IN THE HIGH COURT OF SOUTH AFRICA
(EASTERN CAPE DIVISION)

CASE NO: CA 590/2001

Date delivered: 23 May 2002

IN THE MATTER BETWEEN:

Commissioner For The South African Revenue Service **Appellant**

AND

Heron Heights CC **Respondent**

INCOME TAX - PROCEEDS OF SALE OF LAND - WHETHER CAPITAL ACCRUAL OR REVENUE RECEIPT.

JUDGMENT

KROON J:

INTRODUCTION:

[1] At issue in this appeal is the taxability of a gain of approximately R200 000,00 realised by the respondent close corporation on the sale of two erven at Knysna during the tax year ending 29 February 1996.

The Commissioner (the appellant) assessed the gain to tax as constituting taxable income.

An appeal by the respondent to the Special Court (presided over by *Erasmus* J) against the assessment was successful, that Court having held that the receipt in question was of a capital nature, and therefore not taxable. It is that decision that the appellant seeks to assail in this appeal.

BACKGROUND:

[2] During December 1994 contracts were concluded for the acquisition by the respondent (then to be formed) of the two erven. The respondent was registered as a close corporation on 27 December 1994. Transfer of the properties into its name was effected on 1 March 1995.

[3] The respondent commenced taking certain steps with a view to developing a group housing scheme on the properties. Those steps attracted the intervention of the developer of a neighbouring property ("Group Five"), who objected that the respondent's project would have the effect of interference with the view from the neighbouring property. *Inter alia,* court action to stop the project was threatened. The upshot, after negotiations between the parties, was the acquisition, during June 1995, by Group Five of the erven from the respondent for the sum of R460 000, 00, which transaction generated the profit with which this appeal is concerned.

PRINCIPLES:

[4] S 82 of the Income Tax Act (No. 58 of 1962) saddles an objecting taxpayer with the onus of persuading the Court on a balance of probabilities that the assessment objected to is wrong. In *Reliance Land & Investment Co. (Pty) Ltd v CIR* 1946 WLD 171 at 181-2; 14 SATC 47 at 57, the following *dictum* appears:

> "If the probabilities are evenly balanced, if it is impossible to say affirmatively that the appellant

> company's sale of the properties occurred in the course of mere realisation of an income-producing investment, not in the course of trafficking in property, then it is impossible to say that the Commissioner's decision to the contrary is wrong, and the appellant company has not discharged the *onus* on it under sec. 78 of the Act to show that the purchase price of these properties is not liable to tax chargeable under the Act".

[5] In terms of the definition of "gross income" in s 1 of the Act receipts or accruals of a capital nature are excluded therefrom. (The exceptional instances where capital accruals are taxable are not of relevance).

[6] The question whether an accrual was of a revenue or capital nature is one of law, to be determined on the particular facts (which may be so conclusive as to lead automatically to a decision of law one way or the other). *SIR v The Trust Bank of Africa Ltd* 1975 (2) SA 652 (A) at 666, 671; 37 SATC 87 at 103, 108.

[7] *Inter alia,* the following considerations come into play: Capital may be either fixed or floating: the latter is consumed or disappears in the process of production, the former remains intact (albeit that it may have to be renewed); the question at issue is essentially whether the sale amounted to the realisation of a capital asset or whether it was the sale of an asset in pursuance of a profit-making scheme: the latter connotes the acquisition of an asset and holding it for the purpose of resale, at an opportune time, at a profit, which is then the result of the productive turnover of the capital represented by the asset (the taxpayer's stock-in-trade or floating capital) and therefore constitutes income, in contradistinction to which the former connotes the sale of an asset acquired with a view to holding it (either in a non-productive state, or in order to derive income from the productive use thereof); in the determination of the question into which of these two classes a particular transaction falls, the intention of the taxpayer, both at the time of the acquisition of the asset and at the time of its sale (for the intention might have changed in the interim) is of great, sometimes decisive, importance (although it has not been laid down that a change in policy or intention by itself effects a change in the character of the assets); the mere *ipse dixit* of the taxpayer in this regard cannot, in the nature of things,

be conclusive; it must be tested against all the other relevant considerations; these include, *inter alia*, the objects of the owner, if a company, as laid down in its memorandum of association, the activities of the owner in relation to the land up to the time of the decision to sell it, in whole or in part, the light which such activities throw on the owner's *ipse dixit* as to his intention, the relationship of all of this to the ordinary commercial concept of embarking on a scheme for profit, the taxpayer's other business operations, if any. All of these considerations are guidelines only, none is conclusive and the list is not exhanstive. The Court's findings may be based not only on facts specifically established, but also on inferences justifiably to be drawn therefrom. See, e.g., *CIR v George Forest Timber Co Ltd* 1924 AD 516 at 524; *Natal Estates Ltd v SIR* 1975 (4) SA 177 (A) at 202A-203A; 37 SATC 193 at 219-220*; Elandsheuwel Farming (Edms) Bpk v SBI* 1978 (1) SA 101 (A) at 126B-127H; 39 SATC 163 at 189-190; *CIR v Pick 'n Pay Employee Share Purchase Trust* 1992 (4) SA 39 at 56H - 57F; *Malan v KBI* 1981 (2) SA 91 (C) at 96F; 43 SATC 1 at 7; 1983 (3) SA 1 (A) at 18D-H; 45 SATC 59 at 76-77; *CIR v Richmond Estates (Pty) Ltd* 20 SATC 355 at 366; *ITC 1251* 38 SATC 173; *Ropty (Edms) Bpk v SBI* 43 SATC 141 at 148; *SIR v Cadac Engineering Works (Pty) Ltd* 1965 (2) SA 511 (A) at 520F; 27 SATC 61 at 72.

[8] As to the intention of the taxpayer, the following was said in *Pick 'n Pay* at 58F:

> "Contemplation is not to be confused with intention in the above sense. In a tax case one is not concerned with what possibilities, apart from his actual purpose, the taxpayer foresaw and with which he reconciled himself. One is solely concerned with his object, his aim, his actual purpose."

[9] On the other hand:

> (1) A person who envisages making a profit in either of two ways does not have a "dominant purpose" in respect of one of those manners merely because he prefers the one above the other; in such a case the Court may find that both ways form part of a single scheme of profit-making, which could be brought to fruition

in two alternative manners. *Malan* at 94E-F; *Ropty* at 149.

(2) Where an alleged intention is not attainable in accordance with the objective facts "the inevitable must be taken to have been intended", e.g., a sale for profit in lieu of a development of the land. *ITC 1597* 58 SATC 27; *ITC 1507* 53 SATC 425.

[10] A forced relinquishment of land indicates neither a capital nor an income accrual, but its consequences are the same as those of a voluntary sale. *ITC 1239* 37 SATC 289 at 293-294; *ITC 1507* 53 SATC 425 at 438; *ITC 1547* 55 SATC 19 at 24-25.

THE RESPONDENT'S CASE:

[11] The case which the evidence tendered on behalf of the respondent in the Court *a quo* (given by Messrs Vercueil and Steenekamp) sought to make out, and which, in general, was echoed during argument, proceeded in essence as follows: Vercueil, Steenekamp and two other associates, Messrs Shaw and Hill, were desirous of acquiring the two erven for the purpose of providing themselves with dwelling places. For this purpose they decided to use the vehicle of a close corporation to be formed (i.e., the respondent, of which they became the members), which would acquire the erven and, after rezoning, consolidation , and subdivision of the erven, would sell those portions thereof which were to be occupied by the members, to them at cost. At an early stage, Hill fell out of the picture and his interest in the respondent was taken over by the other three members. The envisaged subdivision was to be into eight units, three of which would be allocated to the members. Although the possibility of the development, for profit on resale, of a group housing scheme on the erven, each of the eight separate units having dwellings thereon, was contemplated (and certain steps were taken to that end - as to which, see below), in fact no decision to develop the property or any portion thereof for financial gain was ever taken; the only firm and positive decision taken was that the personal requirements of Messrs Vercueil, Steenekamp and Shaw would be catered for,

later enlarged to include the provision, also at cost, of one of the subdivided eight erven to Vercueil's mother. The possibility that the remaining erven might have been developed and leased out, so as to be of source of income to the respondent, was also, at one stage during his evidence, mentioned by Vercueil. In the result, the respondent's intentions with the erven were, as it were, overtaken by events; specifically, the intervention of Group Five. The respondent did not have the financial muscle to become embroiled in litigation with Group Five, which might have been a protracted process; it was therefore, in a sense, obliged to sell the erven to Group Five. (For the sake of completeness, it may be recorded that the respondent was offered three options by Group Five: (a) a substantial amendment to the scheme it was envisaging, so as to contain the interference with the view from the property that Group Five was developing; (b) a joint venture between the respondent and Group Five; (c) the sale of the erven to Group Five. In the result, the first two alternatives did not find favour with the respondent; the third one did. The respondent invited Group Five to make an offer for the properties. An initial offer of R320 000,00 was rejected. A counter-offer was requested. The members of the respondent "put a price together which was based on our efforts to that date", which was submitted to Group Five, viz., in the sum of R460 000,00. According to Vercueil, the price was fixed at that "high" figure, in the hope that it would persuade Group Five to lose interest and "go away". However, after initially rejecting the counter-offer as "ridiculous", and unsuccessfully making a further offer of R380 000,00, Group Five in fact did accept the figure fixed by the respondent and insisted on by it).

[12] Mr *Emslie* (who appeared for the respondent), repeating an argument raised by him in the Court *a quo*, submitted that the steps actually taken by the respondent, or which it envisaged taking (details of which are set out below) in respect of the development of a group housing scheme on the property, were no more than steps to set the scene for a possible decision by the respondent in the future to embark on a scheme to sell the surplus property (i.e., that not required for the provision of dwellings to its members) for a profit; the formation of any such intention was, however, conditional on the steps taken and to be taken meeting with success; because that condition was not

fulfilled, no such intention had ever come into being; the one definite intention formulated, to sell to members at cost, fell outside the notion of a scheme embarked upon for profit; the further possibilities, such as an intention of a sale for profit, were dependant on uncertain future events; no trading activities in respect of the land were ever commenced; while the possible formation of an intention of sale for profit might have been something contemplated by the respondent (as to which, see the extract from *Pick 'n Pay*, quoted in para. [8] above), the respondent's factual purpose had in the circumstances in fact never embraced a sale of any portion of the property for a profit; instead, its intention had accordingly been to hold the erven as a capital asset, and that was their nature at the time of the disposal thereof to Group Five. A supplementary submission was that it had been the dominant purpose of the respondent to provide homes for its members (which, intended to be at cost, would not have entailed any profit, and would therefore have constituted a disposition of a capital asset, and not a revenue disposition), and that any possible sale of the remainder of the property - at best, a conditional and speculative prospect - had been no more than an ancillary purpose.

[13] It should be recorded that, on appeal, Mr *Emslie* did not seek to attack the validity of the findings by the Court *a quo* that the evidence tendered on behalf of the respondent had been insufficient to establish that embraced within the respondent's factual purpose was either:

(1) the provision of one of the envisaged subdivided units as a dwelling for Vercueil's mother; or

(2) the leasing by it of the units not required by its members.

That approach was correct, and the aspects referred to do not require any further consideration.

THE DECISION OF THE COURT *A QUO*:

[14] The Court *a quo* found both Vercueil and Steenekamp to have been unsatisfactory witnesses: their evidence was evasive, contradictory and improbable and flew in the face of the documentary evidence, material aspects of which they were unable to explain on their version. Subject to what follows later, it was held that the decision in the matter could not be founded on the evidence of the witnesses, but had to be reached on the basis of inferences to be drawn from the objective facts and the actions of the respondent as reflected in the documentary evidence.

[15] The inference that the Court *a quo* did draw, was that throughout the relevant period (i.e., before the sale of the erven to Group Five) what the respondent intended and was about was the development of a group housing scheme for profit.

[16] The Court *a quo* did, however, accept the evidence of Vercueil and Steenekamp where it was considered that same accorded with the probabilities or was corroborated by other evidence, viz., that it was the intention that Vercueil, Steenekamp and Shaw would each acquire a developed unit at cost, the members of the respondent having initially come together for the purpose of purchasing the erven with the immediate view to building houses for themselves on the property, and that, as already indicated above, it was the intervention of Group Five that led to the sale of the property.

[17] In reaching the conclusion recorded in para. [15] above, the Court *a quo* rejected the argument founded on the contention that the respondent's dominant purpose was to provide dwelling places for its three members. It held that the argument blurred the distinction between the close corporation and its members, and further confused motive with purpose: notwithstanding that the reason why the members initiated the scheme might well have been their wish to have dwellings erected for themselves on the property, it was the respondent's purpose (intention) to develop eight units on the property (as to which, see below), with only three of those units being earmarked for the members; while the members would have obtained their units at cost and these units were therefore

neutral in the matter of profit, the profit motive did attach to the majority of the units. However, so it was noted, there was no formal agreement between the members in respect of the acquisition of units, no enforceable agreement with the respondent thereanent, and no certainty that all three members would have continued with the scheme.

[18] However, the Court *a quo* held that the enquiry did not stop with the findings recorded above. It considered that a further question to be answered was whether a change in the intention of the respondent had not supervened (even though, so it was specifically recorded, such a change in intention had not been pertinently advanced by the respondent). After a reference to certain authorities which concerned the result of a change in the intention of a taxpayer (i.e., from holding an asset as a capital asset to holding it for the purpose of resale on profit), it was recorded that there was no reason why a change of intention should not work the other way (and reference was made to the decision in *New Mines Ltd v CIR* 1938 AD 455 at 461). Such a decision could be forced on a taxpayer, and that, in the view of the Court *a quo*, was what occurred in the instant matter. The respondent had not bought the erven with a view to selling them for profit, nor had it ever been in the business of property speculation (in the context these two comments were intended to refer to a sale of the erven in their undeveloped state); its intention had been to develop a group housing scheme; circumstance then forced it to sell the property as a whole in an undeveloped state. A change of intention, so the Court *a quo* concluded, was implied in the sale.

[19] The Court *a quo* recognized, however, that, as is laid down in the authorities, a change of intention is not the exclusive, or necessarily decisive, consideration. Other significant factors to be considered in the determination of the question into which of the two categories at issue a transaction fell, included, *inter alia*, "the actual activities of the taxpayer in relation to the asset in question" and "the manner of its realisation." In the view of the Court *a quo* these two considerations were of considerable importance in the context of the present case, where the intention of the taxpayer was not brought to fruition. In this

regard three aspects were emphasized: (i) the nature of the objects that were sold compared to what the respondent had intended to market; (ii) the stage of the development of the objects sold; and (iii) the sale of the property.

[20] Shortly stated, the Court *a quo* applied these three considerations in the following manner:

> (1) What was in fact sold, differed so markedly from what had been intended to be sold that they were in fact entirely different things;
>
> (2) Very little had been done in the implementation of the group housing scheme; a great deal of physical effort and expenditure lay ahead. The land at the time resembled *raw materials* rather than *stock-in-trade* or even *work-in-progress* and "raw materials are more likely to constitute a capital asset than would manufactured articles, especially in bulk sale". There was, moreover, no certainty that the scheme would be implemented, with finance being the major obstacle (a loan applied for had not yet been granted and there was no certainty that it would be granted, in whole or even in part).
>
> (3) The actual manner of sale differed markedly from what had been intended, and took place in circumstances unintended, and in fact unforeseen, by the respondent, and which put paid to its intended scheme; the price paid was not because of the value of the property or the prospects of the group housing scheme, but because Group Five had wished to remove a threat to its own development.

[21] On the above approach it was concluded that what the respondent disposed of was a capital asset, the consideration for which was not taxable.

EVALUATION:

[22] At the hearing of the appeal Mr *Emslie* did not seek to persist in the attack, contained in his heads of argument, on the credibility strictures passed by *Erasmus* J on Vercueil and Steenekamp. Similarly, Mrs Battheu, for the appellant, accepted as a premise for her argument the correctness of the finding of the Court *a quo* that the intention of the respondent with the erven embraced the provision of homes for its three members. The attitude of both counsel was correct.

[23] As indicated earlier, Mr *Emslie* did attack the finding of the Court *a quo* that the respondent had formed the intention to sell the remaining five erven as part of a profit-making scheme. In amplification of the argument already recorded, counsel made two further points. First, he submitted that notwithstanding the criticism levelled by *Erasmus* J at Vercueil and Steenekamp, their evidence that no such intention had ever been formed by the respondent should be accepted; the possibility of such sale(s) taking place had been no more than a dream. Second, it was restated that unless and until the conditions applicable to the formation of such an intention were fulfilled, the stage could not have been reached where such an intention could have been formed; and the conditions were in fact never fulfilled.

[24] I have little difficulty in endorsing the conclusion of the Court *a quo* that the two erven were acquired by the respondent with the intention that the major portion thereof, five plots, were to be resold, and the whole venture would realise a profit. I agree that the objective facts, detailed below, (including some not mentioned in the judgement of the Court *a quo*) lead inexorably to the inference that profit-making was the intention with the acquisition of the erven, and that the evidence of Vercueil and Steenekamp to the contrary was properly rejected. As Mr *Emslie* was constrained to concede, the respondent must have had *some* intention with the major portion of the property not required for members' dwellings; that intention could only have been one of two kinds: to hold the erven as stock-in-trade for resale at a profit or to hold the property as a capital asset to serve some other purpose. While Vercueil and Steenekamp sought to resist the reliance on the bases invoked by the appellant for the contention that the former

alternative was correct, no sufficient basis for the latter alternative being correct was laid.

[25] The objective facts pointing to profit-making on resale having been the respondent's intention may be tabulated as follows:

(1) In the application for its registration as a close corporation the respondents's principal business was reflected as "RESIDENTIAL PROPERTY DEVELOPMENT", and in its financial statements for the year ending 31 October 1995 the nature of its business was given as "Eiendomsontwikkeling". These descriptions tie in with an intention of resale at a profit. While, as Mr *Emslie* pointed out, these descriptions, on the face thereof, are not inconsistent with an intention of holding a developed property as a capital asset, the mooting by Vercueil of a possible purpose to be achieved thereby, i.e., in relation to the five surplus erven, viz., the possible leasing thereof, was correctly rejected by the Court *a quo.*

(2) In a letter dated 23 December 1994 the respondent advised its attorneys that "(t)he development will consist of 8 group housing units to be sold under individual title, and that rules would have to be drawn up regulating such matters as aerials, dogs, awnings, shades, etc. The attorneys were instructed to attend to the following:

- Drawing of a Home Owners Agreement;
- Deeds of Sale;
- Future Transfers;
- The CC Agreement.

(3) During December 1994/January 1995 Vercueil, an architect by profession, drew up building plans for the development. The overall plan was styled "PLAN OF PROPOSED SUBDIVISION". According to notes on the document the erven were to be consolidated and rezoned to "group housing" and reciprocal servitudes were to

be registered in favour of a "group housing scheme." The plans provided for eight separate dwelling units arranged in two groups of four each on separate levels. The four plots on the higher level were to be sightly larger than the four on the lower level. On 9 January 1995 Vercueil submitted the plans to the municipality for approval. They were accompanied by an engineer's certificate in respect of the proposed eight erections. The engineers also submitted a letter to the respondent detailing their fees for the project.

(4) At approximately the same time Vercueil submitted an application (said to have been lodged with the Deeds Office) for the rezoning of the properties to allow a group housing scheme thereon. The evidence is not clear whether this application was accompanied by an application for the consolidation of the two erven. It was, however, the respondent's intention to apply for such consolidation, if that had not already been done, and thereafter to apply for the subdivision of the consolidated property into eight plots. It may be noted that prior to Group Five's coming onto the scene the prospects of securing the permission required for the establishment of the group housing scheme appeared to be good: there had been no objections to the relevant advertisements and, in common with the surrounding area which had group housing status, the erven had already been earmarked for group housing.

(5) Vercueil also prepared a document titled "STANDARD SPECIFICATIONS - BUILDING WORK", wherein the work to be undertaken was described as:

- Build 4 group housing units of 209 m²
- Build 4 group housing units of 189 m²

Tenders by suppliers, i.e., subcontractors, for the supply of materials such as, e.g., reinforced concrete, were invited and received. (The document was, however, never sent to any main contractor).

(6) On 31 January 1995 Steenekamp submitted an application for the registration of the respondent as a vendor for purposes of VAT. Therein the main activity of the respondent was given as "townhouse development" and it was further reflected that the "TOTAL VALUE OF TAXABLE SUPPLIES" would be R1,9 million (a figure that Vercueil conceded related to the eight dwelling units on the property).

(7) On 29 March 1995 Vercueil completed viability studies in respect of the four smaller units, the four larger units and of all eight units as a whole. The total itemised costs for the eight units, minus an expected repayment of a VAT input claim by the respondent, were calculated at R1 473 235,08. According to Vercueil the figures *were realistic and the studies indicated that the scheme was viable.*

(8) The respondent approached various institutions for assistance to finance the housing development of the eight units. The amount of the assistance sought, R1,4 million, was based on the viability study undertaken in respect of the eight units. The approach followed on a decision taken at a meeting of the respondent's members that such financial assistance should be sought. Allied to this aspect were Vercueil's admissions relating to certain notes made by him during a telephonic conversation with a representative of one of the banks, that:

> (a) the word "onderbenutting" in the notes had reference to the attitude that if approval for eight units was secured it would make no sense to build only one;
>
> (b) that there would definitely be a financial advantage in building eight units rather than only one unit, of the order of 5 to 10% per unit.

(9) The minutes of a meeting of the respondent on 23 January 1995 reflected a

resolution that there was to be no alteration to the original plan. The only plan the respondent then had was to build eight units. It was also recorded as follows:

> "S.P. (i.e. selling price) R 279 000,00 inc. VAT."

(10) In minutes of a further meeting of the respondent on 13 June 1995 (i.e., after Group Five had intervened), at which certain proposals by Group Five were recorded, the following entry appears:

> "Suggest we declare units to 6 only [Along middle of site only] more space per site …… Prepared to pay profit on 2 X units [R40 000,00]".

After initial evasiveness, verbosity and denials relating, *inter alia*, to the meaning of the word "profit" and (what was obvious) the offer by Group Five to compensate the respondent for the loss of profit on two units, Steenekamp eventually conceded that the respondent had earlier advised Group Five that its intention was to build eight units on the property.

(11) In the letter of objection against the assessment, dated 19 November 1998, addressed to the appellant by the accountants representing the respondent the following passage appears.

> "Oorspronklik was die volgende oorweeg:-
>
> - Om vir elke lid 'n eenheid te bou vir elkeen om te bewoon.
> - Om meer as 3 eenhede te bou *en dan die oorblywende eenhede to verkoop.*
>
> Uiteindelik was daar op 8 eenhede besluit genotuleer in 'n brief gedateer 23 Desember 1994 aan Meyer & Martin Prokureurs"
> (as to which, see (2) *supra*)

[26] *Apropos* the argument of counsel: the fact that bringing an envisaged profit-making scheme to fruition would depend on a number of conditions being fulfilled and a

number of events successfully occurring does not, and cannot, mean that the taxpayer did not form the intention to implement the scheme and reap the profit. On the contrary, the inference *in casu* is that the respondent intended that everything that would be required to transpire, would in fact transpire. Counsel was unable, not surprisingly, to refer to any authority for the proposition that where a profit-making scheme is envisaged, but its successful implementation would depend on the happening of certain events, the required intention to engage in a profit-making scheme, as opposed to what counsel referred to as an "inchoate" (and insufficient) intention, is not to be ascribed to the taxpayer until the conditions in question are actually fulfilled. The decision in *ITC 1659* 61 SATC 239, referred to in para. [32] below is authority against that proposition.

[27] In my judgment, the matter may be resolved on the basis of the following simple approach: The respondent acquired the two erven for the purpose of resale (after the necessary rezoning, consolidation and subdivision had been effected) at a profit (albeit that the sale of portion of the erven, the three units to be allocated to its members, would not attract a profit); the respondent did in fact sell the two erven at a profit (albeit under different circumstances than those originally envisaged - as to which, see below); *ergo*, the profit-making intention having in fact resulted in profit, such profit was correctly assessed to tax.

[28] It is necessary, however, to consider the conclusion of the Court *a quo* that, on the facts, a change of intention had supervened, the result which was that the two erven were dealt with as a capital asset, the profit-making scheme having been abandoned. The approach of the Court *a quo* in this regard has been detailed in paras [18] to [21] above.

[29] It should immediately be recorded that Mr *Emslie* did not seek to support that approach. As already set out, it was counsel's submission that on the evidence there never was a profit-making intention (the corollary of which that there could be no talk of a change of intention to one where the property was held as a capital asset). Counsel frankly stated that, on the premise of the correctness of the finding that the respondent's

intention involved a profit-making scheme, he could not, in the absence of any evidence on behalf of the respondent that there had been such a change of intention on its part, argue that the decision of the Court *a quo* on this score should be confirmed. For my part, I would record that in the absence of any direct or indirect claim in evidence that such a change of intention had supervened, it would be extremely difficult to find as a fact that that had occurred, although, I would suppose, it cannot be excluded that the conduct of a taxpayer and the circumstances may be such that, objectively viewed, the inference is inescapable, or at least sufficiently compelling, that such a change of intention has supervened.

[30] As indicated earlier, the essential basis of the conclusion of the Court *a quo* was that the result of the intervention of Group five was an abandonment of the profit-making scheme that the respondent had intended implementing, and the erven were disposed of in circumstances and in a manner quite different and not previously contemplated; in short, the abandonment of the specific earlier profit-making scheme converted the erven into capital assets.

[31] With respect, I am unable to endorse that approach. The short answer thereto, in my judgment, is that set out in para. [27] above, amplified by a recordal thereof that there was no hint or suggestion in the evidence that after the intervention of Group Five the respondent altered its earlier intention to sell at a profit to an intention to hold the property as a capital asset. Indeed, the somewhat rhetorical question posed by Mrs Battheu during argument bears repetition: having regard thereto that the respondent replaced its earlier intention to develop and resell at a profit with an intention to sell the undeveloped erven, also at a profit, when and under what circumstances was it possible for the change in intention, viz to hold and then dispose of the property as a capital asset, to have taken place?

[32] The circumstances that the mechanics of the resale for profit were different from those originally intended and envisaged and that there was an alleged element of

"compulsion", consequent upon the intervention of Group Five, in the resale actually effected, did not mean that the nature of the asset or the respondent's intention to resell it at a profit had changed. See the principles adverted to in para. [9] above. C.f. in this regard the decision in *ITC 1659*. In that case a close corporation acquired an undeveloped parcel of land for the admitted specific purpose of subdividing same, developing a group housing scheme thereon and reselling the individual units as part of a profit-making scheme. Various steps towards this end were taken. The scheme floundered, however, when the local authority concerned refused, against expectation, to provide bulk services for the development, and the close corporation simply did not have the financial means to supply the services itself and proceed with the development. A buyer came on the scene and the land, undeveloped, was sold to it. An argument, on behalf of the taxpayer, which proceeded along the lines of the approach of the Court *a quo* in the present matter, was rejected in the following terms at 248:

> "That is however not the end of the matter as it was submitted on behalf of the appellant, as I understood the argument, that once it became apparent during or about August 1990 that the appellant would not be able to develop the property, it changed its intention and thereafter held the property as a capital asset. Accepting as one must that the erf constituted floating capital (or stock-in-trate) up to that time, the *onus* lies upon the appellant to establish that it thereafter changed its nature to one of fixed capital, the *onus* of proving 'non-liability' being placed upon it by s 78 of the Act - *cf Goodrick v Commissioner for Inland Revenue 1959 (3) SA 523 (A) at 527H.*
>
> As was stressed in *Bloch v Secretary for Inland Revenue* 1980 (2) SA 401 (C) at 406H, the essence of fixed capital, as distinct from floating capital, is an element of permanency in the sense that there is an intention to keep the asset more or less permanently so as to derive an income therefrom - see further *Sekretaris van Binnelandse Inkomste v Aveling* 1978 (1) SA 826 (A) at 880. The appellant therefore had to establish that it had abandoned its development plans and decided to hold the property with the necessary element of permanency. The only evidence lead by the appellant (that of B) fell short of establishing such a change of intention. Clearly a sense of defeat was experienced by the members of the appellant when it became apparent that their development would not continue, but it was never suggested that the appellant itself (through its members or otherwise) then decided that it would hold the erf indefinitely for a reason of a capital accrual. It seems clear that the members of the appellant just didn't know what to do with the

> property and indeed, as B said, consideration was given to transferring it back to its previous owners. But one cannot lose sight of the fact that both I and H had rendered professional services without charge to the appellant, and it is clear that I wanted to dispose of the property as soon as a substantial offer was forthcoming. The only inference which can be drawn from this is that she wished to recover something out of the property as recompense for her labours. Presumably H found himself in a similar position. That alone is insufficient to show that the erf was no longer part of the appellant's floating capital. Indeed, if anything, it is more consistent with an intention to sell the asset which constituted the appellant's stock-in-trade for the best profit.
>
> In the result, the appellant has failed to discharge the *onus* of establishing that the erf in question was no longer part of its floating capital when it was sold to L".

[33] The circumstance that part of the intention of the respondent was to provide homes for its members at cost does not import a difference that affects the situation, an aspect to which I revert below. Similarly, the case of *CIR v Paul* 1956 (3) SA 335 (A), invoked by Mr *Emslie* in argument, is of no assistance to the respondent. In that case the taxpayer was desirous of purchasing a portion of a parcel of land on which he wished to erect a dwelling for himself. The owner of the land was, however, not prepared to sell the desired portion, but insisted that the taxpayer purchase the whole parcel of land, which the taxpayer was accordingly obliged to do. His intention was, however, immediately to dispose of the surplus portion of the land not needed by him, and he did so, at a profit. The Court held that the sale of that surplus portion was, in the circumstances, not part of a profit-making scheme. It need hardly be stated that the facts of that case are clearly distinguishable from those of the instant matter.

[34] An alternative argument was invoked by Mr *Emslie*. It was founded on the fact that part of the respondent's intention, as found by the Court *a quo*, had been that of the eight envisaged dwelling units three were to be sold to the members of the respondent at cost, i.e. not at a profit. It was contended that to that extent portion of the two erven, the acquisition and holding of which was not accompanied by a profit-making intention, had been acquired, held and disposed of as a capital asset. Accordingly, an appropriate portion of the profit made on the resale should be allocated thereto as a non-taxable

capital accrual. It was suggested that an allocation of three-eighths would be appropriate (if anything, in favour of the appellant on the basis that on the evidence the three units that were to be allocated to the respondent's members would have been three of the larger units, on the upper level with better views, and therefore relatively more expensive). Such an apportionment, if supported by the facts, so counsel argued, would be acceptable in law in terms of the decision in *Tuck v CIR* 1988 (3) SA 795 (A).

[35] Mrs *Battheu* sought to distinguish *Tuck's* case from the present on the basis that in that case there were two different *causae* at issue (the two reasons for the allocation of certain shares to the taxpayer), whereas in the present matter there was a single cause, a sale of property. I am not convinced that the suggested distinction is helpful.

[36] I am persuaded that the argument may be disposed of on another basis. Accepting, without deciding, that there was otherwise a sufficient basis established for the 3:5 ratio contended for the counsel, it seems to me that the inference to be drawn from the facts is that in dealing with the erven as it did (i.e., disposing of same to Group Five, in regard to which sight should not be lost of the fact that the whole of the two properties had remained unsubdivided and undeveloped), the respondent had decided to deal with the *whole* property as constituting the productive turnover of land, the whole property then constituting its floating capital. To that extent, *that* was the change of intention that supervened, not the opposite change of intention found by the Court *a quo*. At least, the contrary was not established by the respondent on a balance of probabilities.

[37] In my judgment, therefore, the respondent did not discharge the onus resting upon it of proving that the assessment in question was wrong.

ORDER:

[38] (1) The appeal succeeds with costs.

2) The order of the Court *a quo* is set aside and for it is substituted the following order:

"The appeal is dismissed and the assessment is confirmed".

F. KROON
JUDGE OF THE HIGH COURT

LUDORF, J

I AGREE.

J.F. LUDORF
JUDGE OF THE HIGH COURT

PILLAY, J

I AGREE

R. PILLAY

JUDGE OF THE HIGH COURT