278/74

IN THE SUPREME COURT OF SOUTH AFRICA

APPELLATE DIVISION

In the matter between:

SECRETARY FOR INLAND REVENUE — Appellant

and

THE TRUST BANK OF AFRICA LTD. — Respondent

Coram: Botha, Holmes, Trollip, Muller, JJ.A. et Galgut, A.J.A.

Heard: 3 March 1975.

Delivered: 20 March 1975.

J U D G M E N T

BOTHA, J.A.:

This is an appeal direct to this Court on a case stated under section 86 of the Income Tax Act 1962 against the decision of the Special Court constituted for hearing income tax appeals arising within the area of

jurisdiction.../2

jurisdiction of the Cape Provincial Division. The appeal is concerned with the taxability under the Income Tax Act 1962 of an amount of R8 028 066 which represents the profits realised by the respondent bank upon the sale of certain shares held by it in a company known as National Fund Holdings (Pty.) Ltd.

The appellant had, for the year of assessment ended 31 December 1969, included the above amount in the respondent's gross income for that year. Against this inclusion the respondent unsuccessfully lodged objection and appeal to the appellant on the ground that the said amount of R8 028 066 was an accrual of a capital nature and therefore excluded from "gross income" as defined in section 1 of the Income Tax Act, and accordingly not subject to tax under that Act. The Special Court on appeal to it upheld the respondent's contention and ordered the appellant's assessment to be set aside and to be referred back to him for re-assessment in accordance

with.../3

with that Court's judgment. Against that decision the appellant now appeals direct to this Court with the necessary consent of the parties.

The respondent was incorporated as a public company in 1954 and is registered as a general bank under the Banks Act 23 of 1965. It carries on the business of banking throughout the Republic. During its earlier years of existence and also when the shares in question were first acquired by it in 1965, the respondent was essentially a Western Cape based bank and was encountering some difficulty in establishing itself in competition with the then existing commercial banks, but it gradually extended its business activities to other parts of the Republic. In 1964 the respondent added to its activities a commercial bank division, and in 1965 it had between 50 and 60 branch offices established in various parts of the Republic, which, however, at that time compared unfavourably with some of the older banks.

The.../4

The business of the respondent is governed by a board of five to eleven directors which meets regularly. The day-to-day running of the respondent's business and the formulation of proposals on matters of policy for submission to the board of directors are, however, entrusted to a management committee consisting of respondent's chief executive officers. It is clear from the stated case that considerable powers in connection with the running of respondent's business were entrusted to the management committee.

The respondent had from its inception invested certain of its surplus funds in quoted equities, as well as in Government and Municipal stocks, as it was authorized to do under its memorandum of association. It is relevant to note at this stage that before the respondent embarked upon share-dealing the matter was discussed with the Registrar of Banks who raised no objection thereto provided the investment was limited to a small amount

of.../5

of respondent's resources and was made in absolutely liquid assets only, such as stock exchange securities. This branch of activity was entrusted to the respondent's investment advisory department, which also advised its clients in regard to the investment of their funds. Respondent's investment advisory department had full authority as regards the buying and selling of specific stocks and shares on behalf of the respondent. The management committee referred to above would only be consulted in matters of general investment policy. The board of directors as such was not troubled in such matters at all.

The accounts of the respondent over the years 1964 to 1969 show that it had purchased and sold stocks and shares on a fairly substantial scale, and that in addition to an annual income in the form of dividends received, it had also made overall annual profits on the realisation of such stocks and shares. Such profits had

always.../6

always been returned by the respondent as income subject to tax under the Income Tax Act.

In 1965 the respondent's management committee mainly consisted of its three chief executive officers, namely, (1) Dr. Jan Marais, who was then the managing director, but became chairman of the board of directors and chief executive officer in 1968; (2) Mr. A.P.J. Burger, the then general manager who in 1968 became the managing director, and (3) Mr. G.R.S. Home, one of the chief executive officers in 1965 who became the general manager in 1968. Under their leadership the respondent's business activities had been diversified to such an extent that in addition to ordinary commercial banking the respondent had become engaged, either directly or through subsidiary companies, in hire-purchase and other types of financing, insurance broking, estate planning, savings and investments, travel services, and so on. The respondent's object was the development of what was termed a "one-stop" service

concept.../7

concept by which the respondent's clients could be enabled to satisfy many of their financial and other requirements within the portals of the respondent's branch offices. Although the respondent with its 50 or 60 branch offices in 1965 compared unfavourably with some of the older banks, it sought to evercome this by maintaining a mobile force of canvassers whose function it was to solicit business in parts of the country where it was not represented.

Shortly after the promulgation of the Unit Trusts Control Amendment Act 65 of 1963 certain influential businessmen, who had done research into the growth fund movement, endeavoured to interest a number of powerful financial institutions in the formation of a growth fund in the Republic. Their object was to find financial institutions willing to stake the minimum capital of R600 000 required by section 3 (2) (b) of the Unit Trusts Control Act 18 of 1947, for the registration of the necessary management company. In the second half of 1964

interest.../8

[illegible]

[illegible] on their [illegible]

[illegible] portion [illegible] responsible [illegible]

Although [illegible] agreement [illegible] criteria

in 19[illegible] compared [illegible] to mention [illegible]

[illegible] to average [illegible]

of [illegible] have [illegible] decision [illegible] benefit [illegible]

[illegible] the country [illegible]

[illegible]

[illegible]

[illegible] have made [illegible]

[illegible] extensive [illegible] future [illegible]

[illegible]

[illegible] their object [illegible]

[illegible]

[illegible] (b) of the [illegible]

[illegible] of 1964

[illegible]

interest in the formation of a growth fund was elicited from the Accepting Bank for Industry whose main shareholders included several powerful financial institutions. Thereafter further financial institutions became interested in the formation of the proposed management company.

When at a meeting of the board of directors of the Accepting Bank for Industry the question of the institutions to be approached to participate as possible shareholders in the proposed management company was discussed, it was realised that what was required was an "outlet" to the public, i.e. an organisation through which the growth fund units could be marketed to the public. It was felt that the respondent, being a "progressive" banking institution, with wide, diversified interests and an active sales organisation, would be an efficient medium through which to market the units. With this object in view the respondent was offered a ten per cent interest in the proposed management company and the appointment as

an.../9

an agent for the sale of units in the proposed growth fund. Dr. Jan Marais, to whom the offer was made, stressed the point that as the respondent had the selling network available for the sale of the units, the respondent should also be appointed as banker to the proposed growth fund. This was agreed to subject to the approval of the board of directors of the proposed management company. Dr. Marais also pressed for a larger interest in the proposed management company, and he was assured that efforts would be made to increase the ten per cent offered.

Participation by the respondent as a shareholder in the formation of the proposed management company was considered by Dr. Marais as a necessary and useful addition to the respondent's banking framework, and the respondent's management committee was persuaded by a consideration of the following factors to recommend to its board of directors acceptance of the offer made -

(a) the merits of such a participation as an investment;

(b)..../10

(b) the banking business which it was expected would accrue to the respondent by reason of its participation, particularly also in the Transvaal where the proposed growth fund was to be based;

(c) the prestige value of being associated with the other participants in the fund and of being a banker to the fund;

(d) the advantage of obtaining what was termed a "priority agency" for the sale of the units of the proposed growth fund, and

(e) the benefit of being able to provide clients of the respondent with another investment facility, which fitted into its "one-stop" service concept.

These factors were stressed in a memorandum prepared by Home and submitted to the respondent's board of directors in support of the management committee's recommendation that the offer made be accepted.

On 30 March 1965 the respondent's board passed a resolution "approving" the acquisition by the respondent

of.../11

of a ten per cent interest in the proposed management company at a total capital outlay of R60 000. There is no documentary evidence of the considerations which led to the adoption of this resolution; but it is clear from the stated case that in the debate which preceded the adoption of the resolution, the collateral benefits which were expected to accrue to the respondent in its banking business from such a participation, apart from the merits of such a participation as an investment, were emphasized by Dr. Marais.

On 17 June 1965 the proposed management company, Fund Advisers Ltd., was incorporated with an authorized share capital of R1 000 000 divided into 2 000 000 shares of 50 cents each. On 4 August 1965 the respondent was alotted 120 000 shares at a cost of R60 000 and on 25 October 1965 it was alotted a further 12 000 shares for which it paid R12 600, being the issue price of R6 000, together with a share premium of R6 600. The number of

shares.../12

shares alotted by Fund Advisers Ltd. totalled 1 200 000 of which the respondent then held 132 000 at a total cost of R72 600.

On 14 October 1965 the proposed growth fund was launched under the name of National Growth Fund with Fund Advisers Ltd. as its management company and the Accepting Bank for Industry as its trustee as required by section 20 of Act 18 of 1947.

During the period November 1965 to January 1966 the nine shareholders in Fund Advisers Ltd. who, it was argued on behalf of the respondent, were in effect partners in the management company, signed what was called a "pre-emption agreement" in terms of which a clog was placed upon the rights of shareholders to dispose of their shares. Briefly, it provided that any shareholder desirous of disposing of his shares had to give written notice thereof to the company's directors, specifying the price and the name of the proposed purchaser. Upon

receipt.../13

receipt of the notice the directors were required to cause the auditors of the company to make a valuation of the shares in accordance with a prescribed procedure. This valuation was then to be delivered by the directors to the offeror of the shares, who could withdraw the transfer notice or allow the matter to proceed. In the latter event copies of the notice and the valuation were to be forwarded to all other shareholders of the company and they were then to be given an opportunity to purchase the shares at either the auditor's valuation or the price fixed in the offeror's notice, whichever was the lower. Only if the other shareholders did not avail themselves of this right of pre-emption was the offeror to be entitled to sell the shares to the person named in the notice.

In addition to this substantial clog placed upon the sale of shares in Fund Advisers Ltd. by the "pre-emption agreement", which had the effect not only of causing long delays but of limiting the price and the

manner.../14

manner of sale, it appears from the stated case that the Registrar of Unit Trusts exercised a strict control over the sale of shares in the management companies of growth funds and demanded that all sales to persons other than existing shareholders be subject to his prior approval.

In June 1967 the authorized share capital of Fund Advisers Ltd. was increased to permit of a one-for-one share issue to its shareholders. In pursuance thereof the respondent applied for and was alotted a further 132 000 shares for a consideration of R66 000. This increased respondent's shareholding in Fund Advisers Ltd. to 264 000 shares at a total cost of R138 600.

Some point was made on behalf of the appellant in this Court of the fact that there was no evidence as to how it came about that more than the 10% interest contemplated in the resolution of the 30th March 1965 of the board of directors was purchased, or as to the specific intention with which the rights issue in June 1967 was

exercised.../15

exercised or as to the person or persons who exercised that right. It does not, however, appear from the stated case that this fact was in issue in the court a quo. The appellant's attitude appears to have been that the full amount of the profits realised was taxable for reasons which applied equally to the profits on all the shares without any distinction between the shares acquired in pursuance of the resolution of 30 March 1965 and those acquired thereafter. The matter was accordingly, so it appears, not investigated, and I do not think it is now open to the appellant to raise it in this Court.

On 1st December 1967 a company known as Fund Holdings (Pty.) Ltd. was incorporated and shareholders in Fund Advisers Ltd. were alotted, upon an exchange basis, shares in Fund Holdings (Pty.) Ltd. in the ratio of one share in Fund Holdings for egery 100 shares held in Fund Advisers. In consequence of this exchange Fund Advisers Ltd. became a wholly owned subsidiary of Fund Holdings (Pty.) Ltd. and the former shareholders in Fund Advisers became

participants, .../16

participants, in the same proportions in Fund Holdings. In accordance with this scheme of re-organisation, the respondent was alotted 2 640 shares in Fund Holdings (Pty.) Ltd. In January 1968 the shareholders in Fund Holdings signed an agreement applying the "pre-emption agreement" in relation to their shareholdings in Fund Advisers Ltd., referred to earlier, to themselves in relation to their shareholdings in Fund Holdings, and on 3 October 1968 Fund Holdings had its name changed to National Fund Holdings (Pty.) Ltd. The exchange of shares on the basis set out above, was brought about in deference to the wishes of the Registrar of Unit Trust Companies who considered that as Fund Advisers Ltd. held shares in certain public companies it should be shorn of those interests so that its accounts would reflect its financial position solely as the managing company of National Growth Fund.

Dr. Jan Marais was a director of Fund Advisers Ltd. from its inception and later of its holding company

National.../17

National Fund Holdings (Pty.) Ltd.

The National Growth Fund grew phenomenally and at a rate in excess of even the most optimistic expectations. At the end of its first year of operations the fund had assets to the value of R4 million which grew steadily to R550 million in May 1969 when the stock market stood at its peak. It then had some 250 000 investors. The respondent was, together with many other institutions, companies and individuals, appointed an agent for the sale of National Growth Fund units. It set about the marketing of these units in an efficient and enthusiastic manner and became the foremost seller thereof, largely because it had the branch offices and field force necessary for that purpose.

In consequence of the fact that the Standard Bank and Volkskas had through their indirect shareholdings in National Fund Holdings (Pty.) Ltd. become aware of the fact that the growth fund business could be profitable, they made an approach to Mr. D.A. Abramson, managing director

of.../18

of Fund Advisers Ltd. and National Fund Holdings, for a larger stake in National Fund Holdings in view of the fact that the two of them with their approximately 1 700 branch offices could offer more than the respondent with its approximately 70 branch offices at that time. None of the shareholders was, however, prepared to sell its shares, but Abramson realised that if the wishes of the Standard Bank and Volkskas for a larger stake could be satisfied, great benefits could accrue to the fund.

Towards the end of December 1968, the respondent decided to establish its own growth fund, and on 18 January 1969 the trust deed for the formation thereof was approved under the Unit Trusts Control Act, 1947. On 14 February 1969 the management company of the fund, being a wholly-owned subsidiary of the Trust Accepting Bank Ltd., was incorporated. In consequence of this development Dr. Jan Marais resigned from the boards of Fund Advisers and National Fund Holdings. Abramson and the

other.../19

other directors of National Fund Holdings saw in this move an opportunity for persuading the respondent to sell its shares in National Fund Holdings in order that the wishes of the Standard Bank and Volkskas for greater participation in National Fund Holdings could be satisfied to the advantage of National Growth Fund.

After prolonged negotiations and hard bargaining, and after the respondent had been placed under considerable pressure to complete the sale of the shares before the end of April 1969 when the S.A.G.E. shares were expected to come on the market with a possible effect on the estimated value of the National Fund Holding shares, a price of R8 166 066 was agreed to for respondent's shares which in the end were taken up only by the Standard Bank and the other shareholders of National Fund Holdings.

It appears from the stated case that the following collateral advantages foreseen by the respondent's

management.../20

management committee in 1965 in fact accrued to the respondent by reason of its shareholding in National Fund Holdings, viz. -

(a) the establishment and operation of a number of valuable current banking accounts pertaining to the National Growth Fund group at certain branch offices of the respondent particularly in the Transvaal;

(b) the short-term investment of funds of the National Growth Fund with the respondent upon which low rates of interest were payable and which constituted a valuable source of funds for banking purposes;

(c) the close association in the National Growth Fund with well established and prominent financial institutions which proved to be of great value to the respondent who had just embarked upon the business of commercial banking;

(d) the acquisition of a "priority" agency for the sale of National Growth Fund units which, apart from enabling the respondent to

earn.../21

earn a considerable amount by way of commission on the sale of the units, also enabled the respondent's canvassers to solicit banking business for the respondent;

(e) the fact that the respondent was enabled to offer a further investment facility to its clients and potential clients.

The question whether the profits realised on the sale of the shares in National Fund Holdings constituted a revenue or capital accrual depended, so the learned President of the Special Court put it -

> "upon whether the purchase, holding and sale of these shares were steps in a scheme of profitmaking, i.e. to make a profit by the re-sale of the shares at an enhanced price; or whether the sale constituted the realisation of a capital asset acquired and held for purposes other than such a profitmaking scheme. This is fundamentally a question of intention, viz. the intention of the appellant in regard to this particular transaction and, more especially, its

intention.../22

intention at the time when the shares were acquired. The appellant being a company, its intention must be sought in the thoughts and acts of the persons who manage and control it. Ultimately this would mean the board of directors but the evidence shows that considerable executive power was conferred by the board upon the management committee, consisting of Dr. Marais and Messrs. Burger and Home. To some extent, depending upon the nature of the matter and the circumstances, the intention of this committee would accordingly represent the intention of the company (see Gower, Modern Company Law, 3rd Edition pp. 148/9). Moreover, even in regard to matters submitted to and decided upon by the full board, the thinking of the management committee, as reflected in its reports and recommendations to the board, would represent an important indication of the intention of the board. It is clear, therefore, that the evidence of the members of the management committee as to the reasons for the acquisition and subsequent sale of the N.F.H. shares is both relevant and instructive as to the intention of the appellant in regard to this transaction."

After.../23

After a detailed consideration of this evidence in the light of the authorities, the court a quo concluded that -

> "In the present case we have accepted the evidence that it was predominantly the prospect of the so-called collateral advantages which induced appellant (now respondent) to acquire the interest in N.G.F.; and we have concluded that as far as the future profitability of the interest was concerned, both as to income production and capital appreciation, the general thinking must have been that, although the venture had a reasonable prospect of being successful, it was somewhat speculative in character. Moreover, there is no evidence to suggest that the interest was acquired with a view to a profitable re-sale: such evidence as there is on this point is to the contrary and the circumstances, e.g. the 'partnership' concept, the clogs on transferability, the collateral benefits, etc., tend to confirm this. No doubt re-sale was never entirely ruled out as a future possibility, given a sufficiently tempting offer - and indeed

that.../24

that is in fact what occurred - but as remarked earlier, a taxpayer is not obliged to exclude the slightest contemplation of a profitable re-sale.

Bearing in mind that when there are mixed purposes the question as to whether one of them can be regarded as being the dominant one is essentially a matter of degree, we have come to the conclusion that in the present case the dominant purpose underlying the purchase of the interest in N.G.F. was the acquisition of the various collateral benefits previously referred to; and that, in so far as the shares were regarded as an investment which might be either held or sold, as alternative methods of making a profit out of them, this purpose played a relatively minor and insignificant role. Furthermore, it seems to us that these collateral benefits were calculated to - and did in fact - extend the bank's framework or, to use the phraseology of Kitto, J., (in National Bank of Australasia Ltd. v. Federal Commissioner of Taxation, (15 A.T.D. 220)) add to its profit-making structure. It is true that, apart from the commissions earned on the

sale.../25

sale of units, the actual figures do not make very impressive reading but, on the other hand, it is clear that certain benefits, such as the use of deposit money, have not been quantified and that others, of a more intangible nature, cannot be quantified. All-in-all the evidence convinces us that not only did appellant anticipate substantial benefits from the collateral advantages but that it in fact enjoyed such. The circumstances relating to the sale of the shares, which have been detailed, are mainly relevant in so far as they throw light upon the purpose for which the shares were acquired. Normally, the relatively early realisation of an asset at a handsome profit - as in this case - would raise the inference that the asset had been purchased with this end in view. The actual circumstances of the realisation in this case tend to rebut that inference in that the sale was precipitated by circumstances - very keen buyers, an exceedingly attractive price, pressure being brought to bear on appellant to sell - which at the time of acquisition could, at most, have been seen as very remote possibilities. .....

To sum up the position then, we

hold.../26

> hold that the acquisition of the interest in N.G.F. was - and was intended to be - in the nature of an extension of, or addition to, the permanent structure upon which appellant's business rested; that the acquisition was quite distinct and different from appellant's normal share-dealing operations and the shares did not become part of appellant's ordinary stock-intrade in this field; and that primarily the shares were acquired not for re-sale or as part of a profit-making scheme but to be held in order to effect the afore-mentioned extension of appellant's business. We accordingly conclude that the interest in N.G.F. constituted a capital asset and that when it was realised the proceeds were not taxable in appellant's hands."

The findings set out in the passage cited above, including the finding as to the intention with which the shares in question were acquired (Cohen vs. Commissioner for Inland Revenue, 1962 (2) S.A. 367 (A D) at p. 377), whether such findings be of primary fact or of inferences therefrom (C.I.R. vs Strathmore Consolidated Investments Ltd.

1959 (1) S.A. 469 (A D) at p. 475), are findings of fact and, therefore, in terms of section 86 (1) of the Income Tax Act unassailable on appeal "except on the ground of lack of evidence on which they could reasonably have been made" (African Life Investment Corporation (Pty.) Ltd. vs Secretary for Inland Revenue, 1969 (4) S.A. 259 (A D) at p. 268) or, as it has also been put, "unless it can be shown that the over all conclusion reached by the special court is one which could not reasonably be reached" (C.I.R. vs Strathmore Consolidated Investments Ltd., (supra) at p. 475).

It was assumed by both counsel that the question whether the profits realised on the sale of the shares in question constitute receipts of a capital or revenue nature, was a question of law in contrast to one of fact. The Special Court's finding of fact may, however, in determining that question, prove wholly decisive for in those cases where the dominant issue is one of the

taxpayer's .../28

taxpayer's intention, the conclusion of law may automatically follow upon the findings of fact. (Secretary for Inland Revenue vs Cadac Engineering, 1965 (2) S.A. 511 (A D) at p. 520). The Special Court's conclusion that the profits realised constituted receipts of a capital nature and were, therefore, not taxable in appellant's hands, followed automatically on the facts as found by the Special Court, particularly its finding as to the intention with which the shares were acquired and held, namely, as a capital asset and not for re-sale or as part of a profit making scheme.

Counsel for the appellant contended, however, that the Special Court erred in law in the significance it attached to the intention with which the respondent acquired the shares in question; in the way in which it sought to ascertain that intention, and in holding that the respondent's intention, as found by the court, served to render the profits realised on the sale of the shares a capital one in the circumstances of the present case.

It.../29

It is true, as Schreiner, J.A., said in C.I.R. vs Richmond Estates (Pty.) Ltd. 1956 (1) S.A. 602 (A D) at p. 610 that -

> "there is no legislative provision that makes the intention of the taxpayer decisive of whether the receipt or accrual was of a capital nature or not",

but the learned Judge of appeal also added that -

> "the decisions of this Court have recognized the importance of the intention with which property was acquired and have taken account of the possibility that a change of intention or policy may also affect the result".

Counsel, however, contended that the Special Court misdirected itself in approaching the enquiry before it on the a priori basis that it is "fundamentally one of intention", and that in order to apply the test as formulated by it, the Court appears to have assumed that a company must always or would normally have a relevant intention, which has to be ascertained as if

the.../30

the Legislature has required a decision thereon. Consequently, so it was contended, the court erred in the manner in which it sought to ascertain the respondent's intention and attached undue weight to the intention as so ascertained.

I cannot agree that the Special Court approached the enquiry before it in the manner suggested. What the Court, in the context of the whole of its judgment, did convey was that the question whether the purchase and sale of the shares were steps in a scheme of profit-making, or whether the sale constituted the realisation of a capital asset acquired for purposes other than such a profit-making scheme was, in the case the court was considering, "fundamentally a question of intention", in other words, that the intention with which the shares were acquired was of the utmost importance, but not necessarily decisive. And that must necessarily have been so. The respondent is a general bank primarily carrying on the

business.../31

business of banking in the Republic. The other objects which it was authorized to pursue, such as dealing in shares, were merely ancillary to its banking business. (Cf. Commissioner of Taxes vs Booysens Estates Ltd., 1918 A.D. 576 at p. 598). The investment of its surplus funds in equities quoted on the stock exchange and thus readily realisable was in accordance with normal banking business (cf. Punjab Co-operative Bank Ltd., Amritsar vs Commissioner of Income Tax, Lahore, [1940] 4 All E.R. 87 at p. 95). In these circumstances the intention with which, or the purpose for which, the shares were acquired was, therefore, fundamental to the question whether they were acquired in order to extend or add to the permanent structure upon which the appellant's banking business rested, or whether they were merely acquired in the ordinary course of its share dealing operations.

It may be that in the case of an investment-dealing

company.../32

company whose business it is "to deal in shares at a profit", or, which means the same thing, whose "appointed means of the company's gains" include "the gaining of profit by selling shares at higher prices than was paid for them", (L.H.C. Corporation of S.A. (Pty.) Ltd. vs C.I.R. 1950 (4) S.A. 640 at p. 645/6, and cf. Durban North Traders vs Commissioner for Inland Revenue, 1956 (4) S.A. 594 at p. 604) the objective factors, such as the objects of the company as set out in its memorandum of association, the actual nature of the company's business, the normal business carried on by companies of that type, and the nature of the transaction, may, in an enquiry as to the purpose for which specific shares were acquired by such a company, assume greater significance than the intention with which those shares were acquired. (L.H.C. Corporation case (supra) at p. 645/7; C.I.R. vs Strathmore Consolidated Investments Ltd. 1959 (1) S.A. 469 (A D) at p. 477/8). The business of such an investment-dealing company is to make a profit on shares either by

holding.../33

holding or selling them. "These are merely alternative methods of dealing with the shares for the purpose of making a profit out of them. In either event there would be 'a productive use of capital employed to earn profits' " - per Solomon J.A. in Overseas Trust Corporation Ltd. vs Commissioner for Inland Revenue, 1926 A.D. 444 at p. 457). In such a case it would be extremely difficult for the company to show that a particular share transaction nevertheless falls outside its normal trading activities in the sense that the shares were not acquired for a profitable re-sale but to be held purely as an investment. (C.I.R. vs Richmond Estates (Pty.) Ltd. 1956 (1) S.A. 602 at p. 607). Where, however, as in the present case, share dealing is carried on by a banker ancillary to its banking business, the question whether a particular share transaction falls within its ordinary share dealing operations, or was intended as an extension of or addition to its banking business and not as a dealing in shares, is a question of an entirely different kind,

in.../34

in the determination of which the intention with which the share transaction was entered into must necessarily be fundamental, even though it may not be decisive.

The respondent being a company, the Special Court held that its intention in regard to the share transaction in question had to be sought in the thoughts and acts of the persons who manage and control its affairs. That would ultimately be the board of directors but, because the evidence showed that considerable powers were conferred by the board upon the management committee consisting of Dr. Marais and Messrs. Burger and Home, the Special Court concluded that the intention of the management committee would, to some extent, depending upon the nature of the matter and the circumstances, represent the intention of the company, and in regard to matters submitted to and decided upon by the full board, the thinking of the management committee, as reflected in its reports and recommendations to the board, would

represent.../35

represent an important indication of the intention of the board.

After a full consideration of the evidence of the members of the management committee as to the reasons for the acquisition and subsequent sale of the shares in question, and the relevant circumstances, the court a quo came to the conclusion set out above, namely, that the acquisition of the shares was, and was intended to be, in the nature of an extension of or addition to the permanent structure upon which respondent's business rested, and that the shares were not acquired for re-sale or as part of a profit-making scheme.

Counsel for the appellant, in challenging the manner in which the Special Court sought to ascertain the respondent's intention, submitted that, with certain immaterial exceptions not relevant in this case, "the only way of ascertaining its (a company's) intention is to

find.../36

find out what its directors acting as such intended", (C.I.R. vs Richmond Estates (Pty.) Ltd. 1956 (1) S.A. 602 at p. 606) and that (again with immaterial exceptions not relevant in this case) the only way to find out what a company's directors acting as such intended is from their formal acts. For this proposition counsel relied on the following statement of Benjamin, J., in Wilson vs Commissioner for Inland Revenue, 1926 C.P.D. 63 at page 70-

> "The company being an artificial entity, its intentions must be determined from its formal acts. There was nothing in the resolutions of the company to indicate an intention to capitalise the £25,000 requisite for the payment of the dividend".

I do not think that Benjamin J., intended to lay down a general rule that a company's intention or purpose in regard to any particular transaction cannot be ascertained in any other way than by its formal acts. I certainly would not be able to subscribe to such a proposition, for it is clear that it could lead to injustice and grave difficulties if the Special Court were,

in.../37

in an enquiry as to a company's intention, to be bound by the formal acts, in the form of resolutions, of that company, particularly where such resolutions may be incorrectly recorded, either deliberately or mistakenly, or where such resolutions are inconsistent with each other or with other relevant facts. Just as there cannot in the case of a one-man company be any reason in principle why it should be incompetent for him to give evidence as to what the intention of his company at any given time was, C.I.R. vs Richmond Estates (Pty.) Ltd. (supra) at p. 606, so I can see no reason in principle why the persons who are in effective control of a company cannot give evidence as to what was the intention or purpose of the company in relation to any matter at any given time. That the management committee was for practical purposes in effective control of the affairs of the respondent bank, is clear from the evidence. It was under its leadership that the respondent's business

activities.../38

activities had been diversified to such an extent that, in addition to ordinary commercial banking, it had become engaged in a number of other incidental business activities as indicated above. I cannot find any reason in principle why the intention of the members of the management committee in regard to any matter in which it was concerned on behalf of the respondent cannot be taken to indicate the intention of the respondent. Confirmation for this principle is to be found in the passage in Gower, Modern Company Law, 3rd Ed. p. 148/9, cited by the learned President of the Special Court, and I cannot find anything in the judgment of the House of Lords in Tesco Supermarkets Ltd. vs Nattrass [1971] 2 All E.R. 127, to which we have been referred by counsel for the appellant, which in this regard is in conflict with that passage. In an enquiry as to the intention with which a transaction was entered into for the purpose of the law relating to income tax, a court of law is not concerned with that kind of

subjective.../39

subjective state of mind required for the purposes of the criminal law, but rather with the purpose for which the transaction was entered into. (Commissioner for Inland Revenue vs Paul, 1956 (3) S.A. 335 at p. 340/1). Why that purpose cannot, in the case of a company, be proved, inter alia, by evidence as to the state of mind or intention of the persons in effective control of the affairs of the company is not clear, and the exclusion of such evidence would in my view be insupportable in law. While such evidence will therefore, always be admissible, the weight thereof must necessarily depend upon the circumstances.

In any event, the special court also found that -

> "it is a fair inference that the manner in which the proposal (to participate in the formation of the management company of the proposed growth fund) was presented to the board in Home's memorandum and Dr. Marais' address would reflect, with reasonable accuracy, the motivation of the board as a whole in coming to the decision to approve the purchase of the shares".

This.../40

This inference, based as it is on a finding of the primary facts, is itself a finding of fact and not assailable in this Court unless, as already indicated, there was no evidence to support it, (C.I.R. vs Strathmore Consolidated Investments Ltd. 1959 (1) S.A. 469 (A D) at p. 475).

In any event, it seems to me that the evidence in regard to the following matters, considered together with the absence of any evidence, as the Special Court found, that the shares in question were acquired with a view to a profitable re-sale, reasonably supports the conclusion of the Special Court in regard to the intention or purpose of the acquisition -

(a) the contents of Home's memorandum and Dr. Marais' address to the respondent's board of directors in which the collateral benefits to the respondent's banking business, which were expected to flow from a participation in the formation of the management company of the proposed growth fund, were set out and in which such participation was for those

reasons.../41

reasons recommended by the management committee;

(b) the fact that the board's resolution of 30 March 1965 "approved" of the recommended 10% interest in the proposed management company being taken up which suggests that the board was persuaded by the reasons advanced by the management committee for its recommendation;

(c) the fact that the collateral benefits foreseen in 1965 in fact accrued to the respondent's banking business by reason of its shareholding in the management company concerned;

(d) the fact that it was the respondent's board of directors itself which approved of the acquisition of the shares and not its investment advisory department which had full authority to invest some of the respondent's surplus funds in quoted equities in its share dealing operations;

(e) the clogs placed upon the sale of the shares in National Fund Holdings by the so-called pre-emption agreement, and by the Registrar of Unit Trusts on the sale

of.../42

of shares in all management companies of growth funds;

(f) the fact that the Registrar of Banks did not approve of banks investing in shares which were not readily realisable, and that the shares in National Fund Holdings were not so realisable;

(g) the manner and the circumstances in which the shares in question were eventually sold;

(h) the fact that some of the collateral benefits which accrued to the respondent's banking business from respondent's share-holding in National Fund Holdings, such as the short-term investment of funds of the National Growth Fund, were withdrawn from the respondent shortly after it had sold its shares in National Fund Holdings, and that the respondent eventually lost all those benefits.

It is true that although the Special Court found that there was no evidence that the shares in question were acquired with a view to a profitable re-sale, it nevertheless took into account that re-sale was never

entirely.../43

entirely ruled out as a future possibility, given a sufficiently tempting offer, which is exactly what in fact eventually occurred. Indeed there was some evidence that the merits of the participation as a possible profitable investment were seriously considered at the relevant time and that it was a factor in the decision of the management committee. No one, however, readily buys property if he expects that he will eventually have to sell it at a loss, and the taxpayer is not required to exclude the slightest contemplation of a profitable resale of the asset. (Commissioner of Taxes vs Levy, 1952 (2) S.A. 413 (A D) 420/1). Although the possibility of a profitable resale of the shares in question was not excluded as a factor in their acquisition, the Special Court found that the dominant factor which induced the respondent to acquire the interest in the formation of the management company of the proposed growth fund was the prospect of the collateral benefits to its banking business. (Levy's case (supra) at p. 421, and African Life Investment

Corporation.../44

Corporation (Pty.) Ltd. vs C.I.R. 1969 (4) S.A. 259 (A D) at p. 269/70).

The question whether any amount received by a taxpayer is a capital or revenue accrual for the purpose of the definition of "gross income" in the Income Tax Act is essentially a question to be decided upon the facts of each case. (Cf. Commissioner for Inland Revenue vs African Oxygen Ltd., 1963 (1) S.A. 681 (A D) at p. 688 and 691). The Special Court found on the facts that the shares in question were acquired for the purpose of extending respondent's income producing concern and not for the purpose of a profitmaking scheme. They constituted, therefore, a source of profit or a capital asset the proceeds of the sale of which were accordingly an accrual of a capital nature. Its findings of fact, reasonably supported as they are by the evidence, are not assailable in this Court, and I am not persuaded that the Special Court

in.../45

in arriving at its conclusion committed any error in law.

The appeal is accordingly dismissed with costs.

D.H. BOTHA, J.A.

Holmes, J.A.
Trollip, J.A.
Muller, J.A.
Galgut, A.J.A. } Concur.