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NATIONAL BANK OF GREECE S.A.
v.
REPUBLIC (COMMISSIONER OF INCOME TAX)

[TRIANTAFYLLIDES, J.]

IN THE MATTER OF ARTICLE 146 OF THE CONSTITUTION

NATIONAL BANK OF GREECE S.A.

Applicant,

and

THE REPUBLIC OF CYPRUS, THROUGH THE COMMISSIONER OF INCOME TAX,

Respondent.

(*Case No.* 262/68).

Income Tax—Bank holding debentures of a company—Conversion of debentures into shares—Acceptance by the Bank of these shares in exchange of said debentures—Shares proved subsequently to be worthless—Whether such loss sustained by the Bank is, for purposes of the Bank's income tax, a deductible trading loss or a non-deductible capital loss—Cf. infra.

*Administrative law—Misconception of the factual situation—Insufficient inquiry—Income tax—*Sub judice *decision treating aforesaid loss as a non-deductible capital loss instead of as a deductible trading loss within the ambit of the said Bank's business—Annulled—Court "inclined" (but not definitely deciding) to treat said loss as a trading loss as aforesaid—Such an inclination sufficient to lead to the conclusion that the* sub judice *decision is, in all probability, based on a misconception of the true factual position—And because in the light only of what has been put before the Court there cannot be a definite pronouncement that that was the only proper conclusion to which the Respondent Commissioner could have arrived in law and in fact—And because* sub judice *decision is based on assumption and without a full inquiry into the real nature of the matter—The Respondent Commissioner seems to have been influenced, more than he should, by the application in an abstract way of the relevant legal principles—The Applicant on his part failing to place before the Respondent irrefutable material which could have resolved all doubts in the latter's mind.*

Misconception of the true factual position—See supra.

Insufficient inquiry into the matter—See supra.

Doubt as to the true position—Should be resolved in favour of the taxpayer—Applicant.

By this recourse under Article 146 of the Constitution the Applicant Bank is challenging the validity of a final decision of the Respondent Commissioner of Income Tax concerning the Applicant's income tax liability in respect of the year of assessment 1961. By virtue of such decision the Applicant was assessed to pay £9,522 by way of income tax in respect of the said year of assessment. In reaching his decision, the Commissioner refused to treat as a trading loss an amount of £42,500, which the Applicant had written off after losing it in the course of a transaction involving 42,000 shares, of £1 each, of a company in South Africa viz. the Union Metal Works (Pty) Ltd.; instead, he treated such amount as a capital loss, sustained through realisation of an investment and, therefore, as not being deductible from other taxable income of the Applicant.

The Court, as at present advised, being inclined—without expressing a final opinion on this point—to treat the loss in question as a trading rather than capital loss and holding that such "inclination" on its part is sufficient to lead it to the conclusion that the subject decision is in all probability based on a misconception of the true factual position and that it has, therefore, to be declared *null* and *void* (on the principle laid down in the case *Nicolaides* v. *The Greek Registrar of the Co-operative Societies* (1965) 3 C.L.R. 585, at p. 600), proceeded to annul the Respondent's decision in question.

The salient facts of the case are briefly as follows:

The Applicant is a branch, in Cyprus, of a banking company registered in Greece. In 1957 the Applicant was the holder of redeemable 4% debentures for £42,500, issued by the aforementioned South African company, the Union Metal Works (Pty) Ltd. In that same year the South African company, which was owing considerably more, through debentures, to the London Branch of the same Greek Bank (of which the Applicant is, as stated, a branch) was reconstructed, apparently with consent of the head office in Greece of the Applicant; as a result new shares were issued equal in nominal value to the outstanding debenture and, thus, the Applicant was given in exchange for the debentures it was holding, 30,000 ordinary

shares of £1 each and 12,500 3% cumulative preference shares £1 each; likewise the London Branch of the Bank received shares in exchange for the debentures it was holding.

Then, in 1959, all the shares of the South African company, which were held by both the Applicant and the London Branch, were sold—being practically worthless—to a certain Mr. Themelis, for only £3,000; such price was never actually received, because its payment was waived in order to defray expenses of the liquidation, soon afterwards, of the said South African company.

As a result, the Applicant received from its head office instructions to write off the amount of £42,500, which represented the value of shares which had turned out to be entirely worthless; and the Applicant proceeded to claim that the said amount of £42,500 was deductible from its taxable income.

The Commissioner of Income Tax giving his reasons for refusing to accept the £42,500 loss, sustained by the Applicant in relation to the shares of the South African company, as being a trading loss, stated that, in his opinion, the said loss was suffered in the course of the realisation of an investment of the Applicant in shares of the South African company, which was "a subsidiary company of the Bank".

On the other hand, it was argued by counsel for the Applicant that the latter acquired shares, issued on the occasion of the reconstruction of the South African company, in order to recover, at the best possible terms, and in a difficult situation, what it was due to it in the form of debentures of such company, which it held; and that in doing so it acted in the ordinary course of banking business; therefore, it was argued, the loss of £42,500 which was suffered as aforesaid by the Applicant, is deductible trading loss, and not a non-deductible capital loss.

Annulling the subject decision, the Court:-

Held, (1). I think there can be no doubt, when one looks at the objects of the banking concern in Greece, of which the Applicant is a branch, that the lending of money and the carrying on of banking business in general are within such objects; and that the debentures of the South African company were acquired in the course of making loans to the said

company and in the course of trading as a bank. It appears, further that the shares in the reconstructed South African company were accepted in exchange of its debentures, in the course of trying to secure recoupment, in a feasible at the time way, of what it was due by the South African company; and that this step was taken within the ambit of trading activities in the field of carrying on banking business. As already stated the said shares proved, eventually, to be worthless.

(2) (a) As at present advised, I am inclined to treat the loss in question (viz. £42,500) as a trading loss, deductible for income tax purposes, and not as a capital loss. (See *inter alia, Californian Copper Syndicate etc.* v. *Harris,* 5 T.C. 159 at pp. 165–166; *Commissioner of Taxes* v. *The Melbourne Trust, Ltd.* [1914] A.C. 1001, at p. 1010; *Punjab Co-operative Bank Ltd Amritsar* v. *Income Tax Commissioner, Lahore* [1940] 4 All E.R. 87).

(b) I have said that I am "inclined" and I have not expressed a final definite opinion on this point, because, on the one hand, such an inclination on my part is sufficient to lead me to the conclusion that the *sub judice* decision is in all probability based on a misconception of the true factual position and it has, therefore, to be declared *null* and *void* (see, *inter alia, Nicolaides* v. *The Greek Registrar of Co-operative Societies* (1965) 3 C.L.R. 585, at p. 600), and, on the other hand, in the light only of what has been put before me by the parties in the course of these proceedings, I am not in a position to pronounce definitely that, in law and in fact, the only proper conclusion to which the Respondent Commissioner could have arrived at was that the said loss is a trading loss.

(3) (a) I think that this is a case in which the Respondent Commissioner has based his decision, to a quite material extent, on assumption, without conducting a full inquiry into the real nature of the matter (see *inter alia, Christides* v. *The Republic* (1966) 3 C.L.R. 732, at p. 755–756). He seems to have been influenced, more than he should by the application in an abstract way of the relevant legal principles. I am, also, of the opinion that the Applicant did not place before the Respondent Commissioner irrefutable material which could have resolved all doubts in the Commissioner's mind.

(b) For these reasons I think that if the Respondent Commissioner intends to pursue this matter further then there

should be the fullest possible inquiry into the true position in all material respects; and it is hardly necessary to stress that the Applicant would be expected to make available to the Commissioner all further relevant information that he may require.

(4) In the result this recourse succeeds. The decision challenged by it is annulled; but in the light of all pertinent considerations there will be no order as to costs.

Sub judice decision annulled.
No order as to costs.

Cases referred to:

Californian Copper Syndicate etc. v. *Harris,* 5 T.C. 159 at pp. 165–166;

Commissioner of Taxes v. *The Melbourne Trust, Ltd.* [1914] A.C. 1001 at p. 1010;

The Royal Insurance Company, Ltd. v. *Stephen,* 14 T.C. 22;

Westminster Bank, Ltd. v. *Osler and National Bank, Ltd.* v. *Baker* [1932] 1 K.B. 668, and on appeal [1933] A.C. 139;

Punjab Co-operative Bank, Ltd. Amritsar v. *Income Tax Commissioner, Lahore* [1940] 4 All E.R. 87;

Reid's Brewery Company, Ltd. v. *Male* [1891] 2 Q.B. 1;

Nicolaides v. *The Greek Registrar of the Co-operative Societies* (1965) 3 C.L.R. 585, at p. 600;

Christides v. *The Republic* (1966) 3 C.L.R. 732, at pp. 755–756).

Recourse.

Recourse against the validity of a decision of the Respondent concerning the Applicant's income tax liability in respect of the year of assessment 1961.

G. Cacoyiannis, for the Applicant.

G. Tornaritis, for the Respondent.

Cur. adv. vult.

The following judgment was delivered by:

TRIANTAFYLLIDES, J.: In this case the Applicant challenges the validity of a final decision of the Respondent Commissioner of Income Tax concerning the Applicant's income tax liability in respect of the year of assessment 1961.

By virtue of such decision the Applicant was assessed to pay—after the Commissioner had rejected a relevant objection of the Applicant—£9,522.975 mils by way of income tax in respect of the said year of assessment. The Commissioner in reaching his decision refused to treat as a trading loss an amount of £42,500, which the Applicant had written off after losing it in the course of a transaction involving 42,000 shares, of £1 each, of a company in South Africa; instead, he treated such amount as a capital loss, sustained through realisation of an investment, and, therefore, as not being deductible from other taxable income of the Applicant (see, in particular, *exhibits A, E, G and I*, which are attached to the recourse).

The salient facts of this case appear to be as follows:–

The Applicant is a branch, in Cyprus, of a banking company registered in Greece.

In 1957 the Applicant was the holder of redeemable 4% debentures for £42,500, issued by the aforementioned South African company, the Union Metal Works (Pty) Ltd.

In that same year this South African company, which was owing considerably more, through debentures, to the London branch of the same Greek bank (of which, as stated, the Applicant is a branch) was reconstructed, apparently with the consent of the head office, in Greece, of the Applicant; as a result new shares were issued equal in nominal value to the outstanding debentures and, thus, the Applicant was given, in exchange for the debentures it was holding, 30,000 ordinary shares of £1 each and 12,500 3% cumulative preference shares of £1 each; likewise, the aforesaid London branch received shares in exchange for the debentures.

Then, in 1959, all the shares of the South African company, which were held by both the Applicant and the London branch, were sold—being practically worthless—to a certain Mr. Themelis, for only £3,000; such price was never actually received, because its payment was waived in order to defray

expenses of the liquidation, soon afterwards, of the South African company.

As a result the Applicant received, from its head office, instructions to write off the amount of £42,500, which represented the value of shares which had turned out to be entirely worthless, and the Applicant proceeded to claim that such amount was deductible from its taxable income.

The Respondent Commissioner of Income Tax in giving his reasons for refusing to accept the £42,500 loss sustained by the Applicant, in relation to the shares of the South African company, as being a trading loss, stated (see *exhibit G*) that, in his opinion, the said loss was suffered in the course of the realisation of an investment, of the Applicant, in shares of the South African company, which was "a subsidiary company of the Bank".

The Applicant's contention, as presented to the Court, is that the Applicant acquired shares, issued on the occasion of the reconstruction of the South African company, in order to recover, at the best possible terms, and in a difficult situation, what was due to it in the form of debentures of such company, which it held; and that in doing so it acted in the ordinary course of banking business; therefore, the loss of £42,500, which was suffered as aforesaid by the Applicant, is a deductible trading loss, and not a non-deductible capital loss.

Counsel for Respondent argued, on the other hand, that the Applicant by converting the debentures into shares, became the holding company of a subsidiary company, viz. the South African company concerned, and that in selling such shares the Applicant suffered a capital loss. In concluding his address counsel for the Respondent appeared to concede that if the Applicant, instead of accepting shares had insisted on payment of the amount due on the debentures and suffered, in the process, the loss in question, then it might be argued that the Applicant had suffered a trading loss.

In so far as the law applicable to a situation of this nature is concerned, I think one of the leading cases is the *Californian Copper Syndicate* (*Limited and Reduced*) v. *Harris*, 5 T.C. 159; its essential facts were that a company had been formed for the purpose, *inter alia*, of acquiring and reselling mining property, and after acquiring and working a copper-bearing property i resold such property to another company,

receiving payment in fully paid up shares of the company; it was held, by the Court of Exchequer (Scotland), that the difference between the purchase price and the value of the shares for which the property was exchanged was a profit assessable to income tax. Lord Justice Clerk stated the following in his judgment (at pp. 165–166):–

> "It is quite a well settled principle in dealing with questions of assessment of Income Tax, that where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income Tax Act of 1842 assessable to Income Tax. But it is equally well established that enhanced values obtained from realisation or conversion of securities may be so assessable, where what is done is not merely a realisation or change of investment, but an act done in what is truly the carrying on, or carrying out, of a business. The simplest case is that of a person or association of persons buying and selling lands or securities speculatively, in order to make gain, dealing in such investments as a business, and thereby seeking to make profits. There are many companies which in their very inception are formed for such a purpose, and in these cases it is not doubtful that, where they make a gain by a realisation, the gain they make is liable to be assessed for Income Tax.
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> What is the line which separates the two classes of cases may be difficult to define, and each case must be considered according to its facts; the question to be determined being—Is the sum of gain that has been made a mere enhancement of value by realising a security, or is it a gain made in an operation of business in carrying out a scheme for profit-making?"

Another leading case is that of *Commissioner of Taxes* v. *The Melbourne Trust, Limited* [1914] A.C. 1001, which was decided by the Privy Council in England on appeal from the High Court of Australia. It was stated in this case (see the judgment of Lord Dunedin, at p. 1010) that the above-quoted principle, from the *Californian Copper Syndicate* case, was a correct statement of the relevant law.

The aforementioned two cases were followed in cases such as the *The Royal Insurance Company, Limited* v. *Stephen*, 14

T.C. 22, *Westminster Bank, Limited* v. *Osler and National Bank, Limited* v. *Baker* [1932] 1 K.B. 668, and on appeal [1933] A.C. 139, and *Punjab Co-Operative Bank, Ltd., Amritsar* v. *Income Tax Commissioner, Lahore* [1940] 4 All E.R. 87.

The *Punjab* case (*supra*) was, indeed, a case in which it was held, by the Privy Council on appeal from the High Court of India, that the buying and selling of securities constitutes part of the normal business of banking and, therefore, that profit made by the Appellant bank as between the selling price and the cost price of certain securities was profit for income tax purposes.

Of course, on the strength of the principle applied in the cases referred to above, the reverse holds good, too; in other words, that where a loss is suffered in the course of the realisation of assets acquired in the process of trading, and not in the course of an investment divorced from trading, such loss is deductible for income tax purposes.

In this respect reference may be made, by way of example, to the case of *Reid's Brewery Company, Limited* v. *Male* [1891] 2 Q.B. 1; the facts of this case were as follows:–

> " The Appellants carried on the business of brewers, and also as a branch or adjunct of their brewery business, the business of bankers and money-lenders, and in the course of such business lent money to their customers on security, and received money on deposit from their customers, who were allowed to draw bankers' cheques or orders on the Appellants. In no case was any loan or advance made by way of permanent investment, but the same was taken only in connection with the current dealings and transactions of the customer with the Appellants, and, in the event of such current dealings or transactions terminating, the loan or advance was required to be paid off, and the account closed. The profits of the brewery were largely increased by the addition of the banking and money-lending business, and the loans were necessary to enable the Appellants to realize profits."

It was held that the Appellants must be taken to have carried on one business only; that the money advanced to customers was used in the business, and not capital invested; and that the Appellants were entitled to the deduction claimed.

Reverting now to the facts of the present case I think there can be no doubt, when one looks at the objects (see *exhibit J*) of the banking concern in Greece, of which the Applicant is a branch, that the lending of money and the carrying on of banking business in general are within such objects; and that the debentures of the South African company were acquired in the course of making loans to the said company in the course of trading as a bank. It appears, further, on the basis of the material placed before the Court, that the shares in the reconstructed South African company were accepted, instead of its debentures, in the course of trying to secure recoupment, in a feasible at the time way, of what was due by the South African company, and that this step was taken within the ambit of trading activities in the field of carrying on banking business. As already stated the said shares proved, eventually, to be worthless.

As at present advised, I am inclined to treat the loss in question as a trading loss, deductible for income tax purposes, and not as a capital loss.

I have said that I am "inclined", and I have not expressed a final definite opinion on this point, because, on the one hand, such an inclination on my part is sufficient to lead me to the conclusion that the *sub judice* decision is, in all probability based on a misconception of the true factual position and it has, therefore, to be declared to be *null* and *void* and of no effect whatsoever (see, *inter alia*, *Nicolaides* and *The Greek Registrar of the Co-Operative Societies* (1965) 3 C.L.R. 585, at p. 600) and, on the other hand, in the light only of what has been put before me by the parties in the course of these proceedings I am not in a position to pronounce definitely that, in law and in fact, the only proper conclusion to which the Respondent Commissioner could have arrived at was that the said loss is a trading loss.

I think that this is a case in which the Respondent Commissioner has based his decision, to a quite material extent, on assumption, without conducting a full inquiry into the real nature of the matter (see, *inter alia*, *Christides* and *The Republic* (1966) 3 C.L.R. 732, at pp. 755–756); he seems to have been influenced, more than he should, by the application in an abstract way of the relevant legal principles.

I am, also, of the opinion—basing myself on what has been

produced in Court—that the Applicant did not place before the Respondent Commissioner irrefutable material which could have resolved all doubts in the Commissioner's mind.

For these reasons I think that *if* the Respondent Commissioner intends to pursue this matter further then there should be the fullest possible inquiry into the true position in all material respects; and it is hardly necessary to stress that the Applicant would be expected to make available to the Commissioner all further relevant information that he may require.

In the result this recourse succeeds. The decision challenged by it is annulled; but in the light of all pertinent considerations there shall be no order as to costs.

Sub judice decision annulled: no order as to costs.