IN THE FIJI COURT OF APPEAL

2014

CIVIL JURISDICTION

CIVIL APPEAL NO. 23 OF 1993
(High Court Civil Appeal No. 16 of 1991)

BETWEEN:

THE COMMISSIONER OF INLAND REVENUE — **APPELLANT**

-and-

BARRIE NELSON SWEETMAN — **RESPONDENT**

Mr. Ian Blakeley and Mr. A. Bale for the Appellant
Mr. M. Johnson and Mr. R. A. Smith for the Respondent

Date of Hearing : 4th May, 1994
Date of Delivery of Judgment : 12th May, 1994

JUDGMENT OF THE COURT

The appeal in these proceedings is against a judgment of the High Court allowing an appeal taken, pursuant to section 69 of the Income Tax Act (Cap.201)("the Act"), against a judgment of the Court of Review and setting it aside. The Court of Review had dismissed an appeal by the respondent in these proceedings ("the taxpayer") against a decision of the appellant in these proceedings ("the Commissioner") disallowing the taxpayer's objection to the assessment of his income during the 1984 taxation year.

In the Court of Review the parties lodged a statement of agreed facts which was in the following terms:-

"1. *The appellant and taxpayer, Barrie Nelson Sweetman, is a Barrister and Solicitor in Fiji. He practices law in Suva with the firm of Munro Leys and Company. One of his two partners in the firm, Dennis Julius Williams has lodged an identical appeal to this Court, action number 4 of 1989, and has agreed by his letter of 30th March 1990 to be bound by the decision in this case.*

2. *The appellant was in partnership with, amongst others, one Michael Desmond Benefield from 1975 until 31st July 1984. Throughout this period, the usual responsibilities of partnership were accorded to each and every member of the firm. Mr Benefield was then dismissed from the firm, subsequently struck off the roll of solicitors and was convicted by the High Court of Fiji for the offence of fraudulent conversion of a sum in excess of $13,000 from two trust accounts of the afore-mentioned firm.*

3. *The taxpayer and his remaining partners decided to reimburse their clients for the misappropriated funds. In 1984, the payments were shown as a deduction from assessable income in the firm's profit and loss account on the basis that the reimbursement payments had been made "wholly and exclusively" for the purpose of their profession in terms of section 19(b) of the Income Tax Act Cap.201.*

4. *The Commissioner of Inland Revenue disallowed this deduction, included the payments as assessable income and taxed the increased profit accordingly. Notice of assessment was issued on 16th November 1988 and the taxpayer objected on 12th January 1989. The Commissioner disallowed the objection on 29th May 1989 and the taxpayer appealled (sic) to this Court on 3rd July 1989."*

The taxpayer gave oral evidence before the Court of Review. That Court's record of his evidence is as follows:-

"In 1975 I admitted Michael Benefield and made an arrangement. He brought his particular skills and knowledge into firm. We understood risks. We probably had 5 other partners; as far as I can remember. Things have become more complex and our methods altered to keep up. We discussed our business affairs from time to time, and we attempted to run an efficient partnership. I do not remember a written agreement with Benefield. In 1984 we discovered defalcations for which he was responsible. He admitted same to us and we dismissed him from partnership. Moneys taken from clients' trust accounts and used by him. We accepted that we had to repay that money and we have done so. It took some time to ascertain extent of defalcations. Amounts not all repaid in the year. I think about $30,000 repaid in 1984.

[To] KEAY [Counsel for the Commissioner]

Firm held in respect at that time, I think. I accept report of disciplinary proceedings in Fiji Times. We never sought to escape liability for any of those moneys and could not have done so.
I accept that I might have been liable myself."

.....

"There were a number of several incidents of theft by Benefield, spread over a period of time, probably over several years, involving a number of different clients. The money represented funds held in our trust account on behalf of various clients, and used on their instructions.
[To] Keay: The funds which were stolen were held in trust for clients and had to be repaid on demand."

Section 61(2) of the Act cast onto the taxpayer the onus of proving that the assessment was incorrect. The sole ground of his objection was that the money paid by the partners to the clients was "wholly and exclusively expended for the purpose of" their profession. The taxpayer did not seek leave of the Court

of Review to appeal to it on any other ground. So, by virtue of section 62(6) of the Act, his appeal was limited to that ground. The Commissioner, however, raised the issue whether the payment was of capital. By virtue of paragraphs (b) and (i) respectively of section 19 no deduction was allowable if the expense was not money "wholly and exclusively expended for the purpose of" the taxpayer's profession or if it was expenditure of a capital nature.

By virtue of section 51 of the Act a partnership is required to make a joint return in respect of its income but no assessment is issued in respect of it. Only the income of each of the individual partners is assessed. The Court of Review received in evidence the assessment of the taxpayer's income and the distribution advice provided to the Commissioner by the partnership. In addition evidence was given orally by the taxpayer.

The Court of Review decided that the expenditure was of a revenue nature and not of a capital nature, so that deduction was not prohibited by section 19(i). However, it decided also that the money was not expended for the purpose of the taxpayer's profession. Accordingly it dismissed the appeal and implicity confirmed the assessment (section 66(1)).

In the High Court no further evidence was adduced. Counsel for the Commissioner informed the learned Judge, Fatiaki J, that the Commissioner was not challenging the Court of Review's

finding that the expenditure was not of a capital nature. Arguments were then presented by counsel for each of the parties; they addressed the section 19(b) issue. Counsel for the Commissioner stressed that, even if the Court found that the money was expended for the purpose of the taxpayer's profession, section 19(b) nevertheless prohibited deduction unless that was the only purpose of the expenditure.

In a closely reasoned judgment His Lordship came to the conclusion that the money was expended wholly and exclusively for the purpose of the taxpayer's profession. He expressly recognised that the taxpayer, with the other remaining partners, was personally liable to make good the deficiency in the trust funds which had resulted from the theft, and that the payment of the money discharged that liability, at least in part. Nevertheless, he found that although the payment had that "beneficial" *effect*, its ***purpose*** had not been to discharge the liability. It was to secure the good name of the firm by making good its clients' loss. Accordingly, section 19(b) did not prohibit the deduction of the expenditure. Although His Lordship allowed the appeal, he did not formally make an order allowing the taxpayer's objection, as we believe the allowing of the appeal required him to do.

The appeal in these proceedings is by the Commissioner. The grounds of appeal are as follows:-

> *"1. **THAT** the learned judge erred in law by failing to hold that the*

expenditure by way of reimbursement to clients of sums stolen by the respondent's business partner was not wholly and exclusively laid out for the purpose of the respondent's profession.

2. ***THAT*** *the learned judge erred in law in holding that the meeting by the respondent of a liability imposed upon him by statute was for the purpose of the firm through which the respondent practised as a barrister and solicitor.*

3. ***THAT*** *the learned judge erred in law in holding that the "co-incidental effect" of the respondent meeting a liability imposed upon him by statute was of such a nature that such expenditure was precluded from having duality of purpose.*

4. ***THAT*** *the learned judge erred in law in not having regard or proper regard to the provisions of the Partnership Act Cap 248.*

5. ***THAT*** *the learned judge erred in law in not holding that the position of the defalcator of the stolen monies had crucial bearing on the deductibility of the expenditure."*

By reason of section 12(1)(c) of the Court of Appeal Act (Cap.12), where the High Court has exercised its appellate jurisdiction under any enactment, any ground of an appeal to this Court can involve only a question of law. Although the primary facts, as set out in the statement of agreed facts, are not in dispute and the credibility of the taxpayer's evidence has not been impugned, the drawing of inferences from those facts and that evidence was required before findings could be made in respect of the purpose of the expenditure. Those findings were

findings of fact, not of law. They cannot be challenged in these proceedings except on either or both of two bases.

The first is that either the primary facts or the taxpayer's evidence or both were misunderstood by His Lordship. The second is that no reasonable decision-maker could have drawn those inferences from those facts and that evidence. All the grounds of appeal essentially relate to the drawing of the inferences and to the facts and the evidence which His Lordship should have taken into account in the process.

Sections 12 and 13 of the Partnership Act (Cap 248) are as follows:-

> *"12. Where-*
> *(a) one partner acting within the scope of his apparent authority receives the money or property of a third person and misapplies it; and*
> *(b) a firm in the course of its business receives money or property of a third person and the money or property so received is misapplied by one or more of the partners while it is in the custody of the firm, the firm is liable to make good the loss.*
>
> *13. Every partner is liable jointly with co-partners and also severally for everything for which the firm while he is a partner therein becomes liable under either of sections 11 or 12."*

At the hearing of the appeal Mr Blakeley made a two-pronged submission. His principal submission was that the agreed facts and the evidence did not permit a finding to be made that the expenditure was money laid out or expended for the purpose of the

taxpayer's profession. His secondary submission was that, even if the agreed facts and the evidence did permit such a finding to be made, they did not permit a further finding to be made that the money was laid out or expended wholly and exclusively for that purpose. Mr Johnson submitted, on the other hand, that His Lordship had been entitled to find that the money was laid out or expended wholly and exclusively for that purpose because the discharge of the liability of the partnership which it achieved was for the purpose of the taxpayer's profession.

Both parties sought support for their submissions from a number of judgments of the Courts in England, Australia and New Zealand. As the relevant legislation in Australia and New Zealand is couched in terms different from those of section 19(b), none of the cases decided in those countries is concerned with interpreting the phrase "for the purpose of the .... profession ... of the taxpayer". However, the relevant English legislation does contain phraseology similar to that in section 19(b), so that the English cases can be more directly relied on for assistance in these proceedings. Nevertheless, it must be said that several of those to which we were referred were concerned more with whether expenditure was wholly and exclusively laid out for the purpose of the taxpayers' trades and professions than with the question whether they were laid out for that purpose at all.

The seminal English case appears to have been **Strong & Co. of Romsey Ltd v. Woodifield** [1906] AC 453. There the words "for

the purpose of the trade" were said to mean for the purpose of enabling a person to carry on and earn profits in the trade. That dictum was applied by the House of Lords in **Morgan v Tate & Lyle Ltd** [1955] AC 21. It was also said in that case (at pages 37 and 47) that, in order to ascertain whether money was expended to serve the purposes of the taxpayer's business, it was necessary to discover the taxpayer's object in making the expenditure. Both that dictum and the dictum in **Strong** were subsequently applied by the House of Lords in **Mallalieu v Drummond** [1983] 2 A.C. 861. As the wording of section 19(b) of the Act is similar to that of the English legislation with which those cases were concerned, and as the subject-matter is substantially the same, we are satisfied that those dicta should be applied in construing section 19(b).

In **Mallalieu** Lord Brightman, with whose judgment three of the other four Lords of Appeal concurred, made the following observations about the ascertainment of the taxpayer's object. At page 1100 Lord Brightman said:-

> *"The object of the taxpayer in making the expenditure must be distinguished from the effect of expenditure. An expenditure may be made exclusively to serve the purposes of the business, but it may have a private advantage. The existence of that private advantage does not necessarily preclude the exclusivity of the business purposes. For example a medical consultant has a friend in the South of France who is also his patient. He flies to the South of France for a week, staying in the home of his friend and attending professionally on him. He seeks to recover the cost of his air fare. The question of fact will be whether the journey was undertaken solely to serve the purposes*

> *of the medical practice. This will be judged in the light of the taxpayer's object in making the journey. The question will be answered by considering whether the stay in the South of France was a reason, however subordinate, for undertaking the journey, or was not a reason but only the effect. If a week's stay on the Riviera was not an object of the consultant, if the consultant's only object was to attend on his patient, his stay on the Riviera was an unavoidable effect of the expenditure on the journey and the expenditure lies outside the prohibition in s.130"*

Again we are satisfied that that is the manner in which the taxpayer's purpose had to be ascertained in the present case. We would add that the approach we have taken is similar to that taken by the Court in **The Commissioner for Inland Revenue v. The Flour Mills of Fiji Ltd** (Civil Appeal No. 6 of 1985, decided on 20th July, 1985) and that we have taken it for the same reasons.

Because the Court of Review made a finding that the risk of defalcation by a partner was inherent in the manner in which the partnership to which the taxpayer belonged was conducted, counsel spent some time discussing two New Zealand cases in which the existence of such an inherent risk was a relevant consideration, **Commissioner of Taxes v. Webber** [1956] NZLR 552 and **W.G. Evans Co. Ltd v. Commissioner of Inland Revenue** [1975] 1 NZLR 425. However, in both those cases the Court was dealing with a loss, not with expenditure; and the statutory provision which it had to apply required the loss to have been "incurred in the production of assessable income for any income year". It is doubtful, in our view, whether the fact that a risk of defalcation by a partner is inherent in the operation of a particular partnership

is relevant to the question whether the object of another partner in incurring expenditure to make good a defalcation when it occurs is to enable him to earn a profit from his profession. Certainly it does not determine that question.

We have set out above the agreed statement of facts that was presented to the Court of Review and the record of the only evidence given in that Court. No evidence was given in the High Court. In giving his evidence in the Court of Review the taxpayer did not expressly state what his object or his motive was. As the onus of proof was on him, his objection was bound to fail unless inferences could be drawn from his evidence and the agreed facts that established that his object was to incur the expenditure for the purpose of being enabled to earn profits from his practice of his profession. As we have stated above, it was Mr Blakeley's contention that those inferences could not be drawn and that His Lordship erred in law in deciding that they could.

After giving the matter careful consideration we have come to the conclusion that inferences could properly be drawn that the expenditure was incurred for the purpose of the taxpayer's profession. We find considerable force in Mr Johnson's argument that, as the partnership's purpose was the practice of law and the liability to make good the defalcation was initially that of the partnership (see section 12 of the Partnership Act (set out above)), the discharging of the liability by the partnership was undertaken for the purpose of the practice of the law, that is to say for the purpose of the profession of the partners together as

a partnership and of each of them individually within the partnership. We are satisfied that the learned Judge did not err in law in making a finding that the expenditure of the money by the taxpayer through the partnership was incurred for the purpose of his profession.

We must turn now, therefore, to the second prong of Mr Blakeley's submission. In **Mallalieu** at page 1103 Lord Brightman, when considering whether certain expenditure had been incurred wholly and exclusively for the purpose of the profession of the taxpayer, a barrister, rejected a view, expressed at first instance and in the Court of Appeal, that "the conscious motive of the taxpayer was decisive". He referred to it as a "narrow approach" and continued:-

> *"Of course the motive of which the taxpayer is conscious is of a vital significance, but it is not inevitably the only object which the commissioners are entitled to find to exist. In my opinion the commissioners were not only entitled to reach the conclusion that the taxpayer's object was both to serve the purposes of her profession and also to serve her personal purposes, but I myself would have found it impossible to reach any other conclusion."*

Each case where a taxpayer asserts that expenditure was incurred wholly and exclusively for the purpose of his trade or profession must be decided on its own facts. It does not assist the taxpayer's case if the taxpayer makes no contemporaneous record of his object in incurring the expenditure and does not give any detailed account of his motivation when making his

objection to the assessment or when presenting his case in the Court of Review. In the present case in his evidence in the Court of Review the taxpayer said:-

> *"We accepted that we had to repay that money and we have done so."*

His only reference to the partnership's reputation was where, in cross-examination, he said:-

> *"Firm held in respect at that time, I believe."*

At no stage did he assert that the money was repaid in order to protect the good name of the firm or that the discharge of his personal liability under section 13 of the Partnership Act, for reasons other than his concern that the partnership should be able to retain its existing clients, was not one of his purposes in incurring the expenditure. Several other purposes were possible, the most obvious being a desire not to be sued personally and not to lose his own ***personal*** (as distinct from his ***professional***) reputation. We hasten to say that such a purpose is an entirely worthy and honourable one. Indeed, it is an admirable purpose; but it is not the same as, or part of, incurring the expenditure solely for the purpose of his practice.

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In deciding whether His Lordship could properly find that the expenditure was incurred for the purpose of the taxpayer's profession, we saw considerable force in Mr Johnson's argument that discharging the partnership's liability enabled the parties to continue to practice. However, it affords, in our view, no support for the making of a finding, based on the agreed facts and the evidence, that the expenditure was incurred wholly and exclusively for that purpose. The onus rested on the taxpayer to prove that the expenditure was deductible. As several purposes in addition to that required by section 19(b) might reasonably have been inferred by His Lordship from the agreed facts and the evidence, we find that he did err in law deciding that the expenditure was incurred wholly and exclusively for the purpose of the taxpayer's profession.

Accordingly, the appeal must be allowed, the judgment of the High Court set aside and the decision of the Court of Review restored. However, before concluding this judgment, we wish to note the possibility that our decision might have been different if the taxpayer had included in his objection a ground of appeal based on section 19(c). We have dealt with this appeal on the basis that *expenditure* was incurred by the taxpayer; it was argued on that basis by both parties. If we were to hold that there was not any *expenditure* but only a *loss*, we should have to

hold also that the taxpayer's objection could not succeed as the only ground for it was based on section 19(b) and not section 19(c). However, many of the cases on which Mr Johnson sought to place reliance concerned ***loss***, not ***expenditure***. In our view a case might possibly have been made out that what was incurred, initially by the partnership, and then consequentially by each of the partners, was a loss. The provisions of section 19(c) are fundamentally different from those of section 19(b); not having heard argument in terms of the provisions of section 19(c), we express no opinion whether the taxpayer might have succeeded if he had added to his objection a ground based on that paragraph. We stress, however, that, because the only ground in the present case was based on section 19(b), this judgment will afford no authority in respect of objections made on a ground based on section 19(c).

Finally, before the hearing and at the commencement of it, the Court was informed that in Civil Appeal No. 24 of 1993 the appellant and the respondent taxpayer, Dennis Julius Williams, would abide the decision made in these proceedings and that judgment should be given in that appeal in the same terms.

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Decision

Appeal Allowed.

Judgment of the High Court set aside.

Decision of the Court of Review reinstated.

Respondent to pay the costs of the Appellant in this appeal and of the proceedings in the High Court and the Court of Review

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Sir Mari Kapi
Judge of Appeal

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Mr. Justice Gordon Ward
Judge of Appeal

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Mr. Justice I. R. Thompson
Judge of Appeal

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