B.6

125/92

CASE NO: 554/90

JACOBUS ALENSON ..... APPELLANT

AND

A B BRICKWORKS (PTY) LTD ..... RESPONDENT

VAN COLLER, AJA :

CASE NO: 554/90

IN THE SUPREME COURT OF SOUTH AFRICA

(APPELLATE DIVISION)

In the matter between:

JACOBUS ALENSON — Appellant

and

A B BRICKWORKS (PTY) LTD — Respondent

CORAM: CORBETT, CJ, HOEXTER, MILNE, JJA, VAN COLLER et KRIEGLER, AJJA

HEARD: 21 MAY 1992

DELIVERED: 1 SEPTEMBER 1992

J U D G M E N T

VAN COLLER, AJA :

Respondent company was established in 1961 and has since then carried on business in Benoni as a

manufacturer of bricks. Appellant is a co-founder, former director and former shareholder of respondent. One Hendrik Dam and appellant became involved in litigation with one another concerning the sale of appellant's shares in respondent to Dam. On 31 January 1985 the litigation culminated in a settlement agreement. Appellant, Dam, respondent and another company, Warren Heights (Pty) Ltd, were the parties to this agreement, in terms of which Dam purchased appellant's entire interest and shareholding in respondent with effect from 31 January 1985. In terms of clause 6 of the agreement, appellant undertook to refund to respondent on demand, 50% of any additional taxation which respondent was or would become obliged to pay to the Receiver of Revenue arising from re-assessments of respondent in respect of financial years prior to 31 January 1985. This date is referred to in the agreement as "the effective date".

During April 1986 the Receiver of Revenue, Benoni ("the Receiver") reassessed respondent in respect of the 1983, 1984 and 1985 years and disallowed as a deduction that portion of the directors' remuneration which he regarded as being excessive. Respondent was called upon to pay an additional amount of approximately R2 000 000 in respect of income tax for the aforesaid three years. After negotiations between the Receiver and respondent's legal representatives, the initial assessment was reduced to the sum of R1 001 000,52 plus interest in the sum of R12 500,00, making a total additional assessment of R1 013 500,52. Although appellant was invited to participate in these negotiations with the Receiver, he did not do so. Respondent paid this amount, but appellant refused to make the 50% refund of the additional assessments. Respondent then instituted action in the Witwatersrand Local Division to recover from appellant what he had

undertaken to pay. Appellant's defence in the court a quo was based on what was referred to in the plea as a proper construction of clause 6. On the basis of this interpretation, to which I shall shortly refer in more detail, it was contended that respondent had failed to make out a case for a refund of the alleged additional taxation. Van der Walt J rejected this defence and gave judgment in respondent's favour in the amount of R457 448,22 with interest at 15% per annum as from 3 March 1987 to date of payment. This amount is R49 302,04 less than the amount claimed in the summons. The reason why the learned trial judge made this deduction will be dealt with later in this judgment. Van der Walt J also allowed the qualifying fees of the expert witness called by respondent.

Clause 6 of the agreement between the parties reads as follows.

> "Alenson hereby irrevocably indemnifies the Company and undertakes to refund to the Company (or to Dam

> in the event of him being called upon to pay any amounts on behalf of the Company) and Dam hereby irrevocably indemnifies Warren Heights and undertakes to refund to Warren Heights (or to Alenson in the event of him being called upon to pay any amounts on behalf of Warren Heights) forthwith on demand, 50% (FIFTY PER CENTUM) of any additional taxation which the Company or Warren Heights is obliged to pay to the Receiver of Revenue arising from the reopening or reassessment of any assessment of the Company or Warren Heights as the case may be, in respect of the financial years of the Company or Warren Heights for any period prior to and including the effective date as a result of the Receiver of Revenue adding back as taxable income of the Company or of Warren Heights, any amounts up to and including the effective date."

Respondent is the Company referred to in clause 6 and the reference to Dam's indemnity to Warren Heights is not relevant in this case.

In its particulars of claim respondent relied upon the indemnity provided for in clause 6 of the agreement and on the reassessments by the Receiver. In paragraph 2(b) of his plea, appellant pleaded that clause 6 of the agreement was void for vagueness.

Paragraph 2(c) of the plea reads as follows:

> "(c) Alternatively to (b), the Defendant avers that on a proper construction of clause 6 the Defendant undertook to refund to the company, or to Dam, 50% of such additional taxation only as the company was obliged to pay the Receiver of Revenue arising from the reopening or reassessment of any assessment of the company for the relevant period."

It will be observed that the wording of clause 6 has been followed in abbreviated form but the construction that appellant sought to place on clause 6 was not pleaded. In paragraph 3(a) of the plea, appellant, with reference to the alleged reassessments by the Receiver, pleaded that he had no knowledge of these allegations. In paragraph 3(b) appellant pleaded as follows.

> "Alternatively to (a) hereof, and in the event of this Honourable Court finding that the Receiver of Revenue reopened and reassessed the assessment of the plaintiff as alleged by the Plaintiff, the Defendant:
>
> (i) repeats paragraph 2(c) hereof;
>
> (ii) avers that the Plaintiff objected to the reassessments in terms of the provisions of the Income Tax Act, but did not pursue

such objection to its conclusion.

(iii) avers that the Plaintiff agreed to pay the sum of R1 013 500,52 to the Receiver of Revenue and that accordingly the obligation incurred by the Plaintiff did not arise in the circumstances set out in clause 6 of the agreement."

At the pre-trial conference it was minuted that appellant did not persist in the plea that the agreement was void for vagueness. It was also minuted that the conclusion referred to in paragraph 3(b)(ii) of the plea was a determination by the Income Tax Special Court.

The evidence adduced by Respondent was firstly that of Mr M W Reynolds, the Receiver of Revenue of Benoni. His evidence was to the effect that the directors' remuneration claimed by respondent as expenditure during the three tax years in question was in excess of what had been incurred in the production of income in terms of the Income Tax Act 58 of 1962. The additional income tax and reassessments related to this excess expenditure. This evidence was supported by

that of Mr Urquhart, who acted on behalf of respondent during the negotiations with the Receiver and who was also called as an expert witness.

Mr Goldblatt who, with Mr Van Blerk, appeared on behalf of appellant, submitted that clause 6 should be construed as follows. The word "obliged" in clause 6 of the agreement should be interpreted to mean "inescapably obliged". Unless respondent alleged and proved that the reassessments were correct in fact and in law, it was not inescapably liable. Such a cause of action was neither pleaded nor was it proved in evidence. It was contended that, had the parties intended that mere liability of respondent under the Income Tax Act would give rise to a liability to refund on the part of appellant, then the clause would have created such an obligation on the issue of a reassessment. The parties would not have used the language "arising from the reopening or reassessment of

any assessment...".

I am unable to agree with this interpretation of clause 6. In my judgment Mr Goldblatt's interpretation is an ingenious attempt to give a meaning to the word "obliged" which, when viewed in its context, and having regard to the nature and purpose of the contract, is an artificial one. The wording of clause 6 is plain. The obligation is on respondent to pay to the Receiver what is owing upon reassessment. This liability would have remained even if there had been an objection to or an appeal against the reassessment. (See s 88 of the Income Tax Act). Appellant clearly has a corresponding obligation towards respondent to pay "forthwith and on demand" 50% of that reassessment. In my view the words "arising from the reopening or reassessment of any assessment..." do not lend any support to Mr Goldblatt's contention. These words merely indicate the source of the additional taxation

and do not detract from the fact that the obligation stems from the reassessment as such. It is also obvious that the purpose of clause 6 was to provide for the contingency of possible additional taxation which could be levied in respect of the financial years prior to the effective date. It was clearly intended for the benefit and protection of respondent and the shareholder Dam. It seems to me therefore more probable that the parties intended that the reassessment itself would at least be prima facie proof of appellant's liability rather than that the correctness of the reassessment should also be proved. It is unlikely that the parties intended to burden respondent with the prejudice which would obviously follow upon appellant's proposed interpretation of clause 6. The contract is therefore also more efficacious from a business point of view if construed in respondent's favour as was done by the court a quo. Cf Mittermeier v Skema Engineering (Pty)

Ltd 1984 (1) SA 121 (A) at 128 A - B.

In an alternative argument it was contended that the trial court erred in deducting only R49 302,04 from the amount claimed instead of reducing it by a further amount of R69 022,87. The learned trial judge made this deduction because he found that the indemnity in clause 6 of the agreement could only extend over 7/12ths of the 1985 tax year, i e from 1 July 1984 to 31 January 1985. The adjustment was accordingly made on the basis of figures submitted by counsel.

Counsel for appellant submitted that the provisions of clause 6 do not justify an interpretation in terms of which appellant would be liable for half of 7/12ths of the full amount added back for the whole of the 1985 tax year. It was argued that there was no evidence to show what amounts of expenditure added back in respect of directors' remuneration had been related to the period 1 July 1984 to 31 January 1985.

Respondent, so it was contended, had accordingly failed to prove that it was entitled to any amount in respect of the 1985 tax year, and consequently the further deduction should have been made.

I shall accept in favour of appellant that clause 6 cannot, with regard to a refund of additional tax, be interpreted to include the full financial year of 1985. It is clear from the evidence to which I have already referred that the directors' remuneration was in reality profits declared to the shareholders and not salary expenditure incurred in order to produce income. The Receiver, in reassessing respondent, did so on an annualised basis and added back a total amount for each of the 1983, 1984 and 1985 tax years. The suggestion that there should have been evidence indicating exactly what each director earned and what services were performed in order to make a proper allocation of the additional tax involves an illogical and impracticable

interpretation of the agreement. It would indeed not have been possible, as was submitted by respondent's counsel, to have led evidence of what amounts of directors' "remuneration" had in fact been incurred during the period 1 July 1984 to 31 January 1985. The parties must have realised that the Receiver of Revenue has regard only to the full tax year of respondent, which runs from 1 July to 30 June each year, and that with regard to the 1985 year there would have to be some adjustment. It must also be borne in mind that the effective date played an important part in the agreement. The purchase price of the shares was payable at that date and appellant severed his ties with respondent as from the effective date. Having regard to all these circumstances it is in my judgment probable that the parties contemplated a pro rata allocation as determined by the trial court and this interpretation should be accepted in preference to that proposed on

behalf of appellant.

The third issue in this appeal relates to the qualifying fees of the witness Urquhart. At the time when the negotiations between respondent and the Receiver took place, Mr Urquhart, apart from being an articled clerk, was also employed as a tax specialist in the firm of attorneys acting on behalf of respondent. A perusal of his evidence shows that he expressed an opinion on two matters. He was of the opinion that the Receiver was entitled to levy the additional assessments for the reasons given by him. Mr Urquhart came to this conclusion on the figures submitted to him. Secondly, it was his opinion, and also his advice to respondent, that the amount at which the Receiver was prepared to settle was so favourable that nothing could be gained in taking the matter to the Income Tax Special Court.

If one has regard to the pleadings, it is clear that the matters on which Mr Urquhart expressed

opinions were not really in issue. The issues were, firstly, whether there were reassessments, and secondly, whether on a proper construction of clause 6 of the agreement, appellant was obliged to pay 50% of the additional tax as reassessed. On these issues the evidence given by Mr Urquhart was unnecessary and irrelevant. Qualifying expenses should only be allowed when the court is satisfied that the payment of such fees was reasonably necessary. The following remarks of Corbett JA in Stauffer Chemical Co and Another v Safsan Marketing and Distribution Co (Pty) Ltd and Others 1987 (2) SA 331 (A) at 355 C - D are apposite.

> "On taxation the qualifying expenses of a witness are not allowed without an order of Court or the consent of all interested parties (see Rule 70 schedule para E6; also Community Development Board v Katija Suliman Lockhat Trust 1973 (4) SA 225 (N) at 228G - 229A; Cilliers Law of Costs 2nd ed para 13.30 at 240). The general rule is that the Court will grant an order for the qualifying fees of a witness only where it is satisfied that the payment of such qualifying fees was reasonably necessary (The Government v the Oceana Consolidated

Co 1908 TS 43 at 48)."

The learned trial judge gave the following reasons for allowing the qualifying fees.

> "Mr Urquhart was not only involved in the negotiations and therefore is an ordinary witness in that respect. But as an expert he also assisted the court by his evidence on the manner of calculation of remuneration and its deduction in relation to either dividends or profit and the norm used. That is not explaining the law to the court but is merely indicative of the practice applied or when applying the law, of which the court is not necessarily cognisant and in that regard his evidence on that aspect was that of an expert, assisted the court, and as such he then stands as an expert witness on that particular aspect."

It is not quite clear to me what norm is referred to nor what assistance was in fact gained from the evidence of the expert witness. Be that as it may, the learned trial judge failed to consider whether it was reasonably necessary for respondent to have invoked the assistance of an expert witness. In not applying the correct principle, the learned trial judge failed to exercise a judicial discretion. The appeal must therefore succeed

on this issue. Appellant's counsel has conceded that success on this aspect only, does not justify an order awarding any portion of the costs of appeal to appellant

The following order is made.

The order of the court a quo allowing the qualifying fees of the expert witness Urquhart is set aside. Save as aforesaid, the appeal is dismissed with costs, including the costs of two counsel.

A P VAN COLLER
ACTING JUDGE OF APPEAL

CORBETT, CJ)
HOEXTER, JA) CONCUR
MILNE, JA)
KRIEGLER, AJA)