[HIGH COURT OF AUSTRALIA.]

ADELAIDE MOTORS LIMITED . . . APPELLANT;

AND

THE FEDERAL COMMISSIONER OF TAXATION . . . . . } RESPONDENT.

H. C. OF A. 1942.

ADELAIDE, *Sept.* 18, 21.

MELBOURNE, *Oct.* 20.

Latham C.J., Rich and Starke JJ.

Income Tax (Cth.)—Company—Whether "private company"—Control—Artificial group of seven selected by Commissioner—Company in which public substantially interested—Income Tax Assessment Act 1936-1940 (*No.* 27 *of* 1936—*No.* 65 *of* 1940), *secs.* 103*, 104.

The three directors of a company, with their "nominees" as defined by sec. 103 of the *Income Tax Assessment Act* 1936-1940, held the major portion of the voting power. The Commissioner of Taxation selected and added to the directors and their "nominees" four other shareholders and their "nominees" so as to make a group of seven persons who, with their "nominees," held ordinary shares carrying more than seventy-five per cent of the voting power. On the basis of this grouping the Commissioner claimed that the company was a "private company" as defined by sec. 103. It was possible to construct a great number of different groups of shareholders such that each group would hold the major portion of the voting power.

* Sec. 103 of the *Income Tax Assessment Act* 1936-1940 provides as follows: —"(1) In this Act, unless the contrary intention appears— . . . 'nominee' of any person means one who may be required to exercise his voting power at the direction of, or holds shares directly or indirectly on behalf of, that person and includes a relative of that person; 'private company' means a company which is under the control of not more than seven persons, and which is not a company in which the public is substantially interested or a subsidiary of a public company; . . . (2) For the purposes of this Division—(*a*) a company shall be deemed to be a company in which the public are substantially interested if shares of the company (not being shares entitled to a fixed rate of dividend, whether with or without a further right to participate in profits) carrying not less than twenty-five per centum of the voting power, have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the year of income beneficially held by, the public (not including a private company) and any such shares have in the course of that year been quoted in the official list of a stock exchange; . . . (*c*) a company shall be deemed to be under the control of any persons where the major portion of the voting power or the majority of the shares is held by those persons or is held by those persons and nominees of those persons or where the control is, by any other means whatever, in the hands of those persons."

Held that the company was not a " private company " as defined by sec. 103.

Per Latham C.J.: The arbitrary selection by the Commissioner of four shareholders to be members of the group above mentioned did not disqualify them from being treated as members of the public in considering whether the public were substantially interested in the company within the meaning of the section. If they had been members of a group which in fact acted together in control of the company so as to be distinguishable for that reason from other shareholders, then, in relation to that company, they might fairly have been said not to be members of the public.

Per Starke J.: The section contemplates and provides for a single group of not more than seven persons of whom it can be established that they, and no other, control the company.

CASE STATED.

On the hearing of an appeal to the High Court by Adelaide Motors Ltd. from an assessment of the company to additional tax under Div. 7 of Part III. of the *Income Tax Assessment Act* 1936-1940 *Williams* J., pursuant to sec. 198 of the *Income Tax Assessment Act* 1936-1940 and sec. 18 of the *Judiciary Act* 1903-1940, stated for the opinion of the Full Court a case which was substantially as follows :—

1. The appellant Adelaide Motors Ltd. (hereinafter called " the company ") is incorporated as a limited company under the laws of South Australia and has its registered office at 79 Pirie Street, Adelaide.

2. On 30th June 1940 the issued capital of the company consisted of 61,700 fully paid one pound shares of which 41,700 were ordinary shares and 20,000 were shares entitled to a fixed rate of dividend being five per cent cumulative preference shares participating *pari passu* with ordinary shares up to eight per cent. There were thirty ordinary shareholders and sixty-eight preference shareholders.

3. Art. 81 of the articles of association of the company provides that every member present in person or by proxy or attorney shall on a show of hands have one vote and every member present in person or by proxy or attorney shall upon a poll have one vote for every share held by him, but by the terms of the special resolution authorizing the issue of the preference shares such preference shares do not confer any right of voting at any meeting or meetings of the company unless the proposition to be submitted to the meeting directly affects the rights and privileges attached to such shares, nor shall they qualify any person to be a director of the company.

4. The following are articles of association of the company relating to the management and control of the company :—

> 90. There shall be not less than three nor more than five directors of the company until otherwise provided by the company in general meeting.

H. C. OF A. 1942.

ADELAIDE MOTORS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

95. A managing director shall not while he continues to hold that office be subject to retirement by rotation and he shall not be taken into account in determining the retirement by rotation of directors but he shall subject to the provisions of any contract between him and the company be subject to the same provisions as to resignation and removal as the other directors of the company and if he cease to hold the office of director from any cause he shall *ipso facto* and immediately cease to be a managing director.

97. The directors may from time to time entrust to and confer upon a managing director for the time being all or such of the powers exercisable under these presents by the directors as they may think fit and may from time to time revoke alter withdraw or vary all or any of such powers.

98. Subject to the provisions of art. 95 at the second ordinary general meeting to be held in the year 1923 and at the second ordinary general meeting to be held in every subsequent year two directors shall retire from office. Subject as last aforesaid the two directors to so retire shall be the two who have been longest in office without re-election and if a greater number than two directors have been in office the same length of time the two directors to so retire shall be the two who by agreement or ballot between such greater number shall be decided as the two to retire.

99. The company at the general meeting at which any retirement of directors takes place in pursuance of art. 98 shall fill up the vacated offices by electing a like number of persons to be directors in the place of the directors so retiring but such retiring directors shall be eligible for re-election.

118. The business and entire management and all affairs of the company shall be vested in and conducted by the directors who may carry on the same in such manner as in their judgment and discretion they may think most expedient; and in addition to the powers and authorities by any Act of Parliament or by these articles expressly conferred upon them they may exercise all such powers give all such consents and make all such arrangements and appointments and generally do all such acts and things as are or shall be by any Act of Parliament or by the memorandum of association of the company or by these articles directed or authorized to be exercised given made or done by the company and are not thereby expressly directed to be exercised given made or done by the company in meeting but subject nevertheless to the provisions of any such Act of

Parliament and of these articles and subject also to such regulations (if any) as are from time to time prescribed by the company in meeting; but no regulation made by the company in meeting shall invalidate any prior act of the Board which would have been valid if such regulation had not been made.

119. Without prejudice to the general powers conferred by the last preceding article and to the other powers conferred by these articles it is hereby expressly declared that the directors shall have the following powers, that is to say, power—

(21) Before recommending any dividend to set aside out of the profits of the company such sum or sums as they think proper as a reserve fund to meet contingencies or for equalizing dividends or for repairing improving and maintaining any of the property of the company or for depreciation and/or for such other purposes as the directors shall in their absolute discretion think conducive to the interests of the company and to invest the several sums so set aside upon such investments including the purchase of shares in any no-liability company but not including shares in this company as they may think fit and from time to time deal with and vary such investments and dispose of all or any part thereof for the benefit of the company and divide the reserve fund into such funds as they may think fit with full power to employ the assets constituting the reserve fund in the business of the company and that without being bound to keep the same separate from the other assets.

142. Subject to the provisions of the agreement mentioned in art. 4 hereof and to the rights of members entitled to shares issued upon special conditions the profits of the company shall be divisible among the members in proportion to the amount of capital paid up or deemed to be paid up on the shares held by them respectively.

143. The directors may from time to time declare and pay such dividends as they may think fit but no dividend shall be payable except out of the profits arising from the business of the company.

144. The declaration of the directors as to the amount of the net profits of the company shall be conclusive.

147. The directors may from time to time pay to the members such interim dividends as in their judgment the position of the company justifies.

H. C. OF A. 1942.

ADELAIDE MOTORS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

5. The directors of the company during the relevant year of income were Lindsay M. Anderson, Fred. S. Mann and Ronald H. Martin. Lindsay M. Anderson was the managing director of the company. The said directors and their relatives on 30th June 1940 held between them 25,400 ordinary shares representing sixty-one per cent of the the voting power made up as follows :—

	Ordinary Shares.	
Lindsay M. Anderson	500	
Mary Anderson, his wife	7,350	
	——	7,850
Fred S. Mann		12,250
Ronald H. Martin	300	
Kathleen Martin, his daughter	1,500	
Henry Martin, his son	1,500	
Ruth Cowling, his daughter	1,500	
H. M. Martin & Son Ltd. (a family company wholly controlled by R. H. Martin) ..	500	
	——	5,300
		25,400

6. The other shareholders of the company on 30th June 1940 held between them 16,300 ordinary shares representing thirty-nine per cent of the voting power. None of such shareholders is an officer of the company nor a nominee of any director or officer of the company.

6A. Seven of the shareholders of the company and their relatives (inclusive of the directors and their relatives as mentioned in par. 5 hereof) together hold 36,850 ordinary shares as shown by the following table :—

F. S. Mann (a director)	12,250	shares
L. M. Anderson (a director) and his wife ..	7,850	,,
R. H. Martin (a director) and his children	4,800	,,
A. E. Pegler and the Estate of H. A. Pegler	6,500	,,
Mrs. H. S. Chaffey	2,500	,,
Mr. and Mrs. Burden	2,300	,,
Mrs. Estella Crawford	650	,,
Total ..	36,850	shares

leaving 4,850 ordinary shares otherwise held.

7. The whole of the ordinary shares of the company were either allotted unconditionally to or have been acquired unconditionally

by the ordinary shareholders and were on 30th June 1940 beneficially held by such shareholders.

8. The company was listed on the Stock Exchange of Adelaide in the year 1925 and since that time its shares both ordinary and preference have been regularly quoted in the official list of the said Exchange and were so quoted during the year ended 30th June 1940.

9. On 5th September 1941 the Deputy Commissioner of Taxation issued a notice of assessment against the company under Div. 7 of Part III. of the *Income Tax Assessment Act* 1936-1940 requiring the company to pay £303 7s. 7d. additional tax on the ground that the company was a private company and was assessable to additional income tax under sec. 104 of the *Income Tax Assessment Act.* It is agreed that if the company is a " private company " it did not make in respect of the period referred to in the notice of assessment a sufficient distribution of its income and the figures appearing in the notice are agreed as correct.

10. On 12th September 1941 the appellant gave a notice to the Deputy Commissioner of Taxation of objection against the said assessment on the grounds :—(1) That the company is not a private company within the meaning of Div. 7 of Part III. of the *Income Tax Assessment Act* 1936-1940. (2) That the company is in fact a public company. (3) That the company is a company in which the public are substantially interested in that shares of the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) carrying not less than twenty-five per cent of the voting power have been allotted unconditionally to and/or acquired unconditionally by and were at the end of the year of income beneficially held by the public and that such shares have in the course of the year of income been quoted in the official list of the Stock Exchange at Adelaide.

11. On 19th January 1942 the Deputy Commissioner of Taxation gave notice to the appellant disallowing the objection and on 23rd January 1942 the appellant in writing requested the Commissioner to treat the objection as an appeal and to forward it to the High Court of Australia and the appeal was forwarded to the High Court of Australia accordingly on 8th August 1942.

12. The parties have appeared before me and agreed that all the facts material to the hearing of the appeal are contained in the preceding paragraphs and upon these facts I state the following questions for the opinion and consideration of the Full Court of the High Court of Australia :—

H. C. OF A. 1942. ADELAIDE MOTORS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

(*a*) Was the appellant on 30th June 1940 a private company within the meaning of Div. 7 of Part III. of the *Income Tax Assessment Act* 1936-1940 ?

(*b*) Was the appellant properly assessed for additional income tax under sec. 104 of the said Act in respect of the year of income ended 30th June 1940 ?

Ligertwood K.C. (with him *Ross*), for the appellant. The relevant provisions of the *Income Tax Assessment Act* 1936-1940 are sec. 103 (1), (2) (*a*), (2) (*c*), sec. 104 and sec. 6, defining "relative." The English enactment on which these provisions are based was considered in *Himley Estates Ltd.* v. *Commissioners of Inland Revenue* (1) and *Tatem Steam Navigation Co. Ltd.* v. *Commissioners of Inland Revenue* (2). If the company is one in which the public are substantially interested, the question of control does not arise. Who are members of the public cannot be dependent on the caprice of the Commissioner. The test is whether an allotment is conditional or unconditional and whether there is any restriction on the transfer of shares. Alternatively, the contrast is between shareholders in actual control and other shareholders. If in fact directors and their nominees control the company, why should they not be regarded as the persons who control it under sec. 103 (2) (*c*) ? "Control" is a practical commercial matter (*Daimler Co. Ltd.* v. *Continental Tyre & Rubber Co. (Great Britain), Ltd.* (3)), and "public" is what is commercially known as the public. In a commercial sense the directors and their families might be said to control this particular company. This satisfies sec. 103 (2) (*c*), and all other members of the company are members of the public. The tests laid down by sec. 103 (2) (*a*) and 103 (2) (*c*) respectively must be applied separately. The former should be applied first, and, if the company comes within that test, it falls outside the provisions relating to private companies. [Counsel also referred to *Girls' Public Day School Trust Ltd.* v. *Ereaut* (4).]

Villeneuve Smith K.C. (with him *Travers*), for the respondent. *Tatem Steam Navigation Co. Ltd.* v. *Commissioners of Inland Revenue* (2) was decided on the definition in the English Acts. The definition in the Commonwealth Act is wider. The management of this company is imputed to seven persons ; therefore the rest are the public. The purpose of the Act is to ascertain whether seventy-five per cent of the holding of ordinary shares is in the hand of seven or

(1) (1933) 1 K.B. 472.
(2) (1941) 2 K.B. 194.
(3) (1916) 2 A.C. 307, at p. 340.
(4) (1931) A.C. 12.

less persons, and, if so, to bring into the area of taxation small groups of persons holding a majority control in a company. The legislature is looking to the beneficial interests of shareholders as the subject of taxation. The terms of the Act authorize the Commissioner to inquire who are the seven largest shareholders.

Ligertwood, K.C., in reply.

Cur. adv. vult.

Oct. 20.

The following written judgments were delivered :—

LATHAM C.J. This is a case stated in an income tax appeal. It raises the question whether the appellant company, Adelaide Motors Ltd., is a private company within the meaning of Part III., Div. 7, sec. 103, of the *Income Tax Assessment Act* 1936-1940. If it is such a company it is subject to tax upon the whole of its " distributable income " as defined by sec. 103 (1) unless it has made " a sufficient distribution of its income of the year of income " as defined by the Act (sec. 103 (2) (*e*) and sec. 104). It is agreed that the company has not made such a distribution. The tax payable is the aggregate of the amount of tax which would have been payable if the company had, on the last day of the year of income, paid the undistributed amount as a dividend to the shareholders who would have been entitled to receive it (sec. 104). If moneys in respect of which tax is paid under these provisions are subsequently paid as dividends the shareholders are entitled to a rebate in their personal assessments (sec. 107). The company pays tax at a high rate for shareholders with large incomes and at a lower rate for shareholders with small incomes, but no provision is made by the statute for any adjustment between shareholders on this account.

A company is a private company which is (1) a company which is under the control of not more than seven persons, and (2) not a company in which the public are substantially interested or a subsidiary of a public company (sec. 103 (1)). (It is not necessary in this case to consider the reference to a subsidiary.) Thus a private company is defined by reference to one positive and to one negative attribute.

The positive attribute of a private company is that it is under the control of not more than seven persons. No facts are stated in the case which go to show that the appellant company is actually under the control of not more than seven persons. The company is managed in the ordinary way by three directors who are elected by the shareholders, but it is not contended that the company is " under the control " of the three directors within the meaning of

H. C. OF A. 1942.

ADELAIDE MOTORS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Latham C.J.

the relevant provisions merely by reason of this fact. Sec. 103 (2) (*c*), however, provides that " a company shall be deemed to be under the control of any persons where the major portion of the voting power or the majority of the shares is held by those persons or is held by those persons and nominees of those persons or where the control is, by any other means whatever, in the hands of those persons." This provision has achieved distinction in the Court of Appeal in England, where it has been formally " censured " as " unintelligible and ridiculous " : see headnote in *Himley Estates Ltd.* v. *Commissioners of Inland Revenue* (1). It provides that a company is deemed to be under the control of " any persons " in each of these cases :— (1) where the major portion of the voting power or the majority of the shares is held by those persons, or (2) is held by those persons and nominees of those persons, or (3) where the control is, by any other means whatever, in the hands of those persons.

" Nominee " is defined in sec. 103 (1) as *meaning* one who may be required to exercise his voting power at the direction of, or holds shares directly or indirectly on behalf of, that person, and as *including* a relative of that person. Presumably this provision should be interpreted as making a relative a nominee whether or not the relative has voting power or shares or, if he has, whether or not he is bound to exercise his voting power at the direction of the person of whom he is a relative. " Relative " means a husband or wife or a relation by blood, marriage or adoption (sec. 6). A cousin fifty times removed is a relative under this definition. Possibly a sufficiently extensive investigation would show that nearly everybody in Australia, and millions of people outside Australia, are " relatives " of nearly everybody else in Australia within this definition. It was pointed out in *Himley's Case* (1) that the definition produces the result that persons who have nothing whatever to do with a company in any capacity are nevertheless " deemed " to be in control of the company—e.g., sons and nephews, as " relatives " of their mothers and aunts, are " nominees " of the latter, who are therefore themselves " in control " of a company in which the sons and nephews happen to hold the majority of shares—though the mothers and aunts have never even heard of the company. This provision was properly described in *Himley's Case* (2) as both bewildering and ridiculous.

Under this provision a company may, at one and the same time, be under the control of each of many groups of persons. Any group of shareholders which can be notionally constituted is in control if those shareholders hold a majority of shares. But any other

(1) (1933) 1 K.B. 472.

groups of persons who or whose nominees (including relatives) hold a majority of shares are equally in control. Further, if *de facto* control is " by any other means whatever " in the hands of another group, that group is also in control.

The issued capital of Adelaide Motors Ltd. consisted at the relevant date of 41,700 fully paid one pound shares and 20,000 one pound preference shares. There were thirty ordinary shareholders and sixty-eight preference shareholders. There were three directors of the company. The three directors, four relatives of the directors, and a company controlled by one of the directors (eight persons) held 25,400 ordinary shares—i.e., sixty-one per cent of the ordinary shares. Other shareholders (who are not " nominees " of the directors) therefore held thirty-nine per cent of the ordinary shares. If preference shares are taken into account (as seems to be proper under sec. 103 (2) (*c*)) the directors and their nominees still held a majority of the shares of the company. Thus, under sec. 103 (2) (*c*) the company may be deemed to be under the control of the three directors, as they and their nominees held a majority of the shares of the company. Thus the company is under the control of less than seven persons.

But many other groups are also " in control " of the company. The Commissioner has chosen a group consisting of seven persons —three directors and four other shareholders, two of whom live at Mildura in Victoria, another at Renmark in South Australia and another at Brighton in South Australia. These persons (with relatives of directors) own 36,850 ordinary shares, leaving 4,850 ordinary shares (less than twenty-five per cent of the ordinary shares) otherwise held. There is no suggestion that these seven persons act together in any manner as a group, but they satisfy the description of persons (and their nominees) holding a majority of shares. This group, therefore, may be deemed to be in control of the company. The Court was informed by counsel for the appellant, without dissent from counsel for the respondent, that no less than 9,086 different groups of seven persons could be selected, each group controlling a majority of shares. In *Himley's Case* (1) there were 6,435 possible similar groups of eight persons : see the report (2). The Commissioner has selected one of these 9,086 groups, and the selection, it is contended, produces the result that the company is subject to the special taxation imposed by Div. 7 of Part III. of the Act. This result follows, it is said, from the fact that only persons outside the group can be regarded as members of the public, and that such persons hold less than twenty-five per cent of the ordinary shares,

(1) (1933) 1 K.B. 472.

(2) (1933) 1 K.B., at p. 487.

H. C. OF A. 1942.

ADELAIDE MOTORS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Latham C.J.

so that the company is not, according to the Act, a company in which the public is substantially interested, and therefore satisfies the negative part of the definition of "private company."

The negative attribute of a private company is defined in sec. 103 (2) (*a*) as follows: "a company shall be deemed to be a company in which the public are substantially interested if shares of the company (not being shares entitled to a fixed rate of dividend, whether with or without a further right to participate in profits) carrying not less than twenty-five per centum of the voting power, have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the year of income beneficially held by, the public (not including a private company) and any such shares have in the course of that year been quoted in the official list of a stock exchange."

For the purpose of applying this provision preference shares must be disregarded. All the ordinary shares of the appellant company were either allotted unconditionally to or have been acquired unconditionally by the ordinary shareholders and were at the relevant date beneficially held by the shareholders. The shares have in each year since the formation of the company been quoted on the official list of the Stock Exchange of Adelaide. The question which falls for decision is whether twenty-five per cent of the ordinary shares were held by "the public."

The Commissioner contends that only persons outside his selected control group can be members of the public for the purposes of this legislation. No persons within the group can, it is said, be members of the public in the relevant sense. If this contention is valid, the public does not hold twenty-five per cent of the shares, and the company is a private company.

Every person in the community is, in the ordinary sense, a member of the public. In this sense all shares of all companies are owned by the public. But sec. 103 (2) (*a*) is based upon an underlying assumption that, in the case of a particular company, it may be possible to mark out some shareholders as not members of the public in relation to that company. Div. 7 of Part III. of the Act is designed to assimilate certain companies (many of which are described as family companies) to firms, and to obtain tax as if the shareholders were partners in a firm. Certain shareholders may correspond to partners, the others being "outsiders"—and therefore members of the public. But in a case such as the present, where it is not shown that the artificially created "control group" is actually a controlling group, it is not easy to apply the rough general conception upon which the statutory provisions are based.

The contention of the Commissioner leads to remarkable results. Each of the 9,086 possible groups excludes certain shareholders. Therefore these excluded shareholders are, according to this contention, members of the public. But they will be included in many of the other groups, and therefore, by the same reasoning, are also not members of the public. The result would be that the term " the public " in sec. 103 (2) (*a*) has no real significance or effect. The question whether a person is or is not a member of the public would be answered in the affirmative or the negative according to whether he is or is not a member of some one artificial group which may be momentarily selected. Upon this view the effect of the legislation is that, whatever the position may be as to beneficial holding of shares and quotation on the Stock Exchange, any company is a private company if any group of seven persons or less can be specified which (with or without " nominees") holds more than seventy-five per cent of ordinary voting shares. In any such case the company would be controlled by not more than seven persons (because they would hold a majority of shares) and would not be a company in which the public is substantially interested (because non-members of the group would hold less than twenty-five per cent of the shares). It would have been easy for the legislature to make such a provision if this is what was intended, as the Commissioner contends. But Parliament has not made this simple provision. On the contrary it has deliberately introduced a reference to the holding of shares by the public. The Court should not ignore this feature of the legislation.

I therefore proceed to consider the relation to the company of the four shareholders whom the Commissioner has added to the directors and their nominees so as to make a control group holding more than seventy-five per cent of the ordinary shares. Is there any particular relation between them and the company which distinguishes them from other shareholders ? If they were members of a group which in fact acted together in control of the company so as to be distinguishable for that reason from other shareholders, then, in relation to the company, they might fairly be said not to be members of the public. But they are not members of any such group. When they are considered as shareholders their relation to the company is precisely the same as that of all other shareholders except the directors. According to any objective test, they are members of the public in exactly the same sense as are the other shareholders. There is no warrant that I can find in the terms of the Act for the proposition that the Commissioner can by a process of arbitrary selection disqualify particular shareholders from membership of the public. The four shareholders mentioned should therefore be held to be members of the public.

H. C. OF A. 1942. ADELAIDE MOTORS LTD. v. FEDERAL COMMISSIONER OF TAXATION. Latham C.J.

This view is not inconsistent in any way with, but is supported by, *Tatem Steam Navigation Co. Ltd.* v. *Commissioners of Inland Revenue* (1). There the question was whether a niece, not being a "relative" within the meaning of the English statutory definition (which is not so wide as the Australian definition) and not being actually under the control of her uncle, who held a large number of shares, should be regarded as a member of the public or not. It was held that she was a member of the public. If she had been a "relative" or a "nominee" of her uncle (who was one of a "control group") the position would, it was assumed, have been different. In the present case the four shareholders mentioned are not relatives or nominees of any of the directors with whom they have been arbitrarily associated as a "control group." The reasoning which was applied in the case cited supports the conclusion that they are members of the public.

The questions asked should be answered as follows:—(*a*) No. (*b*) No. The case with these answers should be remitted to the learned judge who stated it. The respondent should pay the costs of the case.

RICH J. Case stated. The questions submitted are:—(*a*) Was the appellant on 30th June 1940 a private company within the meaning of Div. 7 of Part III. of the *Income Tax Assessment Act* 1936-1940? (*b*) Was the appellant properly assessed for additional income tax under sec. 104 of the said Act in respect of the year of income ended 30th June 1940?

A company by virtue of registration becomes a legal entity, but the quality or character of private or public does not attach to it except through its corporators. The epithet "private" or "public" as applicable to a company has no definite signification apart from legislation. Accordingly one finds in the *Income Tax Assessment Act* 1936-1940 an attempt to bring within the taxgatherer's net firms or partnerships or one-man companies by means of a fictional definition through the well-known device of the words "deemed to be." In spite of the statement of *Rowlatt* J. (2), that its prototype in the *Finance Act* 1922, sec. 21, sub-sec. 6, amended by sec. 31 of the *Finance Act* 1927 "calls loudly for redrafting in the interests of precision", it was adopted with immaterial alterations by sec. 103 (2) (*c*) of the *Income Tax Assessment Act*. A private company registered under the English *Companies Act* 1929 has three features or characteristics: (1) restriction on transfer of shares, (2) limited membership, and (3) prohibition against an invitation to

(1) (1941) 2 K.B. 194.

(2) (1933) 1 K.B., at p. 481.

the public to subscribe for shares or debentures in the company. These *indicia* would not satisfy a taxing Act. And courts are called upon to solve the puzzle set by the " bewildering " definition clauses found in the English *Finance Act* and the Federal *Income Tax Assessment Act*.

The relevant facts in the case stated are that on 30th June 1940 the capital of the subject company was divided into 41,700 fully paid one pound shares and 20,000 one pound preference shares. Ordinary shareholders numbered thirty and preference shareholders sixty-eight. The company had three directors, who with four of their relatives and a company (eight persons) under the control of one of the directors held 25,400 of the ordinary shares or sixty-one per cent; the other shareholders of the company held 16,300 ordinary shares or thirty-nine per cent of the voting power. The whole of the ordinary shares of the company were either allotted unconditionally to or have been acquired unconditionally by the ordinary shareholders and were on 30th June 1940 beneficially held by such shareholders. The company was listed on the Stock Exchange of Adelaide in 1925 and since then all its shares have been regularly quoted in the official list of the Exchange and were so quoted during the year ending 30th June 1940. The articles do not contain any restriction on the transfer of the shares. Each member is entitled to one vote for every share held by him, but preference shareholders have no right of voting except where the proposition to be submitted to the meeting directly affects the rights and privileges attached to such shares, which, moreover, do not qualify any person to be a director of the company. Do these facts bring the company within the definition contained in the Act? The definition is made up of three elements, of which two only are relevant. They are that it is a company which is under the control of not more than seven persons and is not a company in which the public are substantially interested. The first condition was probably aimed at one-man companies, where a sufficient number of persons signed the memorandum of association for one share each so as to qualify the company to be registered but the rest of the shares forming the bulk of the capital remained in the hands of one or more persons. However this may be, the facts in this case do not make the condition of control apply to this company. In my opinion the company is not under the control of any persons within the meaning of sec. 103 (2) (*c*) because the major portion of the voting power or the majority of the shares is neither held by those persons nor by those persons or nominees of those persons nor is the control by any other means whatever in the hands of those persons. The object of this definition is to

H. C. OF A. 1942.

ADELAIDE MOTORS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Rich J.

extend by means of the fiction the control of a company beyond the limits of actual control. The definition of "nominee" in the Federal Act, which transcends the range of the definition in the English Act, would, as the Chief Justice has pointed out, result in relatives reaching astronomical figures. His Honour in his judgment, which I have had the opportunity of reading, and *Romer* L.J. in *Himley Estates Ltd.* v. *Inland Revenue Commissioners* (1), comment on the ridiculous result of an arbitrary grouping of persons in control. But the facts in this case show that the *de facto* control of the company is in the hands of more than seven persons. Thus one element or condition is wanting to comply with the definition. And the other condition is also wanting, because shares carrying more than twenty-five per cent of the voting power have been allotted unconditionally to or acquired by the ordinary shareholders and these shares were on the relevant date—30th June 1940—beneficially held by such shareholders. It is also admitted that the company was listed on the Adelaide Stock Exchange since 1925 and its shares have been regularly quoted in the official list of that Exchange and were so quoted on the relevant date.

Accordingly I answer the questions submitted in the negative.

STARKE J. Case stated in an appeal by Adelaide Motors Ltd. from an assessment under sec. 104 of the *Income Tax Assessment Act* 1936-1940 upon the following questions of law arising upon the appeal:—(*a*) Was the appellant on 30th June 1940 a private company within the meaning of Div. 7 of Part III. of the *Income Tax Assessment Act* 1936-1940? (*b*) Was the appellant properly assessed for additional income tax under sec. 104 of the said Act in respect of the year of income ended 30th June 1940?

The Act by sec. 103 provides:—(1) "private company" means a company which is under the control of not more than seven persons, and which is not a company in which the public are substantially interested or a subsidiary of a public company. (2) (*c*) A company shall be deemed to be under the control of any persons where the major portion of the voting power or the majority of the shares is held by those persons or is held by those persons and nominees of those persons or where the control is, by any other means whatever, in the hands of those persons.

Similar provisions have been described by English judges as "bewildering" and "ridiculous," and so they are if applied in the manner suggested by the Commissioner. In terms the section only refers to a company which is under the control of not more than

(1) (1933) 1 K.B. 472, at p. 487.

seven persons; it contemplates and provides for a single group of not more than seven persons of whom it can be established that they, and no other, control the company. Those persons may control the company because they have the major portion of the voting power, the majority of the shares may be held by them or their nominees, or the control is by any other means whatever in their hands. The section becomes unintelligible if, according to the Act, the control of the company may be deemed to be in any of a number of groups of shareholders not exceeding seven persons, and as in this case, in several thousands of such groups.

In my opinion, the section has no application in such circumstances. The questions stated should be answered :—(*a*) No. (*b*) No.

Questions answered as follows :—(*a*) *No*; (*b*) *No. Case remitted. Respondent to pay costs of case.*

Solicitors for the appellant, *Baker, McEwin, Ligertwood & Millhouse.*

Solicitor for the respondent, *H. F. E. Whitlam*, Crown Solicitor for the Commonwealth.

C. C. B.