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INCOMING FAX

THE FIJI COURT OF APPEAL

Civil Jurisdiction

Civil Appeal no. 44 of 1985

Before the Hon. Sir Clinton Roper, Judge of Appeal and the

Hon. Mr. Justice Mishra, Judge of Appeal and the

Hon. Sir Barry O'Regan, Judge of Appeal Thursday the 5th day

March, 1987 at 9.30 a.m.

Between :

COMMISSIONER OF INLAND REVENUE Appellant

AND

PROPERTY NOMINEES LIMITED Respondent

Mr. S.M. Shah &amp; Mrs. Madhuri Sharma for Appellant

Mr. G. Davies QC and Mr. P. Knight for Respondent

Roper J.A.

This is an appeal against the decision of Kermode J in which he allowed an appeal by the Respondent against a decision of the Court of Review concerning the sale of certain land at Nadi by the Respondent.

These are the facts, which are not seriously in dispute: on the 7th December 1971 Mr. G.L. Gray, a Melbourne Solicitor, concluded negotiations on behalf of Trade Winds Limited, a company incorporated in the New Hebrides, for an option to purchase a block of land (19 acres 32 perches) situated some two miles from Nadi Airport and close by Nadi Town. Trade Winds is a Gray family company over which Gray himself had effective control; and the property in question was owned by Keshra Chandra Verma as Executor of his Father's Estate. The option agreement, executed on the 7th

... provided for a purchase price of \$F120,000, with right of purchase to be exercised by the 31st March 1972. There was provision for extension of the term on a sum of \$4000 which was presumably exercised as the option was not taken up until the 29th April, 1972. It is significant to the case that the option contained a warranty by Keshra Verma that "The said land may be used for the construction of a hotel and motel".

The option Agreement provided that it could be exercised by Keshra Verma or its nominee and in the result Gray, as Trade Nominee, exercised the option and entered into an agreement for sale and purchase with Keshra Verma on the 29th April, 1972. The agreement was executed by Gray "as Trustee for a Company to be incorporated in Fiji under the name of Property Nominees Limited". The Respondent company was incorporated on the 10th July 1972 with a share capital of \$1000 divided into 1000 \$1 shares of which Gray held one share. Gray was an employer or partner in his law firm, R.M. Smith, the Respondent acted as trustee for members of the Gray family.

The first meeting of directors of the Respondent (Gray & Keshra Verma) was held on the 17th July 1972 when the Company confirmed the agreement of the 29th April 1972. Keshra Verma encountered some problems in giving a clear title with the Respondent so that the transfer of the property to the Respondent was not registered until the 19th April, 1973.

On the 27th November 1973 the Respondent sold the whole property to Gray "as Trustee for a company or syndicate to be formed" for \$410,000. The property was actually transferred to Gray himself on the 11th December 1973.

The Respondent did not file a return of income for the year ended 31st December 1973 as it considered that it had earned no profit. But in November 1977 the Commissioner issued a default assessment for that year claiming tax of \$31,666 on the Respondent's return that the estimated profit on the sale of the Nadi land was \$95,000. The Respondent objected to this assessment and filed a return for 1973 showing a loss of \$11,198. The Commissioner countered by issuing a fresh assessment in June 1977 claiming tax of \$93,899 on the basis of a chargeable income of \$281,698. The Respondent lodged an objection to the assessments and three years later, on the 4th November, 1980, the Commissioner gave notice that the objections had been "Wholly disallowed".

The Respondent duly appealed and the matter came before the Board of Review, the hearing extending over some days. Evidence was given for the Respondent by Gray, a Surveyor

Biggs who had been employed by the Respondent to prepare and make planning applications for use of the land as a hotel site, and a Mr. D.A. McIlrath, a Director of a hotel company in Fiji, who gave evidence of the difficulties facing those who sought finance for hotel development at the relevant time.

The question facing the Court of Review was whether the Respondent was caught by proviso (a) to S11 of the Income Tax Act (Cap 201) which reads : -

"Provided that, without in any way affecting the generality of this section, total income, for the purpose of this Act, shall include -

- (a) any profit or gain accrued or derived from the sale or other disposition of any real or personal property or any interest therein, if the business of the taxpayer comprises dealing in such property, or if the property was acquired for the purpose of selling or otherwise disposing of the ownership of it, and any profit or gain derived from the carrying on or carrying out of any undertaking or scheme entered into or devised for the purpose of making a profit; but nevertheless, the profit or gain derived from a transaction of purchase and sale which does not form part of a series of transactions and which is not in itself in the nature of trade or business shall be excluded".

The proviso specifies three situations where a profit or gain from dealings in real property will raise a liability for tax, namely, where the business of the taxpayer comprises dealing in property, where the property was acquired for the purpose of sale or other disposition and where the profit or gain is derived from the carrying out of an undertaking or scheme entered into or devised for the purpose of making a profit.

Before the Court of Review it was the Commissioner's case that the Respondent came within all three limbs of the proviso; however, the Court had no hesitation in concluding that the first limb had no application, there being no evidence that the Respondent's business comprised dealing in land. The Court of Review did however find that the Respondent was caught by the second and third limbs. On appeal Kermode J held that the evidence did not support a finding that the Nadi land had been acquired for the purpose.

of resale; or alternatively, if it could be said that there were two purposes the evidence did not support resale as the dominant one. He further concluded that the Respondent was not caught by the third limb of the proviso. As there is no appeal by the Commissioner against that finding nothing more need be said on that issue.

Before dealing with the specific grounds of appeal it is helpful to consider, in more detail the actions of Gray and the Respondent from the time when the option was first taken up in December 1971 until the sale of the land to Gray by the Respondent two years later. In evidence Gray maintained from the outset that the property had not been acquired with the sole or dominant purpose of resale, but with the purpose of developing a hotel, either alone if finance could be raised, or as a joint venture with a financier, and that the reason the property was ultimately sold was because finance or a backer could not be found.

It is significant as we have said, that the option of the 7th December 1971 contained a warranty that from a Town Planning point of view the land was available for use as a hotel or motel site. Within days of obtaining the option Gray was in touch with a New Zealand firm specialising in hotel and motel furnishings and had advertised in a Hong Kong paper seeking "developers for equity participation" in the hotel venture, or finance on first mortgage. By the 22 February, 1972 Gray had obtained a projected capital commitment and trading result report from a firm of Melbourne Accountants, which was made available to those who had shown an interest in the venture; and in a report of the 24th March the members of the Gray family trust were given details of the proposed hotel scheme. On the 29th March an application was made to the Town Planning Officer in Suva seeking confirmation that the land would be available for hotel purposes; and a firm of Architects in Suva was requested to do what it could by way of representations to ensure that the land was not zoned as a green belt, there having been some suggestion to that effect. On the 29th April the agreement for sale and purchase was signed and the search for finance or a partner in a joint venture continued. On the 10th July 1972 the Respondent was incorporated, and on the 17th adopted the agreement.

On the 31st August 1972 Gray wrote this letter which he accepted in evidence demonstrated a change of attitude regarding the Respondent's future involvement with the land and the hotel project : -

William Charody,  
President,  
Langham Constructions Pty. Ltd.,  
Kandos Street,  
EDMUNDS N.S.W. 2068

Mr. Charody,

Nadi Hotel

Refer to our telephone conversation on the 28th inst.

We have a Company called Property Nominees Limited in Fiji which owns a freehold 19 acre hotel site in Queens Road midway between Nadi and Nadi Airport. This would be without doubt the best site for a major hotel in the entire area.

An application for the site to be zoned for hotel development has been approved by the Town Planning Board of Nadi and the Board has also approved plans for a hotel of 100 bedrooms and all facilities. The construction of a large staff block separate from the hotel has also been approved and it occurred to me that if you were to build this first it would provide some staff accommodation for personnel engaged on your road contract. I had discussions with Mr. Eric Budzynski, your Executive Engineer, when I was in Suva recently and he thought the idea was a good one and suggested contacting you.

Leighton Contractors Limited from Sydney first approached me about our site with the intention of building the hotel to house staff on the assumption that they would be the successful tenderer for the road contract. Leighton's are still interested and Mr. Graham French their Australian Development Manager is doing a feasibility study at the present stage. However, the project would seem to be of greater benefit to the Company constructing the road because both projects could have joint administrative personnel and the occupation of the hotel by your personnel in the first couple of years would supplement the occupancy rate while the hotel was achieving maximum occupancy.

We have had the benefit of the advice of Mr. Colin Thompson who is the Victorian Manager for Travelodge and who was the General Manager for Travelodge Fiji during the construction of its four hotels at Suva, Nadi, Savu Savu and Tavenuni. This must be kept in strictest confidence, at this stage, but Mr. Thompson and his wife are anxious to return to Fiji and

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ould be available to be Manager of the hotel if the special inducement is sufficient. He has studied the economic projections contained in the enclosed submission and believes them to be conservative. I enclose two copies of the submissions along with two copies of sets of plans which have been approved.

You can see we have done a great deal of work on the project over the last nine months and the price asked for the freehold site is \$A380,000, equal to \$20,000 an acre. Compensation for the Architect who drew the sketch plans would be required to an extent of \$10,000 should he not be named as Architect for the project.

We have had major land dealings before in Fiji and sold the land on the corner of Victoria Parade and MacArthur Street on which a nine storey building is currently being constructed by Centaur Properties Limited of Sydney. Mr. John Loxton of Centaur Properties Limited would advise you that he was most satisfied with his Company's purchase and the representations made to him. Mr. Loxton's Company is now interested in office buildings and factories and before we did not offer them the hotel.

That the hotel site is ready for development my Company has been keen to sell the project as soon as possible and naturally you would wish to have an inspection prior to making your decision. I would therefore be available at your expense to visit Fiji with you or one of your Executives at your convenience within the next few weeks.

I look forward to the pleasure of meeting you.

Yours sincerely,

NICK GRAY

He claimed that this change of plan was forced on him because of the inability to obtain finance and his involvement in the purchase of a property in Melbourne and other commitments. However, the Melbourne property was sold at a profit which Gray said enabled him to return to

hotel development project. Further attempts were made to obtain finance or a partner with finance. He received enquiries from people interested in joint participation but they came to nothing.

In February 1973 Gray obtained a valuation of \$30,000 per acre for the land, and a few months later was negotiating to purchase his shares in the Respondent for \$500,000.

In June or July 1973 Gray learned that the land was to be incorporated in Nadi Town so that it had subdivisional potential and at the end of July he instructed surveyors to prepare sketch plans for a subdivision. In October Gray decided to purchase the land from the Respondent for \$500,000. The land was duly subdivided and after some lots had been sold Gray sold his interest for an undisclosed sum.

Turn now to the grounds of appeal and the first two, which can be considered together read: -

THAT the Learned Supreme Court Judge erred in law in holding that the Court of Review, in ruling that the Respondents had failed to prove that its dominant purpose on acquisition of relevant property was not one of disposition, acted upon a view of the facts which could not reasonably be entertained;

THAT the Learned Supreme Court judge erred in law in holding that relevant profits were not taxable as proceeds of sale of property acquired for purposes of disposition, within the second limb of proviso (a) to section 11. Income Tax Act:

The onus was on the Respondent to show on the balance of probabilities that the Nadi land was not acquired with the sole or dominant purpose of resale and it could meet this onus by showing that resale or disposition was not a purpose of acquisition, or that it was not the dominant purpose because another inconsistent purpose influenced the acquisition in an equal or greater degree or because the taxpayer had no firm view as to what he would do with the property after acquisition, with resale being but one of a number of possibilities.

Having considered the evidence relating to the second limb the Court of Review summarised its conclusions in this way:

In the result, therefore, although I am satisfied that Gray started off with the purpose of developing a hotel project, by the time the appellant took over his contract with Keshwa Verma Gray had two purposes, one of developing a hotel project and one of selling the project as soon as he had developed it to saleable proportions. So far from being convinced that the appellants' dominant purpose was to develop a hotel project, I am inclined to the belief that when it acquired the Nadi land it was for the purpose of selling or otherwise disposing of it. At all events the appellant has failed to convince the Court, as a matter of belief, that its dominant purpose was not one of sale".

It would appear from the last sentence of that passage that the Court proceeded on the basis that there was a presumption that the taxpayer had acquired with a sole or dominant purpose of re-sale which the taxpayer had to refute, but that is not the law. (See *Macmine Pty Limited* and *Federal Commissioner of Taxation* 9 ATR 638) ).

On appeal to the Supreme Court that Court was only justified in interfering with the judgment of the Court of Review if it had acted without evidence, or upon a view of the facts which could not reasonably be entertained, or had misdirected itself in law.

In the instant case Kermode J concluded that the Court of Review had taken a view which could not reasonably be entertained if the whole of the evidence had been given proper consideration. He further concluded that the Court had erred in attributing to the Respondent purposes which were those of Gray personally. In other words the Court of Review did not distinguish between actions taken by Gray on his own behalf and those taken on behalf of the Respondent.

It is true, as Mr. Shah submitted that there were elements in the Respondent's evidence, which was primarily the evidence of Gray, which supported the view that the Respondent acquired the property for the purpose of sale, but when the whole of the evidence is considered, and Gray's role at the various times properly interpreted, we are satisfied that Kermode J was right when he said : -

"In my view the Court did err in considering the second limb and it should have held on the evidence that the land was not acquired for the purpose of resale and that if there was more than one purpose the dominant one was acquisition of the land for development and not resale.

The transaction was not, in my view, caught by the second limb."



mass of correspondence produced at the hearing indicated that Gray pursued the hotel project with vigour and indeed resale was the dominant purpose there was really no point in incorporating the Respondent, the matter could have been done with Trade Winds. However, the Court of Review's most serious errors were first, in equating Gray's attempts to obtain finance or equity participation for the hotel project with an intention to sell, and secondly in concluding that the Respondent's purpose on acquisition was to resell from the fact that Gray tried to sell his own shares in the Respondent. Gray's attempted share deal was irrelevant to the inquiry and the involvement of third parties on an equitable basis does not amount to a sale or disposition.

to conclude that the first two grounds of appeal fail.

The third ground of appeal reads : -

"THAT the Learned Supreme Court Judge erred in law in holding that the material time for consideration of the relevant purpose was as at 29th April 1972, being the date of entry by one Gray into an "Agreement" as Trustee for the Respondent, a company not then having a legal existence;"

On this ground the Appellant relies on this passage in the judgment : -

"I would have thought on the facts in this case that in seeking to determine the purpose for which the land was acquired by the appellant it was not when the company adopted that agreement but when Gray as trustee for the appellant entered into the binding agreement that had to be considered."

We see no merit in this ground of appeal. In the result Lord J did not decide the case on the basis of an intention held by Gray earlier than the Respondent's adoption of the agreement and indeed in this passage he appears to have made a finding that the land was acquired for "development purposes" at the time the agreement was adopted : -

"On the unusual facts of this case the Court should not have held that the purpose for which the land was acquired had to be determined at the time the Company formally adopted the agreement. It should, in my view, have held that the purpose was that of Mr. Gray when as trustee for the appellant company, later to be formed, he entered into a binding agreement to acquire the land for the appellant. His purpose was to acquire the land for development purposes and that the purpose still existed when the company adopted the agreement".

ground four reads : -

"THAT the Learned Supreme Court Judge erred in Law in attaching significance to findings as to Respondent's purpose of building an hotel, same being consistent with building for resale;

The point the Appellant was making in this ground of appeal was that acceptance that the Respondent held with the purpose of building a hotel did not preclude the Respondent from having a concurrent and dominant purpose of disposing of the land in an improved condition. So far as we can see it was never put to Gray in cross examination that the Respondent intended to sell the land after the hotel was built; or whether the land would be disposed of by sale or the hotel project by a sale of shares. Apart from that the evidence is not consistent with an intention to sell the land after the hotel was built.

(As an aside we might say that by the time the agreement was adopted by the Respondent the situation was so confused and uncertain that the Respondent could be forgiven for holding the view that it just did not know what it was going to do with the land Gray had committed it to. In the result it disposed of it for a purpose which neither Gray nor the Respondent could have had in contemplation when the agreement was adopted - namely, subdivision).

We see no merit in this ground.

This is the fifth ground : -

"THAT the Learned Supreme Court Judge erred in law in failing sufficiently to advert to the issue of the credibility of the Respondent's principal witness, a matter peculiarly within the purview of the Court of Review;"

We believe it correct to say that at no stage did the Court of Review hold that Gray was dishonest or untruthful, although it is fair to say that because of its conclusions it must have rejected parts of his testimony. However, the Court's view of Gray as a witness of truth must have been influenced by its incorrect approach to the facts and the law. In short, the Court of Review held against Gray on a mistaken basis, at least in part.

There was no suggestion that the mass of documentary evidence produced was fabricated and Gray's evidence appears consistent with it.

We reject that ground.

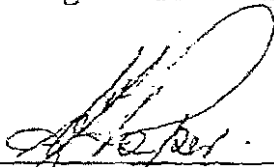
final ground of appeal reads : -

THAT the Learned Supreme Court Judge erred in law in attaching significance to alleged plans by Respondent to sell its shares rather than land held by it, such plans never being implemented and being indicative only of general speculative intent.

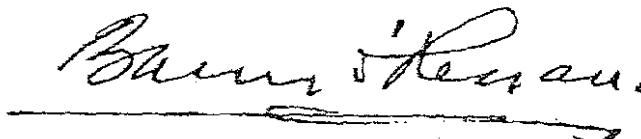
This ground really touches the substance of the case but not in the way suggested by Mr. Shah. It was the Court of Appeal rather than Kermode J which attached significance to Gray's proposed sale of shares and in so doing failed to distinguish between the land owned by the Respondent and the shares owned by Gray and his family and as a result confused the purpose and intentions of the company with those of Gray in his personal capacity.

That ground fails.

The appeal is therefore dismissed with costs to the Respondent to be fixed by the Registrar if not agreed.

  
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