[9] *Nchanga Consolidated Copper Mines Ltd v COT* 1962 1 SA 381 (FC) 388.
[10] *New State Areas Ltd v CIR supra* 622.

trade mark is that it is distinctive. This is not so in the case of a fixed asset which is being leased. The trade mark gives identity to the user thereof and carries with it the reputation associated with the product, whilst a leased premises does not give identity to its lessee, nor does it carry any reputation with it. The court came to the conclusion that, in the present case, the taxpayer derived its structure and goodwill from the trade mark and would be unable to continue its business without the trade mark. The court held that in the case of the lease of a building, the taxpayer would be able to move to another building without its structure or goodwill being affected.

In assessing the court's argument, one should ask whether the differences between the nature of a trade mark and fixed property referred to by the court are sufficient to reject such an analogy. In cases relating to other branches of the law, our courts have found the analogy between rental and royalties helpful and have not been concerned about perceived differences.[11] It is submitted that, in the final instance, in the case of rental and the royalty fee, payment is being made as consideration for the use of another's asset. The fact that these assets may differ in certain respects does not seem relevant when the deductibility of payment for its use is considered.

Albeit in a different context, the Supreme Court of Appeal in *Cactus Investments (Pty) Ltd v CIR*,[12] pointed out limitations in the analogy between rental payable for the use of an asset and interest paid on money borrowed. In that case, the court refused to regard interest paid by a borrower to a lender as payment for the use of money, because in the *Cactus* case, the court dealt with loans for consumption in which the borrower becomes the owner of the money. The court therefore based its rejection on the fact that in the case of a loan for consumption, ownership in the capital sum passed from lender to borrower and, consequently, that no continuing obligation rested on the lender. In the case of a lease, ownership of the asset does not pass and the lessor has the obligation to make the asset available, as well as other continuing obligations.

Returning to the present case and the analogy between rental and royalties, the court seems to have accepted that in both instances the lessor or trade mark proprietor remains the owner of the asset. The court therefore does not distinguish the rental and royalty payments on the same basis as the distinction between rental and interest as set out in the *Cactus* case. The court's argument seems to be based solely on the difference in the nature of the asset. It is submitted that this differentiation is not sufficient to reject the analogy, as in both instances payment is made for the use of another's asset.

Furthermore, while the court's argument that a good trading location

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[11] In *African Gold Recovery Co v Crowns Reef Gold Mining Co* 1899 6 Official Reports 84, it was stated "I will admit that the relations of licensor and licensee are similar to those of lessor and lessee". See also *Wistyn Enterprises (Pty) Ltd v Levi Strauss & Co* 1986 4 SA 796 (T).

[12] 1999 1 SA 315 (SCA).

is not indispensable to the success of the business and that a business may be moved to a different building, might be true in the present case, it certainly is not true in general. Very often trade location is of paramount importance to a business and a move to a different location might render it unable to continue its operations. A specific location may, therefore, in particular circumstances, have goodwill attached to it.[13]

Even if it is accepted that a business could continue unaffected in a different location, it must surely follow that relocation of the business will involve significant costs. The court accepts that the use of the trade mark in this instance meant that the taxpayer did not have to incur the very significant costs of re-branding itself and its product. Would re-branding and relocating not involve similar costs and disruptions and necessitate adaptations by a business?

In conclusion, it is submitted that the analogy between rental and royalties has merit and serves as a useful aid in determining whether the royalty payments were of a capital nature. The writer is of the view that the court was wrong in rejecting the analogy.

4 2 Arguments on behalf of the Commissioner

On the authority of the well known and often quoted passage in *CIR v Genn & Co (Pty) Ltd*,[14] it was argued on behalf of the Commissioner that the closeness of the connection between the expenditure and the income-earning operations had to be assessed, having regard to both the purpose of the expenditure and what it actually affects. The court held that an overly technical classification of a right or benefit should not be followed in determining the nature thereof. A practical and business point of view should rather be taken and, in the present case, this meant that the nature of the advantage sought by the taxpayer is determined by the following factors: most of the taxpayer's competitors operate under well-established international brand names and marks; the trade mark was well established in the South African market and use thereof would enable the taxpayer to differentiate its products from those of its competitors; to avoid the costs of re-branding itself; to enable the taxpayer to take advantage of the reputation of the trade mark in South Africa; to enhance customer loyalty and increase sales and increase market share.

In support of its finding that a practical and business point of view should be followed, the court quotes from an Australian source. It is interesting that the court felt the need to refer to Australian authority, simply to make this point. Rather, one would have expected the court to refer to the test formulated by the Australian courts in determining the

[13] *Rosenbach & Co (Pty) Ltd v Dalmonte* 1964 2 SA 209; *Receiver of Revenue (Cape) v Cavanagh* 1912 AD 464.
[14] 1955 3 SA 293 (A).

difference between expenditure of a capital and revenue nature[15] in support of its finding on the merits of the case. The test used in Australia certainly corresponds closely to the predominant test used in South African courts[16] and guidance on the issue of the deductibility of royalties may be sought from their precedents.[17]

The court did, however, find it necessary to quote from the heads of argument of counsel in *SIR v Cadac Engineering Works (Pty) Ltd.*[18] It is interesting to note that the court does not acknowledge that the passage quoted comes from the heads of argument, nor does it state whether it agrees with this argument or not. The quotation is merely presented as authority for the view that expenditure which is intended to produce income is not for that reason alone categorised as revenue expenditure.

In an argument which is hard to follow, the Commissioner made the point that the taxpayer needed the license to use the trade mark before it could operate its business and that, consequently, the taxpayer was obtaining a source of income, rather than incurring expenditure in working that source. The court dismissed this argument by simply stating that the taxpayer did not require the trade marks to operate its business, because it was already in operation. The agreement was entered into by the taxpayer with its holding company in order to retain and build the business it already operated.[19]

On the strength of *Rand Mines (Mining & Services) Ltd v CIR*,[20] the Commissioner further argued that the agreement between the taxpayer and its holding company did not in itself produce income, but that it created an opportunity for the taxpayer to earn income. Consequently, so the argument went, the expenditure was of a capital nature. In the *Rand Mines* case, the taxpayer's business was to manage and administer mines in the Rand Mines group. An amount paid by the taxpayer to another company as compensation for the cancellation of that company's contract to manage a mine which the Rand Mines group had recently acquired, was disallowed as a deduction. The court held that Rand Mines did not hold the management contracts as its stock-in-trade. Its stock-in-trade was the provision of management services. The fact that the taxpayer's parent company determined when management contracts would be acquired or disposed of played an important role in the court's decision. The management agreements were seen as an opportunity to

[15] Eg in *Sun Newspapers Ltd v The Federal Commissioner of Taxation* 1938 61 CLR 337.
[16] See par 3 *supra*.
[17] Eg *Cliffs International Inc v Federal Commissioner of Taxation* 1979 HCA 8, 1979 142 CLR 140, in which it was found that a royalty payment was of a revenue nature and therefore deductible.
[18] 1965 2 SA 511 (A).
[19] The court's findings in this regard should be contrasted to its findings later in the same judgment where it held in par 44, that "[t]his expenditure is akin to expenditure incurred in setting up a business" and later again, in par 63, that the payments in issue were "in substance a purchase price for a business".
[20] 1997 1 SA 427 (A).

earn income by providing management services and therefore they constituted part of the taxpayer's income earning structure.

In the present case, the court found some merit in the Commissioner's argument that the agreement between the taxpayer and its holding company could be likened to the mine managing contracts in the *Rand Mines* case. The court held that the agreement between the taxpayer and its holding company for the use of the trade mark was a "vital component" of its business, without which its "business or trading prospects are limited". The court also agreed with the Commissioner's submission that the royalty payments were akin to payments made for the acquisition in terms of a franchise agreement.

It is submitted that the *Rand Mines* case may be distinguished from the present one in a number of ways. First, in the *Rand Mines* case, the management contracts themselves, which obliged Rand Mines to render such management services, were the source of income. In the present case, the trade mark itself did not generate any income: it was one of a number of things used by the taxpayer to generate its income form manufacturing and selling certain products. Secondly, in the *Rand Mines* case, the taxpayer did not usually pay for the cancellation of a management contract. The payment also constituted a substantial and once-off amount. In the present case, the taxpayer and its holding company agreed on a market-related rate for the calculation of the royalty and that amount was payable annually, and therefore recurrently, by the taxpayer to its holding company. Nowhere was it argued that these payments were unusual or even substantial in comparison with the taxpayer's business. Thirdly, in the *Rand Mines* case, the taxpayer acquired an asset of a capital nature, namely the management contract which allowed it to render certain services. In the present case the trade mark constituted the asset. The taxpayer never acquired the asset, it merely paid a royalty for the use of the asset.

This point may be illustrated by returning to the analogy of a lease agreement. The court in the *Rand Mines* case compared[21] the acquisition of the management contracts to a situation where a landlord purchases from another landlord the latter's leases, not with a view to their resale, but with a view to acquiring rents payable in terms of these leases. In such a situation the court was of the view that the expenditure incurred by the landlord would be of a capital nature. As stated above, the comparison between the royalty payment in the present case and rental paid to a landlord entails that in both cases payment is made for the use of an asset; in the case of rental, it is for the use of fixed property, in the case of the royalty, it is for the use of a trade mark. In the *Rand Mines* case, the taxpayer paid to acquire a capital asset, namely the management

[21] The court made it clear that the comparison was not entirely valid, but truer than the taxpayer's argument that expenses incurred by a landlord in connection with leases are comparable with the payment for the management agreement.

contract, similar to a situation in which a landlord pays for the acquisition of other leases. In the case of the royalty payments, the taxpayer did not pay its holding company for the acquisition of the trade mark. It paid to use the trade mark. Lastly, in the present case, the court regarded the royalty payment as akin to a payment in terms of a franchise agreement which the court held to be of a capital nature. No authority is provided for the court's decision on this score. However, in the *Rand Mines* case, the court likened the management contracts to franchise agreements, the cost of acquisition of which was not regarded as revenue expenditure. The court in the *Rand Mines* case referred to *ITC 1063*[22] in which it was held that payment to a manufacturer of gramophone records for a sole right of distribution was expenditure of a capital nature. What is interesting to note, however, is that in the *ITC 1063* case, the court specifically found that the payments were not royalties.[23] The payment in that case was for the purpose of *buying* a franchise and, although it was paid in three pre-determined instalments, it could be regarded as a lump-sum payment. It should also be noted that in the *Rand Mines* case the court held that the cost of the *acquisition* of a franchise agreement is of a capital nature. One would therefore be able to argue that the *Rand Mines* and *ITC 1063* cases are authority for the view that a once-off payment to acquire a franchise is of a capital nature.

It is, however, not authority for the view that royalty payments made to the proprietor of a trade mark is of a capital nature. The court in the present case seems to have confused these points as it found that the royalty payments were

> "in substance a *purchase price* for a business which gave a substantial market share in the defined area, similar to a franchise agreement. The payments made to *obtain* these rights must therefore by its very nature be a capital expense" (own emphasis).[24]

Clearly the royalty payments were payments for the use of the trade mark. The taxpayer never acquired or purchased the trade mark.

In *CIR v African Oxygen Ltd*,[25] the taxpayer agreed with a competitor to form a third company, the losses of which the taxpayer undertook to make good in exchange for, *inter alia*, the competitor agreeing not to compete with the taxpayer. The court held that the enforceable right which the taxpayer had to prevent its competitor from competing with it was, in itself, an actual asset. This asset was of a sufficiently enduring nature and, in the absence of a close link between the income-earning operation and the expenditure, this expenditure was held to be of a capital nature. With reference to the above case, the court in the present matter reasoned that the right to use the trade mark is in itself a capital asset.

[22] 27 SATC 57 (N).
[23] *Supra* 58.
[24] Case no 11454 par 63.
[25] 1963 1 SA 681 (A).

It could be argued that the right to prevent someone from competing with a business, which the court in the *African Oxygen* case found to be of a capital nature, is not similar to the right to use a trade mark. Costs spent on eliminating the competition, whether by way of a right to prevent a competitor from trading[26] or by buying out the competitor,[27] are of a capital nature. However, costs spent on paying for the right to use another's asset (although that right may in itself be an asset) should be regarded as being of a revenue nature. This may be explained by returning, once again, to the analogy between rent and royalty. Even though a rental agreement (that is, the right to occupy a premises) may under certain circumstances be regarded as a capital asset in the hands of a lessee,[28] payment of the rental to the landlord is regarded as of a revenue nature. The point is fortified by bearing in mind that, in the present case, the agreement entailed non-exclusive authorisation to use the trade mark. All the taxpayer received was the right to use the trade mark. The taxpayer's competition was not eliminated[29] and, because this authorisation was non-exclusive, the holding company could, if it so wished, authorise any other person to trade in South Africa under the same trade mark.

Next the Commissioner argued that the taxpayer obtained an enduring benefit by entering into the agreement with its holding company. Although the agreement would initially only subsist for a period of two years and thereafter be automatically renewed annually, unless one party gave the other six months' notice, the court found that the taxpayer had acquired an enduring benefit. As stated earlier,[30] the problem with the enduring benefit test is determining the period for which a benefit should subsist in order for it to be "enduring". In *Nchanga Consolidated Copper Mines Ltd v COT*,[31] the court held that an advantage of one year was not an "enduring benefit". In the *Palabora Mining*[32] case it was found that the supply of water eight months earlier was a short-lived advantage, and therefore not of an enduring benefit. In the *African Oxygen*[33] case an agreement for a period of seven years was found to be an enduring benefit. A contract enduring for 20 years was held in the *Rand Mines*[34] case to provide an enduring benefit. In the *ITC 1063*[35] case a right granted for three years, with a right of renewal for a further two years,

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26 *CIR v African Oxygen Ltd supra.*
27 *Cadac Engineering Works supra.*
28 ITC 175 5 SATC 180; SARS Draft Comprehensive Guide to Capital Gains Tax par 24.3 where SARS seem to acknowledge that an amount paid to a lessee for the termination of a lease is of a capital nature.
29 The court acknowledges this by stating repeatedly that the taxpayer needed the trade mark because its competitors used international brand names.
30 Par 3 *supra.*
31 S*upra* 390-391.
32 *Supra 833.*
33 S*upra* 689.
34 S*upra* 435.
35 S*upra* 59.

was found to be "a substantial period" and to constitute an enduring benefit. The correctness of the court's inference in the present case that a contract, initially for two years and thereafter renewable annually unless the required notice was given, is an enduring benefit, is, in the light of the case law cited above, open to doubt.[36]

The court found that the fact that the payments were labeled as royalties was irrelevant in determining whether it was of a capital nature or not. The court also deemed irrelevant to this inquiry the manner of calculating the amount to be paid, namely as a percentage of volume sold, also the fact that the payment was recurrent, as was the point that the taxpayer was not the owner of the trade mark.

The court concluded that the expenditure incurred was to protect and increase the taxpayer's market share and reputation. Consequently, the court held that the expenses related to the taxpayer's income earning structure rather than to its income earning operations and were thus of a capital nature.

5 Applying the Law to the Facts

If one applies the tests to distinguish between revenue and capital expenditure as laid down by the courts[37] to the facts of the present case, a different conclusion may be reached than the one arrived at by the court.

Payments for the right to use another's trade mark (even if the trade mark is a very important part of one's business) is part of the costs of performing the taxpayer's income-earning operations. Such payments cannot be regarded as part of the cost of creating an income-earning structure. It is submitted that, in coming to its conclusion, the court attributed insufficient weight to the fact that the taxpayer was not the owner of the trade mark and that it merely paid for the use of the trade mark. In the *New State Areas*[38]case, the court ruled that an annual redemption payment to the Town Council in respect of sewers located on the mine's property, which consequently had become the mine's property, was of a capital nature and consequently not deductible. A similar payment, in respect of sewers located off the mine's property, was held to be of a revenue nature. The court was of the view that the mine had acquired no asset and that, consequently, the payment was made for the *use* of the Town Council's sewers. In the *Palabora Mining* case, the loss incurred by the taxpayer in constructing waterworks on another's property to enable the taxpayer to receive water earlier than would otherwise have been the case, was regarded as revenue in nature. In that case the taxpayer was not the owner of the waterworks and the court held that such loss never created an asset for the taxpayer. The court held that

[36] *Cf* Du Plessis "Annual Royalty Payments Held to be Non-deductible" March 2006 *De Rebus* www.derebus.org.za [11.05.06].

[37] Par 3 *supra*.

[38] S*upra* 627-628.

the fact that no asset was acquired as a result of the expenditure was always a relevant factor to be taken into account when determining whether expenditure was of a capital or revenue nature. In the present case, the taxpayer was not the owner of the trade mark and merely paid a royalty for the use of such trade mark.

In the *Palabora Mining* case, the court regarded as a cardinal feature of the case the fact that no asset was created in the hands of the taxpayer, together with the fact that the taxpayer's objective with the expenditure was to accelerate the supply of water to the taxpayer. The accelerated supply of water was found by the court not to be an enduring benefit. In other words, although the fact that the taxpayer was not the owner of the asset was an important factor taken into account by the court, this was not decisive. However, coupled with the fact that the taxpayer received no enduring benefit, the court was persuaded that the expenditure was of a revenue nature and therefore deductible.

If this reasoning is applied to the present case, it is clear that the royalty payments should similarly be regarded as revenue in nature. The taxpayer never became the owner of the trade mark and, as argued above, the agreement between the taxpayer and its holding company for the use of the trade mark did not constitute an enduring benefit.

6 Implications of the Judgment

The judgment certainly has implications, not only for payment of royalties on trade marks, but also for royalties on other forms of intellectual property, such as patented inventions or copyright works like computer programs.

The court's finding seems to imply that, if a taxpayer relies solely on one item of intellectual property, which is of crucial importance to the taxpayer's business and determines its identity, the royalties payable in respect thereof will not be deductible. It has been suggested that if the taxpayer relies on more than one trade mark or produces numerous products subject to several licensing agreements, that the judgment will not apply, and that, accordingly, the royalties paid will be deductible.[39] If this is correct, the question arises as to why a taxpayer who uses only one trade mark should be penalised with non-deductibility, whereas a taxpayer using multiple trade marks is allowed deductions. This point reinforces the view that payment for the *use* of an asset is not part of the cost of establishing, improving or adding to the income-earning structure. In other words, paying for the use of a trade mark does not make that trade mark part of the taxpayer's structure. This holds true, whether the taxpayer uses one trade mark or many, and even if the trade mark(s) is(are) very important to the taxpayer's business.

[39] Lessing & Wellsted "Recent Tax Developments" 2005 *Tax Works* vol 22 2-3.

7 Conclusion

It is widely accepted that royalty payments are of a revenue nature and therefore deductible.[40] The court's judgment that the royalty payments are of a capital nature is based on its failure to regard the royalty as payment for the use of another's asset. In this regard, the analogy between royalties and rental paid by a tenant to a landlord would have served as a useful guide in determining the nature of the payment. Furthermore, the case law cited supports the view that in the present case the agreement between the taxpayer and its holding company was not an enduring benefit and should therefore be deductible. This, coupled with the fact that the taxpayer was not the owner of the trade mark, shows that such royalty payment is of a revenue nature and should therefore be deductible.

OPSOMMING

Hierdie artikel bespreek die onlangse beslissing van die Kaapse Belastinghof waarin bevind is dat die betaling van 'n tantième vir die gebruik van 'n handelsmerk en ander simbole nie aftrekbaar is ten einde 'n belastingbetaler se belasbare inkomste te bereken nie. Die hof se beslissing dat hierdie tantième van 'n kapitale aard is word ontleed en gemeet aan die regsbeginsels neergelê deur die howe om te bepaal of 'n uitgawe van 'n kapitale aard is al dan nie. Die gevolgtrekking word gemaak dat die beslissing nie korrek is nie.

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[40] Par 1 *supra*.