



COMMISSIONER FOR INLAND REVENUE v MALCOMESS PROPERTIES (ISANDO)(PTY)
LTD 53 SATC 153

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Division: Appellate
Judges: BOTHA JA, NESTADT JA, KUMLEBEN JA, PREISS AJA AND
NICHOLAS AJA
Date: 15 and 30 November 1990
Also cited as: [1991 \(2\) SA 27\(A\)](#)

Income tax - Property - Profit derived from sale of property - Capital or revenue accrual - Taxpayer acquiring property in 1969 with intention to hold it as a capital asset from which it would derive income by way of rentals - That intention remaining unchanged until 1975 when shareholders in holding company resolved that it be wound up and its assets (which included the said property) be realised - Lessee of property, perturbed by this development, and in order to secure long-term tenure devised scheme for acquisition of taxpayer - Contract concluded whereby lessee purchased entire issued share capital of taxpayer, such agreement being subject to the fulfilment of condition precedent that property be sold to 'reasonably acceptable insurance company or pension fund' - Property sold in 1976 at net profit of R1 127 127 subject to a lease of the property being concluded between purchaser of the property and lessee - Agreement for sale of property being transaction in issue in appeal - Commissioner contending that sale of property part of whole scheme devised by lessee to sell the property for profit and this was attributable to taxpayer because, at time when land sold, lessee was controlling mind of, and had executive control over, taxpayer and hence it was intention of lessee that determined intention of taxpayer in entering into the transaction and such profits accordingly liable to income tax - Held that it was trite that an owner of land is entitled to realise such asset to best advantage and the fact that he does so does not alter what is an investment of capital into a trade or business for earning profits - 'Something more is required in order to metamorphose the character of the asset and so render its proceeds gross income' - In interval between 1975, when decision taken to dispose of land, and disposal of land in 1976 nothing done by taxpayer to metamorphose character of the property - Held that taxpayer did not engage in business of selling the land which in no way could be regarded as its stock-in-trade - On face of it transaction was realisation of a capital asset so that profit accordingly not liable to income tax - Held further that on assumption that intention of lessee's scheme to make a profit on sale of the property, taxpayer not party to that scheme - Taxpayer and lessee operating at arm's length - Lessee's intention or purpose in embarking upon such scheme accordingly having no bearing on question whether taxpayer continued to hold said property as a capital asset - On contention that lessee's intention to make profit on sale of property attributable to taxpayer because its controlling mind at that point in time was in fact the lessee, it was held that lessee's acquisition

Page 154 of 53 SATC 153

of shares subject to condition precedent which was not fulfilled until sale of property and that notwithstanding its ownership of all the shares in the taxpayer, on the facts before the court lessee did not have the de facto control over the taxpayer's activities - Lessee's intention in devising and executing scheme irrelevant to intention of taxpayer in regard to the property - Held accordingly that sale of property had been realisation of capital asset and that profit not subject to income tax.

Respondent company was incorporated on 24 March 1969 when it acquired the Isando property, the property in issue in this appeal.

Various properties, including the Isando property, on which the business of the Malcomess group had been conducted, were owned by the Malcomess family in a company, Malcomess Properties Ltd. Its shares were held by the members of the Malcomess family who had previously held the shares in Malcomess Holdings. Each property was transferred to a separate company which became a wholly owned subsidiary of Malcomess Properties, one of these being the respondent.

The Isando property had been acquired in 1963 by Malcomess Limited, which was described as a 'family company'. Most of its members belonged to the Malcomess family. The business was founded in Kingwilliamstown in 1869, and it was incorporated as Malcomess(Pty) Ltd in 1924. On becoming a public company in 1961 it was named Malcomess Ltd, which became, after a reorganisation in 1968, Malcomess Holdings Ltd. The business of the Malcomess group was two-fold in nature: the distribution throughout South Africa of farming machinery and equipment; and a motor franchise business conducted mainly in the Eastern Province.

Over the years the Malcomess group acquired for the conduct of its business fixed properties in various places

in South Africa. For a long time its headquarters had been in East London, but in the 1950's its centre of operations was moved to the Transvaal. The Isando property was acquired in 1963 to serve as headquarters for the group. The Isando property, on which warehouses, sheds and an office building were erected, became the group's central spare parts warehouse and a significant stockholding area for farming machinery. It was a property of prime strategic importance in the operations of the Malcomess group.

In 1969 and in pursuance of a scheme of arrangement sanctioned by the court, a merger took place between Malcomess Holdings and a company named O Bakke and Co(Pty) Ltd ('Bakke'). In consequence, Malcomess Holdings and Bakke became wholly owned subsidiaries of a company called Malcomess-Bakke Ltd (later changed to Malbak Ltd), which obtained a primary listing on the Johannesburg Stock Exchange of the shares allotted and issued to the former shareholders of Malcomess Holdings and of Bakke in terms of the scheme of arrangement.

In order to facilitate the merger, the properties (including the Isando property) on which the business of the Malcomess group had been conducted, were excluded from the merger and were retained by the Malcomess family. It was nevertheless contemplated that the properties would be leased by the family to the Malbak group. To this end a new company, Malcomess Properties Ltd was formed, as described above. On 4 June 1969 a 'master lease' covering all the properties was concluded between Malcomess Properties as lessor and Malcomess-Bakke Ltd as lessee. By 1975 the shareholders in Malcomess Properties had become disenchanted with their investment and at a meeting held on 23 August 1975 the board of directors agreed that it was in the best interests of the company's shareholders to recommend voluntary liquidation of the company. Effect was given to this recommendation on 23 September 1975 when a special resolution was passed that in terms of s 349 of the Companies Act 1973 the company be wound up voluntarily.

A liquidator was appointed and his brief was to realise, subject to the instructions of the shareholders, all the assets of Malcomess Properties to best advantage. The Malbak

Page 155 of 53 SATC 153

group was perturbed by these developments, some of its companies operated from premises owned by Malcomess Properties, including the most important (Malcomess Ltd) which occupied the Isando property. An approach was made to the liquidator in an effort to buy the properties which Malbak regarded as strategic, or to secure long-term tenure of them. The liquidator's attitude was that he wanted if possible to sell all the properties in one transaction. In order to meet the situation a scheme was devised by Malbak for the acquisition of Malcomess Properties, whereby Malbak would acquire the entire issued share capitals in the companies and provision was made for the calculation of the purchase price 'with a view to ensuring that the shareholders of the seller receive ninety cents per share . . .' The negotiations which followed were brought to fruition in August 1976, when three interdependent agreements were concluded.

On 23 August 1976 a written contract was concluded between Malcomess Properties Ltd (in voluntary liquidation) and Rushton Properties Ltd (which was wholly owned by Malbak). In terms thereof Malcomess Properties sold to Rushton the entire issued share capitals in 'the companies' (which were eleven in number and included Malcomess(Isando)) and the seller's claims on loan account against the companies. The contract was subject to the condition precedent that 'an offer to purchase the property belonging to [the respondent company] is received, such offer to be from a reasonably acceptable insurance company or pension fund'.

On 27 August 1976 respondent sold the Isando property to the Durban Corporation Superannuation Fund ('Durcor') for the sum of R1 500 000. The sale was subject to a lease of the property being concluded between Durcor and Malcomess-Bakke Ltd. On the same day there was executed a notarial deed of lease of the Isando property between Durcor and Malcomess-Bakke Ltd, in terms of which the rental was to be calculated at the rate of 11 per cent of the capital cost of the leased property with provision for escalation.

The agreement for the sale by respondent to Durcor of the Isando property resulted in a net profit of R1 127 127, which the Commissioner for Inland Revenue, in his determination of the liability of respondent to normal tax for the year of assessment ended 31 March 1977, included in its income. An objection by the taxpayer was disallowed, and it appealed to the Transvaal Income Tax Special Court. That court, in which Margo J presided, upheld the appeal and remitted the matter to the Commissioner for reassessment. The present appeal is against that order.

It was common cause that when respondent acquired the Isando property in 1969 it intended to hold it as a capital asset from which it would derive income by way of rentals.

Appellant contended *inter alia*(i) that the disposal of the Isando property to Durcor could not be considered in isolation but must be viewed as part of the whole scheme devised by the Malbak group which, it was submitted, was 'a scheme for selling the property for a profit': a close analysis of the facts demonstrated that 'the scheme' as it evolved, aimed at profit-making and that Malbak had embarked upon a scheme of selling the property for a profit - its dominant intention being either to own the property, or secure a long-term lease, but obviously it wished to make a profit from the acquisition thereof; (ii) that Malbak's intention

to make a profit was attributable to the taxpayer because 'its controlling mind at that point in time was in fact the Malbak group', which 'through Rushton, was in control of the taxpayer at the time the property was sold', because on 23 August 1976 Malbak had acquired all the issued shares in respondent and so had acquired control of the company and at the time the property was sold on 27 August 1976, Malbak 'already had executive control of the taxpayer' and it was, accordingly, the intention of Malbak which determined the intention of the taxpayer in entering into the transaction and (iii) that the advent of the new controllers had brought about a change in respondent's intentions.

Held

- (i) That in considering whether receipts on the disposal of property are capital or revenue accruals, the intention with which the property was acquired is

Page 156 of 53 SATC 153

important, although the capital or revenue character of an asset can be altered by a change of intention.

- (ii) That it is trite that an owner of land, or any other asset, is entitled to realise such asset to best advantage, and the fact that he does so, does not alter what is an investment of capital into a trade or business for earning profits.
- (iii) That 'something more is required in order to metamorphose the character of the asset and so render its proceeds gross income' (*per* Wessels JA in *John Bell & Co(Pty) Ltd v Secretary for Inland Revenue* 1976(4) SA 415(A) at 429C-D; [38 SATC 87](#) at [103](#)).
- (iv) That respondent's intention to hold the Isando property as a capital asset from which it would derive income by way of rentals had remained unchanged until 1975 when the shareholders in the holding company had resolved that the company and its subsidiaries be wound up and its assets realised.
- (v) That during the interval between the decision to realise the assets and the sale of the Isando property in 1976, nothing had been done by respondent to metamorphose the character of the property.
- (vi) That in the present case there were no facts at all which could lead to an affirmative answer to the enquiry whether 'the owner had crossed the Rubicon and gone over to the business . . . of selling such land for profit, using the land as his stock-in-trade' (*Natal Estates Ltd v Secretary for Inland Revenue* 1975(4) SA 177(A) at 203A; [37 SATC 193](#) at [220](#)).
- (vii) That in the interval respondent did no more with the property than receive rentals from it; it did not engage in a business of selling the land, which in no wise could be regarded as its stock-in-trade.
- (viii) That on the face of it the transaction was a realisation of a capital asset, so that the profit was not liable to income tax.
- (ix) That even if it was assumed, without deciding, that the intention of the Malbak scheme had been that a profit should be made for the benefit of Malbak, *inter alia* from the sale of the Isando property, respondent company had not been a party to that scheme; Malcomess Properties and Malbak had operated at arm's length and that Malbak's intention or purpose in embarking upon its scheme had no bearing on the question whether the respondent had continued to hold the Isando property as a capital asset.
- (x) That it is a relevant factor in the appeal that Malcomess Properties and its subsidiaries on the one hand were entirely independent of Malbak and its subsidiaries on the other hand; unless there was something more, the scheme was *res inter alios acta* so far as the respondent was concerned and could not affect its position to its prejudice.
- (xi) That with regard to appellant's contention that Malbak's intention to make a profit had been attributable to the respondent because Malbak had executive control over and was the controlling mind of respondent when the Isando property had been sold, there were two answers -
 - (a) that the entire agreement between Malbak and Malcomess Properties had been subject to a condition precedent which was not fulfilled until the conclusion of the agreement between respondent and the purchaser for the sale of the Isando property, which agreement was itself subject to a lease being concluded between the purchaser and Malbak; and
 - (b) that even if by acquiring all the issued shares in respondent it might be said that it then had a controlling interest in respondent, in the context of ascertainment of the intention of the company, 'control' connoted the *de facto* control of what the company does, of its day-to-day activities, exercised by the persons through whom the company acts; and on the facts before the court, Malbak had not been in control of respondent in that sense.

- (xii) That, accordingly, Malbak's intention in devising and executing its scheme was irrelevant to the intention of respondent in regard to the Isando property.
- (xiii) That, accordingly, respondent's disposal of the property had been the realisation of a capital asset and the profit therefrom not liable to income tax.

Page 157 of 53 SATC 153

Appeal dismissed with costs, including the costs of two counsel.

D M Fine SC (with him *S van Nieuwenhuizen*) for the appellant referred to the following authorities: *Natal Estates Ltd v Secretary for Inland Revenue* 1975(4) SA 177(A) at 203A, [37 SATC 193](#); *Silke on South African Income Tax* 10 ed at 1226; *Hicklin v Secretary for Inland Revenue* 1980(1) SA 481(A) at 485, [41 SATC 179](#); *Commissioner for Inland Revenue v Louw* 1983(3) SA 551(A) at 569H, [45 SATC 113](#); *Commissioner for Inland Revenue v African Oxygen Ltd* 1963(1) SA 681(A) at 691A-D, [25 SATC 67](#); *Commissioner for Inland Revenue v Richmond Estates(Pty) Ltd* 1956(1) SA 602(A) at 607B, 610C-E, [20 SATC 355](#); *Commissioner for Inland Revenue v Lydenburg Platinum Ltd* 1929 AD 137 at 144-5, [4 SATC 8](#); *Reliance Land & Investment Co(Pty) Ltd v Commissioner for Inland Revenue* 1946 WLD 171 at 181, [14 SATC 47](#); *LHC Corporation of SA(Pty) Ltd v Commissioner for Inland Revenue* 1950(4) SA 640(A) at 646G-H, [17 SATC 125](#); *Commissioner for Inland Revenue v George Forest Timber Co Ltd* 1924 AD 516 at 525, [1 SATC 20](#); *Sekretaris van Binnelandse Inkomste v Aveling* 1978(1) SA 862(A) at 880E - F, [40 SATC 1](#); *Commissioner for Inland Revenue v Stott* 1928 AD 252 at 263, [3 SATC 253](#); *John Bell & Co(Pty) Ltd v Secretary for Inland Revenue* 1976(4) SA 415(A) at 429C-D, [38 SATC 87](#); *Elandsheuwel Farming(Edms) Bpk v Sekretaris van Binnelandse Inkomste* 1978(1) SA 101(A) at 119F, [39 SATC 163](#); *Secretary for Inland Revenue v Trust Bank of Africa Ltd* 1975(2) SA 652(A) at 669F-G, [37 SATC 87](#); *Secretary for Inland Revenue v Rile Investments(Pty) Ltd* 1978(3) SA 732(A), [40 SATC 135](#).

E B Broomberg SC (with him *B E Doctor*) for the respondent referred to the following authorities: *John Bell & Co Ltd v Secretary for Inland Revenue* 1976(4) SA 415(A) at 428A ([38 SATC 87](#)); *Berea West Estates(Pty) Ltd v Secretary for Inland Revenue* 1976(2) SA 614(A) at 632 et seq ([38 SATC 43](#)); *Secretary for Inland Revenue v Trust Bank of Africa Ltd* 1975(2) SA 652(A) at 668C ([37 SATC 87](#)); *Commissioner for Inland Revenue v Stott* 1928 AD 252, [3 SATC 253](#), vide the 'Woody Glen' transaction at 258-61; *Arenson v Commissioner for Inland Revenue* 1948(2) SA 795(W), [15 SATC 144](#); *Matla Coal Ltd v Commissioner for Inland Revenue* 1987(1) SA 108(A) at 128H, [48 SATC 223](#); *Commissioner for Inland Revenue v Paul* 1956(3) SA 335(A) ([21 SATC 1](#)); *Constantia Heights(Pty) Ltd v Secretary for Inland Revenue* 1979(3) SA 768(A) at 784A ([41 SATC 77](#)); *Crowe v Commissioner for Inland Revenue* 1930 AD 122 ([4 SATC 133](#)). *Cur adv vult*.

Postea (30 November).

NICHOLAS AJA: On 27 August 1976, erf No 438 in Monteer Road in the township of Isando, Transvaal ('the Isando property') was sold by the then owner, Malcomess Properties(Isando)(Pty) Ltd to the Durban Corporation Superannuation Fund. The sale resulted in a net profit of R1 127 127, which the Commissioner for Inland Revenue, in his determination of the liability of Malcomess(Isando)(Pty) Ltd to normal

Page 158 of 53 SATC 153

tax for the year of assessment ended 31 March 1977, included in its income. An objection by the taxpayer was disallowed, and it appealed to the Transvaal Income Tax Special Court. That court, in which Margo J presided, upheld the appeal and remitted the matter to the Commissioner for reassessment. The present appeal is against that order. The Commissioner for Inland Revenue will be referred to either as 'the Commissioner' or 'the appellant'; Malcomess Properties(Isando)(Pty) Ltd will be referred to either as 'Malcomess (Isando)' or 'the taxpayer'; and Durban Corporation Superannuation Fund will be referred to as 'Durcor'.

The Isando property had been acquired in 1963 by Malcomess Limited, which was described in the evidence as a 'family company'. Most of its members belonged to the Malcomess family. The business was founded in Kingwilliamstown in 1869, and it was incorporated as Malcomess(Pty) Ltd in 1924. On becoming a public company in 1961 it was named Malcomess Ltd, which became, after a reorganisation in 1968, Malcomess Holdings Ltd. (I shall refer, loosely, to the various Malcomess interests as 'the Malcomess group'.) The business of the Malcomess group was two-fold in nature: the distribution throughout South Africa of farming machinery and equipment; and a motor franchise business conducted mainly in the Eastern Province.

Over the years the Malcomess group acquired for the conduct of its business fixed properties in various places in South Africa. For a long time its headquarters were in East London, but in the 1950's its centre of operations was moved to the Transvaal. The Isando property was acquired in 1963 to serve as headquarters for the group. It was 2,8625 hectares in extent and was well-situated for the headquarters of the agricultural machinery and equipment business: it had a railway siding, which provided access to the South African railway system; it was close to Jan Smuts airport which was convenient for the flying in and out of spares; and its proximity to Johannesburg facilitated its business operations, including the discounting of hire-purchase

agreements. The Isando property, on which warehouses, sheds and an office building were erected, became the group's central spare parts warehouse and a significant stockholding area for farming machinery. Plainly it was a property of prime strategic importance in the operations of the Malcomess group.

During the reorganisation in 1968, Malcomess Ltd sold its agricultural machinery business to a newly incorporated, wholly-owned subsidiary named Malcomess Group Activities Ltd. Malcomess Ltd, being now a holding company and also owning the Malcomess Properties, changed its name to Malcomess Holdings Ltd ('Malcomess Holdings'), upon which Malcomess Group Activities Ltd took the name of Malcomess Ltd in order that the goodwill of the farming machinery business, which had operated under that name, should be preserved.

In 1969 and in pursuance of a scheme of arrangement sanctioned by the court, a merger took place between Malcomess Holdings and a company named O Bakke and Co(Pty) Ltd ('Bakke'). In consequence, Malcomess Holdings and Bakke became wholly owned subsidiaries of a company named Malcomess-Bakke Ltd (later changed to Malbak Ltd),

Page 159 of 53 SATC 153

which obtained a primary listing on the Johannesburg Stock Exchange of the shares allotted and issued to the former shareholders of Malcomess Holdings and of Bakke in terms of the scheme of arrangement.

In order to facilitate the merger, the properties (including the Isando property) on which the business of the Malcomess group had been conducted, were excluded from the merger and were retained by the Malcomess family. It was nevertheless contemplated that the properties would be leased by the family to the Malbak group. To this end a new company, Malcomess Properties Ltd ('Malcomess Properties') was formed. Its shares were held by the members of the Malcomess family who had previously held the shares in Malcomess Holdings. Each property was transferred to a separate company, which became a wholly owned subsidiary of Malcomess Properties. It was in this way that the Isando property was acquired by Malcomess(Isando), which was incorporated on 24 March 1969. On 4 June 1969 a 'master lease' covering all the properties was concluded between Malcomess Properties as lessor and Malcomess-Bakke Ltd as lessee. Subsequently the various subsidiaries concluded separate agreements of lease, one of which was between Malcomess(Isando) and Malcomess Ltd. After an initial period of 18 months until 30 September 1975, this lease was to continue in force indefinitely, but it might be cancelled by either party giving to the other not less than 18 months' written notice, which notice might not be given by the landlord to terminate the lease prior to 31 March 1984. The agreed rental was R74 000 per annum, which was subject to escalation at the rate of R8 000 per annum.

By 1975 the shareholders in Malcomess Properties had become disenchanted with their investment; rentals were low, and future dividends were likely to be reduced in real terms if inflation continued at its then current rate. At a meeting held on 23 August 1975, the board of directors agreed after a lengthy discussion that the company had limited long term prospects; furthermore, that it had no younger candidates of the Malcomess family who could take over control of the company after the departure of the present management; and that it was in the best interests of the company's shareholders to recommend voluntary liquidation of the company. Effect was given to this recommendation on 23 September 1975 when a special resolution was passed that in terms of s 349 of the Companies Act 1973 the company be wound up voluntarily.

Appointed as liquidator at a remuneration of R3 000 per annum was Mr Belcher, an East London accountant who had been an adviser to the Malcomess family for many years. His brief was to realise, subject to the instructions of the shareholders, all the assets of Malcomess Properties to best advantage.

The liquidator began negotiations for the sale of the properties owned by the separate companies, or of the shares in such companies. He approached the Mine Officials Pension Fund and the Durban Corporation Superannuation Fund with a view to a possible sale of the Isando property. (At that time the market was inactive and pension funds were about the only people investing in property.)

The Malbak Group was perturbed by these developments. Some of its

Page 160 of 53 SATC 153

companies operated from premises owned by Malcomess Properties, including the most important (Malcomess Ltd) which occupied the Isando property. An approach was made to Mr Belcher in an effort to buy the properties which Malbak regarded as strategic, or to secure long-term tenure of them. (It had no interest in the properties which it did not occupy.) However, Mr Belcher's attitude was that he wanted if possible to sell all the properties in one transaction, and that he would not allow Malbak to 'pick the eyes' out of the portfolio, which would make it difficult for him to dispose of the properties which remained.

Malbak asked an expert, Mr Harry Gottlieb, to examine the property portfolio owned by Malcomess Properties with a view to giving an opinion as to a fair price for its shares. That opinion was given on 3 May 1976. Mr Gottlieb valued each of the properties leased to Malbak on the basis of a percentage return on a lease-back basis, having regard largely to the then current rentals. He valued the Isando property at R800 000, and valued the shares in Malcomess Properties at 82 cents per share.

In order to meet the situation a scheme was devised by Malbak for the acquisition of Malcomess Properties. It was embodied in a report to the board of directors of Malbak by Mr G S Thomas, the group managing director. It stated that the management of Malcomess Properties valued that company at 111 cents

per share. The majority of the properties occupied by Malbak were not subject to leases of sufficiently long duration to attract institutional investors without additional commitments from Malbak, and therefore the winding up of the company would of necessity be dragged out over a number of years. The indications were that a bid for Malcomess Properties of the order of 90 cents per share would be likely to succeed. By working together with an insurance company or pension fund, Malcomess Properties and the Malbak group could negotiate a sale and leaseback of the Isando property. R1 300 000 could be realised on the sale, amounting to a net receipt of R1 235 000. The affairs of the Malbak group could be structured in such a way that the profit of R435 000 (R1 235 000 less R800 000 - as per the Gottlieb valuation) would not be taxable. The following appears from the minutes of a meeting of the directors of Malcomess Bakke Ltd held on 3 June 1976

- '1. Mr G S Thomas submitted a proposal to the meeting in terms of which Malcomess-Bakke Limited could acquire the property companies of Malcomess Properties Limited (in voluntary liquidation), thereby obtaining security of tenure of certain strategic properties.

This proposal involved inter alia Malcomess-Bakke Limited entering into a long lease on one of the properties.

It was agreed that:

The proposal as submitted be accepted and that Mr G S Thomas be empowered to sign all necessary documentation relating to this proposal on behalf of the company.'

At the start of the meeting, Mr D L Keys, who was the chairman of Malbak, 'declared his interest in Malcomess Properties Ltd., being the holder of 279 000 shares in that company, and excused himself from the proceedings'. Mr Keys gave evidence before the Special Court, in the course of which he said that all the negotiations between Malbak and Malcomess Properties were conducted at arm's length. The former was represented by Mr Thomas and the latter by Mr Belcher, who as

Page 161 of 53 SATC 153

liquidator acted in the best interests of the company's shareholders. Mr Thomas's evidence also was that although there was some common directors Malcomess Properties and Malbak were operating totally at arm's length.

The negotiations which followed were brought to fruition in August 1976, when three interdependent agreements were concluded.

On 23 August 1976 a written contract was concluded between Malcomess Properties Ltd (in voluntary liquidation) and Rushton Properties Ltd (which was wholly owned by Malbak). In terms thereof Malcomess Properties sold to Rushton the entire issued share capitals in 'the companies' (which were 11 in number and included Malcomess(Isando)) and the seller's claims on loan account against the companies. Provision was made in clause 4 for the calculation of the purchase price 'with a view to ensuring that the shareholders of the seller receive 90 cents per share . . .'. Clauses 2.1 and 2.3 provided

- '2.1. This entire agreement is subject to the fulfilment of the condition precedent that an offer to purchase the property belonging to Malcomess Isando is received, such offer to be:
 - 2.1.1. from a reasonably acceptable insurance company or pension fund;
 - 2.1.2. irrevocable until 14 August, 1976; and
 - 2.1.3. . . .
- 2.3. Unless the condition precedent is fulfilled by not later than 14 August, 1976, the provisions of this agreement, . . . shall be of no force or effect.'

In terms of clause 3,

- '3. Subject to the fulfilment of the condition precedent the seller hereby sells to the purchaser with effect as from the effective date as one indivisible transaction:
 - 3.1 the shares; and
 - 3.2 the seller's claims.'

(The 'effective date' was defined in clause 1.1.3 as being 1 April 1976.) It was provided in clause 6 that on or before 'the completion date' (which was defined in clause 1.1.4 as being 29 September 1976) the seller would deliver to the purchaser *inter alia* -

- '6.1. certificates in respect of the shares together with transfer forms in respect thereof duly signed as to transferor by the registered holders thereof and currently dated and duly witnessed;
- 6.2. to the extent required by the purchaser, written resignations of those directors of the affected companies who are nominees of the seller;

- 6.3. to the extent required by the purchaser written resignations of the public officers, and secretary of the affected companies;
- 6.4. to the extent required by the purchaser a written undertaking of the auditors of the affected companies agreeing to resign when requested to do so by the purchaser;
- 6.5. a resolution of directors, or shareholders, as the case may be, as required in terms of the articles of association of each of the affected companies, approving of the transfer of the shares as aforesaid;
- 6.6. a resolution of directors of each of the affected companies appointing as directors nominees of the purchaser in substitution for those directors who resign pursuant to clause 6.2., and if there are no such resignations pursuant to clause 6.2. then appointing nominees of the purchaser in addition to the existing directors of the affected companies.'

On 27 August 1976 Malcomess(Isando) sold the Isando property to Durcor for the sum of R1 500 000. The sale was subject to a lease of the property being concluded between Durcor and Malcomess-Bakke Ltd. (It may be noted that even before the Malbak scheme was devised, the liquidator had on his own initiative been negotiating with Durcor for the

Page 162 of 53 SATC 153

sale to it of the Isando property. The liquidator had in fact received an offer for the property which he did not accept.)

On the same day there was executed a notarial deed of lease of the Isando property between Durcor and Malcomess-Bakke Ltd. The lease was initially for a period of 20 years and provided for a right of pre-emption and a renewal option in favour of Malbak upon the termination thereof. The rental was to be calculated at the rate of 11% of the capital cost of the leased property with provision for escalation.

The agreement for the sale to Durcor of the Isando property is the transaction which is in issue in this appeal.

It is well-recognised that in considering whether receipts on the disposal of property are capital or revenue accruals, the intention with which the property was acquired is important, although the capital or revenue character of an asset can be altered by a change of intention. Such a change does not itself effect a change in the character of the asset. It is trite that an owner of land, or any other asset, is entitled to realise such asset to best advantage, and the fact that he does so, does not alter what is an investment of capital into a trade or business for earning profits. In *John Bell & Co(Pty) Ltd v Secretary for Inland Revenue*, 1976(4) SA 415(A), Wessels JA said at 429C-D:¹

' . . . the mere change of intention to dispose of an asset hitherto held as capital does not *per se* subject the resultant profit to tax. Something more is required in order to metamorphose the character of the asset and so render its proceeds gross income. For example, the taxpayer must already be trading in the same or similar kinds of assets, or he then and there starts some trade or business or embarks on some scheme for selling such assets for profit, and, in either case, the asset in question is taken into or used as his stock-in-trade.'

It is common cause that when Malcomess(Isando) acquired the Isando property in 1969 it intended to hold it as a capital asset from which it would derive income by way of rentals. That intention remained unchanged until September 1975 when the shareholders in the holding company, Isando Properties, resolved that it be wound up and its assets (which included the Isando property, held by its wholly-owned subsidiary Malcomess(Isando)) be realised. The property was sold on 27 August 1976. In the interval between September 1975 and August 1976 nothing was done by Malcomess(Isando) to metamorphose the character of the property. In *Natal Estates Ltd v Secretary for Inland Revenue* 1975(4) SA 177(A) at 202G-H,² Holmes JA remarked that in deciding whether a case is one of realising a capital asset or of carrying on a business or embarking upon a scheme of selling land for profit, one must think one's way through all of the particular facts of the case, and then, after setting out a number of important considerations, said at 203A:³

'From the totality of the facts one enquires whether it can be said that the owner had crossed the Rubicon and gone over to the business, or embarked upon a scheme, of selling such land for profit, *using the land as his stock-in-trade*.'

In the present case there are no facts at all which could lead to an affirmative answer to such an enquiry. In the interval Malcomess

Page 163 of 53 SATC 153

(Isando) did no more with the property than receive rentals from it. It did not engage in a business of selling the land, which in no wise could be regarded as its stock-in-trade. It was not argued in this court, as it was argued, unsuccessfully, in the Special Court, that before Malbak arrived on the scene, the liquidator would have been content to sell the property for R800 000, but that after Malbak arrived on the scene and made its suggestions, the liquidator responded to the proposition resulting in the taxpayer selling the property for R1 500 000; and that this indicated a scheme aimed at profit-making by the realisation of the property. In rejecting that argument, Margo J said, correctly in my respectful opinion, that there 'was not any change in the nature of the profit made by the sale of the . . . property. It would remain a capital realisation whether . . . it

was sold for R800 000 or R1,5 million.' (I should add that the change in the value of the Isando property from R800 000 on 3 May 1976, when this was Mr Gottlieb's valuation, to R1 500 000 which was the amount Durcor agreed to pay for it on 27 August 1976, was not brought about by Malcomess(Isando). It was due solely to the fact that Malbak agreed to the termination of its existing lease with Malcomess(Isando) and to a sale to Durcor for R1 500 000 subject to a lease-back which would provide Durcor with an 11% net return on the purchase price.)

On the face of it, therefore, the transaction was a realisation of a capital asset, so that the profit was not liable to income tax.

It appears from the judgment of Margo J in the Special Court that it was urged for the Commissioner that the court should 'take a bird's eye view of the whole set of circumstances which characterise the disposal of the property and which includes the disposal of the shares in [Malcomess (Isando)] by Malcomess Properties Limited in voluntary liquidation to Malbak Limited'. Similarly it was argued in this court that the disposal to Durcor could not be considered in isolation, but must be viewed as part of the whole scheme devised by the Malbak group which, it was submitted, was 'a scheme for selling the property for a profit': a close analysis of the facts demonstrated that 'the scheme' as it evolved, aimed at profit-making and that Malbak had embarked upon a scheme of selling the property for a profit; Malbak's dominant intention was either to own the property, or secure a long-term lease, but obviously it wished to make a profit from the acquisition thereof.

The taxpayer disputed that the dominant purpose of the scheme was to make a profit: the real purpose, it was submitted, was to enable the Malbak Group to get security of tenure over the strategical properties.

It is not necessary for the purposes of this appeal to resolve this dispute: I shall assume without deciding that the intention of the Malbak scheme was that a profit should be made, for the benefit of Malbak, *inter alia* from the sale of the Isando property to Durcor.

That sale was it is true one facet of the entire scheme, but Malcomess(Isando) was not a party to that scheme. Malcomess Properties and Malbak operated at arm's length. As Margo J observed in the judgment of the Special Court, it is a relevant factor in the appeal that Malcomess Properties and its subsidiaries on the one hand were entirely independent of Malbak and its subsidiaries on the other hand. Unless

Page 164 of 53 SATC 153

there was something more, the scheme was *res inter alios acta* so far as the taxpayer was concerned and could not affect its position to its prejudice; and Malbak's intention or purpose in embarking upon it has no bearing on the question whether the taxpayer continued to hold the Isando property as a capital asset.

It was argued however that Malbak's intention to make a profit was attributable to the taxpayer because 'its controlling mind at that point in time was in fact the Malbak Group', which 'through Rushton, was in control of the taxpayer at the time the property was sold'.

Reliance was placed on the statement in *Secretary for Inland Revenue v Trust Bank of Africa Ltd* 1975(2) SA 652(A) at 669F, ⁴ that the purpose for which a transaction was entered into can, in the case of a company, be proved, *inter alia*, by evidence as to the state of mind or intention of the persons in effective control of the affairs of the company; and on the *dictum* by Corbett JA in *Secretary for Inland Revenue v Rile Investments(Pty) Ltd* 1978(3) SA 732(A) at 737D: ⁵

'Where the taxpayer concerned is a company, which can only think and act through the medium of living beings, then, depending on the circumstances, evidence of the state of mind or intention of the persons in effective control of the company may provide an important indication as to the intention of the company itself in relation to the matters in issue (*Secretary for Inland Revenue v Trust Bank of Africa Ltd* 1975(2) SA 652(A) at 669). ⁶ Moreover, account must be taken of changes in shareholding which cause control of the company to pass into new hands since the advent of new controllers may bring about a change in the intentions of the company (see eg *Elandsheuwel Farming(Edms) Bpk v Sekretaris van Binnelandse Inkomste* 1978(1) SA 101(A)).' ⁷

The rationale of the principle was discussed in *Tesco Supermarkets Ltd v Natrass* 1972 AC 153, where Lord Reid said at 170E-F:

'I must first start by considering the nature of the personality which by a fiction the law attributes to a corporation. A living person has a mind which can have knowledge or intention or be negligent and he has hands to carry out his intentions. A corporation has none of these: it must act through living persons, though not always one or the same person. Then the person who acts is not speaking or acting for the company. He is acting as the company and his mind which directs his acts is the mind of the company. There is no question of the company being vicariously liable. He is not acting as a servant, representative, agent or delegate. He is an embodiment of the company or, one could say, he hears and speaks through the *persona* of the company, within his appropriate sphere, and his mind is the mind of the company.'

The learned lord was echoing what Viscount Haldane had said in *Lennard's Carrying Company Limited v Asiatic Petroleum Company Limited* 1915 AC 705 at 713:

'My Lords, a corporation is an abstraction. It has no mind of its own any more than it has a body of its own; its active and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the directing mind and will of the corporation, the very ego and

centre of the personality of the corporation. That person may be under the direction of the shareholders in general meeting; that person may be the board of directors itself, or it may be, and in some companies it is so, that that person has an authority co-ordinate with the board of directors given to him under the articles of association, and is appointed by the general meeting of the company, and can only be removed by the general meeting of the company.'

Page 165 of 53 SATC 153

That passage was quoted and applied by Centlivres CJ in the judgment of this court in *Levy v Central Mining and Investment Corporation Ltd* 1955(1) SA 141(A) at 149-150, and *cf Anderson Shipping(Pty) Ltd v Guardian National Insurance Co Ltd* 1987(3) SA 506(A) at 515H-I. In *H L Bolton(Engineering) Co Ltd v T J Graham and Sons Ltd* [1957] 1 QB 159(CA) at 172 Lord Denning said that the position was made clear by Lord Haldane's speech in the *Lennard's Carrying Co* case:

'A company may in many ways be likened to a human body. It has a brain and nerve centre which controls what it does. It also has hands which hold the tools and act in accordance with directions from the centre. Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the company, and control what it does. The state of mind of these managers is the state of mind of the company and is treated by the law as such.'

Counsel for the appellant submitted that on 23 August 1976 Malbak acquired all the issued shares in Malcomess(Isando) and so acquired control of the company; and that the advent of the new controllers brought about a change in its intentions. He said that at the time the property was sold on 27 August 1976, Malbak 'already had executive control of the taxpayer', and it was the intention Malbak which determined the intention of the taxpayer in entering into the transaction.

To this submission there are at least two answers.

The first is that the entire agreement of 23 August 1976 was subject to a condition precedent which was not fulfilled until the conclusion, on 27 August 1976, of the agreement between Malcomess(Isando) and Durcor for the sale of the Isando property, which agreement was itself subject to a lease being concluded between Durcor and Malcomess-Bakke Ltd, which was also entered into on 27 August 1976. It was submitted on behalf of the Commissioner that the condition was a 'self-imposed one, designed to benefit the Malbak Group'. That may be so, but it was not suggested that the condition was waived by Malbak. It was also submitted on behalf of the Commissioner that because the date of 14 August 1976 had already passed when the agreement was signed on 23 August 1976 the condition precedent could not apply and must be ignored. I do not agree. The sale of the Isando property was an essential part of the scheme, and the parties to the agreement of 23 August 1976 could not have contemplated that it should not be dependent on the conclusion of the sale. In my view the solution to the problem is to regard as *pro non scripto* clause 2.1.2 ('irrevocable until 14th August 1976') and the words 'by not later than 14th August, 1976' in clause 3, and that otherwise the condition precedent remained.

The second answer is this. If Malbak did on 23 August 1976 acquire all the issued shares in Malcomess(Isando), it might be said that it then had a controlling interest in Malcomess(Isando). Compare the definition of '*controlling company*' in s 1 of the Companies Act 1973,

'*controlling company* means a company which directly or indirectly has power enabling it to control another company . . .'

Even so, it would not have been able to exercise control until there had been performance by Malcomess Properties on or before the completion date of the undertakings given in clause 6 of the earlier contract. And in

Page 166 of 53 SATC 153

any case, in the *dicta* quoted above, 'control' does not mean having the power to control the company in the sense of holding the levers of power in the company. In the context of ascertainment of the intention of the company, it connotes the *de facto* control of what the company does, of its day-to-day activities, exercised by the persons through whom the company acts. That that is so, is clear from the *dicta* quoted above. It was not suggested to Mr Thomas in cross-examination on behalf of the Commissioner, nor suggested by counsel in argument, that Malbak was in control of Malcomess(Isando) in that sense. On the contrary, there are in the record copies of two resolutions which show that it was not. One is a copy (certified to be correct by the liquidator) of a resolution passed at a meeting of the shareholders of Malcomess(Isando) held on 27 August 1976 approving and ratifying the agreement entered into on 27 August 1976 for the sale of the Isando property and authorising the directors of the company to give effect to the sale. The other is a copy of a resolution of the directors passed on the same date that the company pass transfer of the Isando property to the Durban Corporation Superannuation Fund.

In my opinion, therefore, Malbak's intention in devising and executing the scheme was irrelevant to the intention of Malcomess(Isando) in regard to the Isando property. The conclusion of the Special Court was clearly right.

The appeal is dismissed with costs, including the costs of two

counsel. Botha JA, Nestadt JA, Kumleben JA and Preiss AJA concurred.

Footnotes

- 1 [38 SATC 87](#) at [103](#).
- 2 [37 SATC 193](#) at [220](#).
- 3 Ibid, at 220.
- 4 [37 SATC 87](#) at [106](#).
- 5 [40 SATC 135](#) at [141](#).
- 6 [37 SATC 87](#) at [106](#).
- 7 [39 SATC 163](#).