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LEGAL STUDIES IN THE PRIVY COUNCIL
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LONDON, W.C.1.

No. 27 of 1958

O N A P P E A L

FROM THE COURT OF APPEAL FOR EASTERN AFRICA

55495

B E T W E E N

GEORGE N. HOURY Q.C. ... Appellant

- and -

THE COMMISSIONER OF INCOME TAX Respondent

C A S E FOR THE RESPONDENT

RECORD

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1. This is an appeal brought by leave from the Judgment and Order of the Court of Appeal for Eastern Africa dated the 2nd April 1958 dismissing the Appellant's appeal from a Judgment of the High Court of Tanganyika, dated the 12th November 1956, which had dismissed the Appellant's appeals against additional assessments to income tax for the years of income 1951 and 1952.

pp.87-98

pp.46-61

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2. The substantial issue of law in this case is as to whether or not undistributed income of a company which is deemed by virtue of section 22 of the East African Income Tax (Management) Act 1952 ("the 1952 Act") to have been distributed as dividends amongst the shareholders can be said to have been "paid" to a shareholder for the purposes of section 24 of the Act, which section is concerned with the treatment of income settled on children of the settlor.

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3. The statutory provisions with which this appeal is directly concerned are those parts of the said sections 22 and 24 of the 1952 Act hereinafter set out:-

"22. (1) Where the Commissioner is satisfied that, in respect of any period for which the accounts of a company resident in the Territories have been made up, the amounts distributed as dividends by that company up to the end of twelve months after the date to which such accounts have been made up, increased by any tax payable thereon, are less than sixty per cent

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of the total income of the company ascertained in accordance with the provisions of this Act 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 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 end of the sixth month after the date to which such accounts have been made up and thereupon the proportionate share thereof of each shareholder shall be included in the total income of such shareholder for the purposes of this Act: 10

Provided that when the reserves representing accumulations of past profits which have not been the subject of an order under this section exceed the paid-up capital of the company together with any loan capital which is the property of the shareholders, or the actual cost of the fixed assets of the company, whichever of these is greater, this sub-section shall apply as if instead of the words "sixty per cent" the words "one hundred per cent" were substituted. 20

(2)

(3)

(4) Where the proportionate share of any shareholder of a company in the undistributed profits of the company has been included in his total income for any year under the provisions of sub-section (1) the tax payable in respect of such proportionate share may (if the shareholder so elects by giving notice in writing to the Commissioner at any time before the due date for the payment of such tax), be recovered from the company and thereupon the Commissioner may serve a notice upon the company stating the sum so payable, and in default of payment the tax may be recovered from the company in the manner provided by section 86; and in any such case the tax paid by the company on behalf of the shareholder shall, upon the subsequent distribution in whatever form of such profits, be recovered by deduction from such distributed profits. 30 40

(5) Where tax has been paid in respect of any undistributed profits of a company under this section, and such profits are subsequently distributed, the proportionate share therein of any shareholder of the

company shall be excluded in computing his total income.

10 (6) When a company is a shareholder deemed under sub-section (1) to have received a dividend, the amount of the dividend thus deemed to have been paid to it shall be deemed to be part of its total income for the purposes also of the application of that sub-section to distributions of profits by that company, and the provisions of this section shall apply accordingly.

20 (7) Where any undistributed portion of the total income of a company has been deemed, by notice given under the provisions of this section, to have been distributed as dividends to the shareholders of that company, the company shall, within twenty-one days of the date of the service of the said notice, furnish each shareholder with a certificate setting forth the amount of the dividend deemed to have been distributed to that shareholder and the amount of tax which the company would be entitled to deduct from such dividend under the provisions of section 41 if such dividend had been paid.

(8)

(9)

(10)

30 (11). Where a trustee is a shareholder deemed under sub-section (1) to have received a dividend, then the Commissioner may, by notice in writing, require the trustee to furnish the name and address of each person having any beneficial interest in the shares held by such trustee; and thereupon the Commissioner may apportion the dividends deemed to have been received in respect of such shares among such persons in accordance with such beneficial interests and such apportioned amounts shall be included in the total income of each such person for the purposes of this Act and the tax thereon may be recovered in accordance with the provisions of sub-section (4).

40 24. (1) Where, by virtue or in consequence of any settlement to which this section applies and during the life of the settlor, any income is paid to or for the benefit of a child of the settlor in any year of income, the income shall be treated for all the purposes of this Act as the income of the settlor for that year and not as the income of any other person.

(2) Subject as hereafter provided, for the purposes of this section -

(a) income which, by virtue or in consequence of a settlement to which this section applies, is so dealt with that it, or assets representing it, will or may become payable or applicable to or for the benefit of a child of the settlor in the future (whether on the fulfilment of a condition, or the happening of a contingency, or as the result of the exercise of a power or discretion, or otherwise) shall be deemed to be paid to or for the benefit of that child; and 10

(b) any income dealt with as aforesaid which is not required by the settlement to be allocated, at the time when it is so dealt with, to any particular child or children of the settlor shall be deemed to be paid in equal shares to or for the benefit of each of the children to or for the benefit of whom or any of whom the income or assets representing it will or may become payable or applicable; 20

(c) in relation to any settlor, only income originating from that settlor shall be taken into account as income paid by virtue or in consequence of the settlement to or for the benefit of a child of the settlor.

(3)

(4) Where by virtue of sub-section (1) any tax becomes chargeable on and is paid by the person by whom the settlement was made, that person shall be entitled to recover from any trustee or other person to whom the income is payable by virtue or in consequence of the settlement the amount of the tax so paid, and for that purpose to require the Commissioner to furnish to him a certificate specifying the amount of the tax so paid; and any certificate so furnished shall be conclusive evidence of the facts appearing thereby. 30

(5) 40

(6) Any income, which is deemed by virtue of this section to be the income of any person, shall be deemed to be the highest part of his income.

(7)

10 (8) This section applies to every settlement, wheresoever it was made or entered into, and whether it was made or entered into before or after the passing of this Act, except a settlement made or entered into before the 1st January, 1939, which immediately before that date was irrevocable, and shall (where there is more than one settlor or more than one person who made the settlement) have effect in relation to each settlor as if he were the only settlor.

(9) In this section -

- (a) the expression "child" means an individual who was under the age of twenty-one years on the 1st January in the year of income and includes a step-child, an adopted child, and an illegitimate child;
- 20 (b) the expression "settlement" includes any disposition, trust, covenant, agreement, arrangement or transfer of assets, but does not include any such disposition, trust, covenant, agreement, arrangement or transfer of assets, resulting from an order of a court unless such order is made in contemplation of this provision;
- 30 (c) the expression "settlor," in relation to a settlement, includes any person by whom the settlement was made or entered into directly or indirectly, and in particular, (but without prejudice to the generality of the foregoing words of this definition) includes any person who has provided or undertaken to provide funds directly or indirectly for the purpose of the settlement, or has made with any other person a reciprocal arrangement for that other person to make or enter into the settlement.

- (d)
- (e)
- (f)

40 4. The facts of the case appear from the Statements of Fact by the Appellant together with an addition thereto agreed by the parties at the hearing in the High Court and are summarised below:- pp.6-10

- (i) The Appellant, an advocate practising in

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Tanganyika Territory, is a shareholder in a private company entitled "Coastal Freights & Co. Ltd." (hereinafter called "the Company").

- (ii) The paid-up share capital of the Company is Shs. 500,000/- divided into 500 shares of Shs. 10,000/- each and at all material times the shareholders were:-

The Appellant.....	251 shares	
The Appellant's wife.....	49 shares	
The Appellant's son Christopher.....	100 shares	10
The Appellant's son Robin.....	<u>100 shares</u>	

Total - 500 shares

- (iii) The Appellant's sons Christopher and Robin were at the material time children within the meaning of section 24 (9) of the 1952 Act and the shares in the Company held by them were transferred to them by the Appellant without consideration, which transfers are agreed for the purposes of Section 24 of the 1952 Act to constitute a settlement made after the 1st January 1939. 20

- (iv) By directions dated 17th November 1954 the Respondent ordered that an amount of Shs. 220,812/- being 60% of the Company's total taxable income of Shs. 368,020/- for the period ended 31st December 1950 be deemed to have been distributed amongst the Company's shareholders as at 30th September 1951 and that an amount of Shs. 167,838/- being 60% of the Company's total taxable income of Shs. 279,730/- for the period ending 31st December 1951 be deemed to have been distributed amongst the Company's shareholders as at 30th June 1952. 30

- (v) The proportionate shares of each shareholder in the said amount of Shs. 220,812/- are:-

	Gross	Tax	Nett	
The Appellant ...	110,848	22,170	88,678	
The Appellant's wife ...	21,640	4,328	17,312	40
The Appellant's son Crhistopher.	44,162	8,832	35,330	
The Appellant's son Robin	<u>44,162</u>	<u>8,832</u>	<u>35,330</u>	
Shs.	<u>220,812</u>	<u>44,162</u>	<u>176,650</u>	

(vi) The proportionate shares of each shareholder in the said amount of Shs. 167,838/- are:-

	Gross	Tax	Nett
The Appellant....	84,255	21,064	63,191
The Appellant's wife...	16,448	4,112	12,336
The Appellant's son Christopher.	33,567	8,391	25,176
The Appellant's son Robin.....	33,568	8,392	25,176
Shs.	<u>167,838</u>	<u>41,959</u>	<u>125,879</u>

20 (vii) The whole of the gross dividends so deemed to have been distributed have been treated by the Respondent as the Appellant's taxable income and after making the appropriate personal allowances and after making allowance for the tax already assessed, tax deducted at source and further Life Assurance Allowance, tax has been charged in an amount of Shs. 104,304/- for the year of income 1951 and in an amount of Shs. 72,900/- for the year of income 1952.

30 5. The Appellant objected to the two Additional Assessments made upon him so far as concerned the attribution to him under Section 24 of the 1952 Act of dividends deemed under Section 22 to have been distributed to his two children. He applied to the Respondent under Section 74 (2) of the 1952 Act to review and revise the said assessments. By two notices dated the 23rd July 1955 the Respondent gave notice to the Appellant that he was not prepared to amend the said assessments and thereupon the Appellant appealed against the said assessments to the High Court of Tanganyika. The Appellant's appeal came on for hearing in the High Court (Lowe, J.) on the 1st November 1956 and on the 12th November 1956 the Court delivered judgment dismissing the appeals with costs.

pp.1-3

pp.4-6

pp.46-61

40 Lowe J. said that the Appellant contended that the assessments were misconceived and erroneous in law because:-

(i) the income deemed to have been distributed under the provisions of Section 22 of the 1952 Act was not income arising by virtue or in consequence of any settlement to which Section 24 of the Act applied;

p.47
11.1-14

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(ii) income deemed to have been distributed under the provisions of Section 22 was not income paid to or for the benefit of a child; and

(iii) Section 24 of the Act could not operate retrospectively in respect of accounting periods ending before its operative date - i.e. 1st January 1951.

pp.47-48

Lowe J. then referred to the agreed facts of the case and to the relevant portions of Sections 22 (1) and 24 of the 1952 Act.

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p.49

p.57 1.30-
p.58 1.38

Lowe J. declined to interpret Sections 22 and 24 by reference to the provisions of similar legislation in the United Kingdom, Indian and South African taxing Acts. The duty of the Court was first to analyse the sections under review before doing anything else and if it was found that the words of those sections left no doubt as to the intention of the legislature there was no need to go further. Lowe J. was not in doubt as to the meaning of Sections 22 and 24.

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p.59 1.25-
p.60 1.15

Lowe J. said that the Appellant, the settlor, and his two children were during the appropriate period shareholders in the Company Coastal Freights & Co. Ltd., a proportion of the income of which Company was directed to be classed as dividends actually distributed and so became taxable. This part of the Company's income no doubt would have gone to the shareholders in due course but it was properly assessable for tax under Sections 8 (the charging section) and 22 of the 1952 Act. Section 24 went further. The income of the Company included certain monies which might have become payable or applicable for the benefit of the two children in the future. Sub-section 2 (a) of Section 24 deemed those monies to be paid to or for the benefit of the children of the settlor and by sub-section (1) any income paid to or for the benefit of a child of the settlor in any year of income was to be treated for all the purposes of the Act as income of the Settlor for that year. The income arose, insofar as the children were concerned, in consequence of the settlement and that income being shown in the accounts of the Company in a year of income to which the Act applied was properly assessable.

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p.60 1.42-
p.61 1.14

Referring to the grounds of appeal in order, Lowe J. held that, as to the first ground, the income deemed to have been distributed under the provisions

of Section 22 of the Act in this case was income arising by virtue or in consequence of the settlement made by the Appellant in favour of his sons and that Section 24 applied. As to the second ground, the income which was deemed to have been distributed under Section 22 was in fact income which had been so dealt with by the Company that it would or might become payable or applicable to the benefit of the sons of the settlor Appellant in the future and so was to be treated as income of the Appellant. As to the third ground, Section 24 of the 1952 Act did not purport to operate retrospectively in respect of accounting periods ending before its operative date, namely 1st January 1951, but it did operate in respect of the income of the Company which was shown in accounts for a period which was itself within the orbit of the 1952 Act.

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6. The Appellant appealed to the Court of Appeal for Eastern Africa against the judgment of the High Court of Tanganyika. The grounds of appeal were:-

(i) That the learned Judge was wrong in law in holding that dividends deemed to have been distributed to infant shareholders under the provisions of Section 22 of the 1952 Act could, in the absence of physical payment be held to be income paid to or for the benefit of a child of the Appellant settlor during the relevant year of income.

p.62 11.1-8

(ii) That the learned Judge was wrong in law in holding that in the circumstances set out in Ground (i) above, such income, if paid to or for the benefit of the child (which was denied) was so paid by virtue or in consequence of the "settlement".

p.62 11.9-13

(The third ground of appeal to the High Court, as to the retrospective operation of Section 24 of the 1952 Act, was not pursued in the Court of Appeal.)

p.66 1.15

7. The appeal came on for hearing (O'Connor P., Forbes J.A., and MacDuff J.) on the 28th February 1958 and on the 2nd April 1958 the Court delivered judgment dismissing the appeal with costs.

pp.87-97

Forbes J.A., who delivered the leading judgment, referred to the agreed facts and said that the short points for decision were (a) whether the notional income arising on settled shares by reason of an order under Section 22 (1) of the 1952 Act was, or was to be treated as "income paid to or for the benefit of a child of the settlor" under Section 24 (1) of the Act,

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p.88 11.12-20

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and (b) if so, whether such income was paid "by virtue or in consequence of" the settlement.

p.88 1.48-
p.90 1.39

Forbes J.A. said that the learned Judge in the High Court, in dismissing the Appellant's appeal, relied largely on paragraph (a) of subsection (2) of Section 24 of the Act as to income so dealt with that it, or assets representing it, may become payable or applicable for the benefit of a child of the settlor in the future. Forbes J.A. thought that the argument of Lowe J. showed some confusion of thought between subsection (1) and subsection (2) of Section 24. Forbes J.A. considered that subsection (2)(a) clearly contemplated a "dealing" with the income by reason of some internal provision within the settlement; in his opinion the assessments could not be supported on the basis of paragraph (a) of subsection (2) of section 24 and he said that in fact counsel for the Respondent had not sought to rely on that paragraph either before the High Court or before the Court of Appeal.

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p.92 11.25-
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As to comparing the provisions of the British Income Tax Act 1952 with those of the 1952 Act, Forbes J.A. found himself unable to derive any useful guidance from a textual comparison between the two sets of provisions and he based his conclusions as to the construction to be placed on Sections 22 and 24 of the 1952 Act purely on a consideration of the provisions of the Act itself.

p.92 1.36-
p.93 1.36

Forbes J.A. agreed with counsel for the Appellant that "paid" in section 24 (1) prima facie meant physically paid and that special provision was necessary to extend that meaning but he considered that such special provision did exist. He did not see any reason why such special provision should be contained within section 24 itself so long as the Act made it clear that the special provision was intended to apply to section 24. The special provision here was that part of section 22 (1) which provided that sixty per cent of the total income of the company should be deemed to have been distributed as dividends and that notional income which was deemed to have been distributed to each shareholder should be included in the total income of such shareholder "for the purposes of this Act." Forbes J.A. held that the plain meaning of the words of the section was that notional income arising in consequence of an order made under section 22 was to be treated for all the purposes of the Act as income actually paid to the shareholder and that, therefore, for the purposes of Section 24 such

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notional income must be treated as income actually paid. He said that this conclusion was not affected by an inference arising from the inclusion of subsection (6) in section 22; the main significance of that subsection was that it made clear that income "deemed to have been distributed" under subsection (1) was regarded as "deemed to have been paid" to a shareholder.

10 Forbes J.A. referred to the argument that a settlor would be unduly prejudiced by being unable to recover from a company under section 22 (4) any tax paid by him on notional income. He said that even if this were so, he would have found difficulty in putting any other construction on section 22 (1) but it appeared to him that by reason of the joint effect of subsection (4) of section 22 and subsection (4) of section 24 prejudice would not in fact result to the settlor.

p.93 l.37-
p.94 l.29

20 Forbes J.A. referred to the submission of counsel for the Appellant that there was no authority for the proposition that "paid" included "deemed to have been paid." Forbes J.A. considered that it was not a question whether the word "paid" ordinarily included "deemed to have been paid" but whether income deemed to have been paid by virtue of the provisions of the Act was to be treated for the purposes of the Act as actually paid. It was necessary to ascertain for what purpose and between what persons the statutory fiction was to be resorted to but that presented no difficulty here. The object of the legislature was to prevent the use of certain devices for the avoidance of tax. These devices were

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p.95 l.33-
p.96 l.20

(a) accumulation of profits by a company so that there was no dividend to include in the shareholders' taxable income and

40 (b) reduction of a taxpayer's income by means of settlements of capital on the taxpayer's children. It appeared to him wholly consistent with the clear object of the legislature that notional income which, under section 22 (1), fell to be included in the total income of a child as arising under a settlement, should be included in the income of the settlor under section 24, and that the persons to whom the statutory fiction created by Section 22 applied must include the person made responsible by the legislature for payment of tax arising under a settlement to which section 24 applied.

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p.96 11.21-40 Forbes J.A. then dealt with the second ground of appeal, namely that the notional payment was not a payment "by virtue or in consequence of the settlement". He said that counsel for the Appellant conceded that if an actual payment of dividend had been made, it would have been a payment "by virtue or in consequence of the settlement," but argued that in the case of a notional dividend it arose by virtue or in consequence of the action of the Respondent and not by virtue of the settlement. 10
 Forbes J.A. could not accept that argument. It was true that an act of the Respondent was necessary to create the notional dividend, but for that matter an act of the company was necessary to create an actual dividend. The fact remained that the notional dividend accrued to the particular infant by virtue of his holding shares settled on him under the settlement. Forbes J.A. considered it clear that the notional dividend could only accrue to the particular child "by virtue or in consequence of" the settlement. 20

p.96 1.49 Forbes J.A. said that he would have ordered that the appeal should be dismissed with costs.

p.97 11.4-9 O'Connor P. and MacDuff J. concurred.

pp.98-100 8. By an Order dated the 19th June 1958, the Court of Appeal for Eastern Africa granted conditional leave to the Appellant to appeal to Her Majesty in Council from the Judgment and Order of that Court and by further Order dated the 27th August 1958, granted final leave to appeal. 30

pp.100-101 9. The Respondent does not seek to rely on that part of the reasoning of Lowe J. which was disapproved by the Court of Appeal.

10. The Respondent humbly submits that the Appeal be dismissed and the Judgment of the Court of Appeal for Eastern Africa be upheld and affirmed for the following among other

R E A S O N S

(1) BECAUSE upon the true construction of subsection (1) of section 22 of the 1952 Act the effect of an order made by the Respondent under that subsection is that sixty per cent of the income of the company concerned is deemed for the purposes of the Act to have been distributed as dividends 40

to the shareholders in proportion to their shareholdings.

- (2) BECAUSE income so deemed to have been distributed as dividends is deemed for the purposes of the Act to have been paid to the shareholders.
- 10 (3) BECAUSE the purposes of the Act include the purposes of section 24 thereof so that income of a company which is deemed by virtue of Section 22 to have been distributed to a child of a settlor should be taken for the purposes of Section 24 to have been paid to that child.
- (4) BECAUSE income which must be taken to have been paid to a child of the settlor in the circumstances of this case was so paid to the child by virtue and in consequence of the settlement admittedly made by the Appellant and not otherwise.
- 20 (5) BECAUSE the reasoning of Lowe J. was right except insofar as concerns his construction and application to this case of paragraph (a) of subsection (2) of Section 24.
- (6) BECAUSE the Judgment and Order of the Court of Appeal were right.

F.N. BUCHER

RODERICK WATSON

No. 27 of 1958

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C A S E FOR THE RESPONDENT

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