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Case No 640/90
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IN THE SUPREME COURT OF SOUTH AFRICA

(APPELLATE DIVISION)

In the matter between:

COMMISSIONER FOR INLAND REVENUE — Appellant

and

PICK 'N PAY EMPLOYEE SHARE PURCHASE TRUST — Respondent

CORAM: HOEXTER, SMALBERGER, GOLDSTONE JJA et NICHOLAS, HOWIE AJJA

DATE OF HEARING: 2 March 1992

DATE OF JUDGMENT: 22 May 1992

J U D G M E N T

NICHOLAS AJA/.....

NICHOLAS AJA:

This is an appeal by the Commissioner for Inland Revenue ("the Commissioner") against a decision of the Cape Income Tax Special Court. The case concerned the liability to normal tax of profits made by Pick 'n Pay Employee Share Purchase Trust ("the Trust"). This was established by the Pick 'n Pay group of companies pursuant to the provisions of s 38(2)(b) of the Companies Act 61 of 1973 to administer a share purchase scheme for the benefit of employees of the group.

In his determinations of the Trust's liability for normal tax in respect of the 1982 - 1984 years of assessment, the Commissioner included the following profits on the sale of shares, namely,

Year of assessment	Profit
1982	R28 006
1983	R31 699
1984	R39 782

and in respect of the 1985 year of assessment he allowed a loss of R70 619 incurred on the sale of shares, and on this basis issued assessments on the Trust.

The Trust lodged objection against these assessments on the ground -

> "... that the proceeds arising upon the disposal of shares by the Trust (constitute) amounts of a capital nature which are accordingly excluded from 'gross income' in terms of the definition of that expression in schedule 1 of the Income Tax Act.
>
> The Trust was created and maintained to enable employees to purchase shares in Pick 'n Pay, their (employer) company. The Trust does not acquire shares with the intention of reselling them at a profit in a scheme of profit-making. It purchases shares in order to make them available to employees entitled to them in terms of its rules, and in terms of its constitution is compelled to repurchase shares from employees who are required to forfeit their holdings.
>
> Accordingly, all gains or losses constitute fortuitous gains or losses of a capital nature and the Trust does not intend to claim as a deduction the R70 619 loss suffered on the re-issue of shares in the 1985 year."

The Commissioner disallowed the objection and the Trust appealed to the Special Court.

In the judgment of the Special Court (in which Tebbutt J presided), it was held that any receipts or accruals to the Trust were of a capital nature and not liable to tax. An order was made upholding the appeal and setting aside "the Commissioner's decision to assess the Trust on the basis that its profits and losses constitute gross income."

Leave having been granted by Tebbutt J, the Commissioner now appeals directly to this court.

The question was not **res nova** in the Cape Special Court. A similar question had been considered in the judgment of Grosskopf J, presiding in the Cape Special Court in a case reported as **ITC No 1413 (1986) 48** SATC 167. The court's finding there was that the appellant had not proved that the surplus on the sale, by a trust created to implement a share purchase scheme for employees, of quoted shares in the employer company, was a receipt or accrual of a capital nature. The appeal was dismissed and the assessments confirmed. Tebbutt J concluded in the judgment under appeal that **ITC No 1413** was distinguishable on the facts, and that in any event it was incorrect and should not be followed. Tebbutt J's judgment has not been reported but an abridged version is to be found in a note in the November 1987 issue of **The Taxpayer** (Vol 36, p 206 at pp 211 ff).

The question arose again in a case heard in the Natal Special Court which is reported as **ITC No 1450** (1989) 51 SATC 70. In the judgment the president, Friedman J, agreed substantially with the reasoning of Tebbutt J.

The Facts

The only witness in the proceedings before the Special Court was Mr Christopher Hurst, who has been for many years the financial director of the Pick 'n Pay group. Although not himself a trustee, he administered the Trust.

He gave a brief description of the structure of the Pick 'n Pay group. It is headed by Pick 'n Pay Holdings Ltd, a company listed on the Johannesburg Stock Exchange. It has a majority holding in Pick 'n Pay Stores Ltd ("Stores"), which is also a listed company. Stores was the holding company until about 1981 when Pick 'n Pay Holdings Ltd was formed upon the restructuring of the group. Stores has a number of wholly-owned subsidiaries, including Pick 'n Pay Retailers (Pty) Ltd ("Retailers"), through which all the group's retail operations are conducted. The participants in the scheme administered by the Trust are mainly employees of Retailers.

It is unnecessary to detail all the provisions of the scheme. I shall refer to them only in their main outlines and to the extent that it is necessary to do so for the purpose of this judgment.

The scheme, entitled "Pick 'n Pay Stores Limited Employee Share Purchase Scheme", was adopted at a general meeting of Stores held on 8 November 1977, and the trustees accepted appointment as such on the same day. Its purpose was set out in the first paragraph -

> "1.1 This scheme is adopted to enable the Company to provide its employees and the employees of its subsidiaries, including directors holding salaried employment or office, with the opportunity of acquiring interests in the share capital of the Company, to provide such employees with incentives to advance the Company's interests, and to promote an identity of interests between such employees

> and the shareholders of the Company."

"The Company" was defined as Pick 'n Pay Stores Ltd, but after the formation of Pick 'n Pay Holdings Ltd the employees and shares of the latter were also treated as falling within the scheme. It was part of the duties of the trustees **inter alia** to subscribe for or purchase shares in the capital of Stores in accordance with the provisions of the scheme; to seek applications from eligible applicants for the purchase of such shares and to sell them to such applicants; and to administer the scheme in order to achieve and maintain the objects stated in paragraph 1.1. The price payable by participants for scheme shares was in practice the middle market price on the Johannesburg Stock Exchange at the time of acceptance of the application concerned. The purchase or subscription price of shares acquired by the Trust was to be met out of loans to be made to the Trust by the companies in the group by which participants were employed. In the ordinary course payment to the Trust for shares by participants was to be made by not later than the tenth anniversary of the date of purchase ("the initial date"), and could, at the option of participants, be made between the fifth and tenth anniversaries of such date. Special provision was made in regard to participants whose employment with the group was terminated prior to the fifth anniversary of the initial date, or at any time on the grounds of dishonest or fraudulent conduct. In such event the Trust was entitled and obliged to purchase and appropriate the relevant shares as the property of the Trust at an amount equal to the amount then owing by the participant in respect of his shares ("the share debt").

Hurst described the operation of the scheme. After an initial allotment of shares by Stores, the Trust acquired scheme shares in one of three ways:

(1) from members of staff who had paid for their shares and wished to realise their holdings;

(2) as a result of the forfeiture of shares by employees who left the group within five years of the initial purchase or were dismissed for fraud or dishonesty;

(3) by purchase on the open market when the Trust did not have available, for issue to applicants for shares under the scheme, sufficient shares acquired under methods (1) and (2).

The price payable for shares under method (1) was the then current middle market price. The price payable for shares under method (2) was the amount of the share debt owed by the employee concerned.

Hurst handed in as Exhibit "B" a document entitled "Share Movement Analysis - 1982 to 1985". It is divided into two main sections: one devoted to Stores, the other to Pick 'n Pay Holdings Ltd. The first column in each section is headed "Date" which, Hurst explained, is the date on which the relevant entry was made in the books of the Trust, and is not necessarily the date of any particular transaction. And an entry could relate to a number of transactions which were lumped together. The next column is headed "Average Acquiring Price", which is the average price of shares purchased. Then there is a column "Shares Acquired", with three sub-columns: "Forfeits", "Ex Staff" and "On Market". "Forfeits" are shares forfeited in terms of the scheme; "Ex Staff" and "On Market" are self-explanatory. There is then a column headed "Issues" which relates to sales of shares to participants, followed by "Average Selling Price" and "Share Balance".

In the case of Stores, the first date given is 31 May 1981 and the last 20 February 1985. There is a total of 120 dates recorded. Entries under "Forfeits" total 39, "Ex Staff" total 50, and "On Market" total 12. There are 25 entries under "Issues".

In the case of Pick 'n Pay Holdings Ltd, the first date given is 10 June 1982 and the last 26 February 1985. There is a total of 98 dates recorded. Entries under "Forfeits" total 9, "Ex Staff" 56, and "On Market" total 5. There are 36 entries under "Issues".

The schedule records a continuous series of share-dealing activities by the Trust during the four years of assessment. The results of these operations are shown on Exhibit "C", which is an analysis of profits earned (and losses sustained) on "reissues" i.e. the sale of shares to participants:-

ANALYSIS OF PROFITS EARNED ON RE-ISSUE OF SHARES

	ON FORFEITS	ON PURCHASES	TOTAL
	R	R	R
1982	97 335	-67 553	29 782
1983	28 231	-2 085	26 146
1984	46 638	-11 638	35 000
1985	185 561	-258 277	-72 716
	357 765	-339 553	18 212

It appears from this that profits were made in each year on forfeits, and that losses were experienced in each year on purchases.

Hurst explained that in cases where forfeited shares had been held by the respective participants for some time,

> "... it invariably occurs that the market value of the shares is higher at the time of forfeiture, and a profit accrues to the Trust."

The reason for the losses "On Purchases" was not investigated in the Special Court. Counsel for the Trust was about to lead the witness in this regard when the president intervened, saying that he did not think it necessary to go through the whole of the schedules - "What we are looking at is the bottom line."

<u>The Law</u>

The starting point of the discussion is the definition of "gross income" in s 1 of the Income Tax Act 58 of 1962 ("the Act"), namely -

> "gross income, in relation to any year or period of assessment, means, in the case of any person, the total amount, in cash or otherwise, received by or accrued to or in favour of such person during such year or period of assessment from a source within or deemed to be within the Republic, <u>excluding receipts or accruals of a capital nature</u> ..."

Reference may also be made to the corresponding provision in s 11 of the Act which sets out the general deductions allowed in the determination of "taxable income". In terms of para (a) of s 11, there shall be allowed as deductions

> "(a) expenditure and losses actually incurred in the Republic in the production of the income, provided such expenditure and losses are <u>not of a capital nature</u>".

(My emphasis in each case.)

(In order to avoid repetition I shall speak in what follows only of "receipts" and "expenditure".)

Because "gross income" comprehends all receipts except those of a capital nature, other receipts must be receipts of an income or revenue nature. Capital is here used in contradistinction to income in its economic sense. The Act does not define either of the expressions, and it is difficult for the purposes of income tax to define them save in relation to one other (see **Commissioner for Inland Revenue v Lunnon** 1924 AD 94 at 98). "Profit or gain may be made in many ways; men may earn it by their labour, by their wits, by their capital ... (I)ncome considered in relation to capital is revenue derived from capital productively employed." (per Innes CJ in **Commissioner of Taxes v Booysens Estates Ltd** 1918 AD 576 at 594-5).

Maritz J said in **Commissioner for Inland Revenue v Visser** 1937 TPD 77 at 81, "If we take the economic meaning of 'capital' and 'income', the one excludes the other." And in **Pyott Ltd v Commissioner for Inland Revenue** 1945 AD 128 Davis AJA said at 135 that he could not understand how a receipt could be "non-capital", and yet "not income", observing that "This is a half-way house of which I have no knowledge."

"Income" is a protean expression whose forms are multifarious. Comprising as it does all receipts (save those of a capital nature) gross income has no definable boundaries. Although labels have been attached to specific kinds of income, the list is **per naturam** not a closed one.

The problems to which the expressions receipts "of a capital nature" and expenditure "not of a capital nature" give rise are perennial and have generated a large number of decided cases, but the tests therein enunciated are not to be regarded as either prescriptive or comprehensive: they do no more than provide guidelines for the solution of the problems which arise. Ultimately each case must be decided on its own facts. Cf the observation of Holmes JA in **Natal Estates Ltd v Secretary for Inland Revenue** 1975(4) SA 177 (A) at 202 G-H:

> "In deciding whether a case is one of realising a capital asset or of carrying on a business or embarking upon a scheme of selling land for profit, one must think one's way through all of the particular facts of each case."

Where profit has resulted from the disposal of the taxpayer's assets, it may be either capital or income, depending on the circumstances. If there was a mere realization of capital at an enhanced value, the entire proceeds would remain capital. But if it was an act done in the ordinary course of the vendor's business (if it resulted from the productive use of capital to earn it), then the resulting gain would be income. (See **Commissioner of Taxes v Booysens Estates Ltd, supra,** at 595; **Overseas Trust Corporation Ltd v Commissioner for Inland Revenue** 1926 AD 444 at 452-3). In the **Booysens Estates** case Innes CJ said:

> "The general rule approved by the Privy Council in **Commissioner of Taxes v Melbourne Trust** (1914, A.C. at p. 1,010), was thus stated in the **Californian Copper Syndicate** case, to which I shall refer again. 'It is quite a well-settled principle in dealing with questions of income tax, that where the owner of an ordinary investment chooses to realize it, and obtains a greater price than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income Tax Act, 1842, assessable to income tax. But it is equally well established that enhanced values obtained from realization or conversion of securities may be so assessable where what is done is not merely a realization or change of investment, but an act done in what is truly the carrying on or carrying out of a business.'"

And in the **Overseas Trust** case, the learned Chief Justice said at 452-3:

> "The reason for the distinction is clear. Where an asset is realised at a profit as a mere change of investment there is no difference in character between the amount of

enhancement and the balance of the proceeds. But where the profit is, in the words of an eminent Scotch Judge, see **Californian Copper Syndicate v Inland Revenue** (41 Sc.L.R, p 694) 'a gain made by an operation of business in carrying out a scheme for profit making,' then it is revenue derived from capital productively employed, and must be income."

A similar distinction has been drawn in regard to the deduction of expenditure under s 11(a) of the Act. In **Commissioner for Inland Revenue, v George Forest Timber Co., Ltd.**, 1924 AD 516 Innes CJ said at 526:

> "Now, money spent in creating or acquiring an income-producing concern must be capital expenditure. It is invested to yield future profit; and while the outlay does not recur the income does. There is a great difference between money spent in creating or acquiring a source of profit, and money spent in working it. The one is capital expenditure, the other is not."

The learned Chief Justice had referred at 524 to the distinction between fixed capital and floating capital, saying,

> "Capital, it should be remembered, may be either fixed or floating. I take the substantial difference to be that floating

capital is consumed or disappears in the very process of production, while fixed capital does not; though it produces fresh wealth, it remains intact. The distinction is relative, for even fixed capital, such as machinery, gradually wears away and needs to be renewed. But as pointed out by MASON J, in **Stephan v Commissioner of Inland Revenue** (1919, W.L.D., at p 5) the two phrases have an ascertained meaning in accountancy as well as in economics. Ordinary merchandise in the hands of a trader would be floating capital. Its use involves its disappearance; and the money obtained for it is received as part of the ordinary revenue of the business. It could never have been intended that money received by a merchant in the course, and as the result of his trading, should not form part of his gross income.

The proceeds of fixed capital stand in a different position. The sale of such capital would, generally speaking, represent a mere realisation, which ought from its nature to be excluded, and which I think the section intended to exclude from the calculation of income."

And in **New State Areas, Ltd., v Commissioner for Inland Revenue** 1946 AD 610, Watermeyer CJ said at 620 - 621:

"As to the latter [sc expenditure of a capital nature] the distinction must be remembered between floating or circulating and fixed capital. When the capital employed in a business is frequently changing its form from money to goods and vice **versa** (e.g., the purchase and sale of stock by a merchant or the purchase of raw material by a manufacturer for the purpose of conversion to a manufactured article), and this is done for the purpose of making a profit, then the capital so employed is floating capital. The expenditure of a capital nature, the deduction of which is prohibited under sec. 11(2), is expenditure of a fixed capital nature, not expenditure of a floating capital nature, because expenditure which constitutes the use of floating capital for the purpose of earning a profit, such as the purchase price of stock in trade, must necessarily be deducted from the proceeds of the sale of stock in trade in order to arrive at the taxable income derived by the taxpayer from that trade. The problem which arises when deductions are claimed is, therefore, usually whether the expenditure in question should properly be regarded as part of the cost of performing the income-earning operations or as part of the cost of establishing or improving or adding to the income-earning plant or machinery ..."

And at 627 the learned Chief Justice said:

"The conclusion to be drawn from all of these cases, seems to be that the true nature of each transaction must be enquired into in order to determine whether the expenditure attached to it is capital or revenue expenditure. Its true nature is a matter of fact and the purpose of the expenditure is an important factor; if it is incurred for the purpose of acquiring a capital asset for the business, it is capital expenditure, even if it is paid in annual instalments; if, on the other hand, it is in truth no more than part of the cost incidental to the performance of the

> income-producing operations, as distinguished from the equipment of the income-producing machine, then it is revenue expenditure, even if it is paid in a lump sum."

In **Secretary for Inland Revenue v Cadac Engineering Works (Pty.) Ltd.**, 1965(2) SA 511 (A) at 522B, Ogilvie Thompson JA said that he preferred the phrase "income-earning structure" to "income-producing machine".

In **Sekretaris van Binnelandse Inkomste v Aveling** 1978(1) SA 862 (A), Rabie JA quoted the passage in the judgment of Innes CJ in **Commissioner for Inland Revenue v George Forest Timber Co Ltd** which is set out above, and said at 880 E to 881 A:

> "Soos blyk uit die aanhaling hierbo, het 'n mens in die geval van vaste kapitaal 'n element van permanentheid, in die sin dat daar 'n bedoeling is om die betrokke bate min of meer permanent te hou met die doel dat dit inkomste moet voortbring. Kenmerkend van bedryfskapitaal daarenteen is 'n bedoeling om die betrokke bate voortdurend in kontant of ander goed om te sit. Hierdie kenmerkende verskil word soos volg in die uitspraak van Viscount HALDANE in **John Smith & Son v Moore (H.M. Inspector of Taxes)**, 12 T.C. 226 op bl 282, beskrywe:

> 'My Lords, it is not necessary to draw an exact line of demarcation between fixed and circulating capital. Since Adam Smith drew the distinction in the Second Book of his 'Wealth of Nations', which appears in the chapter on the Division of Stock, a distinction which has since become classical, economists have never been able to define much more precisely what the line of demarcation is. Adam Smith described fixed capital as what the owner turns to profit by keeping it in his own possession, circulating capital as what he makes profit of by parting with it and letting it change masters.'

Die bogemelde verskil tussen vaste en vlottende kapitaal blyk ook uit **Ammonia Soda Co Ltd v Chamberlain,** (1918) 1 Ch. 266 op bl 286-287, waar SWINFEN EADY L.J. hom o.a. soos volg oor die verskil tussen die vaste en vlottende kapitaal van 'n maatskappy uitgelaat het:

> 'In these cases the capital is fixed in the sense of being invested to be retained by the company more or less permanently and used in producing an income. What is circulating capital? It is a portion of the subscribed capital of the company intended to be used by being temporarily parted with and circulated in business, in the form of money, goods or other assets, and which are intended to return to the company with an increment, and are intended to be used again, and to always return with some accretion.'"

To the last quotation may usefully be added the immediately following sentences in the judgment of Swinfen Eady L.J.:

> "Thus the capital with which a trader buys goods circulates; he parts with it, and with the goods bought by it, intending to receive it back again with profit arising from the resale of the goods. A banker lending money to a customer parts with his money, and thus circulates it, hoping and intending to receive it back with interest. He retains, more or less permanently, bank premises in which the money invested becomes fixed capital."

In **Elandsheuwel Farming (Edms.) Bpk. v Sekretaris van Binnelandse Inkomste** 1978(1) SA 101 (A), Corbett JA said at 118 A-B:

> "Where a taxpayer sells property, the question as to whether the profits derived from the sale are taxable in his hands by reason of the proceeds constituting gross income or are not subject to tax because the proceeds constitute receipts or accruals of a capital nature, turns on the further <u>enquiry as to whether the sale amounted to the realisation of a capital asset or whether it was the sale of an asset in the course of carrying on a</u>

> business or in pursuance of a profit-making scheme. Where a single transaction is involved it is usually more appropriate to limit the enquiry to the simple alternatives of a capital realisation or a profit-making scheme. In its normal and most straightforward form, the latter connotes the acquisition of an asset for the purpose of reselling it at a profit. This profit is then the result of the productive turn-over of the capital represented by the asset and consequently falls into the category of income. The asset constitutes in effect the taxpayer's stock-in-trade or floating capital." (My emphasis).

In this passage the learned judge of appeal pointed to two situations: the sale of an asset in the course of carrying on a business, and the sale of an asset in pursuance of a profit-making scheme. Compare the observation of Holmes JA in **Natal Estates Ltd v Secretary for Inland Revenue supra** at 198 E-G as to the distinction consistently drawn by the Appellate Division between (a) realising a capital asset, and (b) selling an asset in the course of carrying on a business or embarking on a scheme for profit.

Corbett JA pointed out that where a single transaction is involved it is usually more appropriate to limit the enquiry to the simple alternative of a capital realisation or a profit-making scheme. The corollary is that where a series of transactions is involved, the appropriate enquiry is usually whether or not the receipts flow from the carrying on of a business.

(In the **Booysens Estate** case, there was quoted one portion from the judgment of the Lord Justice Clerk in **Californian Copper Syndicate v Inland Revenue** (1904) 4 Sc.L.R. 691 at 694, and in the **Overseas Trust Corporation** case another portion was quoted. The whole of the relevant passage reads as follows:

> "It is quite a well-settled principle in dealing with questions of assessment of income-tax, that where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income-Tax Act of 1812, and therefore assessable to income-tax. But it is equally well established that enhanced values obtained from realisation or conversion of securities may be so assessable where

> what is done is not merely a realisation or change of investment, but an act done in what is truly the carrying on or carrying out of a business. The simplest case is that of a person or association of persons buying and selling lands or securities speculatively in order to make gain, dealing in such investments as a business, and thereby seeking to make profits. There are many companies which in their very inception are formed for such a purpose, and in these cases it is not doubtful that where they make a gain by a realisation, the gain they make is liable to be assessed for income-tax.
>
> What is the line which separates the two classes of cases may be difficult to define, and each case must be considered according to its facts, the question to be determined being, is the sum of gain that has been made a mere enhancement of value by realising a security, or is it, again, made by an operation of business in carrying out a scheme for profit-making."

It is manifest that the first paragraph states the general principles: the second paragraph deals with the application of those principles to the specific case of a single 'operation of business'. The distinction referred to by Corbett JA was therefore not a novel one.)

In an enquiry, whether or not the receipts flow from the carrying on of a business, the emphasis is on the actual operations of the taxpayer. So, in **Commissioner for Inland Revenue v Stott 1928 AD 252**, Wessels JA said at 259:

> "The question we have to determine is whether the facts as set out in the special case show that the proceeds of the sale of the Ifafa and Bluff properties constitute gross income or capital. In order to arrive at this decision it is necessary to know whether the acts of the taxpayer in buying and selling these properties show that he was carrying on the trade or business of a land-jobber."

Cf **Commissioner for Inland Revenue v Leydenberg Platinum** Ltd., 1929 AD 137 at 145-6.

A "business", so far as an individual taxpayer is concerned, is characterized by a series of transactions having an element of continuity, and usually performed in the contemplation of making a profit.

In regard to the first two characteristics, reference may be made to the following dicta:

> "In the case of a company formed for certain purposes, the question of the continuity of the

> acts, which is another factor to be considered in deciding whether a business is carried on, is not of the same importance as in the case of an individual." (per Juta JA in **Platt v Commissioner for Inland Revenue** 1922 AD 42 at 51).
>
> "If you are dealing with a company one of whose objects is to buy and sell land, then the company might well be considered to be doing the business of selling and buying land even though it carries out only a single transaction; but when an individual like a surveyor who is not professedly carrying on the occupation of a land-jobber buys and sells one or more plots of land, he cannot be said **prima facie** to be doing the business of a land-jobber. Before it can be said that an individual is carrying on a business there must be some proof of continuity." (per Wessels JA in **Stott's** case **supra** at 262.)

See also **Commissioner for Inland Revenue v Leydenberg Platinum Ltd., supra, ubi cit.**

As to the contemplation of profit, there are cases in which it has been held that there may be a carrying on of a business without the contemplation of pecuniary gain (**Platt's** case at 50; see also **Modderfontein Deep Levels Ltd. and Another v Feinstein**

1920 TPD 288); but in relation to income tax law the "acquisition of gain or profit is a material factor in the consideration when does a person carry on a business." (Platt's case at 51).

A taxpayer may, in order to establish that receipts are of a capital nature, seek to prove that fact directly; or he may seek to show it indirectly, by inference from the fact that the receipts are non-revenue/non-income.

The latter (indirect) approach was epitomized by Friedman J in ITC No 1450 supra at 77 as follows:

> "Tebbutt J ... approached the matter by enquiring whether or not the profits were revenue profits. Strictly speaking, of course, and having regard to the definition of 'gross income', the real enquiry is whether or not the profits are of a capital nature. But nothing, as I see it, turns on this. Quite clearly profits can only be either of a revenue or of a capital nature. There is no third category. Consequently if profits are not revenue, they must be capital and vice versa."

The indirect approach was followed in **Lunnon's** case **supra**. The question there was whether an amount of a thousand pounds voted to Lunnon some months after the termination of his services as a director, was liable to income tax. Innes CJ said at 98:

> "Now this gift has none of the attributes of income; it was not produced by the respondent's capital, nor was it earned by his labour or his wits or in any other way. There is no recurrence about it. What is sometimes called annuality is not necessarily a decisive test as to whether a receipt or accrual is capital or income; but it [is] an important element to be taken into consideration. And in the present instance it is wholly absent. This grant is a fortuitous addition to the capital of the recipient and it appears to me to be of a capital nature; like any ordinary donation or legacy."

Other instances of fortuitous additions to capital are isolated lottery, betting or sweepstake wins. Cases of fortuitous gains apart, it is difficult to see in what way the indirect approach offers any advantage over the straightforward one. And, involving as it does proof of a negative, the indirect approach may be difficult to apply in practice. It was a rule of the Civil law that **per naturam** a negative is not capable of proof. See **Kunz v Swart & Others** 1924 AD 618 at 653. In dealing with the onus of proof, Voet said (in GANE's translation 22.3.10) that

> "Evidence also is given by him who asserts, not by him who denies, because in the nature of things no proof is possible for one who denies a fact."

See also **Pillay v Krishna & Another** 1946 AD 946 at 952:

> "But there is a third rule, which **VOET** states in the next section as follows: 'He who asserts, proves and not he who denies, since a denial of a fact cannot naturally be proved provided that it is a fact that is denied and that the denial is absolute.' This rule is likewise to be found in a number of places in the **Corpus** Juris: I again give only one version: '**Ei incumbit probatio qui dicit, non** qui negat' (D 22.3.2). The onus is on the person who alleges something and not on his opponent who merely denies it. This rule is stated by Matthaeus, de Prob (8.1) to be **lippis et tonsoribus nota**, that is to say, known to everyone ... Before I leave the subject of the Roman law I should add that the three rules to which I have referred are very shortly referred to, and approved, by Kotze JA in **Kunz v Swart and Others** (1924, A.D. at pp 662, 663)."

The **onus** of proving that any receipt is of a capital nature is upon the tax-payer. In **Elandsheuwel Farming (Edms.) Bpk. v Sekretaris van Binnelandse Inkomste, supra,** Wessels JA discussed the approach to be adopted by a court in considering a question of capital or income, and said at 112 B-C:

> "Ten slotte moet onthou word dat die belastingpligtige met die bewyslas beswaar is ten aansien van sy bewering dat die betrokke ontvangs een van 'n kapitale aard is, en dus nie aan belasting onderhewig is nie. Kyk, bv., **Natal Estates Ltd v Secretary for Inland Revenue,** 1975(4) SA 177 (A.A.) op bl. 202G - 203A, en **John Bell & Co (Pty) Ltd v Secretary for Inland Revenue,** 1976(4) SA 415 (A.A.) op bl. 426F - 427G."

It is true that the question is ultimately one of law: whether receipts are of a capital or revenue nature is an inference from facts, and whether the inference can properly be drawn is a matter of law. Juta JA said in **Platt's case, supra,** at 49 - 50:

> "The proper rule has I venture to think been laid down by LORD PARKER in **Farmer v Cotton's Trustee** (1915, A.C. 922), and it seems to me to

> be confirmed by the weight of judicial decision in the English Courts. He said 'Where all the material facts are fully found, and the only question is whether the facts are such as to bring the case within the provisions properly construed of some statutory enactment, the question is one of law.'"

See also **Commissioner for Inland Revenue v Stott supra** at 259. But the onus of establishing the facts from which the desired inference can and should properly be drawn is on the taxpayer.

A taxpayer who follows the indirect approach must, therefore, establish facts from which it can properly and validly be inferred that the receipts in question are not of a revenue nature.

Whichever approach be adopted, the conclusion should in logic be the same. Contradictory conclusions cannot exist together: one of them must be wrong.

Application of the Law to the Facts

It is clear from the evidence of Hurst, from the provisions of the scheme itself and from the annual financial statements included in the dossier, that the Trust does not possess an income-earning structure. It has no premises or equipment of its own and it does not employ its own staff.

The following is a copy of the Trust's balance sheet at 28 February 1982.

"PICK 'n PAY EMPLOYEE SHARE PURCHASE TRUST
BALANCE SHEET AT FEBRUARY 28, 1982

	Notes	1982 R	1981 R
CAPITAL EMPLOYED			
NON DISTRIBUTABLE RESERVE		153 593	125 587
Net surplus on re-issue of shares			
LONG TERM LIABILITY	2	5 803 168	2 217 028
		R5 956 761	R2 342 615
EMPLOYMENT OF CAPITAL			
LISTED INVESTMENT	3	41 025	-
LOANS TO PARTICIPANTS	4	5 915 736	2 342 615
		R5 956 761	R2 342 615"

The "long-term liability" of R5 803 168 is the total of the amounts lent to the Trust by the Pick 'n Pay group in order to finance the scheme, which were applied towards "loans to participants" totalling R5 915 736. This liability accordingly represents loan capital. The item "non-distributable reserve" is the surplus accumulated over the years in consequence of resales of shares. It appears from the "INCOME STATEMENT FOR THE YEAR ENDED FEBRUARY 28, 1982" that in that year the amount of R28 006 was transferred to non-distributable reserves, and that is the amount of the profit assessed by the Commissioner in the 1982 assessment. There is nothing in the evidence, and nothing in the annual financial statements, to show that the Trust ever held Pick 'n Pay shares (or any shares) as a permanent investment. Under "employment of capital", it is true, there is a "listed investment" of R41 025, but it appears from note 3 that this "comprises 3 250 ordinary shares of 10 cents each in

Pick 'n Pay Stores Limited, acquired but not allocated to participants at February 28, 1982 ..." Hurst's evidence shows that there was no element of permanency in regard to shares acquired. In summary he said:

> At times there was an over-sold situation, when the Trust had had to sell more shares to staff than it had available at the time. Consequently it had to quickly make acquisitions to right the situation ... When going to the market it was always with a view to an imminent issue of shares and being ready for that issue.
>
> The third method of acquisition was to purchase shares on the open market and that was only applied if there were not sufficient shares available to the Trust under methods (1) and (2). The Trust never bought shares 'to stock up'. When going to the market it was always with a view to an imminent issue of shares.
>
> It was never possible that the Trust was sitting with surplus shares that it had to sell on the open market. The Trust had never got into an over-purchased situation. Whenever it purchased it was always with a view to a fairly imminent issue of shares.

On these facts it is plain that none of the shares acquired by the Trust were fixed capital. If they were capital at all, they were floating capital, and when the shares were realised, there was a realisation of floating capital. Thus the receipts could not be receipts "of a capital nature".

The Special Court ignored the direct approach to the question, but adopted the indirect approach. Similarly in ITC No 1450 the Natal Special Court adopted that approach, and was satisfied "substantially for the reasons advanced by Tebbutt J", that the profits made by the appellant in that case constituted receipts of a capital nature.

In the judgment of the Special Court, Tebbutt J referred to a number of cases dealing with "(the) idea of the asset being used in a scheme of profit making", and said:

> "... if the Trust can show that what it did in acquiring the shares and then selling them to its employees, was not in pursuance of a scheme of profit-making, it will have discharged the onus of showing that such profits as it made or losses it sustained were of a capital nature."

In the discussion of the question whether the scheme adopted in November 1977 was a scheme of profit-making, the Special Court placed reliance on the evidence of Hurst, "who made a very favourable impression ... as an honest, fair and completely reliable witness". The conclusion which the Special Court reached was that

> "the considerations put forward by Hurst have persuaded us that the Trust has not embarked on a scheme of profit-making."

I agree with the Special Court that the scheme of the Trust did not have the purpose of making a profit. The acquisition of gain formed no part of the **raison d' être** of the scheme, which, as stated in its introductory paragraph and in Hurst's evidence, was to enable Pick 'n Pay employees to acquire a shareholding in Pick 'n Pay with no immediate capital outlay and with advantageous terms of payment. The only thing that Pick 'n Pay were interested in was getting shares into the hands of employees, and the furthest thing from their minds was whether the Trust would make a profit or a loss. Hurst said, "I am sure we never sat and thought about profits and losses within the Pick 'n Pay organisation." The reason for the 5-year rule was not to enable the Trust to make a profit, but to tie an employee to the group - it would frustrate one of the purposes of the scheme if an employee could "take a short-term profit and run".

In my view, however, the Special Court erred in going on to draw the conclusion that because the Trust had showed that its acquisition and resale of the shares was not in pursuance of a scheme of profit-making, the proceeds were not income and were accordingly of a capital nature. The premise on which the Special Court's conclusion was based is contained in the second paragraph in the judgment in the **Californian Copper Syndicate** case which is quoted above: namely, a gain of a particular kind (sc one made by an operation of business in carrying out a scheme for profit making) - P - is revenue derived from capital productively employed and hence income - Q. From that premise it cannot validly be concluded that a gain not of that kind is non-revenue (non-income). From the premise, if P then Q, the conclusion cannot validly be drawn that if non-P then non-Q; or, substituting real terms, from the premise, if apples then fruit, the conclusion cannot validly be drawn that if non-apples (oranges, say) then non-fruit. The premise P is Q does not state that P is the exclusive condition for Q, but only that Q is a necessary consequent of P.

It follows that the Trust did not discharge the onus of proving that the receipts from the sales of shares were revenue, and hence not of a capital nature.

The test applied in the judgment of the Special Court was not the appropriate test in the circumstances. This was not a case involving a single transaction or isolated transactions, but one involving a series of transactions; and the appropriate enquiry was whether the actitivities of the Trust were such that they amounted to the carrying on a trade or business. A distinction is to be drawn between the **raison d' être** of the scheme and the scheme in action - between the overall purpose of the scheme and the transactions performed in executing it. The real question to be decided is whether the profits resulting from the sale by the Trust of Pick 'n Pay shares were capital or income, and that depends upon whether the transactions were mere realisations of capital at an enhanced value or were acts done in the ordinary course of the Trust's business. (See the **Overseas Trust Corporation** case **supra**.).

In each of the years of assessment, the Trust engaged in share-dealing activities which were characteristic of a business. They were part of a series and they were continuous. In regard to the profit element, it was inherent in all the activities, which were conducted in a fluctuating market, that in the ordinary course they would result in profits/losses. And in the case of forfeited shares which had been held for some time, the accrual of a profit to the trust was "inevitable".

Certain of the provisions of the scheme itself evince a contemplation of surpluses arising from the Trust's operations. Under clause 3.6 the trustees have the power -

> "3.6.3 to invest <u>any surplus moneys</u> of the trust in shares of the Company, or in such other manner as the board may approve".

Clause 13 provides that the group employers of the participants will bear all costs of and incidental to the implementation and administration of the scheme, and in terms of clause 13.2 the Company is to provide

> "all secretarial, accounting, administrative, legal and financial advice and services, office accommodation, stationary and so forth, to enable the trustees properly and efficiently to perform their duties and functions in terms of this scheme."

In terms of clause 13.2.2, however,

> "... the group employers of the participants will be entitled to recover from the trust all the abovementioned costs <u>in the event that the trust is able to pay these costs from its own resources</u> and, in addition, the Company will be entitled to a fee to be determined by the Company for performing the duties and providing the services set out in 13.2.1 above <u>in the event that the trust has any surplus resources</u>."

It is provided in clause 16 that upon termination of the Trust,

> "the assets, if any, of the trust shall be realised and <u>any surplus remaining</u> after the discharge of the trust's liabilities shall be paid over to the Company."

(My emphasis in each case.)

A surplus could be produced only by making profits, and the only resources which the Trust could acquire would be from profits.

By the end of the 1981 financial year the Trust had already accumulated profits amounting to R125 587, and it continued to make profits in each of the following years 1982, 1983 and 1984.

The making of profits from the operations of the Trust must, therefore, have been in the contemplation of the trustees as likely to result from their transactions during those years, and it cannot be said that the profits which did result were unintended. That being so, it is plain that it was not proved that the trustees were not carrying on a business.

Tebbutt J did not deal with this aspect, but Friedman J referred to it in the judgment in **ITC No 1450**. He said at p 78 that one ought not to look simply at the activities of the Trust, but should have regard to the larger scheme of which the activities simply formed a part. He continued:

> "In our view, to say that the share incentive trust actively trades in the shares of the company, is to adopt an unduly narrow approach to the overall scheme in which the trust simply plays a part. The trust does not trade in the true sense of that word. It acquires shares for a particular purpose and that is to allocate these shares to employees who hold important positions in the company and whose continued employment with the company the company seeks to maintain and preserve. There is, in our view, no intention on the part of the company responsible for creating the trust that the trust should, in its own right, operate for the purpose of making a profit. Whether or not the trust makes a profit is entirely fortuitous."

The adoption of a broader approach should not cause one to ignore the nature of the transactions which produced the profits in question. The conclusion that a trust is carrying on a business is an inference to be drawn from its acts, and it does not wholly depend on the intention of the company responsible for creating the trust.

It is true that in performing those transactions the Trust did not carry on a business as the word is ordinarily understood. A profit motive was not the driving force behind its activities. They were subject to constraints not usual in the ordinary share-dealing business: the Trust's buying and selling of shares was not determined with reference to market conditions and it was not entirely within its control: by and large it bought only shares which were forfeited or shares which were offered to it by participants who had paid for them, and it sold shares only to persons entitled to obtain them under the terms of the Trust. But it is irrelevant to the real question for decision that the share-dealing actitivities carried on by the Trust differed from those of the ordinary share-dealing business. The fact is that the Trust was engaged in trading in shares and not in realizing investments. "The essential idea underlying trade is buying and selling." (per Wessels J in the court **a quo** in **Western Deep Levels**

& Another v Feinstein, supra, at 290.) The receipts from such trading had all the attributes of income: they were produced by the Trust's capital; they were recurrent; and they were not fortuitous in any relevant sense. It is true that the acquisition of forfeited shares was not within the control of the trustees, who were obliged to purchase such shares, and could not foresee or determine what shares would become liable to forfeiture, or when. But this does not mean that the receipts from their resale were fortuitous in any relevant sense. They were the result of the trading activities performed by the Trust. It cannot properly be said that the profits realised from those activities were the mere realisation of capital at an enhanced value, or were fortuitous additions to the capital of the Trust.

In my opinion, therefore, the conclusion of the Special Court was wrong.

I would uphold the appeal with costs, and set aside the order of the Special Court and substitute an order dismissing the appeal and confirming the assessments.

H C NICHOLAS
Acting Judge of Appeal

HOEXTER JA] Concurs.

Bib

85A/92

CASE NO 640/90
N V H

IN THE SUPREME COURT OF SOUTH AFRICA

(APPELLATE DIVISION)

In the matter between:

COMMISSIONER FOR INLAND REVENUE — Appellant

and

PICK 'N PAY EMPLOYEE SHARE PURCHASE TRUST — Respondent

CORAM: HOEXTER, SMALBERGER, GOLDSTONE, JJA et NICHOLAS, HOWIE, AJJA

HEARD: 2 MARCH 1992

DELIVERED: 22 MAY 1992

J U D G M E N T

SMALBERGER, JA :-

I have had the privilege of reading the judgment of my learned brother NICHOLAS. He has come to the conclusion that (1) at best for the Trust the shares acquired by it constituted floating capital which on realisation did not amount to receipts of a capital nature; and (2) in any event the Trust failed to establish that the receipts with which this case is concerned were of a non-income and hence of a capital nature. For the reasons that follow I am unable, with respect, to agree with the conclusions reached by him. I shall deal first with the second conclusion, the underlying reason for which is that it was not proved that the trustees were not carrying on a business with the contemplation of making profits.

The Trust can escape liability for normal tax on the profits made in the tax years 1982, 1983 and 1984 provided it establishes that such profits are non-revenue. In the present matter the relevant facts are either common cause or not in dispute. The question whether the receipts are capital or income is a matter of inference from such facts and therefore ultimately a matter of law. The fact that the onus rests on the Trust is accordingly not a material consideration.

There are a variety of tests for determining whether or not a particular receipt is one of a revenue or capital nature. They are laid down as guidelines only - there being no single infallible test of invariable application. In this respect I agree with the following remarks of FRIEDMAN J in ITC 1450 (at 76)

> "But when all is said and done, whatever guideline one chooses to follow, one should not be led to a result in one's classification of a receipt as income or capital which is, as I have had occasion previously to remark, contrary to sound commercial and good sense."

The appropriate test in a matter such as the present is a well established one. The receipts accruing to the Trust will be revenue if they constitute "a gain made by an operation of business in carrying out a scheme for profit-making" in the words of the eminent Scottish Judge in the Californian Copper Syndicate case quoted with approval in the passage from Overseas Trust Corporation Ltd v Commissioner for Inland Revenue 1926 AD 444 at 452-3 referred to in my colleague's judgment. (See, too, Commissioner for Inland Revenue v Stott 1928 AD 252 at 259 - 260; Commissioner for Inland Revenue v Leydenberg Platinum Ltd 1929 AD 137 at 145; Lace Proprietary Mines Ltd v Commissioner for Inland Revenue 1938 AD 267 at 275; Commissioner for Inland Revenue v Strathmore Exploration and Management Ltd 1956(1) SA 591 (A) at 599.) The corollary is that they will be non-revenue if they do not derive from "an operation of business in carrying out a scheme for profit-making". The phrase from the Californian Copper Syndicate case has undergone some measure of refinement in the cases of Natal Estates Ltd v Secretary for Inland Revenue 1975(4) SA 177(A) (at 198 E - G) and Elandsheuwel Farming (Edms) Bpk v Sekretaris

<u>van Binnelandse Inkomste</u> 1978(1) SA 101(A) (at 118 A - B) to the extent that a distinction is drawn between the carrying on of a business and the pursuance of a profit-making scheme. The basis for such distinction is that it is more appropriate to refer to a profit-making scheme where a single transaction is involved. I accept that a series of transactions is characteristic of the carrying on of a business. But irrespective of the number of transactions, whether the receipts that flow from the carrying on of a business are revenue still depends on whether the business was conducted with a profit making purpose, i e as part of a profit-making venture or scheme. To hold otherwise would amount to a departure from the earlier authorities - something clearly never intended in either the <u>Natal</u> <u>Estates</u> or <u>Elandsheuwel Farming</u> cases. In this respect I agree with what is said in <u>Meyerowitz and Spiro</u> on Income Tax: para 299 that "[t]he rather clumsy phrase: 'operation

of business in carrying out a scheme of profit-making' in plain language really means that receipts or accruals bear the imprint of revenue if they are not fortuitous, but designedly sought for and worked for". The application of this test involves a consideration of the objectives of the taxpayer (the Trust) and what its purpose, or if there was more than one, what its dominant purpose was (cf. Commissioner of Taxes v Levy 1952(2) 413 (A)). Transactions involving shares do not differ from transactions in respect of any other property and the capital or revenue nature of a receipt is determined in the same way whether one is dealing with land or shares (Silke on South African Income Tax, 11 ed, Vol 1, 3 -90; cf Deceased Estate v Commissioner of Taxes 1949(4) SA 491 (SR)).

I am unable to agree with NICHOLAS AJA that the Trust was carrying on a business by trading in shares. Whether or not it was doing so must be determined applying ordinary common sense and business standards (cf Rhodesia Railways and Others v Commissioner of Taxes 1925 AD 438 at 462). There was no intention on the part of the Trust to conduct a business in shares. The Trust was to operate primarily as a conduit for the acquisition of shares by employees entitled to them in terms of the scheme's rules. The Trust did not operate along accepted business lines. The normal way in which a trader in shares operates is to buy shares and resell them at a profit (De Beers Holdings (Pty() Ltd v Commissioner for Inland Revenue 1986(1) SA 8 (A) at 30 E). The Trust had no such intention. While a profit motive is not essential for the carrying on of a business, its presence or absence is an important factor in determining whether a business is being conducted. A dealer doing business in shares can be expected to engage freely in the market; to buy and sell at the most advantageous times and prices according to the dictates of the market. This is not what the Trust did. It bought when it was obliged to and sold when it was required to. The constraints placed upon the trustees in dealing with the shares are altogether foreign to trading or business in the accepted commercial sense. On a common sense approach the Trust was not carrying on a business by trading in shares.

But even if the Trust could be said in a broad sense to have been conducting a business, it was not a business carried on as part of a scheme of profit-making. Receipts of a revenue nature (in the form of profits) accrue to a trader who acquires and disposes of shares as part of a scheme of profit-making (cf <u>De Beers Holdings (Pty) Ltd v Commissioner for Inland Revenue</u> (<u>supra</u>) at 30 G). NICHOLAS AJA accepts, in my view correctly, that the purpose of the scheme was not one of profit-making. If that is so it seems impossible to conclude, as a matter of logic, that any business conducted in pursuance of the scheme, and according to the strict letter thereof (which is essentially the case here) could be part of a scheme of profit-making. But apart from this the trustees never intended or designedly set out to make a profit - it was not their purpose to do so. As was pointed out in Secretary for Inland Revenue v Trust Bank of Africa Ltd 1975(2) SA 652 (A) at 669 E - G

> "[i]n 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 state of mind required for the purposes of the criminal law, but rather with the purpose for which the transaction was entered into."

Contemplation is not to be confused with intention in the above sense. In a tax case one is not concerned with what possibilities, apart from his actual purpose, the taxpayer foresaw and with which he reconciled himself. One is solely concerned with his object, his aim, his actual purpose. While they might have contemplated the possibility of profits, it was not the purpose of either the company (Stores) in founding the Trust, or the trustees in conducting the affairs of the Trust, to carry on a profit-making scheme. The sole purpose of acquiring, holding and selling the shares was to place them in the hands of eligible employees. The forfeiture provision was not intended to yield a profit. Its purpose was to deter unwanted resignations.

A different conclusion might have been justified if the making of profits was inevitable. But this was not the case. The prospects of profits were highly problematical. They depended upon the degree of success achieved by the scheme. If it had operated to its full potential, and there had been no forfeitures, there would probably have been no profits. But even accepting that forfeitures were inevitable, whether they resulted in profits being made depended on when they occurred in relation to the date of acquisition of the shares and the state of the market at the time of forfeiture. And the overall profits would depend further on whether other purchases and sales resulted in profits or losses. There were thus a number of variables which could influence the profit factor. That profits were not inevitable is proved by the fact that in the 1985 year of assessment the operation of the scheme showed a loss of R70 619.

In my view, therefore, any receipts accruing to the Trust were not intended or worked for, but purely fortuitous in the sense of being an incidental by-product. They were therefore non-revenue. That makes them accruals of a capital nature falling outside the definition of "gross income" in the Income Tax Act, and therefore not subject to tax. This probably renders it unnecessary to consider NICHOLAS AJA's first conclusion viz that the shares bought and sold by the Trust amounted to floating capital. However, to the extent that it may be necessary I proceed to do so.

In our law no company in the Pick 'n Pay group ("the Group") could itself lawfully assist group employees to purchase or subscribe for shares in any company in the group. That follows from the prohibition against a company purchasing its own shares: Lipschitz NO v UDC Bank Ltd 1979(1) SA 789 (A) at 797 H - 798 A; AA Mutual Insurance Association Ltd v Century Insurance Co Ltd 1986(4) SA 93 (A) at 101 D - E; and the further prohibition contained in s 38(1) of the Companies Act, 61 of 1973 ("the Act") against a company giving financial assistance for the purpose of or in connection with a purchase or subscription by any person for shares of such company.

The reason for the establishment of the Trust is to be found in the provisions of s 38(2)(b) of the

Act. In terms thereof the prohibition contained in subsec (1) does not apply to:

> "(b) the provision by a company, in accordance with any scheme for the time being in force, of money for the subscription for or purchase of shares of the company or its holding company by trustees to be held by or for the benefit of employees of the company, including any director holding a salaried employment or office in the company;"

In my view, there can be no doubt that the Trust was established by Stores in order to act as its alter ego. It is correctly accepted by NICHOLAS AJA, as I have said, that the purpose of the scheme was not one of profit-making. As he puts it:

> "The acquisition of gain formed no part of the raison d'être of the scheme, which, as stated in its introductory paragraph and Hurst's evidence, was to enable Pick 'n Pay employees to acquire a shareholding in Pick 'n Pay with no immediate capital outlay and with advantageous terms of payment. The only thing that Pick 'n Pay were interested in was getting shares into the hands of employees, and the furthest thing from their minds was whether the Trust would make a profit or a loss."

That notwithstanding, NICHOLAS AJA holds that the shares acquired by the Trust constituted floating capital. In my opinion, an analysis of the manner in which the Trust held and dealt with the shares makes that conclusion untenable.

The Trust initially received shares allotted to it by Stores. When it sold those shares to an employee, they were appropriated to him and held in trust by the Trust for at least five years unless the employee left the employ of the Group prior to the expiry of the five year period. In the event of the employee leaving prior thereto, or in the event of the employee leaving at any time in consequence of dishonesty or fraudulent conduct, then such employee would forfeit his shares and his loan account would be credited with whatever amount he might then owe to the Trust. Those shares would then become available for resale to other employees in terms of the scheme.

During the relatively short periods between forfeiture and resale, the shares would be held by the Trust pursuant to and for the limited purposes of the scheme. The position is similar when the Trust acquires shares by way of purchase on the Johannesburg Stock Exchange or voluntarily from employees of the Group. In respect of those shares the trustees were given no discretion. They were obliged to sell them to employees who qualified for and purchased them. The price in terms of the scheme, and as required by the Rules of the Johannesburg Stock Exchange, was the middle market price on the day of the purchase.

Despite what has hitherto been said it is arguable that any intention or contemplation of a profit accruing to the Trust could only have been that of the founder of the Trust, viz. Stores. The fact that the Trust, in effect, is the alter ego of Stores would seem to demonstrate this proposition. In that context, it is consistent that provision is made, on termination of the Trust, for any surplus to be paid over to Stores. However, it is not necessary to decide the point. Whatever the position, for the reasons already advanced, it was not the intention (purpose) of Stores or the trustees that the Trust should carry on business by trading in shares for profit. That conclusion, with respect, effectively disposes of the finding by NICHOLAS AJA that the unsold shares held by the Trust from time to time constituted floating capital. Where no trade is conducted there cannot be floating capital: see Sekretaris van Binnelandse Inkomste v Aveling 1978(1) SA 862 (A) at 880 B - 881 A.

It remains to deal with the Commissioner's application for condonation of the failure to timeously lodge the notice of appeal with the registrar of this Court. A satisfactory explanation for the omission has been tendered. It is averred by the Commissioner that the matter is one of substantial importance: this is a test case for 15 similar cases involving some R18,5 million. The grant or refusal of condonation is partly dependent upon the prospects of success. The Court held over the decision in that regard until it had heard full argument on the merits of the appeal (cf Rennie NO v Gordon and Another NNO 1988(1) SA 1 (A) at 20). This Court is divided as to the outcome of the appeal. The test of reasonable prospects of success on appeal being satisfied, condonation will be granted.

The following order is made:

(1) The application for condonation is granted. The costs in connection therewith are to be paid by the appellant.

(2) The appeal is dismissed with costs, including the costs of two counsel.

J W SMALBERGER
JUDGE OF APPEAL

GOLDSTONE, JA) concur
HOWIE, AJA)