[A. LOIZOU, J.]

1973 Dec. 15

PANOS LANITIS AND SONS (INVESTMENTS) LTD. v REPUBLIC (MINISTER OF FINANCE AND ANOTHER)

IN THE MATTER OF ARTICLE 146 OF THE CONSTITUTION

PANOS LANITIS AND SONS (INVESTMENTS) LTD.,

Applicants,

and

THE REPUBLIC OF CYPRUS, THROUGH THE MINISTER OF FINANCE AND ANOTHER,

Respondents.

(Case No. 417/71).

Income Tax—Interest—Deduction—Private Company—Carrying on business of investment and deriving its income from rents and dividends received from investments—Interest paid by the Company on a loan incurred for purchase of shares in public companies—Not an allowable deduction—As such interest was not expense wholly and exclusively laid out in the production of the income—But the money borrowed was employed as capital—Section 11(1) and 13(e) and (f) of the Income Tax Laws, 1961 - 1969.

Deduction—Income tax—Interest—See supra.

Administrative act or decision—Revocation of—Administrative practice—Effect of—Change of Administrative Practice—Principles applicable—Concessionary administrative practice—May be freely revoked—No legislation required for its change—Respondent Commissioner's previous practice to treat as an allowable deduction interest paid by private companies on loans for purchase of shares in public companies—A concessionary administrative practice—Its termination does not amount to contravention of any general principle of administrative Law—Or of any provision of the Constitution in the sense that same amounts to a violation of the principle of security of law.

Administrative Practice—Change of—See supra.

Concessionary administrative practice—Change of—See supra.

Taxation—Its source in general is the Law—Not only imposition of tax by virtue of custom is excluded, but it is also not possible to abolish a tax by custom.

Custom—Taxation—Imposition or abolition of tax by custom—Excluded—See further immediately hereabove.

Equality—Principle of—Article 28.1 of the Constitution—Decision of the respondent Commissioner disallowing interest paid on money borrowed for purchase of shares in public companies but allowing such interest for shares in private companies—Not violating the principle of equality of treatment—As the distinction made has objective and reasonable justification in view of the many differences between public and private Companies.

The facts sufficiently appear in the Judgment of the learned Judge of the Supreme Court, dismissing this recourse under Article 146 of the Constitution by the tax-payer private Company against the decision of the respondent Commissioner of Income Tax, whereby he, departing from his previous practice, refused to treat as allowable deduction the amount of interest paid by the said Company on a loan incurred for the purchase of shares in public companies.

Cases referred to:

European Investment Trust Co. Ltd. v. *Jackson (H.M. Inspector of Taxes),* 18 T.C. 1;

Anglo-Continental Guano Works v. *Bell,* 3 T.C. 239;

Scottish North American Trust v. *Farmer,* 5 T.C. 693;

Ward (Inspector of Taxes) v. *Anglo-American Oil Co. Ltd.,* 19 T.C. 94;

Ascot Gas Water Heaters Ltd. v. *Duff,* 24 T.C. 171;

Bridgewater and Bridgewater v. *King (Inspector of Taxes),* 25 T.C. 285;

Odeon Associated Theatres Ltd. v. *Jones (Inspector of Taxes)* [1972] 2 W.L.R. 331 and the authorities therein referred to;

P.M. Tseriotis Ltd. and Others v. *The Republic* (1970) 3 C.L.R. 135, at p. 143;

Soteriou v. *The Greek Communal Chamber* (1966) 3 C.L.R. 83, at pp. 104-105;

Mikrommatis and *The Republic*, 2 R.S.C.C. 125, at p. 131;

The Republic v. *Arakian and Others* (1972) 3 C.L.R. 294;

Decisions of the Greek Council of State: Nos. 1185/34 and 343/38.

Recourse.

Recourse against an income tax assessment raised on the applicants for the year of assessment of 1971.

A. Triantafyllides, for the applicants.

A. Evangelou, Counsel of the Republic, for the respondents.

Cur. adv. vult.

The following judgment * was delivered by:-

A. LOIZOU, J.: The question for determination by the Court is whether the payment of interest by the applicant Company on their overdraft, included in the accounts of the Company for the year ended 1970, was allowable deduction in arriving at the profits of the Company for the purposes of income tax for the year of assessment of 1971.

The Company is a private one having its registered office at Limassol. It was incorporated in 1953 for the purpose of carrying on the business of investment and derives its income from rents and dividends received from their investments in shares of Companies. Its share capital is 100,000 shares of £1.- each and for the relevant year its gross receipts were in respect of rents £1,224 and dividends, £13,318.

The applicant Company submitted audited accounts showing a chargeable income of £884. This amount was arrived at after deducting, *inter alia*, the sum of £8,098.

* An appeal has been lodged against this judgment. The appeal has been heard and judgment thereon has been reserved.

485 mils, being interest paid to the Cyprus Popular Bank Ltd., on a current account which the applicant Company was operating with the said Bank. Of this amount the respondent Commissioner considered that a sum of £4,053 represented interest paid in 1970 in respect of the purchase of shares in the said Bank—a public company—to be kept by the applicant Company as an investment, and decided to disallow it on the ground that it was not expenses wholly and exclusively laid out for the production of income. This disallowance results in the applicant Company becoming liable to pay £1,722.525 mils tax over and above the amount stated in their returns. The Commissioner's decision was communicated to the Company by letter dated the 7th April, 1971 (*exhibit* 1), to which an objection was lodged and determined under section 20(5) of the Taxes (Quantifying and Recovery) Law of 1963, Law No. 53 of 1963 as amended by Law No. 61 of 1969; the final decision of the respondent Commissioner was communicated to the applicant Company by letter dated 4th October, 1971 (*exhibit* 3). As against that decision, the present recourse was filed on the 22nd October, 1971, which shows that it has been filed within the period of 75 days prescribed by Article 146.3 of the Constitution.

The *sub judice* decision of the Commissioner not to allow such interest was based on sub-section (1) of section 11 and section 13, paragraphs (e) and (f) of the Income Tax Laws, 1961 - 1969. The corresponding English provisions are the Income Tax Act, 1952, section 137, paragraph (f) and Schedule D applicable to cases 1 and 2, rule 3, paragraph (f) of the Income Tax Act, 1918. I am mentioning them, as the judicial interpretation given to these sections has been relied upon by both counsel and affords, no doubt, guidance and assistance to this Court.

I shall deal with the grounds of law upon which this recourse is based, in the order in which counsel for the applicant Company has argued them, but before doing so, I must say that in this case which is a difficult one, I have been greatly helped by the arguments of counsel on both sides.

His first submission is that on the proper construction of the law, the said interest with which the Company was debited on the Bank overdraft in 1970, was an allowable deduction being an expense incurred wholly and exclusively in the production of their income, that is, the dividends of the investment. In support of this proposition and in addition to referring to section 11(1) of the Income Tax Laws 1961 - 1969, counsel relied on the case of *Scottish North American Tust* v. *Farmer*, 5 T.C. 693. This case concerns a company whose main business was to buy and sell investments and which owing to the value of their purchases of investments abroad exceeding the amount of their available cash they pledged certain of their securities with their bankers in New York to obtain a fluctuating overdraft on which interest was charged at current rates from day to day. Subsequently, in addition to the overdraft, the Bank granted the Company a loan with a fixed maximum for six months at 6 per cent which was renewed for further six months, and then terminated. It was held by the House of Lords that the borrowings were not sums employed as capital within the meaning of the 3rd Rule to the First Case of Schedule D, and that the interest paid to the bankers in New York was deductible, as an outgoing for the purposes of the business, in computing the liability of the Company for assessment. A relevant passage can be found in the judgment of the House of Lords delivered by Lord Atkinson, who, after dealing with a number of authorities, at p. 707 says:

> "These authorities show that money borrowed by such a Company as the appellant Company in this case in the fluctuating temporary manner in which it has been borrowed by them—the daily borrowing and lending of money being part of their trade and business—is not to be treated under the Joint Stock Companies Act as 'capital'. There is nothing to show that that word should bear a different meaning in the Income Tax Acts when applied to the proceedings of Joint Stock Companies. The interest, is, in truth, money paid for the use or hire of an instrument of their trade as much as is the rent paid for their office or the hire paid for a typewriting machine. It is an outgoing by means of which the

Company procures the use of the thing by which it makes a profit, and like any similar outgoing should be deducted from the receipts, to ascertain the taxable profits and gains which the Company earns. Were it otherwise they might be taxed on assumed profits when, in fact, they made a loss."

Useful is to refer to Simon's Income Tax, Vol. II Replacement 1964 - 1965, p. 399 paragraph 620 which each counsel invoked from a different angle in support of his arguments. This paragraph is under the heading, "Interest on Capital". It is stated therein that by section 137(f) of the Income Tax Act, 1952, no sum can be deducted in respect of any sum employed as capital in a trade, and that the Courts have so far taken the view that this rule applies not only to sums which are themselves employed as capital, but also to interest paid on those sums; it then refers to a number of authorities to which I shall revert when I shall attempt a brief review of them.

The passage, however, relied upon more by counsel for the applicant being the following :-

"The question whether or not an item represents capital employed in the trade also arises in relation to borrowed money. The broad distinction is between money which represents mere financial facilities such as a bank overdraft, or money which represents long-term borrowing so that, in effect, the capital of the business is expanded. The result of s. 137(f) in this regard is that interest paid on borrowed money of the latter description cannot be deducted, while interest paid for temporary financial facilities can be deducted. In practice, however, the dividing line is not clearly drawn and although an overdraft may in fact represent a long-term borrowing of capital, interest will usually be allowed. Although the decision in *European Investment Trust Co. Ltd.* v. *Jackson (Inspector of Taxes)* may be regarded as of little value, since the Court of Appeal held that the General Commissioners had decided the case as a question of fact, and that the Court could not interfere, it will nevertheless be noted from the above that the decision has been applied in subsequent

cases. Having regard to the wording of section 137(f), however, the decision may not withstand challenge in a future case."

It may be observed here that this challenge never came before the English Courts and this prophesy of the learned authors cannot be tested any longer, inasmuch as the law in England has been changed by statutory amendment by virtue of section 130 of the Tax Act, 1970. But there is an additional reason why before the amendment of the Law the value of *Jackson's* case was not challenged. This is because it was judicially held that it was the Commissioners who had to decide as a question of fact whether moneys borrowed were sums employed as capital or not and that the Court of Appeal could not interfere with such findings.

The contention of counsel for the respondent Commissioner is that in accordance with the authorities, not only capital was a non deductible expense but also interest paid on capital and that the borrowing of money for the purpose of purchasing the shares in question by the Company was borrowing for the purpose of acquisition of capital.

The authorities relied upon on this point, are the following :-

In the case of *European Investment Trust Co. Ltd.* v. *Jackson (Inspector of Taxes)*, 18 T.C. p. 1, the appellant Company was incorporated for the purpose of carrying on the business of finance. Its main business was the advancing of money for the acquisition of motor cars on the hire purchase system. The Company bought the car in the first instance. The customer paid a deposit and entered into an agreement to hire the car from the Company paying instalments which, in the aggregate, amounted to the balance of the purchase money plus an additional sum which represented the Company's gross profit on the transaction. The American Company who held most of the shares of the appellant Company, was advancing money on interest. The appellant Company claimed that the interest on the additional advances was an admissible deduction in computing the profits for income tax purposes. The General Commissioners on appeal refused the deduction holding that the moneys

advanced by the American Company were moneys employed or intended to be employed as capital in the trade. It was held that there was evidence which the Commissioners could arrive at their conclusion of fact and that they had not misdirected themselves in law.

Finlay J. whose judgment dismissing the appeal was upheld by the Court of Appeal at p. 11 of the report refers to a number of cases including the *Anglo-Continental Guano Works* v. *Bell,* 3 T.C. 239 and deals extensively with the case of *Farmer* (*supra*), pointing out that there was a considerable resemblance between the two cases; they were companies whose business was to buy and sell stocks and shares. They wanted to buy stocks and shares but they had not enough money and they therefore obtained a fluctuating overdraft with Banks in New York.

After quoting the passage from the speech of Lord Atkinson hereinabove set out, he observes that the whole difficulty is to draw the line and to arrive at a correct conclusion upon the facts of the particular case, being easier, as it usually happens, to state a general principle than to apply the general principle correctly, stating the principle in the following words :-

> ".... if you get a company dealing with money, buying or selling stocks or shares, Treasury bills, bonds, all sorts of things, and if you get that company getting, as such companies constantly do get, temporary loans from their bank—accommodation, I suppose, for sometimes twenty-four hours, or even less, sometimes for a good deal longer—if you get that sort of thing, then the interest on that money, the hire, so to speak, paid for that money, may properly be regarded as an expenditure of the business, an outgoing to earn the profits. On the other hand, if the truth of the thing is that by the payment of the interest the company does not obtain mere temporary accommodation, day to day accommodation of that sort, but does, in truth, add to its capital and get sums which are used as capital and nothing else, then I think that in that case all the authorities show that that deduction cannot properly be made."

Useful also is the passage of Romer, L.J. at page 16, who also refers to the *Farmer* case and goes on to say:-

".... a trading company, whose business it was to buy, and re-sell at a profit, investments, borrowed from a bank, for the purpose of enabling it from time to time to purchase the investments which it was going to re-sell, large sums of money. Whether the money was borrowed from a bank or from a finance corporation seems to me quite immaterial. The House of Lords affirming the decision of the Court of Session in Scotland, held that the moneys so borrowed were not sums employed as capital in the trade, within the meaning of what then, I think, corresponded to Rule 3, sub-rule (f). In point of fact, the money which was held not to be capital —although it was capital, as I say, in the sense that it was not income—was, really, what is frequently referred to as circulating capital. But, again, it is impossible, I think, to treat the decision of the House of Lords as laying down that capital, which is used as circulating capital, is not capital within the meaning of sub-rule (f). To start with, they did not in terms, draw any distinction between circulating capital and fixed capital and, in the next place, they did not overrule, although they commented upon, the decision in the *Anglo-Continental Guano Works* v. *Bell* reported in 3 T.C. 239, where money that, so far as I can see, was borrowed and used as a circulating capital, was treated as capital within the meaning of sub-rule (f). The only conclusion that I can draw from those cases, therefore, is this, that, in each case, it is a question of fact whether the capital money borrowed is or is not capital employed in the trade within the meaning of this sub-paragraph, and if the Commissioners have decided, as a question of fact, that it is, then this Court cannot interfere."

In *Ward (Inspector of Taxes)* v. *Anglo-American Oil Co. Ltd.*, 19 T.C. p. 94, the respondent Company whose trading consisted wholly of selling in the United Kingdom (for sterling) petroleum products purchased in America for dollars, had an opportunity of acquiring control of another company's business by the purchase of shares

for 7,000,000 dollars, payable in dollars in New York. Being short of capital, they issued certain notes and then they borrowed on the notes.

On appeal against assessments to Income Tax under Schedule D the Company contended that they were temporary loans and that the interest thereon was an admissible deduction in computing its assessable profits. It was held that the interest on the notes in question was annual interest that it was payable on money employed or intended to be employed as capital in the Company's business and that the interest, the expenses of issue of the Notes and the amount of the exchange adjustments were not admissible deductions in arriving at the Company's profits for Income Tax purposes. After referring to the same line of authorities, such as *Jackson's* case and *Farmer's* case (*supra*), Singleton, J. completes his judgment at page 108 by saying :-

> "It is unnecessary for me to deal further with the matter except to say that bearing in mind the words of Lord Sumner and Lord Parker in the case of *Usher's Wiltshire Brewery, Limited* v. *Bruce,* 6 T.C. 399, and that which was said by Lord Justice Warrington in *Atherton* v. *British Insulated & Helsby Cables,* 10 T.C. at p. 182, I conceive the scheme of that part of the Act and of Schedule D, which deals with profits or gains from trade and deductions which can be made therefrom, to be this : That one must arrive at profits or gains in the ordinary commercial or business sense. Interest on ordinary banker's overdrafts which has arisen for ordinary trading purposes is a legitimate deduction, because it is money wholly and exclusively laid out or expended for the purpose of trade. On the other hand, interest on an issue of notes, whether for one year or for a longer period, may fall, and in the circumstances of this case does fall, into an entirely different category. It seems to me to savour much more of a capital nature or of some fund employed or intended to be employed as capital, and I do not think the issue of notes on which interest accrued would be regarded by business men as of the same nature as facilities obtained for ordinary trading purposes."

Two more cases present the same picture in particular, I wish to refer to the *Ascot Gas Water Heaters Ltd.* v. *Duff (Inspector of Taxes)* 24 T.C. p. 171, where it was held that the test to be applied was whether the sums in respect of which commission was payable constituted temporary accommodation obtained in the ordinary course of carrying on the business of the Company; that the Special Commissioners had not misdirected themselves in Law, and that there was evidence upon which they could arrive at their conclusions of fact, and the *European Investment Trust Co. Ltd.* v. *Jackson* (*supra*) was in fact applied.

At page 176, Lawrence, J. after quoting from the judgment of Romer, J. in *Jackson's* case (*supra*) the passage I have hereinabove referred to, proceeds and says :-

> "It appears, therefore, from those observations of Romer, L.J. that the matter cannot be concluded by considering simply whether the sum in respect of which the sum is sought to be deducted is fixed capital or circulating capital, and it appears to me that the only true principle must be the principle which is laid down by Finlay, J., and which is binding upon me, no other decision or criticism of his statement of the principle having been brought to my notice. The principle, therefore, which the Commissioners ought to have applied in each of these cases was whether the sums in respect of which the commission dealt with in these two cases was payable, were sums which, although capital, were temporary in their nature and might be regarded as an ordinary incident of carrying on the business of the Company."

Finally, we have the case of *Bridgewater and Bridgewater* v. *King (Inspector of Taxes),* 25 T.C. 285 in which the *European Investment Trust Company* and *the Ascot Gas Water Heaters,* cases were applied and it was held that the question whether money borrowed for the purpose of a business is "capital" within the meaning of Rule 3(f) is a question of fact, and that there was evidence on which the Special Commissioners could come to that conclusion.

The conclusion to be drawn from all these authorities is that it is a question of fact in each particular case, whether money borrowed is a mere temporary facility, an ordinary incident of carrying on the business of the Company, in which case interest paid thereon is an outgoing to earn the income and as such deductible as an expenditure of the business, or if, by the payment of interest, the company has in fact added to its capital and got sums which are used as capital so that in effect the business of the company is expanded, when the deduction cannot properly be made.

It is convenient, therefore, at this stage, to consider the factual aspect of this case.

The applicant Company, according to the evidence of its auditor Thiseas Metaxas, created its first overdraft in 1965 for the sum of £36,000, out of which £20,000 were used to acquire the shares in the Popular Bank of Limassol Ltd., and KEO Ltd., at their market value, and the rest in private companies. The shares in respect of which the amount of £20,000 was used, belonged to the late John Eliades, a relative of one of the Directors and shareholders of the applicant Company. He had incurred an overdraft and had difficulty in repaying same, so Mr. P. Lanitis had more or less to acquire his shares.

The borrowing of this money was done by means of a current account whose debit balance by the 31st December, 1969 was £91,178 and the 31st December, 1970 £116,998. The applicant Company had up to 1968 a shareholding of 20 per cent in the Cyprus Popular Bank of Limassol, Ltd. In 1969, when the British Bank of the Middle East obtained 20 per cent of the capital of the Cyprus Popular Bank by a special issue of shares, the percentage of the applicant Company dropped to about 12½ per cent. In 1970, the applicant Company was offered shares by the Popular Bank at an attractive price by way of rights issue shares, that is to say, shares that were offered to existing shareholders in proportion to their shareholding below their market value. In the view of Mr. Metaxas, it was commercially compelling to the applicant Company to buy them, from the point of view of the attractive price, also by comparison to the

dividends they were receiving, and the fact that thereby they were preserving their ratio in the capital.

The applicant Company was submitting its accounts annually to the Income Tax Office and from 1965 when it contracted its first overdraft, until 1969, the interest on loans was treated as a deductible expense. On the 10th September, 1969 the respondent Commissioner sent to all assessing staff with copy to all authorised accountants, including that of the applicant Company, Circular No. IR 118 (*exhibit* 4) in which it is stated :-

> "It has been our practice up to now to admit as a deductible expense payments of interest in respect of money borrowed for any purpose, although in accordance with the Law an expense is allowed only if it is incurred wholly and exclusively in the production of the income.
>
> 2. As from the year of assessment 1970 the concessional deduction in respect of payments of interest should be restricted only in respect of money borrowed for any of the purposes mentioned below :-
>
> (a) The purchase of shares in a private company, or the lending of money to such company for use in its business where the borrower has a substantial holding in the company;
>
> (b) The purchase of an interest in a partnership or the lending of money to a partnership for use in its business, where the borrower is an active partner;
>
> (c) The purchase of plant or machinery by the holder of an office or employment for use in performing the duties of that office or employment;
>
> (d) Any other purpose, provided the amount of interest involved does not exceed £50. If it exceeds £50, an amount of only £50 may be allowed."

According to Mr. Andreas Lanitis, one of the shareholders and Directors of the applicant Company, the practice of the Income Tax Office influenced them in shaping the policy of their Company in buying shares

in public companies, and indeed, it was one of the main advantages that led them to the formation of the Company. The statement of this witness has to be read in conjunction with the contents of paragraphs 6 and 7 of Schedule 'B' which were the facts relied upon in support of the present application, which read:-

> "6. Among the shares purchased by applicants are shares of the Popular Bank of Limassol which have been offered to applicants on a rights issue basis.
>
> 7. Consequently, applicants were obliged to buy the said shares in order to preserve their holding ratio in the said bank which is and was, at all material times about 20 per cent. That ratio is a substantial one and worth preserving in the interests of their business."

No doubt, this practice was one of the factors that influenced the applicant Company to contract loans for the purpose of purchasing shares, but not the only or the predominant one. There were, in addition, other compelling factors, as it appears from the evidence of their auditor, as well as from their own statement of facts hereinabove set out.

Considering the significance attached by the applicant Company in preserving the ratio of their shareholding in the said Bank, which, as stated on their behalf, being a substantial one, was worth preserving in the interest of their business, I have come to the conclusion that the purchase of these shares was an investment and not a purchase for the purpose of trading in them as part of their everyday business. Relevant to this conclusion and indicative of the mind of the applicant Company throughout the relevant years, is the fact that at no time since 1962 shares obtained by the applicant Company were sold, with the exception of 100 shares in the Famagusta Citrus Waste Control Co. Ltd. which were sold in 1967. The proceeds from such sale were not treated as revenue, but as capital return and as such, not taxable. Relevant also is the fact, as it appears from *exhibit* 5, its audited accounts submitted to the respondent Commissioner, that the applicant Company did not treat these shares as stock in trade, but as fixed assets. It should be pointed out,

however, that the *manner* a Company treats a particular item in its accounts, is conclusive only in the absence of any evidence to the contrary.

In Simon's Income Tax (1964 - 1965) Replacement Vol. 2, paragraph 472, p. 288, it is stated :-

> "The taxpayer's method of accounting may be of great importance where an entry is made in the accounts, not for the purposes of convenience, or for the purpose of giving effect to particular notions of account keeping but for the purpose of definitely deciding and of recording the fact that a decision had been come to that a certain payment is to be made out of capital and not out of income, or *vice versa*. In such a case the evidence afforded by the accounts would, in the absence of evidence to the contrary be conclusive on the point. (See *The Central London Rail, Co.* v. *I.R. Comrs,* 20 T.C. 102, 142 H.L.)".

Needless also to observe that in determining which items of expenditure are to be attributed to capital and which to revenue in order to arrive at the profit for income tax purposes in any particular year, the Courts accept the established principles of sound commercial accounting, unless there is a conflict with the statutory provisions. (See in this respect, *Odeon Associated Theatres Ltd.* v. *Jones (Inspector of Taxes)* [1972] 2 W.L.R. p. 331 and the authorities therein referred to).

In the present case it has been argued that to charge the interest in question to revenue, is contrary to the provisions of sections 11 and 13 of the Income Tax Laws (1961 - 1969). Under the said provision any disbursements or expenses not being money wholly and exclusively laid out or expended for the purpose of acquiring the income (section 13(e)) and any capital employed or intended to be employed as capital, are not allowable deductions. Outgoings and expenses are deductible for the purpose of ascertaining the chargeable income of any person, when wholly and exclusively incurred by such person in the production of the income. (Section 11(1)).

The Commissioner of Income Tax by his *sub judice* decision, bearing in mind the totality of the material before him, decided that the interest on the loan for the purchase of shares in public companies was not an allowable deduction, as they were expenses not wholly and exclusively laid out in the production of the Company's income. I have found no reason to disagree with the decision that the money borrowed was employed as capital, and consequently interest paid thereon was not a deductible expense under the Law.

The *Farmer's* case (*supra*) relied upon by the applicant, is clearly distinguishable, because the findings of fact in this case are different from those in that case, where it was the Company's business to trade in shares by buying and reselling them at a profit with money borrowed in a fluctuating temporary manner, the daily borrowing and lending of money being part of their trade and business. The interest was in truth money paid for the use or hire of an instrument of their trade as such, whereas in the case in hand, the Company invested money in an income producing asset. The fact that the borrowing of money by the applicant Company was done by means of a current account and not on a long term borrowing by means of a bond or otherwise, payable on a fixed future date, does not change the position. In my view, it is not the nature of the account as such that determines the purpose for which the money was borrowed.

In all the circumstances, therefore, the money borrowed was employed as capital and as such it was a non-deductible expense, the interest paid thereon falling within the same category, as on the true construction of the law and in particular sections 11 and 13 thereof, interest paid on money borrowed for the acquisition of capital, is not a deductible expense, as not wholly and exclusively laid out or expended for the purpose of acquiring the income.

I turn now to the second ground of law relied upon by the applicant Company, namely, that the respondent Commissioner by discontinuing the practice to treat such interest as an allowable deduction, acted contrary to the general principles of Administrative Law governing the

revocation of administrative acts and/or the change of administrative practice.

By letter of their counsel dated the 26th April, 1971, the applicant Company put their case on this ground, as follows:-

"Alternatively and/or further your decision complained of contravenes the well established principles governing proper administration as well as the revocation of administrative acts and it also infringes the principle of stability of administrative decisions. In this connection we should point out that as, over the past several years you have consistently allowed deduction of such interest, our clients, relying on your aforesaid policy, have changed materially their financial position and they have shaped their financial policy accordingly so that you are now precluded from suddenly changing course without any supervening change in the legislation. You are therefore, hereby requested to let us know the specific matters that prompted you to change your previous practice and decisions on the matter which you consistently followed over the last several years."

The exposition of the law regarding the effect of administrative practice as stated in *P.M. Tseriotis Ltd. and Others* v. *The Republic* (1970) 3 C.L.R. 135 at p. 143 has been invoked by both sides as supporting their respective position. It reads as follows:-

"Of course, if the practice followed in the past by the Department in question was contrary to law, it cannot create a legal rule which would enable the applicants to succeed in these recourses. But, leaving aside the complicated question of principle as to whether or not, and to what extent, custom can be the source of law for administrative law purposes (see Kyriacopoullos on Greek Administrative Law, 4th ed., vol. I, p. 78 - 80 and Dendias on Administrative Law, 5th ed., vol. I, p. 51 - 52), it seems to be sufficiently clear that an administrative practice which is consistent with the correct construction of the relevant legislation is properly

applicable (see Lectures on Administrative Law by Stassinopoullos, 1957, p. 127)."

Relevant to this issue is also what was stated in *Soteriou* v. *The Greek Coommunal Chamber* (1966) 3 C.L.R. p. 83 at pp. 104 - 105. It reads :-

"…. As it is well established that, when the validity of the revocation of a previous administrative decision is examined by a Court of Law, the possible prejudice suffered by a person, who has acted on the strength of such previous decision, is a very weighty consideration so, a fortiori, such prejudice, if any, should have been gone into when deciding whether or not to retire applicant, consequent upon a complete reversal of the previous policy regarding extension of service of schoolteachers—and on which previous policy applicant had already been clearly induced to rely.

Yet, as Mr. Georghiades, has clearly testified, the individual merits of applicant's case, including any relevant financial circumstances, were not gone into, at all in reaching the decision to retire him."

In *Tseriotis* case (*supra*) it was concluded that the practice followed was consistent with and reflected the proper construction as a whole of the then in force relevant legislation, namely, the Customs Management Law, Cap. 319 and that it should have been followed for the purposes of that case as well, whereas in the present case I have already concluded that the practice to allow such deductions was not springing from the construction of any statutory provision or that the practice followed could be in any way consistent with and reflecting the proper construction of the Law. Furthermore, what is a deductible expense under section 11 is not a matter of administrative discretion, but a question of law governed by well settled principles.

On the other hand the decision to retire the applicant in *Soteriou* case (*supra*) was reached in the circumstances already mentioned and before any decision to terminate generally the practice was duly taken. The applicant had suffered a change in his financial and other personal circumstances by relying on the clear

promise originally held out to him that his service would be extended until the age of sixty years. It was in that factual background that the statement of the law hereinabove set out was made and the conclusion reached that the discretion of the administration under the relevant section of the Law was exercised in a defective manner and the outcome thereof had to be annulled.

No doubt, when the administrative practice is a matter of exercise of discretionary power in a certain way, the fact that such practice has lasted for a long time, can possibly have certain consequences in the law of administrative acts and the administration cannot suddenly abandon such a practice without giving reasons for it, but otherwise the administration is not bound, except to the extent of giving reasons for such change; (see Decisions of the Greek Council of State 1185/34 and 343/38 and also Stassinopoullos the Law of Administrative Acts 1951 at p. 19, where it is also pointed out that this freedom in changing a practice is imperative on account of the need that the administrative discretion should be exercised on each occasion freely and unfettered in the light of the particular circumstances). If, however, an administrative practice may be changed as above, in respect of a particular instance, whilst still followed on other instances, a fortiori it may properly be terminated with prospective effect and this is what has happened in the present case.

Therefore, what has been stated regarding the principles of Administrative Law, governing administrative practice and its effect, have to be viewed in the light of the conclusions reached and the circumstances of this case. In fact, it may be pointed out that the decision to change the previously followed practice emanating from a general discretion or policy was within the knowledge of the applicant Company and according to the evidence adduced on their behalf, they could employ other equally favourable methods in time, but they elected not to do so, insisting on their own interpretation of the relevant legislation and the legal effect of such administrative practice.

In any event, the respondent Commissioner could freely terminate these deductions being the result of

concessionary administrative practice. As stated by Stassinopoullos, in The Law of Administrative Acts, 1951, at page 409, the so-called concessionary acts or acts of grace, that is to say those acts that give to the citizen benefits without a corresponding obligation on his part, may be freely revoked.

With respect to the arguments advanced I cannot agree with the proposition put forward by learned counsel for the applicant Company that the administration could not terminate such previous concessionary practice, nor could I agree that such termination amounts to contravention of any general principle of administrative law or of any provision of our Constitution in the sense that same amounts to a violation of the principle of security in law.

As pointed out in Kyriacopoullos, the Greek Administrative Law, 4th ed. vol. A at p. 78, which proposition I fully adopt, the source of taxation in general is the law (this is provided also by Article 24 of our Constitution which says that no tax duty or rate shall be imposed save by or under the authority of a law); and not only the imposition of tax by virtue of custom is excluded, but it is also not possible to abolish a tax by custom or by the non application of a particular statutory provision for a long time.

Ancillary to this ground is the further argument that even if this practice could be terminated, such termination should refer to the future and not to the past; and so interest payable on debts incurred prior to the termination should continue to be disallowed in the future. I am afraid I cannot agree with this proposition, as I am of the view that an administrative practice and concessionary at that, creates no such rights and needs no legislation for its change.

The last ground of law relied upon by the applicant Company, is that the decision to disallow interest paid on money borrowed for the purpose of the purchase of shares in public companies and the distinction made thereby with respect to borrowings regarding purchase of shares in private companies is arbitrary, unreasonable and unjustified and results in discrimination in violation of Articles 24 and 28 of the Constitution.

Counsel for the respondent in support of this differentiation has contended that it was based on a reasonable distinction emanating from the many differences that exist between public and private companies and the reason for the disallowance of interest on monies borrowed for the purchase of shares in public companies is because such shares are clearly held by an individual or company as an investment, whereas the acquisition of shares in a private company is considered to be the result of an arrangement under which the holder carries on his trade or business.

The principle of equality has been considered in a number of judgments of this Court. In the case of *Mikrommatis* and *The Republic,* 2 R.S.C.C. p. 125 at p. 131, the then Supreme Constitutional Court said that "'equal before the law' in paragraph 1 of Article 28 does not convey the notion of exact arithmetical equality but it safeguards only against arbitrary differentiations and does not exclude reasonable distinctions which have to be made in view of the intrinsic nature of things". This proposition has been reiterated in the judgment of the Full Bench of this Court in *Republic* v. *Nishan Arakian & Others* (1972) 3 C.L.R. 294, where a review of the judicial approach of this principle in Greece, the United States and the European Court of Human Rights is made.

It has to be examined, therefore, whether this decision is, as claimed by the applicant Company, contrary to the aforesaid Articles of the Constitution, as being arbitrary and unreasonable.

Under our Companies Law, Cap. 113, registered companies are classified into two broad categories, namely, public and private companies; by section 29(1) of the Law a private company is defined as meaning —

"...... a company which by its articles —

(a) restricts the right to transfer its shares; and

(b) limits the number of its members to fifty, not including persons who are in the employment of the company and persons who, having been formerly in the employment of the company, were while in that employment, and

have continued after the determination of that employment to be, members of the company; and

(c) prohibits any invitation to the public to subscribe for any shares or debentures of the company."

Compliance with these limitations gives to such a private company certain privileges and exemptions under the Law and under the provisions of section 30 a company which stops complying with them, loses such privileges and exemptions and ceases to be a private company.

It will serve no purpose if I enumerate all the differences to be found in the several sections of the Companies Law regarding these two categories of companies. It is sufficient to draw attention to a private company's obligation to restrict by its articles the right to transfer shares and the prohibition therein of an invitation to the public to subscribe for any shares or debentures of the Company, as these, in my view, bear out the distinction made and the reasons for such differentiation which, in the field of Company Law is well established, as it will also appear from what follows :-

In Palmer's Company Law, 21st edition, at p. 36, one reads :-

"Private Companies

Their function

The modern private company serves two purposes : First, to enable those carrying on a family business to avail themselves of the advantages of corporate trading and, secondly, where used as a subsidiary in a group of companies, to avoid, with respect to that part of the group, the strict requirements obligatory for public companies. Although these purposes differ intrinsically, one feature is common to all private companies, a feature which, at the same time, limits the economic use of that form of company : According to its constitution, members of the investing public cannot acquire shares in the private company at will, and where it is intended that the company should be able to

> invite members of the public to acquire a proprietary interest in it without participating in the management, the private company is not the appropriate form and the company has to be formed as, or more frequently converted into, a public company. In many private companies, particularly those carrying on family businesses, the ownership in the company and its management will be in the same hands."

and at p. 337, it is stated :-

> "A private company is normally what the Americans call a 'close corporation'; this means that its members are connected by bonds of kinship, friendship, or similar close ties and that the intrusion of a stranger as shareholder would be felt to be undesirable unless his admission is accepted by those for the time being interested in the company. For this reason in private companies the regulation dealing with the restriction of the right to transfer shares, apart from satisfying a statutory regulation (s. 28(1)(a)), is of particular practical importance."

In my view, these restrictions regarding the free transferability of shares hampers dealings in them and prevents them from being an open investment.

In the circumstances I cannot but conclude that the principle of equality of treatment has not been violated as the distinction made has objective and reasonable justification.

This concludes the points raised in the present recourse, as another ground regarding lack of due reasoning has not been insisted upon and therefore I need not say anything about it as virtually abandoned.

For all the above reasons the present recourse is dismissed.

The importance and novelty of the legal points raised and their being of interest to a wider circle of tax payers, justify me in making no order as to costs.

Application dismissed.
No order as to costs.