



CHIPKIN (NATAL) (PTY) LTD v COMMISSIONER FOR SOUTH AFRICAN REVENUE
SERVICE
[\[2005\] 3 All SA 26 \(SCA\)](#)
67 SATC 243

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Division: Supreme Court of Appeal
Date: 12 and 20 May 2005
Judges: HOWIE P, CAMERON JA, NUGENT JA, CLOETE JA AND PONNAN JA

Income tax - Recoupment - [Section 8\(4\)\(a\)](#) of the Income Tax Act [58 of 1962](#) - Taxpayer having entered into an en commandite partnership which had purchased an aircraft in order to carry on its business, had claimed its pro rata portion of the [s 14bis](#) allowance granted to it in the relevant years of assessment and thereafter disposed of its partnership interest to a new company which acquired a 99,9% interest in partnership - Taxpayer had calculated its pro rata share of the [s 14bis](#) allowance in terms of [s 24H\(5\)\(b\)](#) of Act [58 of 1962](#) - In consideration for the disposal the bank concerned had released the taxpayer from the outstanding balance of the loan which the taxpayer had originally taken out to finance its capital contribution to the partnership - Whether such disposal by taxpayer of its partnership interest gave rise to a recovery or recoupment in terms of [s 8\(4\)\(a\)](#) of Act [58 of 1962](#) of the allowances granted to taxpayer in terms of [s 14bis](#) of the Act - Commissioner for SARS contending that disposal by taxpayer of its percentage interest in partnership resulted in a recoupment in terms of [s 8\(4\)\(a\)](#) of the allowances granted in terms of [s 14bis](#) - Held that where income has accrued to a partner in terms of [s 24H\(5\)\(a\)](#) the partner is also entitled to deduct a proportionate share of deductions and allowances that are granted by the Act thereby arriving at the partners' taxable income in terms of [s 24H\(5\)\(b\)](#) and it is the partner who recoups that allowance when he disposes of his interest - Held that in casu the taxpayer had recouped the cost to it of its share in the asset in respect of which it had made the tax deductions - Held accordingly that taxpayer did recover or recoup (as envisaged in [s 8\(4\)\(a\)](#)) a pro rata portion (calculated in terms of [s 24H\(5\)\(b\)](#)) of the allowance (granted in terms of [s 14bis](#)) in respect of the purchase by partnership of an aircraft on disposal by taxpayer of its partnership interest.

Appellant and eleven others had entered into a partnership and the only disclosed partner was Air Southern Cross Management (Pty) Ltd ('ASCM') and the others, including appellant, were partners *en commandite*.

The partnership agreement provided that 'Each partner shall share in the profits, losses, rights and obligations of this partnership in accordance with his percentage interest, and in the manner provided for in this agreement'.

Appellant's contribution to the partnership was a cash amount, for which it acquired a 30% interest in the partnership.

Page 244 of 67 SATC 243

Appellant financed this contribution by taking out a loan with a bank and ASCM acted as the manager of the partnership and its contribution comprised its skill, management and administration of the business and affairs of the partnership and for this it received a 0,1% interest in the partnership and, in addition, payment of a sum of money from the other partners.

The remaining nine partners also made cash contributions to the partnership and held the remaining 69,9% interest in the partnership.

The business of the partnership was to purchase a particular aircraft and either by itself or with other persons to conduct the business of transporting by air and for reward persons, livestock, goods or mail.

In fact the aircraft had already been purchased by ASCM but it was paid for out of partnership funds and it accordingly became a partnership asset.

The partnership, on the same day that it was formed, entered into a partnership with BOP Air (Pty) Ltd ('the Southern-BOP partnership'), the purpose of which was also to use the aircraft to conduct air transportation business for reward and it did so.

[Section 14bis](#) of the Income Tax Act [58 of 1962](#) provided for an allowance to be deducted from 'the income of any person' in respect of an aircraft acquired by such person on or after the first day of April 1965.

[Section 24H\(5\)\(a\)](#) provides that income that has accrued to partners in common is deemed to have accrued to each of the partners individually in their proportionate shares and where income has accrued to a partner in terms of [s 24H\(5\)\(a\)](#) the partner is also entitled in terms of [s 24H\(5\)\(b\)](#) to deduct a proportionate share of

deductions and allowances that are granted by the Act thereby arriving at the partners' taxable income.

Appellant had claimed its *pro rata* portion of the [s 14bis](#) allowance during the 1989, 1990 and 1991 years of assessment and during appellant's 1992 year of assessment it transferred 99,9% of its 30% interest in The Southern Cross Air Partnership to ASCM.

In consideration for the aforementioned disposal, the bank released appellant from the outstanding balance of the loan which appellant had originally taken out to finance its capital contribution to the partnership.

Respondent, the Commissioner for SARS, held the view that by virtue of the disposal, the *pro rata* [s 14bis](#) allowances previously claimed by appellant were recouped in terms of [s 8\(4\)\(a\)](#) of the Income Tax Act [58 of 1962](#).

Respondent accordingly issued appellant's original income tax assessment for the 1992 tax year on the basis that there had indeed been a recoupment.

Appellant's objection was disallowed and the appeal to the Gauteng Tax Court was unsuccessful, see *ITC 1784* (2004) [67 SATC 40](#), whereupon leave to appeal directly to the Supreme Court of Appeal was granted by the Gauteng Tax Court.

In the court *a quo* Goldblatt J had held that, to the extent that the credit of R6 047 670,18 received by appellant from the bank was compensation for appellant transferring 99% of its interest in the aircraft owned by the partnership, such amount was a recoupment by appellant of allowances granted to it in terms of [s 14bis](#) of the Act.

Appellant contended, *inter alia*, that there was a distinction between the cost to a partner of acquiring a share in the partnership and the cost to the partnership of acquiring an asset and also emphasized the distinction between the disposal by a partner of an interest in a partnership and the disposal by the partners of a partnership asset.

Appellant further contended that the allowances were recouped only when the partnership sold the aircraft in 1995 as the allowances had accrued to the partnership (when it acquired the aircraft) and not to the partners individually (when they each acquired their proportionate shares in the aircraft upon becoming partners) and by the same token it was only when the partnership disposed of the aircraft that the allowances were recouped.

Page 245 of 67 SATC 243

Held

- (i) That appellant did recover or recoup, as envisaged in [s 8\(4\)\(a\)](#), a *pro rata* portion (calculated in terms of [s 24H\(5\)\(b\)](#)) of the allowance deducted under [s 14bis](#) as appellant had made a capital contribution to the partnership that gave it, simultaneously, a 30% share in the partnership and an undivided share in the aircraft and the acquisition of the share in the aircraft entitled appellant to a share of the [s 14bis](#) allowance for the cost of the aircraft; moreover, because of the provisions of [s 24H\(5\)\(b\)](#), the acquisition of the 30% interest in the partnership determined appellant's share of that allowance at 30% and when appellant disposed of 99% of its 30% interest in the partnership, it disposed of a corresponding percentage of its undivided share in the aircraft.
- (ii) That the approach followed by Trollip JA in *Van der Merwe v SIR 1977 (1) SA 462* (A) at 478G-H is not now appropriate inasmuch as [s 24H\(5\)](#) makes it clear that a *pro rata* portion of a deduction or allowance shall be granted in the determination of an individual partner's taxable income derived from the partnership and the entire deduction or allowance is not applied to the globular income of the partnership, which was the approach of Trollip JA.
- (iii) That, therefore, because the partnership is not a taxpayer and regard must therefore be had to the taxable income of each individual partner, and because a portion of the allowance is granted in the determination of each individual partner's taxable income, it is possible for one partner to recoup the amount of the allowance previously granted to such partner even if the other partners recoup nothing and it is to the individual partner that a proportionate share of the allowance accrues when he becomes a partner and it is the partner who recoups that allowance when he disposes of his interest.
- (iv) That there was no justification for the proposition that, notwithstanding the insertion of [s 24H](#) into the Act, the 'taxable income of a partnership trade' must be determined separately, and each partner's taxable income or tax loss is to be brought to account by the individual partners only when the partnership's taxable income or tax loss for the relevant period has been determined in the partnership's own financial statements and nor was there any warrant for reading the word 'partnership' into the definition of 'gross income' as there was no such thing as 'the taxable income of a partnership trade'.
- (v) That [s 24H\(5\)\(b\)](#) expressly provides that the deductions and allowances may be granted in respect of the income each partner is deemed to derive from the partnership business in terms of subs (5)(a) and what must happen in the ordinary course is that for tax purposes at the end of a partner's tax year

(which may not coincide with the interval agreed on by the partners in sharing profits), the income of the partnership will be determined and amounts exempt from tax will be deducted and each partner's share of the income will then be calculated and each partner will then be entitled to that partner's portion of any deduction or allowance in respect of that partner's share to produce that partner's taxable income derived from the partnership.

- (vi) That, accordingly, that appellant did recover or recoup, as envisaged in [s 8\(4\)\(a\)](#), a *pro rata* portion (calculated in terms of [s 24H\(5\)\(b\)](#) of the Act) of the allowance deducted under [s 14bis](#) on the disposal by it of a portion of its interest in the partnership.

Appeal dismissed with costs, including the costs of two counsel.

CLOETE JA:

[1] On 31 March 1989 the appellant and eleven others entered into a partnership named The Southern Cross Air Partnership. The only disclosed partner was Air Southern Cross Management (Pty) Limited ('ASCM'); the others, including the appellant, were partners *en commandite*.

Page 246 of 67 SATC 243

[2] Clause 2.5 of the partnership agreement provided that 'Each partner shall share in the profits, losses, rights and obligations of this partnership in accordance with his percentage interest, and in the manner provided for in this agreement'. The appellant's contribution to the partnership was a cash amount, for which it acquired a 30 *per cent* interest in the partnership. The appellant financed this contribution by taking out a loan with Investec Bank Limited. ASCM acted as the manager of the partnership and its contribution comprised its skill, management and administration of the business and affairs of the partnership. For this it received a 0,1 *per cent* interest in the partnership and, in addition, payment of a sum of money from the other partners. The remaining nine partners also made cash contributions to the partnership and held the remaining 69,9 *per cent* interest in the partnership.

[3] The business of the partnership was to purchase a particular aircraft and either by itself or with other persons to conduct the business of transporting by air and for reward persons, livestock, goods or mail. In fact the aircraft had already been purchased by ASCM but it was paid for out of partnership funds and it accordingly became a partnership asset. The partnership (on the same day it was formed) entered into a partnership with BOP Air (Pty) Limited ('the Southern-BOP partnership'). The purpose of the Southern-BOP partnership was also to use the aircraft to conduct air transportation business for reward and it did so.

[4] [Section 14bis](#) of the Income Tax Act, [58 of 1962](#) ('the Act'), provides for an allowance to be deducted from 'the income of any person' in respect of an aircraft acquired by such person on or after the first day of April 1965. The definition of 'person' in [s 1](#) does not include a partnership and a partnership is not a person at common law.

[5] Income that has accrued to partners in common is deemed to have accrued to each of the partners individually in their proportionate shares by [s 24H\(5\)\(a\)](#), which provides as follows:

- '(a) Where any income has in common been received by or accrued to the members of any partnership, a portion (determined in accordance with any agreement between such members as to the ratio in which the profits or losses of the partnership are to be shared) of such income shall, notwithstanding anything to the contrary contained in any law or the relevant agreement or partnership, be deemed to have been received by or to have accrued to each such member individually on the date upon which such income was received by or accrued to them in common'.

[6] Where income has accrued to a partner in terms of para (a) the partner is also entitled to deduct a proportionate share of deductions and allowances that are granted by the Act - thereby arriving at the partners' taxable income - by [s 24H\(5\)\(b\)](#), which provides as follows:

- '(b) Where a portion of any income is under the provisions of paragraph (a) deemed to have been received by or to have accrued to a taxpayer, a portion (determined as aforesaid) of any deduction or allowance which may be granted under the provisions of this Act in the determination of the taxable income derived from such income shall be granted in the determination of the taxpayer's taxable income so derived'.

[7] The appellant claimed its *pro rata* portion of the [s 14bis](#) allowance during the 1989, 1990 and 1991 years of assessment. During the appellant's 1992 year of assessment, the appellant transferred 99,9 *per cent* of its 30 *per cent* interest in

Page 247 of 67 SATC 243

The Southern Cross Air Partnership to ASCM. In consideration for this disposal, Investec Bank Limited released the appellant from the outstanding balance of the loan which the appellant had originally taken out to finance its capital contribution to the partnership. (The amount of the balance in fact exceeded the amount of the loan).

[8] The Commissioner held the view that by virtue of the disposal, the *pro rata* [s 14bis](#) allowances previously claimed by the appellant were recouped in terms of [s 8\(4\)\(a\)](#) of the Act. That section at all material times provided, to the extent relevant, that:

'There shall be included in a taxpayer's income all amounts allowed to be deducted or set off under the provisions of sections 11 to 20, inclusive . . . whether in the current or any previous year of assessment which have been recovered or recouped during the current year of assessment . . . '.

The Commissioner accordingly issued the appellant's original income tax assessment for the 1992 tax year on the basis that there had indeed been a recoupment. The appellant's objection was disallowed and the appeal to the Johannesburg tax court was unsuccessful. (The judgment of the tax court is reported as *ITC 1784* in [67 SATC 40](#).) Leave to appeal directly to this court was granted by the tax court.

[9] In my judgment, the approach of the Commissioner and the conclusion reached by the tax court are undoubtedly correct. The appellant's counsel stressed the distinction between the cost to a partner of acquiring a share in the partnership and the cost to the partnership of acquiring an asset. That distinction was made by this court in *Rane Investment Trust v Commissioner for South African Revenue Service* [2003 \(6\) SA 332](#) (SCA) para [35]:[1](#)

'The Commissioner argued further, however, that Rane's expenditure was in respect of its acquisition of its partnership share, not in the acquisition of the film. That argument loses sight of the principle that in acquiring the share, Rane was also acquiring, as part of the business of the former partnership, a share in the film - already an asset. It was the expenditure on the film as an asset taken over by the new partnership that was deductible, and not the amount of R90 000 paid to become a partner'.

The appellant's counsel also emphasized the distinction between the disposal by a partner of an interest in a partnership, and the disposal by the partners of a partnership asset. But it does not follow from these distinctions that the appellant did not recover or recoup (as envisaged in [s 8\(4\)\(a\)](#)) a *pro rata* portion (calculated in terms of [s 24H\(5\)\(b\)](#)) of the allowance deducted (under [s 14bis](#)). The appellant made a capital contribution to the partnership that gave it, simultaneously, a 30 *per cent* share in the partnership, and an undivided share in the aircraft. The acquisition of the share in the aircraft entitled the appellant to a share of the [s 14bis](#) allowance for the cost of the aircraft. Because of the provisions of [s 24H\(5\)\(b\)](#), the acquisition of the 30 *per cent* interest in the partnership determined the appellant's share of that allowance at 30 *per cent*. When the appellant disposed of 99 *per cent* of its 30 *per cent* interest in the partnership, it disposed of a corresponding percentage of its undivided share in the aircraft. As Schreiner J (Maritz J concurring) said in *Whiteaway's Estate v Commissioner for Inland Revenue* 1938 TPD 482 at 491:

Page 248 of 67 SATC 243

'[E]ven when no change in the membership of the firm took place, whenever there was a change in the proportion in which the partners were to share in the profits and losses of the business, there was a change in their rights in the partnership assets'.

In order to make its capital contribution and acquire its 30 *per cent* interest in the partnership, which gave it its share in the aircraft (and the right to make the [s 14bis](#) deductions), the appellant took out a loan with Investec Bank; and in exchange for its transfer of its partnership interest and thereby its share in the aircraft, the appellant was credited with the amount owing on that loan (which exceeded the amount originally borrowed). The appellant accordingly recouped the cost to it of its share in the asset in respect of which it had made the tax deductions - as Howie P said in *Omnia Fertilizer Ltd v Commissioner for South African Revenue Service* [2003 \(4\) SA 513](#) (SCA) para [17]:[2](#)

'Where unpaid expenditure has been allowed as deduction from taxable income there is not just an expenditure entry in the taxpayer's books of account reflecting the relevant debt. There is, in addition, an assertion by the taxpayer, accepted and acted upon by the Commissioner, recognising the likelihood, if not the inevitability, that the debt will be paid. That is the basis for regarding the unpaid debts as actual expenditure. If the taxpayer later, in effect erases the debt from its books and treats the amount concerned as available for another purpose, the questions which arise are:

- (a) whether the debt has for some reason ceased to exist and, if not,
- (b) whether the amount unpaid, but expended in the eyes of the tax law, has nevertheless, for all practical purposes, reverted to the taxpayer's "pocket".'

[10] The appellant's counsel submitted that the allowances were recouped only when the partnership sold the aircraft in 1995. The foundation for that submission was that the allowances had accrued to the partnership

(when it acquired the aircraft) and not to the partners individually (when they each acquired their proportionate shares in the aircraft upon becoming partners) and by the same token it was only when the partnership disposed of the aircraft that the allowances were recouped. The argument was advanced on the basis of the following passage in the concurring minority judgment of Trollip J in *Van der Merwe v Secretary for Inland Revenue 1977 (1) SA 462* (A) at 478G-H:

'According to the fundamental provisions of the Income Tax Act, [58 of 1962](#), the "taxable amount" (now termed "taxable income") of the new partnership was its "gross income", *ie*, "the total amount received by or accrued to or in favour" of it during the particular years of assessment, less the permissible deductions for expenses, and allowable abatements and exemptions (see the definitions of the respective expressions in [s 1](#) of the Act)'.

The appellant's counsel submitted with reference to this passage (and I quote from the heads of argument):

'The provisions of [section 14bis](#) of the Act, which provide for the grant of the aircraft allowances, and the provisions of [section 8\(4\)](#), which require any recoupment of such allowances to be included in "gross income", are not exceptions to this basic rule. In other words, if the [section 14bis](#) allowances were granted in the determination of the "taxable income", not of the appellant's own trade, but in the determination of the "taxable income" of the Southern Cross Air Partnership, in accordance with the "fundamental provisions" of the Act as aforementioned, then any recoupment of such allowances must, on the same principles, be taken into account in determining the taxable income of the Southern Cross Air Partnership. By the same token, an amount received by the appellant itself, *ie* an amount not received in common, cannot be treated as a taxable recoupment of amounts expended by the partnership, and in respect

Page 249 of 67 SATC 243

of which an allowance was granted in the determination of the partnership's "taxable income".'

The appellant's counsel went on to point out three alleged anomalies which would arise if the approach for which it contends is not adopted.

[11] The passage quoted from *Van der Merwe* is not to be interpreted as meaning that a partnership is a 'taxpayer' for the purposes of the Act, and that the Act attributes to individual partners a proportionate share of the partnership's 'taxable income' (*ie* income after allowing for deductions and allowances). That is not correct. The Act does not recognise a partnership. It recognises only income (gross income after allowing for tax-exempt income) that accrues to partners in common (in accounting terms, the income of the partnership) which it attributes to them proportionally, and it similarly attributes to the individual partners deductions and allowances that are granted by the Act, with a resultant 'taxable income' of the partners individually. A partnership cannot have a taxable income, simply because it is not a taxable entity. At the time when Trollip JA wrote his concurring judgment in *Van der Merwe*, it was not necessary to emphasize this fact as [s 24H](#) had not yet been introduced into the Act. (The section was inserted by [s 21](#) of Act [90 of 1988](#).) The approach followed by Trollip JA is not now appropriate inasmuch as subs (5) of that section makes it clear that a *pro rata* portion of a deduction or allowance shall be granted in the determination of an individual partner's taxable income derived from the partnership - the entire deduction or allowance is not applied to the globular income of the partnership, which was the approach of Trollip JA. The significance of the difference is this. Because the partnership is not a taxpayer and regard must therefore be had to the taxable income of each individual partner, and because a portion of the allowance is granted in the determination of each individual partner's taxable income, it is possible for one partner to recoup the amount of the allowance previously granted to such partner even if the other partners recoup nothing. It is to the individual partner that a proportionate share of the allowance accrues when he becomes a partner, and it is the partner who recoups that allowance when he disposes of his interest.

[12] The appellant's counsel referred to a number of sections in the Act in support of the proposition that the expenses and losses of a partnership business cannot be used in reduction of income derived by the partners from another trade. That proposition is obviously correct. But it is no justification for the further proposition advanced by counsel that (notwithstanding the insertion of [s 24H](#) into the Act) what counsel termed 'the taxable income of a partnership trade' must be determined separately, and each partner's taxable income or tax loss is to be brought to account by the individual partners only when the partnership's taxable income or tax loss for the relevant period has been determined in the partnership's own financial statements. Nor is there any warrant, as counsel suggested, for reading the word 'partnership' into the definition of 'gross income' so that that definition would (to the extent relevant to the present matter) be understood as follows:

'In the case of any partnership, the total amount in cash or otherwise, received by or accrued to or in favour of such partnership . . . during such year or period of assessment . . . including, without in any way limiting the scope of this definition, such amounts (whether of a capital nature or not) so received or accrued as are described hereunder, namely-

...

- (n) any amount which in terms of any other provision of this Act is specifically required to be included in the partnership's income, and for the purposes of this paragraph all amounts which in terms of subsection (4) of section *eight* are required to be included in the partnership's income shall be deemed to have been received by or to have accrued to the partnership from a source within the Republic notwithstanding that such amounts may have been recovered or recouped outside the Republic .

The fallacy of this approach is that it seeks to treat a partnership as a taxpayer, which it manifestly is not. There is no such thing as 'the taxable income of a partnership trade'. Nor does the fact that the income, deductions and allowances of the trade carried on by each partner in a partnership must be calculated separately from that of any other trade carried on by such partner, necessitate the approach urged on us by counsel. [Section 24H\(5\)\(b\)](#) itself expressly provides that the deductions and allowances may be granted in respect of the income each partner is deemed to derive from the partnership business in terms of subs (5)(a). What must happen in the ordinary course is that for tax purposes at the end of a partner's tax year (which may not coincide with the interval agreed on by the partners in sharing profits), the income of the partnership will be determined; amounts exempt from tax will be deducted; each partner's share of the income will then be calculated; and each partner will then be entitled to that partner's portion of any deduction or allowance in respect of that partner's share to produce that partner's taxable income derived from the partnership. The appellant's counsel submitted that this approach is divorced from reality in that accounts are invariably drawn up according to the method set out by Trollip JA in *Van der Merwe*. But the point is that for the purposes of [s 24H\(5\)](#), the manner in which the calculation has to be done is as set out above.

[13] It remains for me to deal with the anomalies which the appellant's counsel said would result from this approach.

[14] First it was submitted that the [s 14bis](#) allowances will be recouped twice: when the appellant sold its partnership interest and again when the partnership sold the aircraft. The answer is that only such portion of the [s 14bis](#) allowance as had not already been recouped by the appellant, would be recouped by the appellant when the aircraft was sold.

[15] Second, it was submitted that the Act does not contemplate a recoupment when an asset, in respect of which allowances have been deducted, is still in use. The answer is that a recoupment occurs when a taxpayer recovers what the taxpayer expended and for which the taxpayer was allowed a deduction; and whether or not the asset is still in use, is irrelevant.

[16] Third, it was submitted that if, at a stage when the aircraft is still owned by the partnership, a partner is individually subject to tax on recoupment in respect of the aircraft in view of what counsel termed 'a mere change in the profit sharing between the partners', it becomes impossible to apply the complex provisions of [ss 14bis](#) and 8(4) on an ongoing basis as contemplated in those sections. In the present matter there is much to be said for the blunt comment by the court *a quo* that 'the disposal of the share in the partnership is a poorly disguised manner of disposing, *inter alia*, of ownership of a share in the aircraft'. But taking the argument of the appellant's counsel at face value, the answer is that the calculations are not impossible; and the fact that in a particular case (unlike the present) it may be difficult to calculate the different recoupments and allowances, does not detract from the fact that an individual partner may have recouped what such partner expended.

[17] The appeal is dismissed with costs, including the costs of two counsel.

Howie P, Cameron JA, Nugent JA and Ponnann JA concurred.

Footnotes

- 1 [65 SATC 333](#) at [344-5](#).
- 2 [65 SATC 159](#) at [163](#).