HIGH COURT OF JUSTICE (CHANCERY DIVISION)—2ND NOVEMBER, 1960

COURT OF APPEAL—3RD, 4TH AND 5TH MAY, 1961

HOUSE OF LORDS—5TH AND 6TH FEBRUARY, AND 15TH MARCH, 1962

J. P. Harrison (Watford), Ltd.

v.

Griffiths (H.M. Inspector of Taxes) [1]

Income Tax, Schedule D—Purchase and sale of shares—Dividend-stripping—Claim for relief for loss—Whether carrying on trade of dealing in shares.

The Appellant Company carried on the business of merchants but on 8th October, 1953, *its memorandum of association was amended to enable it to carry on,* inter alia, *the business of share dealing. On 4th December,* 1953, *it purchased for* £16,900 *all the issued share capital of C Ltd. On 26th January,* 1954, *C Ltd. declared a dividend of* £28,912 13*s.* 3*d., and the Appellant Company later sold the shares for* £1,000. *The Appellant Company did not buy or sell any other shares in* 1953–54, *but it admittedly carried on a trade of dealing in shares in* 1954–55.

In an application for adjustment of its liability for 1954–55 *under Section* 341 *of the Income Tax Act,* 1952, *and Section* 15 *of the Finance Act,* 1953, *the Company included,* inter alia, *a loss of* £15,900 *in respect of the transaction. The Special Commissioners held that the Company was not carrying on a trade of dealing in shares during the year* 1953–54 *and disallowed the application in so far as it related to the transaction.*

Held, *that, on their findings of fact, the Commissioners' decision could not be justified.*

CASE

Stated by the Commissioners for the Special Purposes of the Income Tax Acts under the Income Tax Act, 1952, Section 64, and the Finance Act, 1953, Section 15.

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 26th May, 1959, the parties to the present appeal attended before us in connection with an application for relief under Section 341 of the Income Tax Act, 1952, made by J. P. Harrison (Watford), Ltd., for the year 1953–54 to which H.M. Inspector of Taxes had objected pursuant to Section 15 of the Finance Act, 1953. At the outset we heard argument as to what was the issue we had to determine. It was argued by Counsel for J. P. Harrison (Watford), Ltd., that our duty was to hear and determine an objection by H.M. Inspector of Taxes to its application and that it was accordingly for H.M. Inspector of Taxes to make good his objection. On consideration of the terms of the said Section 341 and the said Section 15 we decided that our duty was to hear and determine J. P. Harrison (Watford), Ltd.'s application for relief. The facts set out in paragraphs 2 to 8 inclusive and in paragraph 10 hereof were admitted or proved before us.

[1] Reported (C.A.) 105 S.J. 425; (H.L.) [1962] 2 W.L.R. 909; 106 S.J. 281; [1962] 1 All E.R. 909; 233 L.T.Jo. 205.

2. J. P. Harrison (Watford), Ltd. (hereinafter called "the Company"), was incorporated in 1948 and carried on business as merchants up to some date in the year 1953–54 when that business ceased. Its memorandum and articles of association are annexed hereto, marked "A", and form part of this Case[1]. For the year 1952–53 the Company incurred in the said business a loss of £13,585, which was admittedly available for carry forward to 1953–54 for the purposes of relief under the said Section 341 by virtue of the said Section 15 of the Finance Act, 1953. The question for our determination was whether the Company's transactions in shares of Claiborne, Ltd., as hereinafter detailed, constituted a trade or an adventure in the nature of trade in which the Company sustained a loss in 1953–54 available for further relief under the said Section 341.

3. At an extraordinary general meeting of the Company held on 8th October, 1953, the following resolutions were passed as special resolutions:

"(1) Resolved that the provisions of the Memorandum of Association of the Company with respect to the objects of the Company be altered by inserting therein immediately after paragraph A the following new paragraph namely:—

To carry on the business of buying or otherwise acquiring and selling, exchanging, turning to account or dealing in and disposing of or otherwise turning to account real property, chattels real and personal, shares, stocks, bonds, debentures or other securities of any company or corporation or any participations in syndicates or other rights or interest which may seem capable of profitable handling.

(2) Resolved that the Articles of Association of the Company be altered in that Clause 66 of Table "A" to the Companies Act 1929 shall henceforth not apply to the Company and Article 2 of the Articles of Association of the Company shall be amended accordingly."

4. On 4th December, 1953, the Company purchased all the issued share capital (1,000 £1 shares) of Julius Bendit, Ltd., for £16,900, borrowing £15,900 for the purpose from another company, Boclift, Ltd. Shortly afterwards Julius Bendit, Ltd., changed its name to Claiborne, Ltd., by which name it is hereinafter referred to. The shares of Claiborne, Ltd., were bought by the Company on a blank transfer, which was not registered and was passed on to the purchaser when the Company sold the shares on 4th June, 1954. The Company paid no Stamp Duty on the purchase of these shares.

5. Claiborne, Ltd., had carried on business as cloth merchants up to 30th November, 1953, when such business ceased. At the time of the purchase of all its issued shares by the Company, Claiborne, Ltd., had no business but had considerable accumulated profits available for dividend; it was simply a company pregnant with dividend. The Company purchased the shares with a view to obtaining a dividend against which it could claim to set off its losses.

6. On 26th January, 1954, Claiborne, Ltd., declared a dividend of £28,912 13*s*. 3*d*., less Income Tax £13,010 14*s*.; and the net dividend of £15,901 19*s*. 3*d*. was received by the Company.

7. On the same day, 26th January, 1954, the directors of the Company resolved:

(i) that out of the £15,901 19*s*. 3*d*. received as aforesaid, the Company should repay £15,900 to Boclift, Ltd., and

(ii) that the 1,000 £1 shares in Claiborne, Ltd., be resold to a company named Lewistown, Ltd., for £1,000.

The said shares were in fact sold to Lewistown, Ltd., for £1,000 on 4th June, 1954.

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[1] Not included in the present print.

8. A copy of the Company's accounts for the year ended 31st March, 1954, is annexed hereto, marked "B", and forms part of this Case(1). The gross amount of the Claiborne dividend (£28,912 13*s.* 3*d.*) is shown as credited to the Company's trading and profit and loss account. The Claiborne shares figure in the Company's trading and profit and loss account at £1,000, as part of its "folio of securities" held at the end of the year.

9. We had no evidence that the Company bought or sold any shares in the year 1953–54 apart from the purchase of the said shares in Claiborne, Ltd.

10. It was not disputed that in the following year (1954–55) the Company was carrying on a trade of dealing in shares. A schedule of the Company's purchases and sales of shares subsequent to April, 1954, is annexed hereto, marked "C", and forms part of this Case(1).

11. It was contended for the Company:

(1) that the Company was, in the year 1953–54, carrying on a trade or an adventure in the nature of a trade, consisting of dealing in shares;

(2) that the Company sustained a loss in the said trade of dealing in shares of £15,900 in 1953–54.

12. It was contended by H.M. Inspector of Taxes, the Respondent in this case, that the Company was not carrying on a trade or an adventure in the nature of trade, of dealing in shares, in 1953–54.

13. We, the Commissioners who heard the appeal, found that the Company's transaction in the shares of Claiborne, Ltd., was not entered into as part of any trade of dealing in shares and was not an adventure in the nature of trade, and that the Company was not carrying on any such trade in 1953–54. Accordingly we allowed the application only to the extent of a loss of £3,314, which was agreed between the parties as being the correct figure in relation to the loss sustained by the Company in its trade as merchants.

14. Immediately on our determination of the application the Company declared to us its dissatisfaction therewith as being erroneous in point of law and in due course required us to state a Case for the opinion of the High Court pursuant to the Income Tax Act, 1952, Section 64, and the Finance Act, 1953, Section 15, which Case we have stated and do sign accordingly.

15. The question of law for the opinion of the Court is whether there was evidence on which we could arrive at our findings set out in paragraph 13 hereof.

H. G. Watson
R. A. Furtado
} Commissioners for the Special Purposes of the Income Tax Acts.

Turnstile House,
94–99, High Holborn,
London, W.C.1.
16th December, 1959.

The case came before Danckwerts, J., in the Chancery Division on 2nd November, 1960, when judgment was given against the Crown, with costs.

Mr. Roy Borneman, Q.C., and Mr. P. J. Brennan appeared as Counsel for

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(1) Not included in the present print.

the Company, and Mr. C. F. Fletcher-Cooke, Q.C., and Mr. Alan Orr for the Crown.

Danckwerts, J.—This is an appeal from a decision by the Commissioners for the Special Purposes of the Income Tax Acts, and I may say at once that I feel the greatest difficulty in understanding how the Commissioners came to the conclusion to which they did. So far as I can tell, they did not care for the particular transaction which was carried out by the Appellant Company (and that kind of transaction has subsequently been restricted by Statute as to its effect), but at the date when this transaction was carried out it was perfectly allowable and nothing can be said against it.

The shortest course would be for me to read the facts. The Appellant Company

> "was incorporated in 1948 and carried on business as merchants up to some date in the year 1953–54 when that business ceased."

I think one may call it, from its original memorandum, something of the nature of an import-export company. Its memorandum and articles of association are annexed to the Case and form part of it.

> "For the year 1952–53 the Company incurred in the said business a loss of £13,585, which was admittedly available for carry forward to 1953–54 for the purposes of relief under Section 341 by virtue of . . . Section 15 of the Finance Act, 1953."

The question for the Commissioners' determination was

> "whether the Company's transactions in shares of Claiborne, Ltd.",

as detailed in the Case,

> "constituted a trade or an adventure in the nature of trade in which the Company sustained a loss in 1953–54 available for further relief under . . . Section 341. . . . At an extraordinary general meeting of the Company held on 8th October, 1953, the following resolutions were passed as special resolutions: '(1) Resolved that the provisions of the Memorandum of Association of the Company with respect to the objects of the Company be altered by inserting therein immediately after paragraph A the following new paragraph namely:—To carry on the business of buying or otherwise acquiring and selling, exchanging, turning to account or dealing in and disposing of or otherwise turning to account real property, chattels real and personal, shares, stocks, bonds, debentures or other securities of any company or corporation or any participations in syndicates or other rights or interest which may seem capable of profitable handling'."

Then there was an alteration of the articles to which I need not refer.

> "On 4th December, 1953, the Company purchased all the issued share capital (1,000 £1 shares) of Julius Bendit, Ltd., for £16,900, borrowing £15,900 for the purpose from another company, Boclift, Ltd. Shortly afterwards Julius Bendit, Ltd., changed its name to Claiborne, Ltd., by which name it is hereinafter referred to. The shares of Claiborne, Ltd., were bought by the Company on a blank transfer, which was not registered and was passed on to the purchaser when the Company sold the shares on 4th June, 1954. The Company paid no Stamp Duty on the purchase of these shares."

That, I should have thought, was some indication, if I may say, that it was a very temporary transaction and the shares had been acquired for quick disposal.

> "Claiborne, Ltd., had carried on business as cloth merchants up to 30th November, 1953, when such business ceased. At the time of the purchase of all its issued shares by the Company, Claiborne, Ltd., had no business but had considerable accumulated profits available for dividend; it was simply a company pregnant with dividend."

I do not know what that means, but it may mean that speculators in regard to a matter of this sort could guess with fair certainty that a large dividend would shortly be declared.

(Danckwerts, J.)

> "The Company purchased the shares with a view to obtaining a dividend against which it could claim to set off its losses.. . . On 26th January, 1954, Claiborne, Ltd., declared a dividend of £28,912 13*s.* 3*d.*, less Income Tax £13,010 14*s.*; and the net dividend of £15,901 19*s.* 3*d.* was received by the Company. . . . On the same day, 26th January, 1954, the directors of the Company resolved: (i) that out of the £15,901 19*s.* 3*d.* received as aforesaid, the Company should repay £15,900 to Boclift, Ltd., and (ii) that the 1,000 £1 shares in Claiborne, Ltd., be resold to a company named Lewistown, Ltd., for £1,000"

—that is to say, at par.

> "The said shares were in fact sold to Lewistown, Ltd., for £1,000 on 4th June, 1954."

Then the accounts of the Company are exhibited, and I do not think I need go into them. Paragraph 9 of the Case says:

> "We had no evidence that the Company bought or sold any shares in the year 1953–54 apart from the purchase of the said shares in Claiborne, Ltd."

Paragraph 10:

> "It was not disputed that in the following year (1954–55) the Company was carrying on a trade of dealing in shares. A schedule of the Company's purchases and sales of shares subsequent to April, 1954, is annexed hereto . . . and forms part of this Case."

Pausing there, I may say it was contended, contrary to what was put forward on behalf of the Company, that one was not entitled to consider what happened in subsequent years for the purpose of reaching a conclusion in regard to the year 1953–54, which was the year which was material. That, to my mind, cannot be so, because it seems to me an important circumstance in the present case that prior to the alteration of its memorandum and its objects this Company was a trading company, and what it did in the year following the year under consideration was that it continued to be a trading company; and in my view it never was anything else on the findings but a trading company. The transactions which it carried out, it seems to me to follow inevitably, were transactions carried out by the trading company in the course of its trade.

Then the contentions are set out, and in paragraph 13 we find the conclusions of the Commissioners:

> "We, the Commissioners who heard the appeal, found that the Company's transaction in the shares of Claiborne, Ltd., was not entered into as part of any trade of dealing in shares and was not an adventure in the nature of trade, and that the Company was not carrying on any such trade in 1953–54. Accordingly we allowed the application only to the extent of a loss of £3,314, which was agreed between the parties as being the correct figure in relation to the loss sustained by the Company in its trade as merchants."

Now, the natural question which arises is that which was asked by Lord Radcliffe in the case of *Edwards* v. *Bairstow*, 36 T.C. 207, at pages 229–230. If the transaction is not one in the course of trade, what is it? Mr. Fletcher-Cooke, on behalf of the Crown in the present case, said it was not trade because the shares were bought for consumption, or the dividends were consumed. That seemed to me to be applying language which might be understandable in the case of persons who are natural persons and who buy something like a dozen of port for the purpose of consuming the port, but necessarily unreal and inapplicable in the case of a company which cannot by its nature have enjoyment of that kind. When you find that there is a trading company and it acquires the shares in question for the purpose of making a profit out of those shares, and it makes profit by getting an enhanced price on resale or by getting an advantage out of the temporary possession of the shares in

(Danckwerts, J.)

the form of dividend, to my mind it is dealing in the shares in the course of its trade and not in any other capacity whatever.

Therefore, I come to the conclusion that the result reached by the Commissioners in this case is one which cannot be justified upon their own findings of fact, and it was quite unreasonable having regard to those findings and cannot, therefore, stand.

Mr. Roy Borneman.—Would your Lordship accordingly allow the appeal and direct that the Special Commissioners—

Danckwerts, J.—Do I remit it to them to reconsider the matter on the basis of my decision?

Mr. Borneman.—Would it not be the best way for your Lordship to remit it to the Special Commissioners to deal with the application for repayment on the basis of your Lordship's decision?

Danckwerts, J.—Yes, I think that is right.

Mr. Borneman.—Would your Lordship allow the appeal with costs?

Danckwerts, J.—With costs, yes.

The Crown having appealed against the above decision, the case came before the Court of Appeal (Pearce, Upjohn and Donovan, L.JJ.) on 3rd, 4th and 5th May, 1961, when judgment was given against the Crown, with costs (Donovan, L.J., dissenting).

Mr. C. F. Fletcher-Cooke, Q.C., and Mr. Alan Orr appeared as Counsel for the Crown, and Mr. Roy Borneman, Q.C., and Mr. P. J. Brennan for the Company.

Pearce, L.J.—The Respondents, whom I will call "the Company", carried on business as merchants up to some date in 1953. In October, 1953, the Company altered its memorandum and objects, adding as one of its objects, "To carry on the business of", *inter alia*, " . . . dealing in . . . shares". On 4th December, 1953, it bought 1,000 £1 shares, being the whole issued share capital of Claiborne, Ltd., for £16,900, borrowing £15,900 for this purpose. Claiborne, Ltd., had no business, but it had large accumulated profits available for dividend. It was simply a company pregnant with dividend. The Company bought the shares with a view to obtaining a dividend against which it could claim to set off its losses. On 26th January, 1954, Claiborne, Ltd., declared a dividend of £28,912 13*s.* 3*d.*, less Income Tax of £13,010 14*s.* The net dividend of £15,901 19*s.* 3*d.* was received by the Company, which used it to repay the £15,900 it had borrowed. It resold all the shares in Claiborne, Ltd., for £1,000 on 4th June, 1954. There was no evidence that the Company bought or sold any other shares in the year 1953–54. But from May, 1954, onwards it admittedly carried on a trade in dealing in shares, making various purchases and sales.

In respect of the shares of Claiborne, Ltd., the Company had thus paid out £16,900 and received back £16,901 19*s.* 3*d.*, if one adds the dividend received to the £1,000 realised on the resale. The object of the transaction was this. If the Company was entitled to claim that in 1953–54 it was carrying on the trade (which, by Section 526, Income Tax Act, 1952, includes an adventure in the nature of trade) of dealing in shares, it was entitled to set off for relief under Section 341 the loss made in 1953–54 in respect of the

transaction in the shares of Claiborne, Ltd. That loss was £15,900, being the difference between the purchase price of £16,900 and the resale price of £1,000. The net dividend received from Claiborne, Ltd., having already suffered tax under Section 184, would not be brought into the computation of the receipts of the trade.

The Special Commissioners held that the transaction was not entered into as part of any trade of dealing in shares and was not an adventure in the nature of trade, and that the Company was not carrying on any such trade in 1953–54.

Danckwerts, J., reversed this finding. He said(1):

> ". . . it seems to me an important circumstance . . . that prior to the alteration of its memorandum and its objects this Company was a trading company, and what it did in the year following the year under consideration was that it continued to be a trading company; and in my view it never was anything else on the findings but a trading company. The transactions which it carried out, it seems to me to follow inevitably, were transactions carried out by the trading company in the course of its trade."

He concluded(1):

> "When you find that there is a trading company and it acquires the shares in question for the purpose of making a profit out of those shares, and it makes profit by getting an enhanced price on resale or by getting an advantage out of the temporary possession of the shares in the form of dividend, to my mind it is dealing in the shares in the course of its trade and not in any other capacity whatever."

The Crown first contend as a general proposition that, owing to the very nature of this transaction, it could not be part of a trade of dealing in shares, regardless of whether it was an isolated transaction or one of many transactions. For this was a purchase designed to strip the shares of their dividend, to destroy their value and to resell them at a price that had been thus deliberately lowered. Its object was not to deal in shares, but to eviscerate and discard them. The fact that a compensating benefit had been obtained by receipt of the dividend was, it was argued, irrelevant, since the dividends obtained are not part of the dealing in shares and are not taken into account in computing its profits.

I cannot agree with so technical and artificial a contention. In deciding whether the Company has carried on the trade of dealing in shares we must give the words a reasonable meaning. The profits accruing from dealing in shares cannot be so narrowed as to exclude dividend benefits received by the dealer. If a dealer buys shares for £5,000, receives from them a net dividend of £2,000 and resells them for £4,000, he has from a commonsense point of view made a profit of £1,000 on a deal in shares. If he regularly carried out transactions such as that, it would be unreal to say that he was not carrying on the trade of dealing in shares simply because he had his eye mainly or entirely on the dividend rather than on the selling price. It is true that, when the accounts fall to be analysed, for tax purposes the dividends are excluded from the trading receipts. That is due to the effect of Section 184, Income Tax Act, 1952. It was laid down in *Commissioners of Inland Revenue* v. *Blott*(2) and *Bradbury* v. *English Sewing Cotton Co. Ltd.*(3) that, since dividends have already suffered tax by deduction, they do not suffer further tax by inclusion in a trader's receipts. Therefore, in making out accounts for tax purposes, dividends that have suffered tax are artificially excluded. That is now a convention of the Crown in dealing with the matter. Nevertheless, that does not

(1) *See* page 285 *ante*. (2) 8 T.C. 101. (3) 8 T.C. 481.

(Pearce, L.J.)

alter the fact that dividends may be properly regarded for normal purposes as part of the receipts of a dealer in shares. Moreover, the fact that the Legislature has found it necessary to prevent dividend-stripping by Statute tends to indicate that the Crown's wide proposition is not correct. Therefore, a man can, in my judgment, be properly said to trade in dealing in shares when he makes transactions whereby he relies on the dividends to make good a deliberately intended loss on the selling price of the shares. It does not follow, however, that because the Crown's general proposition is too wide, therefore in the present case the Company was in fact trading in dealing in shares.

The Crown's alternative contentions have greater force. It is argued that the Commissioners' decision on the particular facts of this case was correct, or that, at the least, it was a not unreasonable view on a question of fact and therefore cannot be over-ruled by this Court.

There are three matters on which the Crown rely as taking the transaction in the shares out of the category of trade. First, it is said the deal was an isolated transaction, since there were no other share transactions between the alteration of the memorandum in December, 1953, and the other dealings in shares from May, 1954, onwards. Secondly, it was a transaction by a company that had never had any previous dealings in shares. Thirdly, the object of the transaction was not to make a profit but to secure a fiscal advantage; it was a deliberate and admitted dividend-stripping operation.

The first two points have little force. Section 526, Income Tax Act, 1952, includes in the word "trade" an adventure in the nature of trade in order that "trade" may cover an isolated transaction that has not the continuity or repetition usually connoted by trade. This transaction was carried out very soon after the alteration of the memorandum. The absence of other activity by the Company during the first four months of the Company's new powers under its altered memorandum focuses attention on the nature of the one transaction, but unless other reasons show that the transaction was not a trading activity, its isolation and the initial absence of other business would not produce such a conclusion.

The real force of the attack upon the transaction is in the third point. That was plainly the ground on which the Commissioners came to their decision.

The Company admits the fiscal object of the transaction, but contends that that does not remove its commercial characteristics. It relies on an observation of Lord Radcliffe in *Edwards* v. *Bairstow*, 36 T.C. 207, at page 230:

> "This seems to me to be, inescapably, a commercial deal in second-hand plant. What detail does it lack that prevents it from being an adventure in the nature of trade, or what element is present in it that makes it capable of being aptly described as anything else?"

What element makes the present transaction capable of being described as anything else; and, if it is not trade, what is it?

One starts with the fact that this transaction was a purchase and sale of shares by a commercial company, which had recently altered its objects so as to allow it to deal in shares. And four months after this transaction one finds several purchases and sales of shares with no apparent ulterior fiscal object. Clearly, such surrounding circumstances have a part in any decision as to the nature of the transaction: see *F. P. H. Finance Trust, Ltd.* v. *Commissioners of Inland Revenue* (*No.* 1), 26 T.C. 131, *per* Viscount Maugham at page 150, and *per* Lord Atkin at page 151. Such matters are in no wise

conclusive. But they give a different shade of colour to the transaction than that which it would have worn had it been carried out by a professional man who had never had any dealings in shares. In this case the stage was clearly set for a commercial transaction. In such a setting, had this transaction produced a profit on the resale of the shares, any Court must have held that the profit had been made in the trade of dealing in shares or in an adventure in the nature of trade. The only possible grounds for saying that this was not a trade transaction are the absence of profit, or the fact that the object was fiscal.

As to the former ground, if a transaction from a commercial point of view yielded a substantial foreseeable loss, that fact might in some circumstances be cogent evidence to show that the transaction was not genuine and was not trade. But in this transaction there was from the commercial point of view little, if any, loss. There was, in fact, a gross profit of £1 19*s.* 3*d.* It cannot be said that profit was not the object. For the object was a substantial profit through repayment of tax. Then, can a transaction which would in other respects be commercial lose its commercial nature simply because its object is to secure a financial advantage through repayment of tax? No case suggesting such a principle has been cited to us. If such a principle exists, it must be a question of degree. A genuine farming business cannot cease to be a business merely because a partial, or even the main, object of it is the recovery of tax. When, however, that, or any other commercial transaction, is not genuine, when it is a sham simply designed to produce a tax result, it can no doubt be said not to be a commercial transaction at all. But here there is nothing to suggest that the transaction was a sham. It was a clear and obvious commercial transaction of sale and resale which, by virtue of the Crown convention of excising the dividend from the profit and loss account, produced a large theoretical loss which in turn, as the law then stood, produced a valuable but unpraiseworthy tax benefit. It was a genuine transaction, though its object was unmeritorious.

In my judgment, that ulterior and unmeritorious object does not justify the Court in holding that the transaction was not trade or an adventure in the nature of trade. There is no other fact to justify such a finding. While I sympathise with the view that led the Special Commissioners so to hold, they were not, in my judgment, entitled to do so. I would dismiss the appeal.

Upjohn, L.J.—I agree with the judgment that has just been delivered and with that of Danckwerts, J. The question that we have to consider, and the only question, is whether the learned Judge was right in holding that, to adopt the words of Lord Radcliffe in *Edwards* v. *Bairstow*, 36 T.C. 207, the true and only reasonable conclusion contradicted the determination of the Commissioners that this was not an adventure in the nature of trade.

The real attack by the Crown upon the transaction is that admittedly the only object of the adventure was that the profit lay in the anticipated recovery of Income Tax. We start with this, that in marked contrast with the case recently determined by Buckley, J., of *Johnson* v. *Jewitt*[1], this was a real transaction: there was a purchase of shares for a real commercial money consideration, albeit financed by borrowed money. A real cash dividend was declared by Claiborne, Ltd., from its own real assets; and there was a real sale, again for an appropriate commercial consideration, of the shares at the conclusion of the transaction.

The Company had assumed very wide powers of dealing in shares. Let me

(1) *See* page 231 *ante*.

(Upjohn, L.J.)

read the powers it had conferred upon itself by a special resolution of 8th October, 1953: power

> "To carry on the business of buying or otherwise acquiring and selling, exchanging, turning to account or dealing in and disposing of or otherwise turning to account real property, chattels real and personal, shares, stocks, bonds, debentures or other securities of any company or corporation or any participations in syndicates or other rights or interest which may seem capable of a profitable handling."

A dealer in shares having such powers may acquire a share anticipating a profit on a resale, but he may acquire it hoping to make a profit in other ways. He may acquire the shares hoping that the profit will lie in the declaration of a large dividend, or by the repayment of sums of money on a reduction of capital, or on a dividend declared in a liquidation. All those are profits for which he must account. But he may acquire shares and turn them to account in other ways, and that is what happened in this case. The Company was naturally anxious to take advantage of its tax position, having substantial losses on its former trade of merchant which could be set off against subsequent profits. It was in a position where it was able to acquire the whole share capital of Claiborne, Ltd., a company no longer trading but having substantial assets available for payment of dividend from which Income Tax could properly be deducted under Section 184 of the Income Tax Act, 1952. As Claiborne, Ltd., was not trading, the payment of that dividend automatically reduced the value of the shares by the net amount of the cash so paid out by way of dividend, so that, so far as the purchase and sale of the shares was concerned, there was automatically a loss, and the whole profit lay in the anticipated recovery of Income Tax.

This to my mind, however, was a perfectly lawful, legitimate commercial transaction entered into for the purpose of making a profit on the adventure, a profit by recovery of Income Tax. I cannot myself see how you alter the essential nature of that transaction in the way of trade by giving it the label of "dividend-stripping" or regarding it with distaste. Dividend-stripping has become a well-known commercial operation which has been carried out by persons in recent years to such an extent that Parliament has, very properly, thought fit to put an end to what may well be stigmatised as a very undesirable practice; but I cannot see how the object of making the profit by obtaining a recovery of tax by virtue of the real merchanting loss and the equally real—though, in morals only, more artificial—loss on the purchase and sale of Claiborne shares can alter the character of a commercial transaction, or prevent it being properly described as an adventure in the nature of trade.

In my judgment, like my Lord, I think the only reasonable conclusion to reach is that this was an adventure in the nature of trade, and the learned Judge reached a perfectly correct conclusion. My Lord has pointed out that, when dealing with the tax computation of companies and individuals dealing in stocks and shares, it is the conventional practice to omit from the credit side dividends which have suffered a deduction of tax under Section 184 of the Income Tax Act, 1952, and that is in the ordinary case no doubt a perfectly sensible way of regarding the matter. But the true way of computing profits, in my judgment, is that all the profits for the year of assessment must be brought in, and all the losses are debited against that; and therefore the relevant transaction for tax purposes should be regarded thus. On the profits side you bring in the gross amount of the dividend of £28,912. Against that you deduct the losses: there was an admitted loss on merchanting which, for the purpose of argument only, has been treated as being £16,899. To that must be added the loss on the sale of the Claiborne shares, £15,900.

That makes a loss of £32,799, which is greater than the profit, therefore on that year the Company did not make a profit but made a loss. Therefore, says the Company, it must be adjusted under Section 341 because no tax should have been paid but, in fact, tax has been suffered by deduction from the gross dividend of £28,912: that tax should be returned to the Company.

I do not want to suggest for one moment that Section 341 is not appropriate, in these circumstances, to recover tax. All I do desire to say is this, that we are not concerned with that question. All that this Court is deciding is that the transaction in question was an adventure in the nature of trade. When it is remitted to them, it will be a matter for the Commissioners to consider whether Section 341 is applicable to the state of circumstances I have mentioned or not.

I agree that this appeal should be dismissed.

Donovan, L.J.—In my judgment, the Special Commissioners here made no error of law, and an error of law alone justifies the Court in interfering. I do not find it possible to say that the only reasonable conclusion they could reach was that this single dividend-stripping operation was part of a trade. It is true that it occurred soon after the Company had altered its memorandum and articles of association so as to enable it to trade in stocks and shares. To take power so to trade is one thing, and actually so to trade is another.

The arguments for the Company substantially consist of selecting a number of passages from authorities which catalogue certain *indicia* of trading and then saying: "They are all present here". For example, did the Company proceed in the same way as an acknowledged trader in stocks and shares would do—a test which is taken from *Commissioners of Inland Revenue* v. *Livingstone*, 11 T.C. 538, at page 542. I respectfully think that the fallacy lurking in this line of approach can be shown by a simple example. A company with power in its memorandum to trade in real estate decides to sell some real estate. It goes about the business, doing exactly what a trader in that line would do, by the employment of agents, advertising and so on. There is a sale and a profit; but it turns out that the company has sold a factory which was part of its fixed capital. This is not trading: and so, looking at all the facts, one sees the true situation.

Next, it is argued on behalf of the Company: What does this transaction lack in order to make it a trade? This really is only another way of asserting that all the characteristics one finds in admitted trading are present here. Again, if I may say so without disrespect, I find the argument unsound. Everything which has a head, a body, two legs and two arms is not a human being. The Commissioners were bound to take a comprehensive view of the facts: and when they found that this was an isolated transaction; that, whereas a dealer in shares hopes to make a profit by buying and selling, these shares were bought deliberately to sell at a loss; that the objective was the dividend; and that the prime purpose of the whole transaction was purely a fiscal one; they were, in my opinion, entitled to say that it was not a trading operation.

I agree they might have taken the other view, more especially had they found the transaction embedded in a series of stock and share dealings. But on the facts as they were, I am quite unable to hold that they could not reasonably decide as they did.

I would add one other matter only, that is to say that this case does not raise the question whether it is correct or incorrect, in such a case as this, to omit a dividend of the kind the Company received from the computation of a trading loss for the purpose of relief under Section 341.

Mr. Roy Borneman.—Would your Lordships dismiss the appeal with costs?

Mr. C. F. Fletcher-Cooke.—I cannot resist that. May I have leave to appeal to the House of Lords?

Pearce, L.J.—Yes, leave to appeal to the House of Lords.

The Crown having appealed against the above decision, the case came before the House of Lords (Viscount Simonds and Lords Reid, Denning, Morris of Borth-y-Gest and Guest) on 5th and 6th February, 1962, when judgment was reserved. On 15th March, 1962, judgment was given against the Crown, with costs (Lords Reid and Denning dissenting).

The Solicitor-General (Sir Jocelyn Simon, Q.C.) and Mr. Alan Orr appeared as Counsel for the Crown, and Mr. Roy Borneman, Q.C., and Mr. P. J. Brennan for the Company.

Viscount Simonds.—My Lords, upon an appeal by the Company against the rejection by the Inspector of Taxes of its application for relief under Section 341 of the Income Tax Act, 1952, the Commissioners for the Special Purposes of the Income Tax Acts found that a certain transaction was not entered into by it as part of any trade of dealing in shares and was not an adventure in the nature of trade. They stated a Case at the request of the Company, stating that the question of law for the opinion of the Court was whether there was evidence on which they could arrive at their finding. This question was answered in the negative by Danckwerts, J., who held that the Commissioners' determination could not be justified by their own findings of fact, and was quite unreasonable having regard to those findings. His decision was affirmed by the Court of Appeal (Pearce and Upjohn, L.JJ., Donovan, L.J., dissenting). My Lords, when the question is asked whether there was evidence upon which the Commissioners could arrive at their findings, I take it that this means whether (to adapt the words of my noble and learned friend Lord Radcliffe in *Edwards* v. *Bairstow* [1]) the contrary conclusion is the true and only reasonable one. This can only be determined by a close scrutiny of the evidence led before the Commissioners. In this case the relevant evidence can be shortly summarised.

The Respondent Company was incorporated in 1948 and carried on business as merchants up to some date in the year 1953–54, when that business ceased. In that year it incurred a loss of £13,585, which was admittedly available to carry forward to the year 1953–54 for the purpose of relief under Section 341 of the Act. In October, 1953, the Company's memorandum of association was duly altered so as to enable it to carry on the business of buying and selling (*inter alia*) stocks, shares, bonds and debentures or other securities of any company. On 4th December, 1953, the Company purchased all the issued share capital, amounting to 1,000 £1 shares, of Julius Bendit, Ltd., for £16,900. For that purpose it borrowed £15,900 from another company called Boslift, Ltd. Shortly afterwards Julius Bendit, Ltd., changed its name to Claiborne, Ltd. Its shares were bought by the Company on a blank transfer, which was not registered and was passed on to the purchaser when the Company resold the shares on 4th June, 1954. No Stamp Duty was paid by the Company on the purchase of the shares. (I mention these facts as they appear in the Case, but cannot attach any relevant significance to them.)

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(1) 36 T.C. 207.

(Viscount Simonds)

Claiborne, Ltd., had carried on business as cloth merchants up to 30th November, 1953, when that business ceased. At the time of the purchase of its shares by the Company, Claiborne, Ltd., had no business but had considerable accumulated profits available for dividend. It was described by the Commissioners as

> "simply a company pregnant with dividend",

and they added:

> "The Company purchased the shares with a view to obtaining a dividend against which it could claim to set off its losses."

On 16th January, 1954, Claiborne, Ltd., declared a dividend of £28,912 13*s.* 3*d.* less Income Tax £13,010 14*s.*, and the net dividend of £15,901 19*s.* 3*d.* was received by the Company. On the same day the directors of the Company resolved (1) that, out of this sum of £15,901 19*s* 3*d.*, the Company should repay £15,900 to Boslift, Ltd.; (2) that the 1,000 £1 shares in Claiborne, Ltd., should be resold to a company called Lewistown, Ltd., for £1,000. They were, in fact, so sold. There was no evidence that the Company bought or sold any other shares in the year 1953–54, but it was not disputed that in the following year (1954–55) it was carrying on the business of dealing in shares.

This, my Lords, is the sum of the evidence upon which the Commissioners determined that the Company's purchase and sale of the Claiborne, Ltd., shares was not entered into as part of any trade of dealing in shares or an adventure in the nature of trade. As the Commissioners made no other finding than that which I have mentioned, it must be assumed that their determination can only have been based on the facts (1) that the Claiborne transaction was an isolated one in the year of assessment and (2) that the shares were purchased with a view to obtaining a dividend against which it could claim to set off its losses.

The first of these reasons, if not formally abandoned, was not seriously maintained before your Lordships, and appears to me quite unsustainable.

It was the second reason that was urged as justifying the Commissioners' determination. I hope that I do no injustice to the argument for the Crown if I say that it rested entirely on the proposition that the essence of a trading transaction is that its object is to make a profit and that the found object of this transaction was the ulterior one of obtaining a dividend against which it could claim to set off its losses. This proposition was supported by the fact that the shares were bought for £15,900 and sold for £1,000—a transaction which, thus baldly stated, could not be regarded as a favourable, or even a normal, one from the point of view of a dealer in shares. But, my Lords, attractive as this proposition is, and attractively as it was advanced by the then Solicitor-General, it does not convince me. Here was a Company whose object it was to deal in shares. It entered into a commercial transaction which, though it might be given an invidious name, contained no element of impropriety, much less of illegality. I can find nothing that enables me to say that it is not a trading transaction, and echo the question asked by the majority in the Court of Appeal: "If it is not that, what is it? (1)" No doubt, many observations that have been made *alio intuitu* will be found to the effect that trade is carried on with a view to a profit. But this proposition is not universally true, nor can it be tested merely by ascertaining the difference between the purchase price (or, it may be, the manufacturing cost) of an article and the selling price of that article. For a dealer may seek his profit, if a profit is essential, otherwise than by an enhanced price upon a resale, as by a declaration of dividend, a repayment upon a reduction of capital or upon a liquidation

(1) *See* page 288 *ante*.

(Viscount Simonds)

of the company whose shares he has bought. It appears to me to be wholly immaterial, so long as the transaction is not a sham (as was the case in *Johnson* v. *Jewitt* (1), 40 A.T.C. 314) what may be the fiscal result, or the ulterior fiscal object, of the transaction; and since this can be the only ground upon which the Commissioners could have reached their determination, I must conclude that it cannot be upheld.

I would dismiss this appeal, with costs.

Lord Reid.—My Lords, this case arises out of a claim made by the Respondent for relief under Section 341 of the Income Tax Act, 1952. The claim is based on alleged loss in the trade carried on by it; its validity depends on whether a certain transaction was done in the course of, or as part of, that trade. The Special Commissioners found that the transaction

> "was not entered into as part of any trade of dealing in shares and was not an adventure in the nature of trade",

and accordingly only allowed a part of the claim. The question before your Lordships is whether that finding must be held to be wrong.

The transaction in question was a simple one. A company called Claiborne, with a share capital of 1,000 £1 shares, had ceased to trade; but it held accumulated profits, which had borne tax, amounting to some £15,900. On 4th December, 1953, the Respondent bought these shares for £16,900. The Commissioners found as a fact, and it is not disputed, that it bought the shares with a view to obtaining a dividend against which it could claim to set off losses. Claiborne, now controlled by the Respondent, duly declared a dividend on 26th January, 1954, and the net sum of £15,901 19*s.* 3*d.* was received by the Respondent. The shares were then immediately sold for £1,000. So the Respondent made neither profit nor loss beyond having to pay any expense involved in carrying through these operations: it spent £16,900 and it got back £15,901 19*s.* 3*d.* plus £1,000. But it got what it had planned to get, a large dividend paid out of money which had borne tax. If this was a trading operation, that enabled it, as the law then stood, to recover from the Revenue a large amount of Income Tax which it had never paid.

The trade of the Respondent was originally that of merchants. In that trade it incurred substantial losses. It ceased to carry on that trade, but was entitled to carry forward a loss which was available to be taken into account in its claim for relief under Section 341. In October, 1953, two months before it bought the Claiborne shares, it altered its memorandum of association, taking power

> "To carry on the business of buying or . . . selling, . . . or dealing in . . . or otherwise turning to account . . . shares . . . or other securities of any company . . . which may seem capable of profitable handling".

Then it bought these shares. It did not buy any other shares during that financial year, but it bought some 20 parcels of shares during the next financial year.

If the law requires that I must look solely at the purchase and sale of the shares, then that was undoubtedly trading. A company having power to deal in shares bought 1,000 shares and sold them a few months later. But if the law does not prevent me from looking at the substance of the matter, then the operation appears in a very different light. What the Respondent did was to lay out £16,900 in such a way that it was able to ensure that nearly 95 per cent. of that sum would quickly come back into its hands in

(1) *See* page 231 *ante*.

(Lord Reid)

the form of dividend which had borne tax. The only advantage which it sought to get, or could get, out of the transaction was the acquisition of a right to recover from the Revenue tax which had been paid by somebody else. It could not buy such a right directly; the purchase and sale of the shares were steps which it had to take in the process of acquiring it. If I am entitled to have regard to the substance of the transaction, the real question appears to me to be whether acquiring a dividend which has borne tax for the sole purpose of using it to recover tax from the Revenue must be held to be trading because in the course of acquiring it shares were bought and sold.

The first question must be whether there is any clear guidance from authority. I do not think there is. There is certainly nothing binding on this House; and I cannot find anywhere any clear support for the main argument submitted by Counsel for the Respondent, that you must look solely at the purchase and sale of the shares and must not look at the expectation or intention of the taxpayer in buying them or at the result of the initial purchase of the shares. Cases such as *Rutledge* v. *Commissioners of Inland Revenue* (1929 S.C. 379, 14 T.C. 490) show that, at least in the case of an individual, his object and intention when buying property are very relevant. And where, for example, a company which trades in property buys property to be used for its office, its object and intention are certainly relevant to show that the price was not a trading expense.

The Respondent relied on what was said in five cases. In each the question was whether there was trading or an adventure in the nature of trade. Certainly these cases establish that operations of the same kind as, and carried on in the same way as, those which characterise ordinary trading should be held to be trading though there may be no intention to earn profit or though the transaction may be an isolated one. In *Commissioners of Inland Revenue* v. *The Incorporated Council of Law Reporting* (3 T.C. 105), *Carnoustie Golf Course Committee* v. *Commissioners of Inland Revenue* (1929 S.C. 419, 14 T.C. 498) and *Commissioners of Inland Revenue* v. *The Stonehaven Recreation Ground Trustees* (1930 S.C. 206, 15 T.C. 419) there was no intention or attempt to earn a profit, but profit was in fact made. *Commissioners of Inland Revenue* v. *Livingston and others* (1927 S.C. 251, 11 T.C. 538) and *Edwards* v. *Bairstow* ([1956] A.C. 14, 36 T.C. 207) were cases of isolated transactions where a profit was earned. But in none of these cases were the activities which were held to be trading mere steps towards an operation which was not of a trading character at all. The gist of the present operation was to create a claim against the Inland Revenue; and it is well settled that recovering tax from the Revenue is not a trading activity, and expense incurred in seeking to recover tax is not a trading expense (see *Commissioners of Inland Revenue* v. *Dowdall O'Mahoney & Co., Ltd.* (2), [1952] A.C. 401, and cases there cited).

The question has been asked in a number of cases: "If this was not trading, what was it?" With all deference to those who have used that argument, I do not think that it is very useful in most cases. Human affairs—and business affairs—are of infinite variety. They do not fit neatly into categories or classes. Innominate contracts and transactions are of frequent occurrence, and I would not expect to find appropriate names to denote new kinds of operations devised for the sole purpose of gaining tax advantages. In the present case the question is not what the transaction of buying and selling the shares lacks to be trading, but whether the later stages of the

(1) 33 T.C. 259.

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(Lord Reid)

whole operation show that the first step—the purchase of the shares—was not taken as, or in the course of, a trading transaction.

The Commissioners had to determine whether the Respondent's claim for relief under Section 341 was valid. Admittedly, that depended on whether the Respondent bought and sold these shares as part of the trade of dealing in shares or as an adventure in the nature of trade. If it did not, it gets no advantage out of the transaction and its claim for relief is greatly reduced. Like any other tribunal, the Commissioners had first to find the facts: they did so, and no question arises about that. Then they had to consider the words of the Act and determine whether those words applied to those facts. Ultimately, Counsel did not seriously contend that in this case it makes any difference whether one takes the word "trade" or the phrase "an adventure in the nature of trade"; and I do not think it does, so I shall simply take the word "trade".

Any decision by any Court or other tribunal whether the words of an Act apply to the facts of a particular case must, unless the matter is concluded by authority, ultimately depend on its knowledge of the usage of the English language in ordinary affairs of the kind with which the particular Act is concerned. The Court or tribunal may be assisted by legal principles or by so-called rules of construction, but these cannot solve the question. The question whether the words of an Act apply to particular facts is generally called a question of law. But to my mind it is in reality neither a question of law nor a question of fact. It cannot be solved either by the application of legal principles or by evidence. A Court or tribunal could no doubt proceed by first translating the words of the Act into other words (whether or not those other words be called the "meaning" of the words of the Act) and then seeing whether those other words apply to the particular facts. But we have been warned time and again that it is dangerous and wrong to proceed in that way. The question is whether the words of the Act apply to the facts of the case. In some exceptional cases the question whether a particular word or phrase in an Act applies to particular facts has come to be regarded, for reasons that I do not fully understand, as a question of fact. A line of authorities, culminating in *Edwards* v. *Bairstow* [1], [1956] A.C. 14, has decided that that is so as regards the word "trade" in the Income Tax Act. But I can find no reason for supposing that the nature of the judicial process is different when the question is said to be one of fact from what it is when the question is said to be one of law. I do not know what novel method the Commissioners could adopt in determining whether the word "trade" applies to particular facts. Like any Court or other tribunal, they must defer to authority which is binding on them and pay heed to what has been said in authorities which are not directly in point. But, having done so, I cannot think that they must proceed in some way different from the way in which a Court proceeds, or the way in which they themselves must proceed, when deciding as a question of law the application of some other words in the Act. Where, as in this case, the question is a question of fact, that means that the decision of the Commissioners cannot be reviewed by the Court. But if the decision of any tribunal on a question of fact is unreasonable, looking to the facts on which it is based, the Court can and must intervene. The question in this case, is, therefore, not whether the Commissioners were wrong but whether their decision was unreasonable. I hope that what I have said is consistent with *Edwards* v. *Bairstow*, but after much study I find myself unable to discover where I have gone wrong in what I have said.

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[1] 36 T.C. 207.

(Lord Reid)

I have already said that the question in this case does not appear to me to be concluded by authority. Therefore, in light of such knowledge as I may have of the usage of the English language, and in particular of its usage in business affairs, I must put to myself the question whether it is unreasonable to say that the operations of the Respondent in this case were not trading or that the word "trade" does not apply to them. It would seem that one reason why this question was held to be one of fact was that the word "trade" is more indefinite than most words used in Acts of Parliament, and Parliament has not chosen to define it, except by a definition which repeats the word. So there are many cases where there is room for a difference of opinion, and I think that this is one of them. I am not prepared to say that the opinion of the Commissioners is unreasonable; and, if that be so, this appeal ought in my judgment to be allowed.

I would add that what I have said does not mean that it would never be unreasonable to say that a case of dividend-stripping was not trading. There may well be elements of trading involved in other cases to such an extent that it would be unreasonable to deny that there was trading. The question may be one of degree. But in the present case almost the whole of the money put out, some 95 per cent., was transformed into a dividend, and the Commissioners were, I think, well entitled to say that was not trading.

Lord Denning.—My Lords, your Lordships are here faced for the first time with a "dividend-stripping" transaction. What is it? To put it bluntly, it is a way of getting money out of the Revenue authorities. To succeed in it, the prospectors must get into their hands (1) a dividend on which tax has been paid; and (2) losses sustained in trade. They then claim repayment of the tax on the ground that it is relief due to them on account of the losses.

The best way to understand it is to take first a straightforward case of "relief against losses". Suppose a man carries on the trade of farming and makes a loss on it of £250 in the year. But he has also an investment in shares which brings him in a dividend of £450, tax paid. When grossed up, that means that his investment income is £750; but before he receives it, tax of £300 has been deducted at source, so that he only receives the net sum of £450. He has thus suffered tax on the full £750. But, under the provisions for relief against losses, he is entitled to set off the farming loss of £250 against his investment income of £750. So he ought only to bear tax on £500, not on £750. To get the position straight, he can claim repayment of the tax on the £250. In short, he can claim from the Revenue the tax on his loss of £250.

Now turn to the present case. A Company called Harrison was in business as merchants. It did badly and made a loss of £13,585. So it closed down its merchants' business. It had no investment income, as the farmer had, on which to claim repayment of tax. But it set to work to get such an income. It got to know of a company called Claiborne, dealing in cloth, which had made a profit on its trading. Claiborne had made a profit of £28,912 13*s.* 3*d.* It had paid tax on that sum amounting to £13,010 14*s.* That left it with a balance of £15,901 19*s.* 3*d.* in hand, which was available to distribute to its shareholders as net dividend. It then closed down its business. Here was a ripe subject for a dividend-stripping operation. Harrison decided to buy up all the shares of Claiborne, full of dividend; take out the dividend for itself; and re-sell the shares, shorn of dividend.

It required a good deal of skill to bring this about. In the first place, Harrison had to change its way of life. It had to turn itself from a dealer in merchandise into a dealer in shares. So it altered its articles of association

(Lord Denning)

for the purpose. It had also to buy all the shares of Claiborne so as to get control of it. There were 1,000 of these shares, and they were worth a good deal of money because Claiborne had £15,901 19*s.* 3*d.* in hand available for dividend. But Harrison had not got any money to pay for these shares: it had to borrow it from another company. It borrowed the sum of £15,900 in the sure knowledge that it would soon get it back in dividend. And so it did. Harrison bought the 1,000 shares in Claiborne for £16,900 (£15,900 plus £1,000); it used its control of Claiborne so as to distribute a dividend to itself of £15,901 19*s.* 3*d.*, and with that sum it paid back the £15,900 it had borrowed; and then it resold the shares for £1,000.

Now, what was the net result of that "dividend-stripping" operation? In point of fact (apart from tax benefits) Harrison made a gross profit of £1 19*s.* 3*d.* This trifling sum was, of course, not the object of the exercise. The object was two-fold: first, to get a dividend in hand on which tax had already been paid; secondly, to get losses in hand which would serve as a basis for a claim for repayment of tax. The *losses* of Harrison came to £29,485, as follows:

	£	£
Losses on merchandise		13,585
Loss on the shares of Claiborne,		
bought for	16,900	
sold for	1,000	
Loss	15,900	15,900
		29,485

The *dividend* in hand came to £28,912 13*s.* 3*d.* gross:

	£	*s.*	*d.*
Net dividend	15,901	19	3
Tax paid	13,010	14	0
Gross dividend	28,912	13	3

So situated, Harrison could claim to be in the same position as the farmer. It had made losses of £29,485, but profits of £28,912 13*s.* 3*d.* It could set off the losses against the profits and say it had made no profits at all. Yet tax had already been paid of £13,010 14*s.* It was entitled, therefore, to claim repayment of that tax—the whole of it—from the Revenue authorities. Indeed, it inserted it in its accounts as "Income Tax recoverable (not yet agreed), £13,010 14*s.*"

There is one thing, however, which is essential to the claim of Harrison for repayment of tax. The losses must be sustained in a "trade": and the word "trade" includes "every trade, manufacture, adventure or concern in the nature of trade". Harrison therefore sought to say that this dividend-stripping transaction was an "adventure in the nature of trade". The Commissioners held that it was not such an adventure, and so put their foot down on any repayment.

Harrison appealed to the High Court seeking to get the decision of the Commissioners reversed. Now, the powers of the High Court on an appeal are very limited. The Judge cannot reverse the Commissioners on their findings of fact. He can only reverse their decision if it is "erroneous in point of law". Now here the primary facts were all found by the Commissioners.

(Lord Denning)

They were stated in the Case. They cannot be disputed. What is disputed is their conclusion from them. And it is now settled, as well as anything can be, that their conclusion cannot be challenged unless it was unreasonable, so unreasonable that it can be dismissed as one which could not reasonably be entertained by them. It is not sufficient that the Judge would himself have come to a different conclusion. Reasonable people on the same facts may reasonably come to different conclusions, and often do. Juries do. So do Judges. And are they not all reasonable men? But there comes a point when a Judge can say that no reasonable man could reasonably come to that conclusion. Then, but not till then, he is entitled to interfere. It is just like the position with juries in the old days, when questions arose whether goods were "necessaries", whether words were "defamatory", or whether conduct was "negligent". It was a question of law for the Judge to rule whether the inference *could* reasonably be drawn, but a question of fact for the jury whether it *ought* to be drawn. Likewise, we have nowadays the cases before magistrates whether a speed was "dangerous"; or before the Lands Tribunal whether part of a plant was "in the nature of a structure"; or before the Commissioners of Income Tax whether a transaction was an "adventure in the nature of trade". It is a question of law for the Judge whether the conclusion *could* reasonably be drawn, but (given that it could reasonably be drawn) it is a question of fact for the tribunal whether it *ought* to be drawn.

Mr. Borneman urged your Lordships to say that on the undisputed facts the Commissioners *could* not reasonably have come to the conclusion they did. There was only one true and reasonable conclusion to which the Commissioners could come, namely, that the transaction was an "adventure in the nature of trade". Here was a Company, he said, which was authorised to deal in shares. It bought shares, received a dividend from those shares, and then sold them. What detail does it lack, he asked, that prevents it being an adventure in the nature of trade?

To this I would reply by asking another question: *What detail must it have* to render it an adventure in the nature of trade? What are the characteristics of such an adventure? For unless you first define what detail it must have, you cannot say what detail it lacks. Parliament did not vouchsafe an answer. It did not define a "trade". And I do not know that any Judge has attempted it. Try as you will, the word "trade" is one of those common English words which do not lend themselves readily to definition but which all of us think we understand well enough. We can recognise a "trade" when we see it, and also an "adventure in the nature of trade". But we are hard pressed to define it. Donovan, L.J., gave an apt illustration[1]. Is a monkey a "human being" or an animal "in the nature of a human being"? It has a head, a body, two legs and two arms. What detail does it lack? Or, nearer still, take a gang of burglars. Are they engaged in trade or an adventure in the nature of trade? They have an organisation. They spend money on equipment. They acquire goods by their efforts. They sell the goods. They make a profit. What detail is lacking in their adventure? You may say it lacks legality, but it has been held that legality is not an essential characteristic of a trade. You cannot point to any detail that it lacks. But still it is not a trade, nor an adventure in the nature of trade. And how does it help to ask the question: If it is not a trade, what is it? It is burglary, and that is all there is to say about it. So, here, it is dividend-stripping and nothing else.

Short of a definition, the only thing to do is to look at the usual characteristics of a "trade" and see how this transaction measures up to them. Usually

(1) *See* page 291 *ante*.

(Lord Denning)

in trade, the trader makes many trading transactions. But that is not essential. An isolated transaction may do. Usually the object of the trader is to make a trading profit. But that is not invariable. Remember the hobby-farmer. But when you find that it was an isolated transaction, as this was, and it was not the object to make a trading profit, as there was none here, you at least have some grounds—and reasonable grounds at that—for thinking there was not a trade nor an adventure in the nature of trade. The Judges below seem to have realised this, and only got over it by finding that the profit motive was present. They thought this transaction had as its object the making of profit, and was therefore an "adventure in the nature of trade". Thus Danckwerts, J., said (1) that Harrison acquired "the shares in question for the purpose of making a profit out of those shares". Pearce, L.J., said (2) that "the object was a substantial profit through repayment of tax." Upjohn, L.J., said (3) the purpose was "making a profit on the adventure, a profit by recovery of Income Tax."

Mr. Borneman did not seek to support this reasoning. He was reluctant to accept the gift thus held out to him. He feared the dangers of it. He had to admit that the object of Harrison was not to make trading profits. It was to get repayment of tax, which is a very different thing. Can repayments of tax be properly described as profits of a trade? Surely not. If it were so, the repayments of tax which a dividend-stripper received would be profits of his trade which he would have to bring into computation for tax. That would be absurd. It would mean that the Revenue could levy tax on its own repayments to the dividend-stripper. Whoever heard of such a thing? Pushing aside the proffered gift, Mr. Borneman sought to tempt your Lordships with fruit of his own growing, not tasted here before. He said that the *object* of the transaction was irrelevant. So was the *result* of it. You must look at the transaction free of any prepossession about tax repayments. And when you do this, you see only a dealer in shares who buys shares, receives a dividend from them and then sells them again. What is this, he asks, but an "adventure in the nature of trade"?

My Lords, you have indeed here a question of law, if you please to treat it as such. The contention comes to this: You should split the dividend-stripping transaction into two parts. You should look only at one-half of the transaction and turn a blind eye to the other half. You are to look at the purchase and sale of shares, but not at the repayment of tax. And, when you look at the purchase and sale of shares, you are not to have regard to the motive behind it. You must disregard the fact that it is done with a view to create a trading loss, and you must treat it as a normal transaction in share dealing. My Lords, I do not believe there is any rule of law which requires the Commissioners to disregard the object of the transaction or its result. There are occasions when a reasonable man may turn a blind eye to the facts, but this is not one of them. To my mind, the Commissioners were entitled to see these people as they really are, prospectors digging for wealth in the subterranean passages of the Revenue, searching for tax repayments. They are not simple traders dealing in stocks and shares. I am not prepared to say that the Commissioners were unreasonable, so unreasonable that they could not reasonably come to their conclusion.

I find myself in full agreement with the judgment of Donovan, L.J., and I would allow this appeal.

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(1) *See* page 285 *ante*. (2) *See* page 289 *ante*. (3) *See* page 290 *ante*.

Lord Morris of Borth-y-Gest.—My Lords, the question which arises in this appeal is whether the transaction of the Respondent (the Company) in the shares of Claiborne, Ltd., was entered into as part of any trade of dealing in shares or was an adventure in the nature of trade. If the transaction was so entered into, the Company will pursue its application for relief under Section 341 of the Income Tax Act, 1952. In this appeal your Lordships are not concerned to consider that application or its results.

The Company bought the shares in question on 4th December, 1953. The shares consisted of all the issued share capital of Julius Bendit, Ltd. Shortly afterwards Julius Bendit, Ltd., changed its name to Claiborne, Ltd. When, on 4th December, 1953, the Company bought the shares, the memorandum of association of the Company, as altered, showed that among the objects of the Company was that of carrying on the business of buying or otherwise acquiring and selling or dealing in and disposing of shares and stocks of any company. On 26th January, 1954, Claiborne, Ltd., declared a dividend. The net dividend was received by the Company. On 4th June, 1954, the Company sold the shares. There was no evidence that in the year 1953–54 the Company bought or sold any other shares, but it was not disputed that in the following year the Company was carrying on a trade of dealing in shares.

There has never been any doubt as to what was the motive or reason which inspired the decision of the Company to enter into the transaction in regard to the shares. It was expressed by the Commissioners in the words:

> "The Company purchased the shares with a view to obtaining a dividend against which it could claim to set off its losses."

The Company considered that if it bought the shares and obtained a dividend the result would be that it could obtain a recovery of tax.

The facts, which are not in dispute, are clearly set out in the Case Stated; and in reference to them the Commissioners found that the Company's transaction in the shares was not entered into as part of any trade of dealing in shares and was not an adventure in the nature of trade, and that the Company was not carrying on any such trade in 1953–54.

My Lords, on the principles laid down in *Edwards* v. *Bairstow* (1), [1956] A.C. 14, it seems to me that the present is eminently a case in which a Court is entitled, if it so thinks, to say that the only reasonable conclusion on the facts found is inconsistent with the determination of the Commissioners.

It has not been, and could not be, suggested that the transaction of the Company in the shares was a sham transaction. The Company bought the shares, received a dividend and then sold the shares. These facts seem to me to point firmly to the conclusion that the transaction was entered into as part of a trade of dealing in shares or was an adventure in the nature of trade. The inherent nature of the transaction suggests a trading operation. It is said, however, that the inherent nature of the transaction becomes altered by virtue of the objective of the transaction. It is said that the Company embarked upon a dividend-stripping operation, and that accordingly the transaction should not be regarded as a trading transaction but as a fiscal transaction.

My Lords, it seems to me that a trading transaction does not cease to be such merely because it is entered into in the confident hope that, under an existing state of the law, some fiscal advantage will result. In judging as to the essential nature of a transaction it will often be relevant and of assistance to consider the objects and intentions which are the inspiration of the trans-

(1) 36 T.C. 207.

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action. In the present case, however, I cannot think that there is room for doubt as to the essential nature of the transaction: it was a transaction which was demonstrably of a trading nature, and it was not divested of that nature merely because it was entered into with the expectation that as a result (but not as part of the trading activity of the Company as such) some tax recovery might be claimed.

It is doubtless true to say that, in general, a trader embarks upon trade with the intention of making a profit, but it cannot be said that if this intention is lacking there is no carrying on of a trade. A trade may be carried on with the knowledge that losses will result. Equally, it seems to me that if, on any ordinary examination of them, certain transactions must be regarded as trading transactions or adventures in the nature of trade, they do not cease to be such because those conducting them have embarked upon them with a view to obtaining some fiscal benefit. It was urged in the present case that the transaction in the shares of Claiborne, Ltd., ought to fail to be regarded as a trading transaction because in its real nature it was a fiscal transaction. My Lords, I cannot regard these as alternative descriptions. There may be trading transactions which can be the prelude, if the state of the law so allows, to tax-recovery activities. If tax recovery is possible it is as taxpayers and not as traders that the recovery is obtained. The possibility of tax recovery may be a result made possible by the trading activity; but I am unable to accept that if a transaction, fairly judged, has in reality and not fictitiously the features of an adventure in the nature of trade, it must be denied any such description if those taking part in it had their eyes fixed upon some fiscal advantage.

My Lords, on the facts found in the present case I am driven to the conclusion that the transaction in the shares was entered into as part of a trade of dealing in shares or was an adventure in the nature of trade. I would dismiss the appeal.

Lord Guest (Read by Lord Denning).—My Lords, the Respondent Company carried on business as merchants until some date in the year 1953–54. On 8th October, 1953, the memorandum of association was altered so as to include among the objects of the Company the dealing in stocks and shares. On 4th December, 1953, the Company purchased all the issued share capital in Julius Bendit, Ltd., for £16,900, borrowing £15,900 for the purpose. Julius Bendit, Ltd., thereafter changed its name to Claiborne, Ltd. Claiborne had carried on business as cloth merchants up to 30th November, 1953, when that business ceased. At the time of the purchase Claiborne had considerable accumulated profits available for dividend. There is a finding by the Special Commissioners that :

> "The Company purchased the shares with a view to obtaining a dividend against which it could claim to set off its losses."

Claiborne, on 26th January, 1954, declared a dividend of £28,912 13*s.* 3*d.* less Income Tax £13,010 14*s.*, and the net dividend of £15,901 19*s.* 3*d.* was received by the Company. Out of the £15,901 19*s.* 3*d.* received the Company repaid the loan; and then, on 4th June, 1954, it sold the shares in Claiborne for £1,000. The Company did not buy or sell any shares in the year 1953–54 apart from the purchase of the Claiborne shares, but in the following year the Company bought and sold a number of shares. The question for determination by the Commissioners was whether, during the year 1953–54, the transaction in the shares of Claiborne constituted the carrying on of trade or an adventure in the nature of trade. The Company claimed that it was carrying on trade or an adventure in the nature of trade consisting of dealing

(Lord Guest)

in shares and that it sustained a loss, in dealing with these shares, of £15,900, being the difference between the price paid for the shares of £16,900 and the price realised of £1,000 upon sale of the shares. This loss, it claimed, was available for relief under Section 341 of the Income Tax Act, 1952. The Commissioners found that the transaction was not entered into as part of any trade of dealing in shares and was not an adventure in the nature of trade, and that the Company was not carrying on any such trade in 1953–54. Danckwerts, J., and the Court of Appeal reversed the determination of the Commissioners and held that the Company was carrying on trade during the relevant period.

The finding of the Commissioners cannot be disturbed unless it was arrived at upon a view of the facts which could not reasonably be entertained (*Edwards* v. *Bairstow*, [1956] A.C. 14, *per* Viscount Simonds at page 29 and Lord Radcliffe at pages 36 and 39 (1)). The Commissioners give no reasons for their finding: they simply state the facts and their conclusion. One is therefore left in doubt as to the reasons which led them to their conclusion. It can, of course, be said that their finding was upon a review of all the facts. But if it can be substantiated that any reason which they might have had for holding that the Company was not trading is not a good reason in law, their finding cannot stand. The test put in *Edwards's* case would then be satisfied.

I therefore proceed to examine the grounds put forward by the Crown for supporting the decision of the Commissioners. At one stage it was suggested that because this was an isolated transaction, the Company could not be said to be trading. The Solicitor-General, however, did not suggest that this by itself was a ground upon which trading in this case could be negatived. No doubt if the Respondent had been a private individual this might have been a cogent reason, although there are many cases where an isolated transaction has been held to amount to trading (see *Rutledge* v. *Commissioners of Inland Revenue*, 14 T.C. 490). But where the Company has power under its memorandum of association to indulge in a particular activity and the transaction contains otherwise all the *indicia* of trading in that line of business, the fact that it was an isolated transaction is, in my opinion, *nihil ad rem*. In any event, regard must be had to the subsequent dealings in shares by this Company; and, so viewed, this was not an isolated transaction, but one of many.

It was argued for the Crown that as the objective of trading was in general the making of a profit, a transaction which was aimed at making a loss with a view to a fiscal advantage could not in any circumstances amount to trading. The fallacy underlying the Crown's argument is, in my view, the confusion of the trading activities of a concern with the result of these activities. An individual or a company can conduct their business in the most extravagant way; they can conduct it with the certainty of making a loss. But the Revenue is not concerned with the particular method of trading, they are only concerned with the results of the business. If there are profits or gains and the business is a trade, then Income Tax is payable. If there are losses, relief is available under Section 341. It was also argued for the Crown that recovery of tax was not part of the trading activities of a company and that therefore tax repaid was not part of the profits of a trade. I agree. Neither payment of tax nor recovery of tax is part of the trading activities of a company, they are the results which the law imposes on the trade. A number of citations

(1) 36 T.C. 207, at pp. 224, 229 and 231.

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from cases were quoted in order to show that to ascertain whether there was trading it was relevant to look at the object, result or intention of the activity (see, for example, *Commissioners of Inland Revenue* v. *Livingston*, 11 T.C. 538, *per* Lord President Clyde at pages 542–3; *Commissioners of Inland Revenue* v. *The Stonehaven Recreation Ground Trustees*, 15 T.C. 419, *per* Lord President Clyde at page 426). No doubt if it is established that a transaction is entered into with the evident intention of making a profit, that may be a strong indication that the Company was trading. But the corollary by no means follows that the absence of an intention to make a profit, or the intention to make a loss, negatives trading. The test is an objective one. The question to be asked is not, *quo animo* was the transaction entered into, but what in fact was done by the Company (see *Commissioners of Inland Revenue* v. *Incorporated Council of Law Reporting*, 3 T.C. 105, *per* Coleridge, C.J., at page 113; *Carnoustie Golf Course Committee* v. *Commissioners of Inland Revenue*, 14 T.C. 498, *per* Lord President Clyde at page 510).

I therefore conclude that neither the fact that the Company intended to make a loss nor the fact that the Company intended to make a fiscal advantage out of the transaction negatives trading. In my opinion one has to look at the transaction by itself irrespective of the object, irrespective of the fiscal consequences, and ask the question in Lord President Clyde's words in *Livingston's* case (1):

> "[are] the operations involved . . . of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made"?

The Company had power to deal in shares, it bought shares, it received a dividend on these shares, it sold the shares. This was just the ordinary commercial transaction of a dealer in shares. I ask myself the question put by Lord Radcliffe in *Edwards* v. *Bairstow* (2), [1956] A.C. 14, at page 37:

> "What detail does it lack that prevents it from being an adventure in the nature of trade, or what element is present in it that makes it capable of being aptly described as anything else?"

What is it if it is not trade? In my view the transaction in question was an adventure in the nature of trade, and the Commissioners had no grounds upon which they could hold that it was not.

I would dismiss the appeal.

Questions put:

That the Order appealed from be reversed.

The Not Contents have it.

That the Order appealed from be affirmed and the appeal dismissed with costs.

The Contents have it.

[Solicitors:—Mackrell & Co.; Solicitor of Inland Revenue.]

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(1) 11 T.C., at p. 542. (2) 36 T.C. 207, at p. 230.

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