1976, 8

IN THE PRIVY COUNCIL No. 12 of 1974

O N A P P E A L

FROM THE COURT OF APPEAL OF JAMAICA

B E T W E E N :

THE TRUSTEES OF SERAMCO LIMITED SUPERANNUATION FUND — Appellants

- and -

THE COMMISSIONERS OF INCOME TAX — Respondent

CASE FOR THE APPELLANTS

RECORD

1. This is an Appeal from a Judgment and Order of the Court of Appeal of Jamaica (Luckhoo Ag.P., Smith J.A. and Edun J.A.) dated 20th December 1973, allowing an Appeal by the Respondent from the Judgment of Grannum J. dated 7th March 1969 under which the Respondents' Appeal against a decision of the Income Tax Appeal Board dated 6th March 1967 was dismissed. By its decision the Income Tax Appeal Board unanimously allowed the Appeal of the Appellants against the decision of the Respondent dated the 9th February 1965 refusing the Appellants' claim for a refund of £37,368 under Section 63 of the Income Tax Law, Law 59 of 1954: (all section references in this Case are to the Income Tax Law, Law 59 of 1954 unless otherwise stated). p. 49 pp.31,41 p. 2

2. (i) The Appellants are the present Trustees of a Deed of Trust dated 16th January 1964 establishing a superannuation fund for the benefit of the male employees of Seramco Limited (hereinafter called "Seramco"). p.130

RECORD

p. 129

(ii) Seramco was incorporated on 28th August 1963. In October 1963 the directors of Seramco decided to set up a superannuation fund for its male employees. To this end they retained the services of Carp Corporation Limited ("Carp") to prepare a draft Trust Deed and Rules. On 18th December 1963 Carp sent these documents to the Respondent for approval under Section 25.

p.197-210

(iii) The tax consequences of approval of a superannuation fund under Section 25 are as follows :-

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(a) The income of the fund is exempt from income tax (Section 7(1)) and

(b) annual contributions to the fund are, by Section 25, permissible deductions in computing the profits or gains of the payers.

pp.197-199

(iv) On 21st December 1963, at a meeting of the directors of Seramco, the persons named in the draft Trust Deed had been appointed the first Trustees of the superannuation fund. On 29th December 1963 the Respondent had communicated his verbal approval Following this a meeting of the Trustees was held, on 30th December 1963, at which it was resolved that a superannuation fund be established on the terms contained in the draft Trust Deed and that contributions payable thereunder be made with effect from 1st January 1964. Bankers, auditors and solicitors of the fund were appointed, the chairman undertaking to obtain an engrossment of the Trust Deed and Rules for formal execution by the Trustees and to make the necessary arrangements to open a bank account.

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p.214

pp.197-210

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p. 143

(v) By letter dated 8th January 1964 the Respondent gave written approval to the Scheme with effect from 1st January 1964, (imposing certain conditions).

p. 130

(vi) On 16th January 1964 the Deed of Trust was engrossed and executed.

RECORD

(vii) In about March 1964 the Appellants were approached by the shareholders of a company called Seaforth Sugar and Rum Limited (hereafter called Seaforth) with a view to selling them all the shares in Seaforth. (Those shareholders are hereafter called "the Seaforth shareholders").

(viii) On 22nd June 1964 the Appellants entered into an Agreement (hereafter called the "Share-Sale Agreement") with the Seaforth shareholders whereby the Appellants agreed to buy all the issued shares of Seaforth for £407,934. Under this Agreement (Clause 2) share transfers were to take place forthwith and these were duly effected. Clause 3 of the Share Sale Agreement provided that the purchase price be paid by the following instalments:- p. 144 p. 145 p. 145

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£54,500 on or before 1st July 1964
£62,500 on or before 31st January 1965
£62,500 on or before 30th June 1965
£12,500 on or before 31st July 1965
£62,500 on or before 30th September 1965
£62,500 on or before 30th September 1965 (sic)
£62,500 on or before 31st October 1965
£62,500 on or before 30th November 1965
£28,434 on or before 31st December 1965.

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By Clause 7 the Vendors (the Seaforth Shareholders) were given an option (exercisable at any time before 31st December 1965) to re-purchase all the shares from the Appellants for £215,904. p. 148

(ix) At the date of the Share Sale Agreement Seaforth had a large fund of unappropriated profits.

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(x) At all material times the issued share capital of Seramco was £22. At the time of the Share Sale Agreement the superannuation fund amounted to about £400. The purchase price of the shares, less the amount of £215,904 (the price at which the shares could be re-purchased by the Seaforth shareholders) could only have come from the unappropriated profits of Seramco. In other words the Appellants and the Seaforth Shareholders were engaged in what is commonly called dividend stripping. p. 4. 1.10

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RECORD

p.169-172

(xi) In the course of a meeting of the directors of Seaforth held on 23rd June 1964 the following took place :-

p.171 l.8

(a) The transfers of shares from the Seaforth shareholders to the Appellants were approved,

p.171 ll.12-38

(b) Changes in the members of the board took place and in particular three of the Trustees of the superannuation fund were appointed as directors,

p.172 l.3, p.172 l.8, p.172 l.17

(c) A resolution to recommend that the 10 dividend of 48½ per cent gross be paid out of the undistributed profits of Seramco up to 30th September 1963 was opposed by three directors (representing the Seaforth shareholders) but passed by a majority of one.

p.183 l.15, p.184 l.25

(xii) On 23rd July 1964 the Respondent was asked by letter sent on behalf of Seramco and Seaforth to authorise the payment of a dividend by Seaforth to Seramco "without deduction of tax and to allow the amount which would have otherwise have been 20 deducted as a credit to the Company (Seaforth) in respect of its own income tax liability". (By the first proviso to Section 21(1) the Respondent is given power to authorise such a payment.) On 25th July 1964 the Respondent duly gave such authorisation.

p.185 l.11, p.186 l.2

(xiii) On 1st July 1964 the Annual General Meeting of Seaforth was held and the resolution to make a final dividend of 48½ per cent gross in favour of all shareholders appearing on the 30 list at 1st July 1964 was duly passed.

p.186 l.30

(xiv) On 2nd July 1964 the Secretary of Seaforth wrote to the Respondent informing him that dividends in the sum of £100,686 had been paid to the Appellants. The letter requested that Seaforth's 1964 Assessment be credited with £37,757.5 being the amount that would otherwise have been deductible from the dividends. In consequence of this letter the Respondent asked Mr. D.W.B.Myers, one of the Appellants, to see him: 40

RECORD

Mr. Myers did so. There followed a letter to Seaforth from the Respondent dated 28th July 1964 revoking the authority to make dividend payments to the Appellants without deduction of tax. — p.188 l.25

(xv) On 11th December 1964 a meeting of the Board of Directors of Seaforth was held. A dividend of £62,280 net, which represented a gross dividend of 48 per cent (being £99,648 less £37,368), paid out of the accumulated profits of Seaforth up to 30th September 1964 was proposed. This was again opposed by the three directors representing the Seaforth shareholders but passed by a majority of one. — p.189; p. 189 l.29; p. 189 l.35; p. 190 l.4

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(xvi) On 28th December 1964 an annual general meeting of Seaforth was held and the declaration of the above dividend was approved. — pp.190-191

(xvii) On 5th January 1965 Messrs. Myers, Fletcher and Gordon wrote to the Respondent on behalf of the Appellants making "a re-claim under Section 63....for the amount of £37,368 being the amount of tax withheld on the dividend". — p.192 l.22

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(xviii) On 9th February 1965 the Respondent wrote two letters :-

(a) to the Appellants withdrawing his approval of the superannuation funds with effect from 8th January 1964 and — p. 194

(b) to Messrs. Myers, Fletcher and Gordon for refusing the Appellants' claim for a refund of £37,368. — p. 195

3. There are three questions in issue in this Appeal :

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(i) Whether Section 63(3) gives no right of Appeal where, as here, the Respondent has refused to make a refund: this point is referred to in Paragraph 7 below as "the Right of Appeal, Section 63".

(ii) Whether or not the superannuation fund had been established under irrevocable trusts on 8th January 1964: this is referred to as "the Validity Point", Section 25(2).

RECORD

(iii) Whether Section 10(1) applies, on the basis that the transaction was artificial or fictitious, to enable the Respondent to disregard the transaction, this is referred to as "the Section 10(1) Point."

4. The Statutory Provisions relevant to these questions are set out at the end of this Case.

p.1

5. On 6th March 1967 the Income Tax Appeal Board allowed the Appellants' Appeal deciding the following points :- 10

(i) The Appellants did have a right of Appeal under Section 63 notwithstanding the fact that no repayment had been made by the Respondent;

p.10 1.35

(ii) The Respondent's purported withdrawal on 9th February 1965, of his approval of the superannuation funds with effect from 8th January 1964 was ineffective;

p.12 ls.13-17

(iii) Section 10(1) did not apply to enable the Respondent to disregard the relevant transactions on the basis that they were "artificial or fictitious"; 20

p.13 ls.10-17

(iv) The Appellants had not (as the Respondent had contended) acted beyond their powers in taking part in the management of Seaforth: they had not taken on the management of Seaforth;

p.13 ls.17-29

(v) The Appellants had not destroyed the bona fides of the application for approval of the superannuation fund.

p.13 ls.30-38

pp.13-17

6. The Respondent appealed, by Notice of Appeal dated 3rd April, 1967, to the Supreme Court. 30 The Appeal was heard by Grannum J. in Chambers and he gave a written judgment on 7th March 1969. The learned Judge dismissed the Appeal on the following grounds :-

p.37 ls.1-6

(i) Section 63 did not bar the Appellants right of Appeal;

(ii) The superannuation fund had been properly approved by the Respondent in his letter of 8th January 1964;

RECORD
pp.37-38
ls.13-21

(iii) As the Respondent could withdraw approval only prior to service of notice on the Appellants and as exemption from income tax could only cease as from the date of that notice, the Respondent's puported withdrawal of approval with effect from 8th January 1964 was ineffective;

p.39
1.28-34

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(iv) The transactions in question were neither artificial nor fictitious: accordingly Section 10 did not apply to enable the Respondent to disregard those transactions.

p.40 ls.
35-41

7. On 1st July 1969 the Respondent gave notice of Appeal to the Court of Appeal in Jamaica on the grounds therein set out. The Court of Appeal unanimously allowed the Respondent's Appeal.

pp.42-46

p. 49

The Right of Appeal, Section 63.

Each member of the Court of Appeal decided, against the Appellants that in the circumstances Section 63(3) gave no right of Appeal from the Respondent's refusal of the Appellants claim for a refund of tax.

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Luckhoo Ag.P. construed Section 63(3) as giving a right of Appeal only where the Commissioner found, on a claim duly made, that tax had been overpaid and had made repayment in a sum less than the amount claimed by the taxpayer.

pp.70-74
p.74 ls.9-14

Smith J.A. found nothing in the history of the Section supporting the conclusion that a right of Appeal existed where the Respondent had refused to make any repayment. As the second reason he decided, having compared Section 63(3) with other provisions in the Income Tax Law giving the right of Appeal that, if it had been intended that the right of Appeal under Section 63(3) should be in respect of the decision of the Commissioners, the word "decision" would have been used in the same way as it was used in Sections 15(3) and 53(1).

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pp.83-85

p.84
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p.85 1.20

p.86 ls.
12-17

RECORD

pp.86-87

Smith J.A.'s third reason was that, by virtue of the language of Section 63(1), there could be no right to a refunds, nor any question of an Appeal under sub-section (3), unless it had been "proved to the satisfaction of the Commissioner" that some refund was due: where as here, the Commissioner was not satisfied, there could be no question of an Appeal. He also concluded that, because the word "amount" when used for the second time in Section 63(1) plainly referred to a plus amount, that word could not include a nil amount when used in sub-section (3).

p.86 ls. 31-4

p.87 ls.1-25

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p.128 ls.5-8

Edun J.A. expressed the view, without giving reasons, that the Appellants had no right of Appeal.

It is submitted for the Appellants that the decision of the Court of Appeal on this issue can not stand. If correct, that conclusion leads to the absurd situation of the taxpayer who has a right of appeal when he gets a refund of a sum of money representing 95 per cent of his entitlement but no right of appeal when nothing is refunded.

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pp.83-85

As to the first reason expressed by Smith J.A. it is respectfully submitted that he has not properly appreciated the history of the legislation. Prior to 1954, the taxpayer had the right to apply to the Commissioner of Income Tax for a refund in a case where he was liable to pay some tax or no tax at all: (see Income Tax Law 1920 (No.39) section 25 and Income Tax (Amendment) Law, 1941 (No.6) section 30, (which sections are set out in the judgment of Luckhoo Ag.P.) Consequently he could apply to the Commissioner for a refund where the amount of tax payable was nil. When the right of appeal was granted to the taxpayer in 1954, it was clearly the intention of the legislature to grant a right of appeal from the refusal of the Commissioner to make a refund in any circumstance in which the application could be made to the Commissioners. As an application could be made to the Commissioner for a refund when no tax was payable by the taxpayer, this circumstance should be one of those in respect of which a right of appeal was granted.

pp.72-73

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RECORD

As to Smith A.J.'s second reason, it is submitted that this places undue emphasis upon differences of wording in Sections which have no necessary reference to each other and which were introduced into the Code at different times and, presumably, by different draftsmen.

pp.85-86

The approach of Smith J.A. in this third reason puts too much weight, it is submitted, on the phrase "proved to the satisfaction of the Commissioner". In the Port of London Authority v. Commissioners of Inland Revenue 12 Tax Cas. 122 Scrutton L.J. said, at page 143,

pp.86-87

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> "that the Act instead of using the phrase "if the Commissioners decide that", or "if it is proved before the Commissioners", uses the phrase "if it is shown to the satisfaction of the Commissioners", does not seem to me enough to make their decision final in a case where no satisfactory reason should be given why their decision should be final....:

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that remark is, it is submitted, equally true in the present case. It appears most illogical to attempt to distinguish between the Commissioner's decision as to the amount of an excess payment (which is plainly appealable) and the existence of an excess payment (which, on Smith J.A.'s analysis is unappealable).

It is further submitted that the fact that the first reference to "amount" in Section 63(1) includes a nil amount (a proposition apparently accepted by Smith J.A. on page 87), provides strong support for the Appellants' contention that the word "amount" in sub-section (3) equally includes a nil amount.

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The Validity Point, Section 25(2)

Luckhoo Ag.P. decided, on the first limb, in favour of the Appellants, Grannum J's conclusion of fact that there was a trust in existence on 8th January 1964 (the date of the Respondent's letter giving approval) should stand. On the second

pp.57-61

p.60 ls. 1-10

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RECORD

pp.61-66 limb, i.e. whether the fund was established under irrevocable trusts, he decided against the

p.62 l.37 - p.63 l.6 Appellants. The effect of Rule 12 was to make the trust revocable. Because the Rule directed that the residue be paid over to the employer and gave the Trustees no discretion over the application of that residue when the fund was wound up in consequence of the employer ceasing to make

p.55 ls.7-10 contributions, there was a power of revocation reserved to the employer. 10

pp.75-80 Smith J.A. decided in favour of the Appellants on both limbs. He decided that the Respondent's

p.79 l.6-24 purported approval of 8th January 1964 was valid. Approval under Section 25 was not invalidated on the grounds that the Deed of Trust had not been executed by the date of approval. Section 25(2)(a) did not confine funds capable of approval to those established under Trust Deeds: and Rule 4(1) and Condition 1 in the Schedule 2, of the Income Tax (Superannuation Funds) Rules 1955 were ultra vires 20 in so far as they purported to restrict the irrevocable trusts to trusts created by deeds. On the evidence, irrevocable trusts had been created in consequence of the meeting of 30th December 1963 and the fund had been established as from 1st January 1964. Accordingly, when the Respondent gave written approval on 8th January 1964, the fund had already been established under irrevocable trusts. Smith J.A. further decided that, as the draft submitted for approval was executed without 30 alteration, the Respondent's approval of the draft extended to the Deed of Trust to make the fund established under the Deed an approved fund under Section 25.

p.80 ls.1-23 On the second limb Smith J.A. decided that the trusts were irrevocable and accordingly, satisfied the requirements of Section 25(2). A provision such as Rule 12 might make the fund and trusts terminable, but this provision would not make the trusts any the less irrevocable up to the 40 time of termination.

Edun J.A. expressed no opinion on this issue.

On this issue the Appellants respectfully adopt the reasoning of Smith J.A. at pages 75-80. The Appellants will further argue that the word "irrevocable" when used in relation to a settlement should be taken to have the technical and precise meaning which it bears in conveyancing (see the decision of Lord Greene M.R. in Jenkins v. Commissioners of Inland Revenue 26 Tax Cas. 265 at page 281); the fact that a settlor is able to bring a settlement to an end, even where (as in the Jenkins case and as here in consequence of Rule 12) he will restore the settled funds to himself as a result, will not prevent the settlement from being irrevocable.

RECORD

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Section 10(1), Artificial or Fictitious Transactions

On this issue the Court of Appeal was divided; only Smith J.A. deciding for the Appellants.

Luckhoo Ag.P. concluded that the Share-Sale Agreement was not an ordinary commercial transaction of sale and purchase with an option for re-purchase, it was really a device adopted to achieve the fiscal ends of enabling the Seaforth shareholders to receive as capital an amount which, if otherwise received by them, would have come from profits exigible to tax and of enabling the Appellants to make a gain of £8,000. As such a device the transaction was artificial and the Respondent was entitled under Section 10(1) to disregard it.

pp.66-70
p.69 ls. 11-14
p.68 ls. 36-48
p.69 ls. 40-48

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Smith J.A. decided that, as far as the Appellants were concerned, the transaction was artificial: this did not, however, justify the Respondent's refusal of repayment. It was artificial in a limited sense only: that was, in so far as it had been claimed to have been an investment by the Appellants under the Rules of the fund. Section 10(1) could not be applied to the Appellants because there was no tax liability - either of the fund or of the Appellants qua Trustees - which could, under the Section, have been said to have been affected by the transaction.

pp.87-94
p.93 ls. 11-12
p.93 ls. 35-39
p.93 ls. 40-50

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Edun J.A. decided that the proper analysis of the transaction was that, inter alia, the Share-Sale

pp.94-128

RECORD
p.126 ls. 43-50 p.127 ls.1-4 p.128 ls.2-3

Agreement was artificial or fictitious, the Seaforth Shareholders never parted with beneficial ownership of the shares and the dividends never became the property of the Appellants: accordingly the Respondent was entitled to disregard it.

p.40 1.40

p.63 1.40, p.119

p.40 ls. 11-14

The Appellants submit that the transaction was neither fictitious nor artificial. The Judge in Chambers found this as a fact. He did not misdirect himself as to the legal meaning of those words. The meaning which he gave to those words was in no significant respect different from that adopted by Luckhoo Ag.P. and Edun J.A. In any event, if the definitions of "artificial" and "fictitious" given by Luckhoo Ag.P. are applied to the primary facts as found by the Judge in Chambers, the transaction could not be described as artificial or fictitious. The transaction was not one type of transaction fashioned to resemble another type of transaction. It was a purchase and re-sale of shares and was found as a fact to have been a real transaction for the purchase and resale of shares. It is respectfully submitted the conclusion of Luckhoo Ag.P. at page 69 constitutes a departure from his own (correct) definition of the word "artificial".

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It is further submitted that, even if the transaction were artificial, Section 10(1) could have no possible application to the Appellants in the present case. Its scope is limited to "any transaction which reduces or would reduce the amount of tax payable"; and the remedy which it prescribed is that the persons concerned should be "assessable accordingly". These words are wholly inappropriate to deprive a body which is exempt from tax of its statutory right to a tax repayment. The Appellants adopt the reasoning of Smith J.A. in this respect.

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p.93 ls. 41-50

If the view be taken that exempt bodies should not participate in dividend stripping transactions, the appropriate remedy lies, it is submitted, in legislation and not in an attempt to bring the facts of the matter within the scope

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of a provision which clearly was not intended to cover them. The Legislature has, in fact, adopted the appropriate remedy, for dividend stripping transactions entered into on or after 11th June 1970 by the inclusion, in the Code, of Section 10B as a result of the enactment of the Income Tax (Amendment) Act 1970. Reference will, in this context, be made to the speech of Lord Wilberforce in Ransom v. Higgs [1974] 1 W.L.R. 1594 pp. 1613H and 1614A-B.

RECORD

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8. The Appellants humbly submit that the decision of the Court of Appeal is wrong and ought to be reversed and that this Appeal should be allowed with costs here and below for the following among other

REASONS

(1) BECAUSE the Appellants are entitled under Section 63 to appeal against the Respondent's refusal to make a refund.

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(2) BECAUSE the superannuation fund was validly established under irrevocable trusts on 8th January 1964.

(3) BECAUSE Section 10(1) does not apply to enable the Respondent to disregard the transaction or any part of it; nor does it deprive the Appellants of the right to a refund of tax.

(4) BECAUSE the decision of Grannum J. was correct.

MICHAEL NOLAN
R. MAHFOOD
S.J.M. OLIVER

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STATUTORY PROVISIONS

1. The Law may be cited as the Income Tax Law, 1954.

2. (1) In this Law unless the context otherwise required -

....

"approved superannuation fund" means a superannuation fund approved under this Law or under the Income Tax Law before its repeal by this Law;

....

7. There shall be exempt from tax - 10

....

(1) the income of an approved superannuation fund:

Provided that this provision shall have effect subject to the provisions of Section 25;

....

10. (1) Where the Commissioner is of opinion that any transaction which reduces or would reduce the amount of tax payable by any person is artificial or fictitious, or that full effect has not in fact been given to any disposition, the Commissioner may disregard any such 20 transaction or disposition, and the persons concerned shall be assessable accordingly.

....

25. (1) Subject to the provisions of this Law and to any regulations and rules made thereunder any sum paid by an employer or employed person by way of contribution towards an approved superannuation fund shall, in computing profits or gains for the purpose of an assessment to income tax, be allowed to be

deducted as an expense incurred in the year in which the sum is paid:

....

(2) The Commissioner may approve any superannuation fund for the purposes of this Law, but he shall not, except as hereinafter provided approve any fund unless it is shown to his satisfaction that -

(a) the fund is a fund bona fide established under irrevocable trusts in connection with some trade or undertaking carried on in the Island by a person residing therein;

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....

(c) the employer in the trade or undertaking is a contributor to the fund;

....

Provided that the Commissioner may, if he thinks fit, and subject to such conditions, if any, as he thinks proper to attach to the approval, approve a fund, or any part of a fund, as a superannuation fund for the purposes of this Law -

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(i) notwithstanding that the rules of the fund provide for the return in certain contingencies of contributions paid to the fund; or

....

63. (1) If it be proved to the satisfaction of the Commissioner that any person for any year of assessment had paid tax, by deduction or otherwise, in excess of the amount with which he is properly chargeable, such person shall be entitled to have the amount so paid in excess refunded and the Commissioner shall make the refund accordingly. Every

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claim for repayment under this section shall be made within six years from the end of the year of assessment to which the claim relate.

....

(2) Except as regard sums repayable on an objection or appeal, no repayment shall be made to any person in respect of any year of assessment as regards which such person has failed or neglected to deliver a return, unless it is proved to the satisfaction of the Commissioner that such failure or neglect to deliver a return did not proceed from any fraud or wilful act or omission on the part of such person. 10

(3) Any person who objects to the amount of any repayment made by the Commissioner may appeal to the Revenue Court in the same manner as an appeal may be made against an assessment.

No. 12 of 1974

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O N   A P P E A L

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B E T W E E N :

THE TRUSTEES OF SERAMCO LIMITED SUPERANNUATION FUND — Appellants

- and -

THE COMMISSIONER OF INCOME TAX — Respondent

CASE FOR THE APPELLANTS

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