

IN THE COURT OF REVIEW

No. 1 of 1979

Between:

KELTON INVESTMENTS LIMITED

Appellant

and

COMMISSIONER OF INLAND REVENUE **Respondent**

Mr. M.D. Benefield for the Appellant.

Mr. M.J. Scott and Ms. Helu for the Respondent.

JUDGMENT

This is an appeal from the disallowance by the Commissioner of Inland Revenue of the taxpayer's objection to an assessment of \$29,774 as income rather than treating it as a capital accretion. The assessment arises out of the purchase by the taxpayer Kelton Investments Ltd of a block of 20,000 shares in Desbro Steel Rolling Mills Ltd from Burns Philp (South Sea) Co. Ltd. at \$2.25 a share and the sale of those shares less than two months later at \$3.75 a share.

Kelton Investments Ltd is a private company in which James Michael Ah Koy, his wife and children are the shareholders. James Michael Ah Key although not the principal shareholder and is the governing Director, with the powers which go with that position. He may, I think, be described as a highly successful businessman and in 1976 or thereabouts he became interested in Desbro Steel Rolling Mills Ltd in which the majority interest was held by the Sennik family, who one way or another held 62.5% of the capital of the Company. W.R. Carpenter (South Pacific) Ltd and Burns Philp (South Sea) Co. Ltd each held 20,000 shares amounting in each case to 7.23% of the total

...held 20,000 or 7.23%

number of shares issued. Mr. Ah Key held net shares. Desbro Steel Rolling Mills Ltd, which I shall call Desbro had fallen upon evil days, the nature of which need not be particularised here, and begun to look round for assistance, the Sennik family being willing, of necessary, to sell out their shareholding. Mr. Ah Key thought to take control of Desbro and put out feelers not only to the Senniks but also to Burns Philp (South Sea) Co. Ltd, with whose Manager at the time he appears to have been on very friendly terms. He became very friendly also with the Senniks and on 16th June 1976 became an alternate director to Desraj Sennik, becoming a substantive director on 31st August 1976. He had not yet become a shareholder but a director did not need to be a shareholder. He made an offer to the Senniks to buy their shares at \$2.25 a share, but without success, and in 1976 and 1977 made various offers going as high as \$3.25 a share for the Senniks' shares but none were acceptable to the Senniks. He then brought Desraj Sennik and his son Subhas Chandra Sennik who were then managing the business, to Mr. Lyle Cupit, the Managing Director of W.R. Carpenter Ltd (South Pacific). That was on 10th March 1977.

There Mr. Cupit, on behalf of his company offered to buy the Sennik shares for \$3.75 a share. He made a holograph memorandum of what was agreed upon at that meeting, and because it seems to be the most material fact in the case, I set it out in full.

DESBRO STEEL ROLLING MILLS

Closing offer accepted

\$3.75 per share

for 173050 shares

= 62.57%

Carpenters already held 20000 or 7.23%

10/3/77

\$648,937

Offer subject to Fiji Government permitting

- (a) Takeover and engineering inspection of plant.
- (b) 1. Ah Koi to make and get acceptance of his offer to purchase 20,000 shares before any further negotiations; and of course
2. Ah Koi also tendering for 3,500 shares BP Trustee Co. as a condition, but if the report

Meeting Sennik (Senior) Subash Sennik and J. Ah Koi.

Mr. Ah Key had talked to Burns Philp (South Sea) Co. Ltd about their shares in Desbro and on 10th March 1977, after his meeting with Mr. Cupit they were offered to him at \$2.25 a share. He accepted the offer and paid a sum of \$45,000 the following day and the relevant instrument of transfer was signed on 5th April 1977 and approved by the Desbro Board of Directors on 5th May. On 25th April 1977 Carpenters made a formal offer for the Sennik shares which was accepted on the 27th idem and on the latter day made a formal offer to Kelton Investments Ltd offering to buy the shares which Kelton Investments Ltd had bought from Burns Philp (South Sea) Co. Ltd six weeks before. That offer was accepted the same day. On 26th June 1977 the Central Monetary Authority approved the transfer of the Senniks' shares to W.R. Carpenter (South Pacific) Ltd. In due course Kelton Investments Ltd. made their tax return representing a sum of \$29,774 the proceeds of the sale of the Desbro shares as a capital accretion. The Commissioner of Inland Revenue demurred.

The matter falls to be determined under proviso (a) to section 11 of the Income Tax Act. Section 11 is a section giving a very comprehensive definition of total income and is followed by twenty-two provisos, of which the first is relevant to these proceedings. The provisos start off:

" Provided that, without in any way affecting the generality of this section, total income, for the purpose of this Act, shall include -

- (a) any profit or gain accrued or derived from the sale or other disposition of any real or personal property or any interest therein, if the business of the taxpayer comprises dealing in such property, or if the property was acquired for the purpose of selling or otherwise disposing of the ownership of it, and any profit or gain derived from the carrying on or carrying out of any undertaking or scheme entered into or devised for the purpose of making a profit; but nevertheless, the profit or gain derived from a transaction of purchase and sale which does not form part of a series of transactions and which is not in itself in the nature of trade or business shall be excluded.

The Commissioner of Inland Revenue contends that the profit is caught as being property acquired for the purpose of selling or otherwise disposing of it and he says that first it has not been shown that the shares were not acquired for the purpose of resale and secondly that it is not shown that a commission business is not established, an instance of which is the purchase and sale of these particular shares. I begin by observing that the onus of proof rests upon the taxpayer see S.70(2) of the Income Tax Act 1974. I think that the onus is fairly described by Hunt J. in F.L.T. v. Nixon [1979] 10 A.T.R. 62, 66 -

" Juries in civil cases every day are directed by reference to a pair of scales in which the evidence and the arguments of the plaintiff are placed on the one side and on the other are placed the evidence and arguments of the defendant. The juries are told that if the plaintiff succeeds, in their estimation in weighing down these scales ever so slightly he has discharged the onus of proving to their reasonable satisfaction that whatever he asserts is more probably correct than not. I do not see why a similar degree of proof is not applicable where the taxpayer is obliged to establish the absence of a particular

intention in purchasing shares. *

I accept that statement as correct.

Mr. Ah Key was the principal witness for the taxpayer, and he was cross-examined at some length. He admitted the contents of the memorandum made by Mr. Cupit to be substantially accurate, although he cavils at the use of the term 'intermediary' which Mr. Cupit used to describe him in a telex to his Chairman of Directors - a term which Mr. Cupit agrees to have been used somewhat loosely. Mr. Ah Key apparently rang Mr. Rowland, the Manager of Burns Philp (South Sea) Co. Ltd on the evening of the day he spoke to Mr. Cupit and the Senniks and arranged to buy Burns Philp's shares at \$2.25 a share, and the following day he paid \$45,000, although the relevant share transfer was not signed until 5 April 1977.

There is a provision in Desbro's Articles (Article 25) which confers certain rights of pre-emption in favour of existing members of the company, and which have to be exhausted before shares can be transferred to non-members. Mr. Ah Key said that when he purchased the shares from Burns Philp he still intended to try to obtain either a controlling interest or a substantial minority interest in the Desbro Company, and that he only relinquished that idea when he found that Carpenters had bought the Sennik shares and were in a position to shut him out. He therefore sold his shares to Carpenters. Mr. Ah Key's evidence as to his purpose or object or his state of mind must, of course be scrutinised most closely see Pascoe v. Commissioner of Taxation (1956) 30 ALJ 402, 403; AITR 315.

There is no doubt in my mind that Mr. Ah Key's original intention was to obtain control of Desbro because he thought he could operate it at a profit and his efforts to the Senniks and his approach to the Bank were all conducive

to that end. But it is significant that he did not buy Burns Philp's shares until after Carpenters through Mr. Cupit had agreed to buy the Sennik's shares. The fact that the agreement was merely oral is not, I think, to the point. In my view Mr. Ah Koy bought Burns Philp's shares at \$2.25 a share at a time when he knew that Carpenters had bought the Sennik shares at \$3.75 a share and would buy his shares for the same price. Mr. Ah Koy admitted that he learned of Carpenter's interest in Desbro on 10th March 1977, and knowing that, he paid out \$45,000 in buying Burns Philp's shares. It is significant that he paid Burns Philp immediately, although a form of transfer was not signed until 5th April 1977. I think that it must be borne in mind that Carpenters were not prepared to approach Burns Philp direct, and were not prepared to complete the purchase of the Sennik shares unless Burns Philp could be bought out. Hence Mr. Cupit required an intermediary. Mr. Ah Koy was that intermediary. He was not Mr. Cupit's agent. He was being allowed to take his profit. Mr. Cupit anticipated that he would have to pay \$3.00 a share. In the event he bought for \$2.25. I do not believe that Mr. Ah Koy still intended after the meeting of 10th March to obtain control of Desbro. In his own words, he did not have the business muscle to compete with Carpenters. I do not believe, either, that at that stage he expected that there would be any obstacle either from Desbro's directors or from the Central Monetary Authority to the transfer of the Sennik's shares to Carpenters or that the condition of the plant would stand in the way. There may have been the hope that Carpenter's engineering inspection would induce Mr. Cupit to go back on the transaction, but I think it was a hope rather than an expectation. I am not sure whether he realized that Desbro's directors could not stop the transfer to Carpenters under the pre-emptive clauses. It will be noted that he sold Kelten's shares to Carpenters while the transfer of Sennik's shares was still under consideration by the Central Monetary.

Authority. It would appear that Carpenters applied for consent to the purchase of the Sennik shares on 25th April 1977. It was granted on 28th April. Mr. Ah Koy accepted Carpenters offer to purchase his shares on 27th April.

But the question which has to be answered in cases of this kind, it has been said, is what was the dominant motive of the taxpayer when he acquired the interest which is challenged: see C.I.R. v. Thompson in the Fiji Court of Appeal (Civil Appeal No. 8 of 1979). So here the question to be answered is what was the dominant motive of the taxpayer when it bought Burns Philp's shares in Desbro Steel Rolling Mills Ltd - was it with a view to resale at a profit. It has been pointed out that it is a question of fact as to whether the taxpayer had that motive.

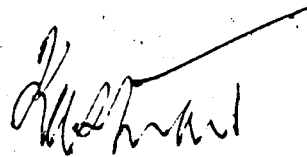
I do not attach a great deal of importance to the lack of a feasibility study. Mr. Cupit probably obtained that to satisfy his directors: Mr. Ah Koy had merely to satisfy himself. Nor to his approaches to the Bank for a sum which, if Mr. Cupit's evidence is accepted, was quite inadequate to make Desbro a viable concern. Mr. Ah Koy was satisfied that he could make Desbro profitable with the money he was able to raise from the Bank together with what he had on deposit with Burns Philp. Nor do I attach much importance to the fact that the taxpayer's memorandum of association permits it to deal in commissions and to sell, dispose of and deal in its property. Its main object is to deal in merchandise and in particular typewriter, accounting, adding, calculating, dictating, duplicating, addressograph machines and such like. The objects upon which the Commissioner lays stress are usual provisions which are found in the memorandum of association of most companies and they are included so that the company will not be restricted in carrying out its normal operations. But I am interested in, and do attach importance to the fact that the

taxpayer retained these shares for only approximately seven weeks, as it seems to me that the fact that the taxpayer held the shares for such a short time is strong evidence that he acquired them for purposes of profit making. Mr. Ah Koy's evidence on this point is that when he realised that Carpenters proposed to buy the Sennik shares he changed his mind about trying to acquire control of Desbro and decided to sell. He said in cross-examination that he realised that unless he got the Sennik shares he could not control Desbro, and I do not accept that when he purchased Burns Philp's shares, he still intended to try to control Desbro. He said that after 11 March 1977 he discovered he could not compete with Carpenters. I do not accept either of those statements. I am satisfied that he bought Burns Philp's shares with the intention of selling them to Carpenters at a profit.

But purpose is not necessarily the same as intention: see Plimmer v. Commissioner of Inland Revenue (No.2) (1958) NZLR 147, 150. Here Mr. Ah Koy knew that Carpenters were taking over Desbro. He had agreed with Mr. Cupit that he would buy Burns Philp's shares. He had a pretty good idea that he could acquire them for considerably less than \$3.75 a share. He had received from Mr. Cupit a promise that Carpenters would buy those shares at \$3.75 if he wanted to sell them. In these circumstances I draw the inference that Mr. Ah Koy's purpose - and indeed I think his only purpose - was to make a profit by buying these shares cheaply from Burns Philp and selling them to Carpenters. The fact that he accepted Carpenters offer promptly when it was made seems to me confirmation of my estimate of his purpose.

The Commissioner also contends that the taxpayer was carrying out a scheme devised for the purpose of making a profit. In the light of my finding above I do not consider it necessary to enter into a discussion of this aspect of

the matter. The appeal will be dismissed and the applicant will pay the Commissioner's costs to be agreed or taxed.



(K.A. Stuart)

SUVA,

7th March, 1981.