PC
GGL 6.2

Judgment 3/1964

IN THE PRIVY COUNCIL No. 32 of 1962

ON APPEAL

FROM THE FEDERAL SUPREME COURT OF THE FEDERATION OF RHODESIA AND NYASALAND

78519

B E T W E E N THE COMMISSIONER OF TAXES .. Appellant

- and -

NCHANGA CONSOLIDATED COPPER MINES LIMITED Respondent

CASE FOR THE RESPONDENT

Record

1. This is an appeal from a judgment of the Federal Supreme Court of the Federation of Rhodesia and Nyasaland (Sir John Clayden, C.J., Sir Francis Briggs, F.J., and Quenet, F.J.) delivered on the 7th day of November 1961 allowing an appeal by the Respondent from a judgment of the High Court of Southern Rhodesia (Young,J.) dated the 9th day of May 1961 whereby an appeal by the Respondent against the disallowance by the Commissioner of Taxes of an objection to an income tax assessment made upon it was dismissed. pp.159-189 pp.143-155 pp. 4 & 5

2. The matter arises upon an assessment to income tax made upon the Respondent for the year ending 31st March 1959. The issue is whether a sum of £1,384,569 paid in the circumstances hereinafter described by the Respondent to Bancroft Mines Limited was deductible in determining the pp. 1 & 2

Record

taxable income of the Respondent for the year ending 31st March 1959. The contention of the Commissioner, which was rejected in the Federal Supreme Court, is that it was not deductible because it was expenditure of a capital nature. The contention of the Respondent is that it was not expenditure of a capital nature and was properly deductible under the relevant statutory provision.

3. The relevant statutory provision is contained in Section 13 of the Income Tax Act 1954 of the Federation of Rhodesia and Nyasaland :-

No.16 of 1954

> "13 (1) For the purpose of determining the "taxable income of any person, there shall "be deducted from the income of such person "the amounts set out in this section.
>
> "(2) The deductions allowed shall be -
>
> "(a) Expenditure and losses (not being expenditure and losses of a capital nature) wholly and exclusively incurred by the taxpayer for the purposes of his trade or in the production of the income."

4. The facts of the case as found by Mr.Justice Young appear in his judgment and are set out in the judgments delivered in the Federal Supreme Court. Certain inferences drawn from the evidence by Mr. Justice Young are in issue as being unsupported by, or contrary to, the evidence but the primary facts of the case are not in dispute and may be summarised as follows :-

pp.143-155

(a) The Respondent was one of three copper

mining companies in Northern Rhodesia which together formed what was called the Anglo-American Group. The other two companies were Bancroft Mines Limited (hereinafter called Bancroft) and Rhokana Corporation Limited (hereinafter called Rhokana). The three companies were independent companies but had overlapping directorates and each used the Anglo-American Corporation of South Africa Limited as secretary and technical adviser. Mr. Acutt, the sole witness in the case, was at the material time joint deputy chairman of the Anglo-American Corporation of South Africa Limited and was deputy chairman of each of the three mining companies. The production from all three companies was marketed by a common sales department through the British Metal Corporation, which entered into forward sales commitments on the basis of production estimates supplied by each of the mining companies. The price of the copper was not fixed by these commitments but was dependent on the market price when the copper was sold. Each company was responsible for the fulfilment of its own commitments.

(b) The Respondent and Rhokana had old established and prosperous mines with relatively low production costs and high profits but

Record

Bancroft at the beginning of 1958 was still a comparatively new mine which had not yet been established on a paying basis. There were special problems connected with the development at the Bancroft mine and production was relatively small and production costs high.

(c) The estimated production of the three companies for the year 1958 was 270,000 tons of which the Respondent's share was 140,000 tons, Rhokana's 90,000 and Bancroft's 40,000. At the material time some 240,000 tons of this estimated production had been committed to forward sales contracts. In 1957 the world supply of copper had outstripped demand and the price of copper on the world market was falling sharply, so that from a peak price of £436.10s. per long ton in March 1956 it had fallen to £176. 5s. per long ton in December 1957. Most of the major world producers of copper had cut production during 1957 with the object of improving the price although there was no binding agreement between them to do so.

(d) By the end of 1957 the Anglo-American Group were the only very large scale producers who had not made a cut. It was regarded as essential by the directorates that the companies in the Group should make a cut and it was agreed in principle that they should make a cut of 10% for

one year. In January 1958 a joint discussion took place in Salisbury as to how this cut should be applied. The 10% cut involved the reduction of Group production from the estimated figure of 270,000 tons to 243,000. Bancroft's 10% share of this reduction would have been 4,000 tons which would have meant a loss of some £650,000 revenue and Bancroft owing to its special difficulties could not accept that loss. The suggestion that the Respondent and Rhokana should relieve Bancroft by together bearing the burden of the whole group reduction was rejected because it was not justified from their points of view. The solution to the problem which was finally chosen as being in the best interests of all three companies was for Bancroft to go out of production altogether for the year commencing March 1958 and for the Respondent and Rhokana to undertake the whole of the Group's reduced production target of 243,000 tons. This would mean not only that they would avoid a cut in production but that they would have to produce an extra 13,000 tons of which the Respondent was to take up 9,000 tons. The Respondent and Rhokana were to pay Bancroft a sum which would enable it to meet its interest charges and provide for development work so that the mine would be ready to produce at its full rated

Record

capacity when it came back into production at the end of the year. This sum was agreed at £2,165,000 of which the Respondent's share was to be £1,384,569 calculated on the proportionate production tonnage taken up by the Respondent and Rhokana. The loss of profit which the Respondent would have sustained from a straight 10% cut and the loss, or benefit, under the proposed arrangement were both dependent on the world price of copper but it was calculated that the Respondent would do better under the arrangement than under a straight 10% cut, unless the price of copper fell below £130 per long ton, and this was not expected, and would benefit by about £600,000 if the price of copper stayed where it was. These calculations are shown on the Graph which was Exhibit 13 before

p. 194(a) the High Court and is set out in the Record. This arrangement was accepted by all three companies and was embodied in an exchange of letters. The letter of offer written by the Respondent to Bancroft dated 27th January 1958

pp.196-198 is set out in full in the Record at pages 196 - 198 and the letter of acceptance from Bancroft to the Respondent is set out in full in the

p. 199 Record at page 199.

(e) In pursuance of this agreement the Respondent paid Bancroft the sum of £1,384,569

Record

in the year ending 31st March 1959. This payment appears in the Respondent's accounts for the year ended 31st March 1959 as revenue expenditure. These accounts are set out in the Record at pages 201 and 202. pp.201 & 202

(f) The Respondent in its tax returns for the year ended 31st March 1959 treated the payment as an allowable deduction under the provisions of Section 13(2) of the Income Tax Act 1954. No.16 of 1954

5. The Commissioner of Taxes in an assessment dated 25th January 1960 excluded the said payment from the computation of the Respondent's taxable income. The Respondent objected to this exclusion but the Commissioner of Taxes disallowed this objection by a letter dated 25th February 1960. By a letter dated 7th March 1960 the Respondent gave notice of appeal to the High Court of Southern Rhodesia against the decision of the Commissioner of Taxes. The Respondent's case (as Appellant in the High Court) is set out in the Record. The Respondent contended that the said payment was a deduction allowed under Section 13 of the Income Tax Act 1954. The Commissioner of Taxes contended in his case that the said payment was not a deduction allowed under Section 13 because

pp.1 & 2
pp.3 & 4
pp.4 & 5
pp.5 & 6
pp. 6-8
No.16 of 1954
pp. 9-10

Record

either it was not an expense wholly and exclusively incurred by the Respondent for the purposes of its trade or in the production of the income since it was made for the purposes of Bancroft's trade or alternatively it was expenditure of a capital nature.

6. (a) The appeal was heard in the High Court of Southern Rhodesia before Mr. Justice Young on

pp.143-155 10th and 11th April 1961 and on 9th May 1961 he gave judgment in favour of the Commissioner on

p. 155 the ground that the Respondent had failed to discharge the onus of showing that the expenditure was not of a capital nature.

p. 143 (b) At the beginning of his judgment Mr.Justice Young said that Mr. Acutt, the only witness who had given evidence at the hearing, had been entirely objective and helpful.

(c) Mr Justice Young rejected the first con-

pp.147 & 148 tention of the Commissioner, that the payment to Bancroft was not deductible because it had been made to assist Bancroft. He held that on the evidence the arrangement was in the interests of the Respondent qua trader and qualified as expenditure wholly and exclusively incurred by it for the purposes of its trade. This contention, having been rejected by Mr. Justice Young, was not pursued by the Commissioner of Taxes, either before the Federal Supreme Court

or in his Petition to the Privy Council, and is not now relevant to this appeal.

(d) Mr. Justice Young then considered the question whether the expenditure was not of a capital nature. He posed the test that expenditure was of a capital nature if the intention was to create, add to or improve the present investment position designed to produce income in the more or less distant future. That basic idea appeared to be implicit in most of the leading decisions. He referred to Viscount Cave's dictum in British Insulated & Helsby Cables Ltd. v. Atherton :- p. 148 (1926) A.C. 205 at p.213 10 Tax Cas. 155 at p.192

> "But where an expenditure is made, "not only once for all, but with a view "to bringing into existence an asset or "an advantage for the enduring benefit "of a trade, I think that there is very "good reason (in the absence of special "circumstances leading to an opposite "conclusion) for treating such an expenditure as properly attributable not to "revenue but to capital."

(e) Within the limits of the principle the question where to draw the line between capital and revenue payments was one of secondary fact. The Commissioner had contended that two benefits to the Respondent's trade were sufficiently enduring to qualify as capital outlay, first the avoidance of dislocation of trade which would have resulted from an application of the 10% cut to the Respondent's production pp.148 & 149 p. 149

Record

and, second, the elimination of a competitor and the capture of an increased share of the market. Mr. Justice Young pointed out that the agreement did not last more than 12 months and that in April 1959 Bancroft resumed production with a capacity of 50,000 tons as compared with its capacity of less than 40,000 in 1957. The 10% cut in the group production was removed in the middle of 1958 and it had always been recognised that output restriction was not a long term solution to the problem and that the cuts would be removed in due course. But Mr. Acutt, while he had been of the opinion that the arrangement with Bancroft had had no enduring effect on the Respondent had agreed that the application of the cut to the Respondent would have meant something

p. 150 of an upheaval. Mr. Justice Young then referred

p. 151
23 Tax Cas. 71 to three more cases which in his opinion supported the principle he had formulated. He said that the case of United Steel Companies Ltd. v. Cullington showed that the advantage did not have to last for an indefinite period to indicate capital expenditure. He then referred to a

61 C.L.R. 337 at p.362 passage from Dixon J. in Sun Newspapers Ltd. v. Federal Commissioner of Taxation which said that recurrence and endurance were not conclusive factors but both were a matter of degree in the

pp.153 & 154 circumstances of the particular case. The

facts of the present case revealed the following features: (1) The Respondent had treated the expenditure as being on revenue account and (2) the payment had been made out of circulating capital and not out of, nor in connection with, fixed capital. Both those features were in the Respondent's favour but were not conclusive and their value was limited. (3) The expenditure was of a very large sum and apparently quite unique. It was incurred with the object of turning what promised to be a substantial set back (the 10% cut) into a positive advantage. Not only would any dislocation of the Respondent's business organisation be avoided but the development promised to be favourable to the Respondent. (4) The transaction temporarily eliminated a competitor from the market but it was realised that Bancroft would come back into the market stronger than before. (5) The expenditure was not recurrent except in the sense that cuts in copper production were likely to recur and that a comparable situation might theoretically arise.

(f) Mr. Justice Young concluded his judgment with the following paragraph :- pp.154 & 155

> "Weighing together these features
> "in the light of the authorities, I have
> "come to the conclusion that, on the
> "evidence, it is a possible and a proper
> "inference that, to borrow the words of

Record

61 C.L.R.337

"Dixon J. in the Sun Newspapers case at "page 364:

> "'In principle the transaction must be "'regarded as strengthening and pre- "'serving the business organisation or "'entity, the profit yielding subject, "'and affecting the capital structure'
>
> "of Nchanga. The chief object was to "preserve from impairment and dislocation "Nchanga's organisation. The probabilities "are that the advantages of this to "Nchanga's business were lasting, or, at "any rate, sufficiently lasting to qualify "as an 'enduring' advantage within the "meaning of Viscount Cave's dictum. If "that inference has not been displaced "(and I think it has not), my conclusion "must be that Nchanga have failed to dis- "charge the onus of showing that this "expenditure was not of a capital nature. "On this aspect of the case my decision is "for the Commissioner.
>
> "That means that the appeal fails and "is dismissed."

pp.156-158 7. The Respondent by notice of appeal dated the 7th June 1961 appealed from the said judgment of Mr. Justice Young to the Federal Supreme Court. The said appeal came on for hearing on 16th and 17th October 1961 and on 7th November 1961 the Federal Supreme Court

pp.159-189 (Sir John Clayden C.J., Sir Francis Briggs, F.J., and Quenet, F.J.) gave judgment unanimously allowing the appeal and ordering the Commissioner of Taxes to amend the assessment by allowing the deduction in question.

8. (a) The leading judgment in the Federal Supreme Court was delivered by Sir John Clayden

pp.159-173 C.J. He decided that a question of law was

involved in the appeal and not merely a question of fact and that it was therefore open to the Court to reconsider the case. There were, he said, many difficulties in the concluding paragraph of Mr. Justice Young's judgment. The way in which the paragraph was stated showed that the approach was that a taxpayer who did not displace a proper inference, although it might not be the probable one, could not succeed. He thought that this misdirection had coloured the whole approach. The finding as to the "chief object" was at variance with the finding in the previous paragraph (feature (3)) and was also not at all supported by the evidence. He thought that Mr. Justice Young had misunderstood not the law as to what was capital expenditure but the law as to how it could be proved that expenditure was not of a capital nature. Furthermore the Commissioner of Taxes had not argued that a question of law was not involved.

pp.161-163

(b) Before considering the case generally Sir John Clayden dealt with two matters, the finding of the "chief object" and the forward sales contracts. He said that the only possible basis for the finding that "the chief object was to preserve from impairment and dislocation Nchanga's organisation" lay in a

pp.163-166

chance remark by Mr. Acutt when he was being cross-examined in regard to Bancroft. It had never been suggested on the papers or in the cross-examination that the proposed cut in production would have impaired or dislocated the Respondent's organisation. If the finding of dislocation referred to the dismissal of employees, and it was in that context that Mr. Acutt's remark had been made, there was no evidence that it would have affected the mine organisation at all. If the finding referred to any other dislocation it was contrary to the evidence which was that there was great flexibility in the Respondent's mine and that the 10% cut in the Respondent's production would have had very little effect except in regard to operating costs. The avoidance of increased cost of production was bound up with the purpose of making a profit and was not the avoidance of any dislocation. He considered that there was no evidence on which to base the finding that the chief object was to preserve from impairment and dislocation Nchanga's organisation. The evidence was that there would not have been any dislocation of Nchanga's business organisation. The matter of the forward contracts had been made much of but he did not consider that any inference should be drawn that a tonnage

A B C

committed for sale had any special value. No price had been fixed in the forward sales and the Respondent had not acquired by its payment the benefit of any contract at a fixed price. There was nothing to show that there would have been any difficulty in selling at market prices tonnage not committed for sale.

(c) Sir John Clayden considered next the meaning of expenditure of a capital nature in Section 13. He said that the English and Australian cases on capital expenditure were obviously applicable although they dealt with statutes where the words were not in exactly the same form. In South Africa the wording was the same and in New State Areas Ltd. v. Commissioner for Inland Revenue Watermeyer C.J. had said that the problem was usually whether 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 had said that the conclusion to be drawn from the English cases was that the true nature of each transaction must be enquired into to determine whether the expenditure attached to it was capital or revenue. The test which had been formulated by Viscount Cave in Atherton's

pp.166-169

1946 A.D. 610

(1926) A.C. 205. 10 Tax Cas.155

Record

case had great authority but was by its terms of limited application. It applied only when there was a payment "once and for all". He thought that initially a general test should be applied in preference to the Atherton test which could always be applied later if the general test did not indicate a result. In the present case the circumstances were very special and the payment, thought quite unusual, was associated with the normal operations of the taxpayer and he therefore would first try to determine whether according to the true nature of the expenditure it was made as part of the cost of performing the income earning operations or as part of the cost of the income earning machine or structure.

pp.169-170 (d) In his view the Respondent had spent the money to get the right for one year to produce more of its own copper than it would otherwise have been entitled to produce, but the Respondent's income earning structure was not added to by what the Respondent spent. The expenditure was not made as part of the cost of the income earning structure. The expenditure was part of the cost of the income earning operations. It reduced the cost per ton of the whole of the

pp.170-171 production. It enabled the Respondent to avoid a cut in production, with its resultant increase in the cost of its product, and indeed to

increase its production.

(e) The Commissioner had made a submission that since the payment in Bancroft's hands was a capital receipt it was a capital payment by the Respondent but, assuming that it was a capital receipt by Bancroft, that fact had no real bearing on the Respondent's liability. The Commissioner had also submitted that the payment was made to buy out a competitor but in the view of Sir John Clayden these mines were not in competition with each other and except in so far as they were forced to cut production to keep up the world price of copper they were selling all the copper that they could produce. Moreover the effect of the payment was to get Bancroft out of its difficulties so that at the end of the year it could be a strong competitor. He considered that there was no evidence on which the finding of Mr. Justice Young that the transaction temporarily elimated a competitor could be based. pp.171-172

(f) Approaching the case on the general test Sir John Clayden considered that the Respondent had proved that on the balance of probabilities the payment was not of a capital nature. He did not think that the test in Atherton's case applied because there were special circumstances within the terms of the test but pp.172-173 (1926) A.C. 205.10 Tax Cas.155

Record

assuming that it did apply he did not think that it showed that the expenditure was capital. The payment had been made "once and for all" and there had been an advantage to the Respondent in being able to produce more than it could otherwise have done but he did not think that the advantage could be regarded as one of "enduring benefit" for the Respondent's trade. Mr. Justice Young's finding on this point had been based on the advantage being the avoidance of dislocation of the Respondent's organisation. That must now be left aside and the only advantage was therefore limited to a year, for the closing down of Bancroft and the agreed cut in production came to an end then. The restoration of the Respondent to its former position came not as a result of the payment but because the cut had ceased. It had been a temporary arrangement to meet a temporary position and he considered that the test from Atherton's case would not show the payment to be capital. He would therefore allow the appeal.

(1926) A.C. 205. 10 Tax Cas. 155

pp.173-188

9. Sir Francis Briggs, F.J. concurred. He said that Mr. Justice Young had directed himself correctly as to the distinction between capital and revenue payments. He criticised the concluding paragraph of Mr. Justice Young's

p. 177

p. 179

judgment and said that the question was not what inference could be drawn but what inference should be drawn as being most fully in accord with the evidence and probabilities taking into account that the onus lay on the taxpayer to establish his facts on the balance of probabilities. He did not think that it could be said in strictness that there was no evidence to support the learned judge's findings for it must be accepted that a 10% cut in production would probably have resulted in some slight degree of impairment and dislocation of the Respondent's organisation and the avoidance of this was an advantage which was to some extent lasting, but the Supreme Court was entitled to reverse the judge if the true and only reasonable conclusion on the evidence was the opposite of that found. The judge had given reasons for his finding and had made a finding on the credibility of Mr. Acutt. Sir Francis Briggs agreed with the Chief Justice that the reference to an "upheaval" was directed solely to the position of the staff. There was evidence that the Respondent's organisation would not have been materially impaired or dislocated by a temporary cut in production. In his view the evidence accepted as true and candid contradicted the judge's findings in every respect

p.180

p.186

Record

for it was clear on the evidence that the Respondent's directors were not in the least concerned with strengthening or preserving the business organisation as a whole: their object was to avoid a large temporary loss of revenue and if possible to enhance profits over the same short period. In his view the judgment was self-contradictory and on the finding as to the credibility of Mr. Acutt there could be only one true and reasonable conclusion, that the payment was a revenue transaction. He agreed with the reasons given by the Chief Justice for adopting this view and would allow the appeal.

pp.187-188

pp.188 & 189

10. Mr. Justice Quenet also concurred. In his view the words "it is a possible and a proper inference" used by Mr. Justice Young in his concluding paragraph must be understood to mean "a possible and the proper inference", but with this exception he agreed with the conclusions of the Chief Justice and Sir Francis Briggs.

11. The Commissioner of Taxes petitioned Her Majesty in Council for special leave to appeal from the judgment of the Federal Supreme Court and an order granting special leave to appeal was made on 27th June 1962.

pp.190-192

12. The Respondent humbly submits that the

decision of the Federal Supreme Court is right and should be affirmed and that this appeal should be dismissed with costs for the following amongst other

R E A S O N S

(1) BECAUSE the payment to Bancroft was expenditure (not being expenditure of a capital nature) wholly and exclusively incurred by the Respondent for the purposes of its trade or in the production of the income and was therefore under the provisions of Section 13 (2) (a) of the Income Tax Act 1954 a proper deduction in the determination of the Respondent's taxable income. No.16 of 1954

(2) BECAUSE Mr. Justice Young's finding that the payment was expenditure of a capital nature was wrong in law and contrary to the evidence; the only true and reasonable conclusion which could be drawn from the evidence was that the payment was not expenditure of a capital nature.

(3) BECAUSE there was no evidence to support Mr. Justice Young's finding that the chief object of the transaction was to preserve from impairment

and dislocation the Respondent's organisation or his finding that the payment temporarily eliminated a competitor. A

(4) BECAUSE the payment was not made with a view to procuring an advantage for the enduring benefit of the Respondent's trade. B

(5) BECAUSE the Federal Supreme Court were right in holding that the payment was made by the Respondent as part of the cost of performing its income earning operations and was not expenditure of a capital nature. C D

(6) BECAUSE, the purpose of the arrangement being to cut the aggregate production of the three mines in the group by 10% in an attempt to arrest the fall in the price of copper, the payment was made in order that while that purpose was achieved the Respondent might not only avoid any cut in its own production but even increase it slightly. E

(7) BECAUSE the payment was not made for a right to produce or sell copper but was paid as part of an arrangement between the three companies in the

group made in their mutual interest for the purpose of achieving a voluntary cut in production and the sum paid by the Respondent to Bancroft represented the Respondent's share of the group's revenue loss caused by the cut and was itself expenditure on revenue account.

(8) BECAUSE the decision of the Federal Supreme Court was right.

HEYWORTH TALBOT
F.N. BUCHER
J.HOLROYD PEARCE

No.32 of 1962

IN THE PRIVY COUNCIL

ON APPEAL

FROM THE FEDERAL SUPREME COURT OF THE FEDERATION OF RHODESIA AND NYASALAND

BETWEEN

THE COMMISSIONER OF TAXES
Appellant

- and -

NCHANGA CONSOLIDATED COPPER MINES LIMITED
Respondent

CASE FOR THE RESPONDENT

LINKLATERS & PAINES,
Barrington House,
59/67 Gresham Street,
London, E.C.2.
Solicitors for the Respondent.