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UNIVERSITY OF LONDON
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-3 JUL 1956
INSTITUTE OF ADVANCED
LEGAL STUDIES

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No. 42 of 1953.

In the Privy Council.

ON APPEAL

FROM HER MAJESTY'S COURT OF APPEAL FOR EASTERN AFRICA

BETWEEN

THE COMMISSIONER OF INCOME TAX . . *Appellant*

AND

H. BJORDAL . . . . *Respondent.*

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Case for the Appellant

RECORD.

1. This is an appeal from a Judgment and Decree of Her Majesty's Court of Appeal for Eastern Africa, dated the 28th April 1952, allowing an appeal against a Judgment and Decree of His Majesty's High Court of Uganda, dated the 29th June 1951, whereby it was ordered that the appeal of the Respondent from the decision of the Appellant for the year of assessment 1950 that Bjordal Mines Limited was not a Company in which the public was substantially interested within the meaning of Section 21 of the Income Tax Ordinance 1940 of the Uganda Protectorate be dismissed.

pp. 13–24.
pp. 6–9.

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2. Income tax is empowered in the Uganda Protectorate by the said Income Tax Ordinance, No. 8 of 1940 as amended by later Ordinances.

Section 7 of the said Ordinance imposes a charge to income tax upon the income for the year of assessment commencing on the 1st January 1940 and for each subsequent year of assessment of, *inter alia*, any person resident in the Protectorate accruing in, derived from, or received in the Protectorate and/or another East African territory in respect of specified sources of income.

Section 8 of the said Ordinance provides, *inter alia* and subject to qualifications which are not presently material, that tax shall be charged levied and collected for each year of assessment upon the income of any person for the year immediately preceding the year of assessment.

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Section 27 of the said Ordinance provides for the tax to be levied upon persons other than individuals at the rates specified therein and upon individuals at the rates specified in the Third Schedule to the Ordinance.

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Section 2 of the said Ordinance defines, *inter alia*, the expression " year of assessment " as meaning the period of twelve months commencing on the 1st January 1940 and each subsequent period of twelve months.

Section 21 of the said Ordinance No. 8 of 1940 in its original form read as follows :—

" 21. Where it appears to the Commissioners that with a " view to the avoidance or reduction of tax a company controlled " by not more than five persons has not distributed to its share- " holders, as dividend, profits made in any period ending after the " 1st January, 1939, which could be distributed without detriment 10 " to the Company's existing business, he may treat any such " undistributed profits as distributed ; and the persons concerned " shall be assessable accordingly."

By Section 5 of Ordinance No. 11 of 1943 the foregoing Section 21 was replaced so far as relates to profits made after the 31st December 1942, by a new provision which reads as follows :—

" 21. (1) Where the Commissioner is satisfied that in respect " of any period for which the accounts of a company resident " in the Protectorate have been made up, the profits distributed " as dividends by that company up to the end of the sixth month 20 " after the last date upon which its accounts for that period are " required by virtue of the provisions of the Companies Ordinance, " to be laid before the company in general meeting, increased by any " tax payable thereon are less than sixty per cent. of the total income " of the company ascertained in accordance with the provisions " of this Ordinance for that period, he may, unless he is satisfied " that having regard to losses previously incurred by the company " or to the smallness of the profits made, the payment of a dividend " or a larger dividend than that declared would be unreasonable, " by notice in writing order that the undistributed portion of 30 " sixty per cent. of such total income of the company for that " period shall be deemed to have been distributed as dividends " amongst the shareholders as at the said last date and thereupon " the proportionate share thereof of each shareholder shall be " included in the total income of such shareholder for the purposes " of this Ordinance :

" Provided that—

" (*a*) when the reserves representing accumulations of past " profits which have not been the subject of an order " under this subsection exceed the paid up capital of 40 " the company, together with any loan capital which is " the property of the shareholders, or the actual cost " of the fixed assets of the company whichever of these " is greater, this subsection shall apply as if instead of " the words ' sixty per cent.' the words ' one hundred " ' per cent.' were substituted ;

" (*b*) this subsection shall not apply to any company in " which the public are substantially interested or to a

RECORD.

" subsidiary company of such a company if the whole
" of the share capital of such subsidiary company is held
" by the parent company or by the nominees thereof.

" (2) For the purpose of this section a company shall be
" deemed to be a company in which the public are substantially
" interested if shares of the company (not being shares entitled to
" a fixed rate of dividend, whether with or without a further right
" to participate in profits) carrying not less than twenty-five per
" cent. of the voting power have been allotted unconditionally to,
10 " or acquired unconditionally by, and are at the end of the said
" period beneficially held by, the public (not including a company
" to which the provisions of this section apply), and if any such
" shares have in the course of such period been, in fact, freely
" transferable by the holders to other members of the public.

" (3) Where the proportionate share of any shareholder of a
" company in the undistributed profits of the company has been
" included in his total income for any year under the provisions of
" subsection (1) of this section the tax payable in respect thereof
" shall be recoverable from the company if the shareholder so
20 " elects by giving notice in writing to the Commissioner at any
" time before the due date for the payment of such tax. The
" Commissioner may serve a notice upon the company stating the
" sum so payable, and in default of payment the tax shall be
" recoverable from the Company in the manner provided by
" section 71 of this Ordinance.

" (4) Where tax has been paid in respect of any undistributed
" profits of a company under this section, and such profits are
" subsequently distributed, the proportionate share therein of any
" shareholder of the company shall be excluded in computing his
30 " total income.

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

" (6) Where any undistributed portion of the total income
" of a company has been deemed, by notice given under the
" provisions of this section, to have been distributed as dividends
" to the shareholders of that company, the company shall within
" twenty-one days of the date of the service of the said notice
40 " furnish each shareholder with a certificate setting forth the amount
" of the dividend deemed to have been distributed to that shareholder
" and the amount of tax which the company would be entitled to
" deduct from such dividend under the provisions of section 29
" of this Ordinance if such dividend had been paid.

" (7) (*a*) Where the period for which the accounts of a company
" are made up began on or after the 1st January, 1943, the provisions
" of this section shall apply to the profits of such period ;

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"(*b*) where the period for which the accounts of a company "are made up began on or before the 31st December, 1942, and "ended after that date, the provisions of this section shall apply to "the profits of such portion of the period as falls after such date."

3. By virtue of Section 118 of the Uganda Companies Ordinance extraordinary and special resolutions of a company require to be passed by a majority of not less than three-quarters of the members of the company voting upon them.

4. This appeal is concerned with the meaning and effect in relation to an assessment for the year of assessment 1950 by reference to the year of income 1949 of the new Section 21 so introduced by Ordinance No. 11 of 1943. 10

pp. 2–4.

5. The facts of the case at all material times appear from the Statements of Fact by the Respondent and Appellant, items 3 and 4 in the Record of Proceedings and the Articles of Association of Bjordal Mines Limited and are summarised below :—

(I) Bjordal Mines Limited (hereinafter referred to as "the "Company") was a limited liability company registered at Kampala, Uganda, on 25th March 1948 and has its registered offices in the Uganda Protectorate. 20

(II) The authorised capital of the Company was Shs.250,000 divided into 12,500 shares of Shs. 20/- each. The share capital was divided into 8,125 "A" shares of which 7,632 were issued and 4,375 "B" shares, all of which were issued. The "A" shares were not transferable without the consent of the directors. The "B" shares were freely transferable and had equal voting and dividend rights with the "A" shares.

(III) The Respondent was the holder of 7,632 "A" shares and 1,249 "B" shares in the company. The other shares were held by :— 30

(*a*) Sverre Hendrik Bjordal holding 3,121 "B" shares ;

(*b*) L. G. Appendin and four other persons each holding 1 "B" share.

(IV) The directors of the Company were the Respondent, Sverre Hendrik Bjordal (who is a brother of the Respondent) and L. G. Appendin. By virtue of Article 80 of the Company's Articles of Association the Company might by extraordinary resolution remove any director before the expiration of his period of office. By virtue of Article 84 the Respondent became the first chairman and managing director of the Company and was entitled to continue in those offices so long as he held not less than ten per cent. of the share capital. 40

(V) By an agreement dated 25th March 1948, the Respondent sold to the Company various mining titles and rights, then held by him, in consideration of the allotment to him of 12,000 shares in the

RECORD.

Company being shares of " A " and " B " class in such proportion as the Respondent should elect, all to be credited to the Respondent as fully paid up. The shares were allotted on the 19th April 1949, in the proportion of 7,632 " A " shares and 4,368 " B " shares.

(VI) By an indenture dated 19th April 1948, the Respondent sold 3,120 of the " B " shares so allotted to him to Sverre Hendrik Bjordal for the sum of £18,720.

(VII) On 13th April 1947 (Quare 1949) one " B " share was transferred by E. H. St. John Shelton to S. H. Bjordal.

10 (VIII) The only transfers of any of the shares are those set out in the preceding two sub-paragraphs.

(IX) The income of the Company for the year 1949 as computed for income tax purposes was Shs. 161,340/– of which no portion was distributed as dividends.

(X) The Appellant served notice under Section 21 of the Ordinance deeming 60 per cent. of that sum to have been distributed among the shareholders. This amounted to a sum of Shs. 96,804/– of which the Respondent's proportionate share was Shs. 71,602/–.

(XI) The Respondent was assessed in Notice of Assessment 20 No. 20831 for the year of assessment 1950 relating to the year of income 1949. The said Notice of Assessment included as income of the Appellant the sum of £3,580 in respect of dividends deemed to have been distributed as dividends among the shareholders of the Company under Section 21.

6. The Respondent disputed this assessment and thereupon the Appellant certified his decision under Rule 4 of the Income Tax (Appeals to the High Court) Rules 1944 to the effect that— p. 2.

(A) the Company was a company to which Section 21 (1) of the Ordinance applied and that the proviso (*a*) and (*b*) thereto 30 did not apply to the Company ; and

(B) the Company was not a company in which the public was substantially interested as defined by Section 21 (2) of the Ordinance.

7. The Respondent appealed to the High Court of Uganda against this decision of the Appellant. The appeal came on for hearing in the High Court (Pearson, J.) on the 31st May 1951 and on the 29th June 1951 the Court delivered judgment dismissing the appeal with costs. pp. 5–9.

The learned judge stated the question in issue as being whether Sverre Bjordal holds his shares as a member of the public within the meaning of Section 21 (2) of the Income Tax Ordinance, adding that Sverre Bjordal 40 is a director and the Secretary of the Company and is Hendrik Bjordal's brother and that Sverre Bjordal had bought the shares from his brother at a high premium. p. 7, ll. 1–4.

The learned judge set out the submissions of the Commissioner of Income Tax in support of the assessment that Sverre Bjordal is not a p. 7, ll. 5–12.

member of the public because (1) he is a brother of Hendrik Bjordal who has the controlling interest, 75 per cent., of the shares and voting power; (2) he is an officer of the Company; (3) the disposition of the shares to him by his brother on the formation of the Company indicates that Hendrik Bjordal retained control of them. He added that counsel for the Commissioner in these proceedings submitted that the Acts and Ordinances contemplate some shareholders who are not members of the public although he admits he cannot define them.

p. 7, ll. 13–19.

The learned judge went on to say that counsel for Hendrik Bjordal submits that the shareholders who are to be distinguished from the public 10 are such shareholders as have control by means of a holding of shares that gives them a preponderance of voting power; that this argument is based on Section 21 (6) of the United Kingdom Finance Act 1922; and that relationship and the acquisition of the shares from the brother are irrelevant, relying upon *Tatem Steam Navigation Co., Ltd.* v. *C.I.R.* [1941] 2 K.B. 194.

p. 7, ll. 20–34.

The learned judge took the view that the case of *Tatem* disposes of the arguments of counsel for the Commissioner on the first and third points.

p. 7, ll. 35–45.

He went on to say that the second point of counsel for the Commissioner, viz., that Sverre Bjordal was an officer of the Company impressed him as being more probable: that officers and directors of a company are 20 distinguishable from the public, but added that he could find nothing to distinguish directors and managers from the public in this sense.

p. 7, l. 46.

p. 8.

The learned judge went on to consider the submission of counsel for Hendrik Bjordal that those in control are to be distinguished from other shareholders, these latter being the public. The learned judge went on to say that in the Company in question, Hendrik Bjordal certainly has the controlling interest but raised the question as to whether more than one person jointly may have controlling interest and to put this question: Is Sverre Bjordal in control jointly with his brother? The learned judge answered this question by saying that Sverre Bjordal can be so long as he 30 co-operates with his brother but that, if he ceases to co-operate, Hendrik Bjordal outvotes him and takes all control out of his hands. The learned judge added that the company appeared to him to be just such a company as was contemplated by Scott, L.J., in the *Tatem* case referred to above: the control—voting power—is in the hands of two directors and they are

p. 9, ll. 4–6.

running it in their own interests just as if the company were a firm. He concluded by finding that the company is a company controlled by two directors and by upholding the decision of the Commissioner that the public is not substantially interested in it.

8. Hendrik Bjordal appealed to the Court of Appeal for Eastern 40 Africa against the judgment of the High Court of Uganda. The appeal came on for hearing on the 10th January 1952 (Nihill, P., Worley, V.-P. and Ainley, J.), and on the 28th April 1952 the Court delivered judgment

pp. 13–23.

allowing the appeal of Hendrik Bjordal with costs there and in the High Court of Uganda.

The salient points in the judgment of the learned Vice-President, who delivered the leading judgment, are as follows: He referred to the

pp. 13–16.

terms of Section 21 of the Ordinance and to the relevant facts as taken fom the statement of facts filed by the parties in the appeal to Pearson, J.

The learned Vice-President then added that counsel for both parties were agreed that the expression "the public" used in Section 21 (2) was used in contradistinction to certain persons or a class or classes of persons are impliedly excluded and that the task of the Court was to determine who is excluded. p. 16, ll. 22–26.

The learned Vice-President added that three views had been put before the Court. The contention of Hendrik Bjordal as Appellant was that the proper test is *de facto* control of the company; the person who is not a member of the public is one who can control the company by voting 10 power, i.e., who holds more than 50 per cent. of the voting rights. It is thus said of Hendrik Bjordal that the other shareholders are members of the public and since they hold more than the prescribed minimum of shares, the company is one in which the public are substantially interested. He added that the power of management of the company exercised by the board of directors is to be distinguished from the control exercised by Hendrik Bjordal who holds the majority of voting rights and can remove the directors at any time. p. 16, ll. 27–40.

The second view mentioned by the learned Vice-President, as that approved by Pearson, J., was that the company was controlled jointly by 20 Hendrik Bjordal and Sverre Bjordal and that the public were therefore not substantially interested in it. The learned Vice-President quoted a passage from the judgment of Pearson, J., and went on to add that in many companies the control is shared by more than one shareholder but that this is not the position with this company: Sverre Bjordal could only be jointly in control so long as he co-operates with Hendrik Bjordal. The learned Vice-President added that such precarious control could not suffice to take Sverre Bjordal out of the ranks of the public. p. 17, ll. 1–42.

The learned Vice-President then mentioned the third view put forward by counsel for the Commissioner, namely that both Hendrik Bjordal and 30 Pearson, J., had erred in accepting, as the test, control of voting power. The learned Vice-President went on to refer to Section 21 of the United Kingdom Finance Act 1922 and to certain text-book views on this point, adding that under the United Kingdom legislation a company such as this would be caught by the provision as to control by not more than five persons but that the repeal of the corresponding provision in Uganda in 1943 had opened a way of escape. p. 17, ll. 44–47. p. 18. p. 19, ll. 1–9.

The learned Vice-President then examined the argument of the Commissioner stating that the argument proceeded in two stages. The first is that the true and only test to be applied to the local section is 40 whether, looking at all the circumstances, the Court considers the public is substantially interested: this is a question of fact and the Court is not asked to lay down any general rule, but is merely asked to say on the facts of this case that Sverre Bjordal is not a member of the public: and that it would be a travesty of fact to hold that the company is one in which the public are substantially interested. p. 19, ll. 10–17.

The second stage of the argument for the Commissioner is that however difficult might be the application of that test in some cases, there is no difficulty in the present case because there is one class of persons which could never fall within the definition of the public, namely, the p. 19, ll. 18–34.

directors of a company. The learned Vice-President added that in matters such as the issue of a prospectus this clear distinction is no doubt drawn, but it seemed to him as capricious and precarious as the test of joint control postulated by the trial judge. The learned Vice-President asserted that Hendrik Bjordal, the Appellant in these proceedings, could, by the exercise of his voting powers, remove all or any of the present directors and replace them by some or all of the nominee holders of one share each, in which event Hendrik Bjordal and Sverre Bjordal would thus become members of the public by this test.

p. 19, ll. 27–29.

p. 19, ll. 35–47.

The learned Vice-President then reverted to the first stage of the argument of the Commissioner, shortly that the Commissioner or the Court should decide the question of who is or who is not a member of the public on the facts of each case but rejected that test. 10

p. 20, ll. 3–44.
p. 21, ll. 1–4.

The learned Vice-President posed the question : who is to be excluded from the category of the public, and said he could agree with counsel for Hendrik Bjordal that a person who holds more than 50 per cent. of the voting rights and so controls the company could never be treated as a member of the public for the purposes of the section but he went on to add that he was not persuaded that it necessarily followed that all the other shareholders automatically fall into the class of " the public." The learned 20 Vice-President did not propose to attempt to lay down any general rules but, approaching the matter from the point of view that Sverre Bjordal is *prima facie* a member of the public, he asked himself on what grounds he could be excluded from that category, adding that he had already indicated his reasons for rejecting his directorship and the test of joint control. He went on to reject the relationship between Hendrik Bjordal and Sverre Bjordal as being relevant. He said it was true that there did not appear to have been any issue of shares to the public in any real sense of those words but nevertheless he could not see any good reason in law for holding that Sverre Bjordal had ceased to be a member of the public 30 by reason of his acquisition of his shares and he would therefore allow the appeal.

p. 21, ll. 10–20.

Nihill, President, adopted the reasons given by Worley, Vice-President, adding that he recognised that the finding seems contrary to common sense but that the question was the construction of Section 21 of the Uganda Ordinance.

p. 22, ll. 5–19.

Ainley, J., stated that plainly it is the small group in control which is to be feared, and that when eventual control is widely spread or when the small group is restrained by the influence of substantial interests outside the group, the danger is lessened or disappears, adding that in 40 England, " the public " are obviously contrasted with the small defined group who are capable of taking control ; that in Uganda all companies are caught unless the public are substantially interested ; and that a substantial interest is defined as in England ; but that no reference is made to control nor is " the public " defined.

p. 22, ll. 24–47.
p. 23, ll. 1–22.

Ainley, J., agreed with the Vice-President that officers and directors can scarcely be regarded as excluded from the public. He added that the legislature must have meant this at least : that where a company is found

in the exclusive control of a small group of persons, the members of that group at any rate are not members of the public ; regarding that as the only interpretation which makes any sense at all of the section. He went on to say that " where it can be ascertained that a small group of persons "have joined forces and placed themselves in exclusive control of a company, "then I think it would be permissible to say that those within the group "were not members of the public." He added that the degree of concentration of control which is to exclude those who exercise it from " the public " must have been left by the legislature to the common sense of the Commissioner and the Courts. Thus where a managing director held 76 per cent. of the voting power little difficulty would be found in saying that the necessary degree of concentration had been reached and that the public did not hold 25 per cent. of the shares. Ainley, J., added that in this case Hendrik Bjordal holds 75 per cent. of the voting power and shares and for that reason and only for that reason Hendrik Bjordal must be excluded from the public. Ainley, J., concluded by saying that in the absence of provisions such as those contained in the English Act it seemed to him impossible to say that Sverre Bjordal is within the controlling group and that he thought unless one can place Sverre Bjordal there, he remains a member of the public, and that all one could say with certainty was that Hendrik Bjordal controlled the Company. He added that if it were possible to infer that the two brothers co-operated, the Company would be caught, but that there was insufficient before the Court safely and fairly to make the inference and that there appeared no reason to exclude Sverre Bjordal from the ranks of the public and that the public were substantially interested and that he regretfully concluded that the Company escaped the meshes of Section 21 and the appeal should be allowed.

p. 22, ll. 36–40.

p. 23, l. 1.

9. It is respectfully submitted that the judgments of Worley, Vice-President and Ainley, J., contain errors on the face of them which vitiate the reasoning which led to the conclusions arrived at by them. In particular, Worley, Vice-President, stated that Hendrik Bjordal, holding the majority of voting rights, could remove the directors at any time. This statement, it is submitted, is at variance with the provisions of Section 118 of the Uganda Companies' Ordinance referred to in paragraph 3 above and Article 80 of the Company's Articles of Association, inasmuch as under the said Article a director can be removed before the expiration of his period of office only by an extraordinary resolution which, under the said Section 118, requires a majority of not less than three-quarters of the members of the company. The same error is repeated in the judgment of Worley, Vice-President, at page 19, lines 27–9 of the Record. As regards the judgment of Ainley, J., at page 23, line 4 of the Record, the statement that Hendrik Bjordal held 75 per cent. of the voting power is incorrect inasmuch as he held only 8881 of the 12,007, issued shares. The position in truth and in fact was that Sverre Bjordal, by virtue of his holding 3,121 out of the 12,007 issued shares, was in a position to " block " any extraordinary or special resolution of the company ; could not be removed from his directorship without his consent ; and was therefore, in terms of ultimate control, an indispensable member of the small group consisting of his brother and himself in a position to control the company.

p. 16, ll. 37–38.

10. A Decree in accordance with the Judgment of the Court of Appeal was made on the 28th April 1952 and against the said Judgment and Decree this appeal is now preferred to Her Majesty in Council, the Appellant having been granted leave to appeal by an Order of the Court of Appeal dated the 28th April 1953.

p. 25.

11. The Appellant humbly submits that the decision of the Court of Appeal for Eastern Africa is wrong and should be reversed and that this Appeal should be allowed with costs both here and below for the following among other

REASONS

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(1) BECAUSE on the proper construction of Section 21 it is a question of fact whether or not any particular shareholder falls within the description " the public " and this question falls to be decided by reference to all the circumstances of the particular case and on that ground the finding of the trial Judge should be upheld.

(2) BECAUSE the directors of a company do not properly fall within the description " the public " in relation to that company.

(3) BECAUSE shareholders who, individually or as members of a group, control the affairs of a company by the exercise of both voting power and the power of administration do not fall within the description " the public."

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(4) BECAUSE S. H. Bjordal was a member of such a controlling group made up of himself and H. Bjordal who between them owned all the shares in the Company save five.

(5) BECAUSE H. Bjordal was a necessary member of the group controlling this Company in that his co-operation was essential to procure the passing of extraordinary or special resolutions by the Company.

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(6) BECAUSE S. H. Bjordal does not fall within the description " the public " in Section 21 on the facts of this particular case and having regard to the influence of his shareholding, his security of tenure as a director of the Company and his relationship to his brother H. Bjordal.

(7) BECAUSE the decision of the Court of Appeal for Eastern Africa fails to give due weight to the concluding words of the said Section 21 (2).

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(8) BECAUSE the reference thereunder to " other members " of the public " casts light to an extent not appreciated by the said Court of Appeal on the concept of " the " public."

(9) BECAUSE no other member of the public in ordinary parlance would be in any reasonable sense in a position in any way comparable to that of Sverre Bjordal having regard to his special position in the company in the respects mentioned above.

(10) BECAUSE the Judgment of Pearson, J., in the High Court of Uganda was right.

(11) BECAUSE the Judgments of the Court of Appeal for Eastern Africa were wrong.

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JOHN SENTER.

RODERICK WATSON.

No. 42 of 1953.

In the Privy Council.

ON APPEAL
from Her Majesty's Court of Appeal for Eastern Africa

BETWEEN

THE COMMISSIONER OF INCOME TAX . . *Appellant*

AND

H. BJORDAL . . . *Respondent.*

Case for the Appellant

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