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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

B E T W E E N :-

THE COMMISSIONER OF TAXES
(Respondent) Appellant

- and -

NCHANGA CONSOLIDATED COPPER MINES LIMITED
(Appellant) Respondent

C A S E FOR THE APPELLANT

Record

1. This is an appeal by special leave 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 May, 1961, whereby an appeal by the Respondent against the disallowance of its objection to an income tax assessment made upon it for the year ending 31st March, 1959 was dismissed. pp.159 et seq. pp.143 et seq. pp. 3,4.

2. The Assessment under appeal was made in respect of the Respondent's income from copper mining and the question at issue is whether, as contended by the Respondent and as held by the said Federal Supreme Court, a sum of £1,384,569 paid in the circumstances hereinafter described by the Respondent to Bancroft Mines Limited (hereinafter called "Bancroft") falls to be included as an expenditure on

revenue account in the computation of the said income, or whether, as contended by the Appellant, the said sum falls to be excluded from such computation as being an expenditure on capital account.

3. Section 13 of the Income Tax Act, 1954, of the said Federation, so far as relevant to the said issue, provided at all material times as follows :-

"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 tax- "payer for the purposes of his trade or in "the production of the income;"

pp.159 et seq.

4. The facts of the case are set out in the judgments delivered in the Federal Supreme Court and may be summarised as follows :-

(i) In Northern Rhodesia there are three copper mining companies in what is called the Anglo-American Group, namely Rhokana Corporation Limited (hereinafter called "Rhokana"), the Respondent, and Bancroft, these being independent companies but with overlapping directorates and with the Anglo-American Corporation of South Africa Limited acting as secretary, and providing technical advice, for each company. In 1958 Rhokana and the Respondent were old established mines but Bancroft was a mine in the process of development and experiencing difficulties in regard to both mining operations and finance.

(ii) In 1957, the price of copper having fallen, most of the major world producers voluntarily cut their production with the object of raising the world price. It was regarded as essential that the mines in the Anglo-American Group should adopt the same policy and, in order to discuss how this could be done, a meeting was held at Salisbury in January, 1958. At that time the estimated production of copper of the three mines for

1958 was 270,000 tons of which Rhokana and the Respondent were expected to produce 230,000 tons, and Bancroft 40,000 tons, and it was calculated that a 10% cut, which was regarded as essential, would reduce this production to 243,000 tons, being 207,000 tons for Rhokana and the Respondent, and 36,000 tons for Bancroft. As a result of the discussion it was considered that the best interests of each mine would be served if Bancroft were to cease production for a year in return for a money payment by the other two mines, and the other two mines were to produce the 36,000 tons which Bancroft would otherwise have produced, and in pursuance of this scheme a letter dated 27th January, 1958 was written by the Respondent to Bancroft containing the following offer :- p.196

> "In consideration of your ceasing production for one year on the basis set out in this letter, Rhokana and ourselves jointly undertake the payment to your Company of a total sum of £2.165 m. during the year that your company will not have been in production. The payments will be made monthly, the first being on or about 31st March, 1958. The proportions payable by Rhokana and ourselves will be a matter for settlement between the two Companies."

This offer, which was separately confirmed by Rhokana, was accepted by Bancroft. p.199.

(iii) As a result of the above arrangement the combined production of Rhokana and the Respondent for their financial year 1958 was 243,000 tons, being 13,000 tons in excess of their estimated combined production of 230,000 before the cut, and such excess was divided between Rhokana and the Respondent in the proportion of 4 to 9, with the result that the Respondent was enabled, while the Group made a cut of 10%, to produce 9,000 tons in excess of its estimated production without a cut. It was agreed between Rhokana and the Respondent that, having regard to their respective shares of the 36,000 tons of production made available by Bancroft, the Respondent should contribute £1,384,569 to the total payment to be made

as aforesaid to Bancroft and the Respondent paid to Bancroft the said sum of £1,384,569 in the year ending 31st March, 1959.

5. The said payment made by the Respondent having been excluded from the computation of the
p.3 Respondent's income in the aforesaid assessment, the Respondent objected to such exclusion and,
p.4 the said objection having been disallowed by the
p.5 Appellant, appealed to the High Court of Southern Rhodesia. In such appeal it was contended for the Appellant, firstly, that the said expenditure was not wholly and exclusively incurred by the Respondent for the purpose of its trade or in the production of its income, and, secondly, that the said expenditure was of a capital nature, but the said first contention was rejected by the High Court and has not been further pursued by the Appellant.

6. On the hearing of the said appeal, which came before Mr. Justice Young on the 10th and 11th April and 9th May, 1961, the only witness called was Mr. K.C. Acutt who was at all material times joint deputy chairman, and resident director in the Federation, of the Anglo-American Corporation of South Africa Limited, and deputy chairman of each of the three mining companies;
pp. 10-33 who in his evidence in chief for the Respondent testified to the matters summarized in paragraph
p.196 5 above, and produced the aforesaid letter dated 27th January, 1958; and who was described
p. 143, l.16 by Mr. Justice Young as being "entirely
pp. 33-136 objective and helpful". The cross-examination of Mr. Acutt on behalf of the Appellant was largely directed to the first contention above-mentioned but his evidence included the following passages :-

Evidence in Chief :-

p.15, l.44 Q. "At this meeting, what view was taken of the consequences of a cut in the production of the three mines?"

A. "It was clear that a cut would have serious consequences to Rhokana, Nchanga and Bancroft."

p.32, l.39 Q. " --- Could this agreement have been of any enduring benefit?"

A. "I don't think so. The agreement was to

operate for a period of one year only and it was to attempt to rectify the temporary excessive supply over demand at the time, which was one of the causes of the decline in prices. It was a short term problem which was aimed, as far as Nchanga was concerned -- at maintaining and if possible increasing Nchanga's profits during the period of one year, during which the agreement was to operate."

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Cross-examination :-

Q. "For the privilege of producing these additional 9,000 tons and also in order to cut its own production, Nchanga was prepared to pay £1,384,000 to Bancroft and the balance of £780,000 odd Rhokana would be similarly prepared to pay to Bancroft?" p.112, l.10

A. "In order not to cut its production."

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20 Q. "---Whatever made you think of it?" p.116, l.12

A. "Well, the Consulting Engineers pointed out that from Nchanga's point of view it was worth while them doing this business, merely from a pure financial gain point of view rather than cut."

Q. "It was quite revolutionary from the point of view of the Bancroft community to close down that mine?" p.117, l.1

30 A. "Yes, my Lord. Going to another point, if I may, exactly the same point would occur if either of the other two mines reduced. You would have had an upheaval at three mines, because it would have been necessary for them probably to reduce their staff."

Q. "--- You then said there were figures to show that it would be inadvisable for Nchanga and Rhokana to cut?" p.117, l.24

Record

A. "That if they cut clearly there was going to be hardship on certain members of their staff as well, and the whole cost of their staff as well, and the whole cost of their production is increased by the lowered production. --- The discussion was how best to achieve an overall reduction in the tonnage of copper --- and it led, I think, to a very understandable point being made by the Consulting Engineers that quite clearly if Bancroft, which was the highest cost producer, went out altogether there were immense gains for Rhokana and Nchanga possible if they took up the additional tonnage ---."

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p.124, l.23. Q. "And the other suggestions were that if you save us the trouble of cutting our production and give us the chance to produce an additional amount of copper, we shall give you an additional amount of money that you require for development?"

A. "Because it is profitable for us to do so."

pp.143-155 7. In his judgment Mr. Justice Young said that he could find no sufficient basis for the suggested conclusion that the transaction was
p.148, l.1 substantially a subsidy to Bancroft to enable them to put their house in order, and accordingly he was against the Appellant on the first contention above mentioned. He had found the
p.148, l.6 second question more difficult but in his
p.153, l.5 view the facts of the case disclosed the following features.

(1) and (2) The Respondent in fact treated the expenditure as on revenue account and it was paid out of circulating capital. These
pp.153-4. circumstances favoured the Respondent's case but in the view of Mr. Justice Young their value was limited having regard to certain observations made by Lord Greene in Associated Portland Cement Ltd. v. I.R.C., 1946 1 A.E.R. 70-71.

p.154, l.31 (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 organization be avoided but the development promised to be favourable to the Respondent.

(4) The transaction temporarily eliminated a competitor from the market though it was realized that Bancroft would come back into the market stronger than before. p.154, l.38

(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. p.154, l.43

Weighing together these features in the light of the authorities Mr. Justice Young came to the conclusion that on the evidence it was a possible and a proper inference that the transaction in question (in the words used by Owen Dixon, J. in Sun Newspapers Ltd. -v- Federal Commissioner of Taxation, 61 C.L.R. at p.364) "must be regarded as strengthening and preserving the business organization or entity, the profit yielding subject, and affecting the capital structure" of the Respondent. The chief object was to preserve the Respondent's organization from impairment or dislocation. The probabilities were that the advantages to the Respondent's business were lasting, or at any rate sufficiently lasting to qualify as an "enduring" advantage within the meaning of Lord Cave's statement in Atherton's case, 1926 A.C. at p.213. If the above inference has not been displaced, as Mr. Justice Young thought that it had not, his conclusion must be that the Respondent had failed to discharge the onus of showing that the expenditure was not of a capital nature. p.154, l.50 p.155, l.6 p.155, l.12

8. The Respondent having appealed from the said judgment of Mr. Justice Young to the Federal Supreme Court the said appeal came on for hearing on the 16th and 17th October, and 7th November, 1961, and on 7th November 1961 the Supreme Court gave judgment allowing the appeal and ordering the Appellant to amend the assessment by allowing the deduction in question. p.156 pp.159 et seq. pp.189-190

9. The leading judgment in the Supreme Court was delivered by Sir John Clayden, C.J., who said that there were many difficulties in the last paragraph (introduced in the foregoing pp.159-173 p.162,l.28

summary by the words "Weighing together - ") of the judgment of Mr. Justice Young. There was a finding of fact as to the "chief object" which was not only at variance with the finding (3) in the preceding paragraph but was also unsupported by the evidence, and the way in which the conclusion was reached indicated that the approach made was on the basis that a taxpayer who did not displace a proper inference, which might not be the probable one, could not succeed. The only possible basis for the finding as to the "chief object" lay in a chance remark made by Mr. Acutt. If the finding, when it referred to impairment and dislocation, was directed to the dismissal of employees (and no other "dislocation" could be found suggested in the case) the witness's answers did not show that this would have affected the mine organization at all. Mr. Acutt's reference to "upheaval" appeared to relate to the mining communities, and if the finding referred to any other impairment or dislocation (apart from increased cost of production) the evidence was quite contrary to it for Mr. Acutt had said that at the Respondent's mine great flexibility was possible both in plant and mining operations. In so far as the avoidance of increased cost of production was a purpose of the payment, as of course it was, this was bound up with the purpose of making a profit and not the avoidance of any dislocation.

p.163, l.49

p.164, l.28

p.164, l.41

p.165, l.3

10. In a case, such as this, where the circumstances were very special and the payment, though quite unusual, was associated, whether as a capital or non-capital payment, with the normal operations of the taxpayer, Sir John Clayden thought it proper to try first 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. In his view the Respondent 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 he did not see that this added anything to the Respondent's income-earning structure. On the contrary it seemed to him that what had happened was that a producer, faced with an increase in the cost of his product because of a cut in production, had found a way to increase

p.169, l.20

p.169, l.39

p.170, l.36

his production and so keep his cost down, and such a management of his affairs was, in the view of Sir John Clayden, part of the cost of income earning operations.

11. It had been submitted for the Appellant that the payment was in effect made to buy out a competitor but in the view of Sir John Clayden these mines were not in competition with each other, for, except in so far as they were forced to cut production in order to keep up the world price of copper, they were selling all that they could produce. Finally, if the test to be applied was that propounded by Lord Cave in Atherton's case, the payment here in question had been made once and for all but if the avoidance of dislocation was put aside, as Sir John Clayden thought it must be, the only advantage to the Respondent was that of being able to produce, during one year, more than it could otherwise have done, and this could not be regarded as an "enduring benefit". p.171, l.16 p.172, l.20

12. Sir Francis Briggs concurred. 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 Nchanga's organization" and that the avoidance of this was an advantage which was to some extent lasting, but the Supreme Court was entitled to reverse the learned judge if the true and only reasonable conclusion on the evidence was the opposite of that found. The cross-examination of Mr. Acutt had been almost exclusively directed to the Appellant's first contention and Sir Francis Briggs agreed with the Chief Justice that the reference to an "upheaval" was directed solely to the position of the staff. In his view the evidence, accepted as true and candid, in effect contradicted the judge's findings in every respect for it was clear on the evidence that the Respondent's directors were not in the least concerned with strengthening or preserving the business organization 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. On the finding as to credibility of Mr. Acutt pp.173-188 p.180, l.23 p.184, l.1 p.186, l.12 p.186, l.31

there could, in the view of Sir Francis Briggs, be only one true and reasonable conclusion, that the payment was a revenue transaction.

pp.188-9. 13. Mr. Justice Quenet also concurred. In his view the words "it is a possible and a proper inference" used by Mr. Justice Young 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.

14. Since the said Judgments were delivered the House of Lords has held in Rolls-Royce Ltd. -v- Jeffrey (Inspector of Taxes) 1962 1 W.L.R. 425, that the question whether a payment is made for income tax purposes on capital or on revenue account is a question of law as to the proper conclusion to be drawn from the primary facts. For the Reasons given below the Appellant will contend that as a matter of law the proper conclusion on the facts of the present case is that the payment in question was made on capital account. With regard to the primary facts and the inferences therefrom the Appellant also submits the following respectful criticisms of the said judgments.

(i) That the Supreme Court paid too much regard to the cross-examination of Mr. Acutt and too little to the question whether upon the
p.196 documents, including the said letter dated 27th January, 1958, and the evidence as a whole, the proper conclusion was that the said payment was made on capital account.

(ii) That the Supreme Court, and individual members thereof, were in error in the following conclusions:-

(a) Sir John Clayden, in holding that Bancroft and the Respondent were not in
p.171, l.30 competition and that the payment in question could not therefore have been made with the object of temporarily eliminating a competitor.

p.164, l.41
p.186, l.11 (b) The Court, in the view that Mr. Acutt's reference to an "upheaval" was directed solely to the position of the employees and not at all to the effect upon the Respondent's organisation.

(c) Sir Francis Briggs, in the view that Mr. Justice Young, because he referred to Mr. Acutt as "entirely objective and helpful", had thereby committed himself to accepting the accuracy of everything that Mr. Acutt said. p.177, 1.12 p.187, 1.39

(d) Sir John Clayden, in the view that, because the expenditure had the effect of reducing the cost per ton of the Respondent's production, it was thereby stamped with the character of a payment on revenue account. p.170, 1.36

(e) Sir Francis Briggs, in the view that the expenditure was so stamped if "its object was to avoid a large temporary loss of revenue and if possible to enhance profits over the same short period". p.186, 1.41

15. The Appellant humbly submits that the decision of the Supreme Court is wrong and should be reversed and that this appeal should be allowed for the following among other

R E A S O N S

(1) BECAUSE the said payment made by the Respondent to Bancroft was, for the purposes of the said Section 13 (2) (a) of the said Income Tax Act, 1954, and also on general income tax principles, a payment on capital account, or alternatively because Mr. Justice Young was entitled on the evidence to hold that the Respondent had not discharged the onus of establishing that the said payment was made on revenue account.

(2) BECAUSE Sir John Clayden rightly selected as a test of capital expenditure "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", but came to a wrong conclusion in attempting to apply that test to the facts of the case.

(3) BECAUSE the payment in question was made by the Respondent for a right or quasi-right to carry on its trade more extensively than would otherwise have been practicable or possible, and such a payment is on authority a payment made on capital account.

(4) BECAUSE the said payment secured an "enduring benefit" to the Respondent, within the meaning of the test laid down by Lord Cave in Atherton's case, in that it represented the price paid by the Respondent for a right or quasi-right to carry on its trade more extensively than would otherwise have been practicable or possible, and because the Supreme Court misunderstood and misapplied the said test.

(5) BECAUSE the said payment was made in order to put the Respondent into the position of being able to make a profit and was therefore, on authority, a payment on capital account.

(6) BECAUSE the criticisms directed by Sir John Clayden and Sir Francis Briggs to the concluding paragraph of the Judgment of Mr. Justice Young were misconceived.

(7) BECAUSE the reasoning of the said judgments delivered in the Supreme Court was not well founded.

(8) BECAUSE the decision of Mr. Justice Young was right and ought to be restored.

ROY BORNEMAN

ALAN S. ORR

No. 32 of 1962

IN THE PRIVY COUNCIL

O N A P P E A L

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

B E T W E E N :-

THE COMMISSIONER OF TAXES (Respondent) - Appellant

- and -

NCHANGA CONSOLIDATED COPPER MINES LIMITED (Appellant) - Resoondent

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C A S E FOR THE APPELLANT

COWARD, CHANCE & CO.,
St.Swithin's House,
Walbrook,
London, E.C.4.

Solicitors for the Appellant.