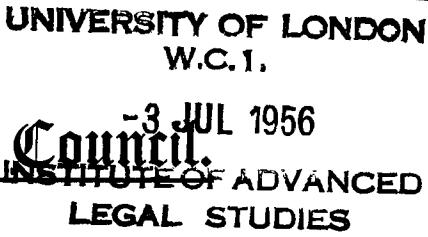


3, 1955



PC 6-5-3

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In the Privy Council.

No. 42 of 1953.

ON APPEAL FROM HER MAJESTY'S COURT OF APPEAL FOR EASTERN AFRICA

BETWEEN

THE COMMISSIONER OF INCOME TAX *Appellant*

AND

H. BJORDAL *Respondent.*

CASE FOR THE RESPONDENT

RECORD

1.—This is an appeal brought by leave from a judgment of the Court of Appeal for Eastern Africa, pronounced on the 28th day of April, 1952, allowing the Respondent's appeal against the judgment of the High Court of Uganda, which had dismissed the Respondent's appeal from a decision of the Appellant dated the 29th day of January, 1951.

2.—The question submitted for the decision of the Court of Appeal arose in reference to an assessment to Income Tax made upon the Respondent for the year of assessment 1950, which assessment included the sum of £3,580 in respect of dividends deemed to have been distributed as dividends to him as a shareholder of Bjordal Mines, Limited, by reason of an order made by the Appellant under Section 21 of the said Income Tax Ordinance, 1940, as amended by the Income Tax (Amendment) Ordinance, 1943, Section 5.

3.—The substantial question of law arising on this appeal is whether the decision of the Court of Appeal for Eastern Africa holding that Bjordal Mines, Limited, was at the relevant time a company in which the public were substantially interested is correct in law.

4.—Section 21 (1) of the Income Tax Ordinance, 1940, as amended by Section 5 of the Income Tax (Amendment) Ordinance, 1943, provides that the Commissioner may, in certain circumstances, by notice in writing order

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that the undistributed portion of 60 per cent. of the total income of a company resident in the Protectorate shall be deemed to have been distributed as dividends among the shareholders, and that the proportionate share thereof of each shareholder shall be included in his total income for the purposes of the Income Tax imposed by the Ordinance. By virtue of proviso (b) the subsection is not to apply to *inter alia* a company in which the public are substantially interested. By subsection (2) a company is to be deemed to be a company in which the public are substantially interested if shares (not being shares entitled to a fixed rate of dividend, whether with or without a further right to participate in profits) carrying 10 not less than 25 per cent. of the voting power have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the said period beneficially held by the public, and if any such shares have in the course of such period been, in fact, freely transferable by the holders to other members of the public.

The relevant statutory provisions are as follow :—

“ Section 21 (1) Where the Commissioner is satisfied that in “ respect of any period for which the accounts of a company “ resident in the Protectorate have been made up, the profits “ distributed as dividends by that company up to the end of the 20 “ sixth month after the last date upon which its accounts for that “ period are required by virtue of the provisions of the Companies “ Ordinance, to be laid before the company in general meeting, “ increased by any tax payable thereon are less than sixty per “ cent. of the total income of the company ascertained in “ accordance with the provisions of this Ordinance for that period, “ he may, unless he is satisfied that having regard to losses “ previously incurred by the company or to the smallness of the “ profits made, the payment of a dividend or a larger dividend “ than that declared would be unreasonable, by notice in writing 30 “ order that the undistributed portion of sixty per cent. of such “ total income of the company for that period shall be deemed to “ have been distributed as dividends amongst the shareholders “ as at the said last date and thereupon the proportionate share “ thereof of each shareholder shall be included in the total income “ of such shareholder for the purposes of this Ordinance :

“ Provided that—

“ (a) * * * *

“ (b) this subsection shall not apply to any company in “ which the public are substantially interested or to a subsidiary 40 “ company of such a company if the whole of the share capital “ of such subsidiary company is held by the parent company or “ by the nominees thereof.

“ (2) For the purpose of this section a company shall be “ deemed to be a company in which the public are substantially

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" interested if shares of the company (not being shares entitled to a fixed rate of dividend, whether with or without a further right to participate in profits) carrying not less than twenty-five per cent. of the voting power have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the said period beneficially held by, the public (not including a company to which the provisions of this section apply), and if any such shares have in the course of such period been, in fact, freely transferable by the holders to other members of the public."

Prior to amendment by Section 5 of the Income Tax (Amendment) Ordinance, 1943, Section 21 was in the following form :—

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" Where it appears to the Commissioner that with a view to the avoidance or reduction of tax a company controlled by not more than five persons has not distributed to its shareholders, as dividend, profits made in any period ending after the 1st day of January, 1939, which could be distributed without detriment to the company's existing business, he may treat any such undistributed profits as distributed, and the persons concerned shall be assessable accordingly."

5.—The material facts in this case are set forth in the Statement of pp. 2-4 Facts filed by the Appellant and the Respondent, and are summarised as follows in the judgment of the Vice-President of the Court of Appeal :— pp. 14-15

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(i) Bjordal Mines Ltd. is a limited liability company registered at Kampala, Uganda, on 25th March, 1948, and has its registered offices in the Uganda Protectorate. (I refer to it hereafter as the Company.)

(ii) The authorized capital of the Company is Shs. 250,000 divided into 12,500 shares of Shs. 20/- each. The share capital is divided into 8,125 "A" shares and 4,375 "B" shares, of which the "A" shares are not transferable without the consent of the directors. The "B"s hares are freely transferable and have equal voting and dividend rights with the "A" shares.

(iii) The Appellant is the holder of 7,632 "A" shares and 1,249 "B" shares in the Company. The other shares are held by :—

- i. Sverre Hendrik Bjordal holding 3,121 "B" shares ;
- ii. L. G. Appenden and four other persons each holding one "B" share.

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(iv) The directors of the Company are the Appellant, Sverre Hendrik Bjordal (who is a brother of the Appellant) and L. G. Appenden ; and these three persons hold between them all the issued "A" shares and all but four of the issued "B" shares.

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(v) By an agreement dated 25th March, 1948, the Appellant sold to the Company various mining titles and rights, then held by him, in consideration of the allotment to him of 12,000 shares in the Company being shares of "A" and "B" class in such proportion as the Appellant should elect, all to be credited to the Appellant as fully paid up. The shares were allotted on the 19th April, 1948, in the proportion of 7,632 "A" shares and 4,368 "B" shares.

(vi) By an Indenture dated 19th April, 1948, the Appellant sold to Sverre Hendrik Bjordal 3,120 "B" shares out of the said 10 4,368 "B" shares allotted to the Appellant for the sum of £18,720.

(vii) On 13th April, 1947 (Quaere 1949) one "B" share was transferred by E. H. St. John Shelton to S. H. Bjordal. The only transfers of any of the said shares are those set out in this and the preceding paragraph.

(viii) The Appellant was assessed in Notice of Assessment No. 20831 for the year of assessment 1950 relating to the year of income 1949. The said Notice of Assessment included as income of the Appellant the sum of £3,580 in respect of dividends deemed to have been distributed as dividends among the shareholders 20 of the Company under Section 21 of the Ordinance.

(ix) The income of the Company for the year 1949 was computed for income tax purposes was Shs. 161,340/-, of which no portion was distributed as dividends. The Respondent served notice under Section 21 deeming 60 per cent. of that sum to have been distributed among the shareholders. This amounted to a sum of Shs. 96,804/-, of which the Appellant's proportionate share was Shs. 71,802/-.

p. 2

6.—The decision of the Commissioner, against which the Respondent appealed to the High Court of Uganda, was in the following terms :—

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(1) That Bjordal Mines, Limited, a limited liability company registered at Kampala, Uganda, on the 25th day of March, 1948, and having its registered offices in the Uganda Protectorate is a company to which Section 21 (1) of the Income Tax Ordinance, 1940, applies and that the provisos (a) and (b) of the said section do not apply.

(2) That Bjordal Mines, Limited, is *not* a company in which the public is substantially interested as defined by Section 21 (2) of the Income Tax Ordinance, 1940.

The effect of this decision was that the Respondent became liable to 40 Income Tax upon £3,580, the appropriate apportioned part of the income of Bjordal Mines, Limited, for the year 1949 deemed to have been distributed to him as dividend.

7.—The Respondent appealed against the decision of the Commissioner to the High Court of Uganda, under the provisions of Section 62 of the Ordinance. The appeal was heard on 31st May, 1951, and on 29th June, 1951, Pearson, J., delivered a reserved judgment in which he held, in effect, that “the public” in the relevant section were contrasted with the persons having control of the company by voting power. After considering the judgments delivered in the Court of Appeal (England) in *Tatem Steam Navigation Co. v. Commissioners of Inland Revenue*, (1941) 2 K.B. 202, and the provisions of Section 21, of the United Kingdom Finance Act, 1922, he came to the conclusion that although Harald Bjordal, the Respondent (in the judgment referred to as Henrik Bjordal), could outvote his brother Sverre Bjordal, yet nevertheless the control of Bjordal Mines, Limited, was in the hands of its two directors, Harald and Sverre, and he upheld the decision of the Commissioner that the public was not substantially interested in the Company.

8.—The Respondent appealed to the Court of Appeal for Eastern Africa against the decision of Pearson, J., and the appeal was heard on the 10th January, 1952. On the 28th April, 1952, the Court (Nihill, P., Worley, V.P., and Ainley, J.) delivered a reserved judgment, unanimously allowing the appeal.

Worley, V.P., after setting out the relevant facts and statutory provisions, came to the conclusion that the important thing in the appeal was to ascertain the meaning of the word “public” in the section under consideration. The word in its widest sense included everyone and anyone, but both parties were agreed that the word was used in Section 21 (2) of the Ordinance in contradistinction to certain persons, or a class or classes of persons, who were impliedly excluded. Three views had been put before the Court.

The Respondent (there the Appellant) contended that the proper test 30 was *de facto* control of the Company. The public were for the purposes of the subsection contrasted with one who could control the Company by his voting power, that is to say, who held more than 50 per cent. of the voting rights. Since the Respondent held more than 50 per cent. of the voting rights, the other shareholders were, *vis-à-vis* him, members of the public.

The second view was that of the learned trial Judge who held that the control of the Company by voting power lay in the hands of the two directors, who could not therefore be considered as members of the public. This view Worley, V.P., rejected on the facts of the case. Sverre Bjordal was only jointly in control of the Company so long as he co-operated with the Respondent. Such precarious control was not sufficient to take him 40 out of the ranks of the public.

The third view, that of the Appellant (there the Respondent), was that control of voting power was not the proper test to apply. Section 21 of the United Kingdom Finance Act, 1922, was concerned with companies controlled by not more than five persons. The limitation of the operation of

RECORD

the section by reference to the conception of control was absent from Section 21 of the Uganda Ordinance, although it had formed part of its repealed predecessor. The true and only test to be applied was whether the Court, looking at all the circumstances of the case, considered that the public was substantially interested in the company. This was a question of fact. Upon the facts of the present case it would be ludicrous (argued the Appellant) to hold that the Company was one in which the public were substantially interested. Further, however, difficult might be the application of the test in some cases, there was no difficulty in the present case because the director of a company could never fall within the definition of 10 "the public."

Worley, V.P., agreed with the contention of the Appellant (there the Respondent) that the Commissioner was entitled to consider the case of each shareholder on its merits, but subject to the condition that certification must be made, not capriciously, but for legal reasons and on settled legal principles. A person who held more than 50 per cent. of the voting rights and so controlled the Company could never be treated as a member of the public for the purposes of the section, and he was not persuaded that it necessarily followed that all the other shareholders automatically fell into the class of "the public." But 20 approaching the matter from the point of view that Sverre Bjordal was *prima facie* a member of the public he asked himself on what ground he could be excluded from that category. The relationship of the Respondent and Sverre Bjordal was not relevant. Further, Sverre did not cease to be a member of the public because the Respondent's object in selling shares to him was to reduce his own liability to tax. There was no evidence to support the assumption that Sverre Bjordal's shares were subject to any condition. It was true that there did not appear to have been any issue of shares to the public in any real sense of those words, but he could see no good reason in law for holding that Sverre Bjordal ceased to be 30 a member of the public by reason of his acquisition of shares. Accordingly he came to the conclusion that the Respondent must succeed in his appeal.

p. 21

Nihill, P., adopted the reasons given by Worley, V.P., notwithstanding that, on a first appreciation of the facts relating to the Company, the finding that it was one in which the public were substantially interested seemed contrary to common sense. The question was however one of construction and it was not the function of the Court to repair a breach caused by a legislative enactment.

pp. 21-23

Ainley, J., considered that the section was aimed against an individual or his associates who formed an incorporated company to run a business, 40 but retained control by means of voting power so as indefinitely to withhold from distribution and assessment profits which would ultimately benefit those in control. Where, however, control was widely spread, or where the small controlling group was restrained by substantial interests outside the group, the danger of tax avoidance was lessened. Section 21 of the United Kingdom Finance Act, 1922, brought out this idea with clarity

12 & 13 Geo. 5,
ch. 17

by defining what was regarded a dangerous concentration of control, and in considering whether the Company was one in which the public was substantially interested, "the public" were obviously contrasted with were small defined group who were capable of taking control of the Company.

In Uganda, however, the relevant section *prima facie* applied to all companies and no reference to control occurred in it. No clear indication was given as to what members of the Company were, or were not, members of the public, although the legislature clearly intended to contrast one class of members with another.

- 10 Ainley, J., agreed that officers and directors of the Company could not for the purposes of the section be regarded as excluded from the category of the public. If the section was to be given a meaning it must be construed upon the footing that, where a company was found in exclusive control of a small group of persons, members of that group were not members of the public. In the absence of express statutory provisions it was impossible to say that Sverre was a member of the controlling group and unless he could be placed within that group he remained a member of the public.

- 9.—By an Order dated 8th September, 1952, the Court of Appeal, for Eastern Africa granted conditional leave to the Appellant to appeal pp. 24-25
20 to Her Majesty in Council from the final judgment of that Court and by further Order dated 28th April, 1953, granted final leave to appeal. p. 25

- 10.—The point for decision in this case turns solely upon a proper construction of the meaning of the word "public" in Section 21 (2) of the Ordinance. That word in the ordinary usage of the English language means and includes all the members of the community. Indeed it is significant that the primary definition of the word in Section 22 (2) of the East African Income Tax (Management) Act, 1952 (which was enacted after the decision of the East African Court of Appeal in the present case) is "the community as an aggregate, not in its organised capacity." If any restriction is to be placed upon the meaning of the word, therefore, it can only be by necessary inference from the context in which it appears in Section 21. No such inference, it is submitted, can be drawn, unless it is that "the public" is contrasted with some person who, by reason of his voting power, is in a position to exercise control over the Company's dividend distributions, or with some group of persons who have bound themselves to act in concert and are in a position to exercise such control. If such a contrast is to be drawn as regards Bjordal Mines Limited it can only be between Harald Bjordal, the Respondent (who controlled 71,602 votes out of a total of 96,804) and the other shareholders including Sverre Bjordal, who are therefore to be regarded as members of the public.

- 11.—The Respondent humbly submits that the judgment of the Court of Appeal for Eastern Africa is right and ought to be affirmed for the following among other

REASONS

- (1) BECAUSE the Income Tax Ordinance, 1940, as amended, nowhere defines "the public," and accordingly that expression must be understood to include all members of the community, unless and to the extent that its context compels the inference that some person or persons are to be excluded from its scope
- (2) BECAUSE the distinction implied by the use of the expression "the public" in the context in which it occurs is between (i) those persons who, either solely or as members of a group bound to act in concert, are in control of the company, and 10 (ii) other shareholders.
- (3) BECAUSE the control of Bjordal Mines Limited, was in the hands of Harald Bjordal (the Respondent) alone.
- (4) BECAUSE Sverre Bjordal, and the five other shareholders who together held beneficially shares in Bjordal Mines Limited, carrying not less than twenty-five per cent. of the voting power, which shares had been unconditionally acquired by them and were freely transferable by them, were all members of the public.
- (5) BECAUSE Bjordal Mines Limited, was a company to which 20 the provisions of Section 21 (1) of the Uganda Income Tax Ordinance, 1940 (as amended) did not apply.
- (6) BECAUSE the reasoning in the decision of the Court of Appeal for Eastern Africa was well-founded.

F. HEYWORTH TALBOT.

H. MAJOR ALLEN.

In the Privy Council.

No. 42 of 1953.

ON APPEAL FROM HER MAJESTY'S COURT OF
APPEAL FOR EASTERN AFRICA.

BETWEEN
THE COMMISSIONER OF
INCOME TAX *Appellant*
AND
H. BJORDAL *Respondent.*

CASE FOR THE RESPONDENT

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