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# AN HISTORICAL PERSPECTIVE

# OF INCOME TAX LEGISLATION

# IN SOUTH AFRICA

# 1910 TO 1925

DISSERTATION

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# CHAPTER ONE

## INTRODUCTION

INTRODUCTORY REMARKS

This work considers the period from Union, 31 May 1910 until promulgation of the Income Tax Act No. 40 of 1925.(1) It will describe the means, both financial and otherwise, by which the fledgling Government of the Union of South Africa contrived to balance its budget, and will consider the various sources of revenue available up to 1914, when the Government of Gen. Louis Botha first decided that a tax on income was necessary in order to maintain the solvency of the new State. Similarly the political pressures which shaped the nature of the Income Tax Acts up to 1925 will be discussed, and the political principles (or expediencies, depending on the degree of cynicism of the reader) which led the parties in power from time to time to make the decisions they did regarding the provisions of the various Acts. The effect of external political situations such as the Great War of 1914 - 1918 will be examined, as will the consequences of the rebellion of 1914 and the strikes of 1913 and 1922. The legislation predictably spawned a considerable body of litigation as taxpayers hastened to find and exploit loopholes in it; the resultant Income Tax Cases, in the Income Tax Special Court, Supreme Court and Appeal Court, formed the embryo of a body of judicial precedent which today encompasses some two thousand case reports. A few of the cases decided in the period up to 1925 are still quoted today; for example, CIR v Lunnon 1924 AD 1 SATC 7. The relevant cases from the period will enjoy consideration, with descriptions of how their verdicts affected

either subsequent income tax principles or later legislation. Also considered will be the inception during this period of the way in which income tax legislation largely develops: the legislature promulgates an Act, the taxpayers discover legitimate ways to reduce their tax burden and the Minister of Finance consequently causes the Act to be changed in order to protect the tax base. Thereupon the resolute taxpayers seek loopholes anew.

The effect of economic conditions on income tax legislation will engage attention; several such conditions cast their shadows into the House of Assembly during that 15 year period, notably the post-war recession and the drought of 1919.

The selection of this period is apposite for several reasons:

- it covers the period during which income tax legislation came into being;
- it includes several notable political occurrences, thus making possible a consideration of their effect on income tax legislation;
- it includes a natural cataclysm, namely a major drought, which also had an effect on subsequent Income Tax Acts;
- a sufficient number of income tax cases was heard during the period to afford a fair indication both of how the body of case law would develop and how it would perpetually interplay with the legislation;

- it clearly illustrates the differences between the two great political parties of the time, differences largely caused by the vested interests of each; the dominant South African Party, with its need to retain the support of the commercial and particularly the mining sectors, and the smaller but even then growing National Party with its face set firmly towards the rural constituencies and the embattled farmers;
- the period culminates in the Income Tax Act of 1925, a significant change from its predecessors, and the second Income Tax Act of the Pact Government.

The imposition of taxes by the respective provinces does not form part of this work, as the scope of the discussion is limited to the various Income Tax Acts, and their development has been overseen by the central government.

## DEVELOPMENT AND PROGRAMMES OF SOUTH AFRICAN POLITICAL PARTIES

In any study of the development of income tax legislation it must be borne in mind that the economic, financial and consequently taxation policies of the respective political parties in Parliament would inevitably be coloured by their respective political philosophies. It is therefore necessary to consider the origins of these parties and their philosophies.

D W Kruger (2) considers the origins of the various parties, commencing in the period immediately after the Anglo-Boer War. A great political revival had taken place among Afrikaners shortly after the peace had been declared. The first major event in the formation of what were to become the participants on the South African political stage was a great popular meeting held at Heidelberg in July 1903, at which Gen. Louis Botha urged the convening of a 'people's congress' to consolidate the ranks of his followers.(3) Botha pressed this suggestion on several later occasions, and his efforts bore fruit when a congress was held in Pretoria in May 1904 and 'Het Volk' came into being.

The proposed policy of this party would be to embrace all shades of moderate White opinion, because of Botha's determination to build a new future on the principle of conciliation. He envisaged a union of the politically disparate Afrikaner elements such as 'hensoppers', 'bittereinders' and 'National Scouts', and

the moderate English groups 'who had a permanent stake in the country'.(4)

The principles of the party were: conciliation between Dutch and English; broad tolerance in all things; a united nation; religious instruction in schools; mother tongue instruction in schools; and an end to the importation of Chinese labour for the gold mines, coupled with protection of White labour. Botha enjoyed the support of the moderate English-speaking Transvaal Responsible Government Party founded in 1904 by E B and Harry Solomon, which favoured self-government for the colony. This was despite the fact that the promotion of Afrikaans interests was a strong motive force in Het Volk.

The attitude of Botha towards the moderate members of the English-speaking population reflected the philosophy which he had evinced since he had first become involved in politics as a member of the Volksraad of the Transvaal Republic in the decade before the Anglo-Boer war. L M Thompson (5) states that Botha had gravitated towards those members who had sought to accommodate the Uitlanders. When war came he committed himself fully to the republican cause and became Commandant General of the Boer forces. However, he was realistic enough to recognise when the time came to seek surrender terms, and when peace arrived he accepted that the destiny of the former Boer republics lay within the British Empire.

He appears to have been sincere in this belief, but it also served two political purposes: it brought nearer the date when his country might achieve responsible government; and it made his policies more attractive to the British-born voters of the Transvaal, who constituted nearly half the electorate.

Botha, then, embarked on a policy of conciliation founded upon four courses of action: the wartime divisions amongst the Afrikaners were to be forgiven, if not forgotten, by accepting the 'hensoppers' and 'National Scouts' back into the Afrikaner body politic and cultural; the gulf between members of the two White language groups in the Transvaal was to be bridged by the fusion of the two stocks; this fusion was to extend throughout South Africa in the course of forming a united nation from the four colonies; and this nation was to be a loyal member of the Empire.

Thompson (6) quotes several examples of this creed in speeches by Botha; the principle of conciliation and accommodation seems indeed to have permeated the whole life of this man, destined to lead his country into Union only eight years after its devastation.

Such a philosophy led naturally to the creation of Het Volk with its moderate approach.

Ranged against Het Volk and its followers was the Transvaal Progressive Association, which had come into existence in 1904

under the auspices of a group of ex-Uitlander representatives of the mining interests: Sir George Farrar, Sir Percy Fitzpatrick and Sir Abe Bailey.

L M Thompson (7) makes it clear that the relationship between Het Volk and the Progressives was not entirely hostile. Indeed, Fitzpatrick went to some lengths in attempting to secure 'complete and real co-operation' between Boer and Briton. However, some of his fellows, notably Farrar and Chaplain, distrusted the Afrikaner leaders. Botha, of course, sincerely strove for a meeting of moderate minds and would, no doubt, have welcomed co-operation from the Progressives. At the same time, he had to beware about alienating the support of large numbers of his followers who were still very antagonistic towards anything British. This group included the Cape Afrikaner politicians led by F S Malan and J W Sauer, whose Afrikaner Bond supported the redoubtable John X Merriman.

Botha must also have realised that a large proportion of the revenue of the Transvaal and subsequently the Union would come from the gold mining industry. By the same token, Het Volk was clearly a potentially powerful organisation and therefore a possible future government; the mining interests would have to deal with whichever party was in power, despite their own pervasive influence. The relationship between Het Volk and the mining interests, then, would have been one of opposition tempered by the knowledge that each needed the other: the party needed revenues from gold mines in order to meet the expenditures

necessary to establish its legitimacy as a government, and the mines needed an orderly state in which to operate. Yudelman (8) makes this point in propounding his theory that whichever government happened to be in power in South Africa (or, by implication, the Transvaal before Union) would inevitably have closer ties to the capitalists than to the working class, despite the conventional wisdom that Nationalist governments, and in particular the Pact Government of 1924, championed the Afrikaner white working class.

Yudelman (9) proceeds with the theory that the Transvaal and Union were fledgling capitalist states with enormous twin problems: those of raising revenue, for which purpose the mines were indispensable; and of achieving legitimation via support of the White electorate, many of whom were from the increasingly urbanised and unemployed Afrikaner section from which Botha sought support.

Small wonder, then, that Botha allowed his natural tendency towards moderacy and conciliation to lead him towards the mining interests as represented by their Progressive Party and in particular Sir Percy Fitzpatrick, whilst simultaneously seeking to retain his standing with his Afrikaner power base.

In the Orange River Colony, too, the development of an Afrikaner political movement with strong cultural ties took shape, with mass congresses in Brandfort in 1904 and Bloemfontein in 1905 under the leadership of Gen. J B M Hertzog. These congresses

concerned themselves largely with the anglicising policy in the schools, and resulted in the formation of the 'Orangia Unie'.

In both former Boer republics, therefore, political parties were formed to protect and further Afrikaner interests. In the Transvaal with its proportionately greater English population, there was perhaps a more conciliatory attitude.

Looking ahead to economic and fiscal policies as they were manifested ten to twenty years later in Parliamentary debates on taxation, it is worth pointing out here that Het Volk had its power base in a relatively industrialised society with a heterogeneous population, whereas the Orangia Unie sprang from a far more homogeneous population in a substantially rural environment. The subsequent concern of Gen. Hertzog and his party for the effect of income tax legislation on farmers is quite understandable given this background, an attitude which was carried forward into the National Party after its formation in 1914. (See discussions of the 1917 and 1925 Acts.)

Given the large pool of labour on the mines and in ancillary industry together with the urge of white workers to protect themselves against the perceived dangers to their livelihood from Black and Chinese labour, it was inevitable that labour would seek to achieve some political power. Several labour-type parties came into existence; for example, the Independent Labour Party under H W Sampson. These amalgamated in January 1910 under the leadership of Col. F H P Cresswell to form the South

African Labour Party.

In 1907 Mr (later Sir) John Fraser formed the Constitutional Party in the Orange River Colony. The party opposed responsible government and 'never amounted to much'. (10)

Developments in the Cape Colony were broadly similar to those in the two northern colonies, except that the oldest party had its origin as early as 1883. This, the first generally well-supported party, was the Afrikaner Bond led by J.H. Hofmeyr.(11) Possibly its formation was hastened by the fact that from 1881 Dutch was used in the Cape Parliament. The party principles had a broad South African base and interpreted the word 'Afrikaner' very widely. At first it stressed farming interests, but its concerns soon spread to colonial and even national matters. Hofmeyr expressed the need for strong South African unity and was therefore the forerunner both of what was to become the South African Party of Botha in 1911 and of Hertzog's National Party in 1914; a factor common to all three parties was the embodiment of a South African national spirit.

'British' attitudes were no less apparent in the Cape than in the Transvaal and Orange River Colony, and Sir L S Jameson founded the Progressive Party of the Cape, which tried to suspend the constitution of the Cape after the Anglo-Boer War.

In Natal, by contrast, there were no political parties by the time of Union, and the elected members were mostly independents

who generally supported Botha.

There was thus a situation where Afrikaner Bond, Het Volk and Orangia Unie followed generally similar principles of broad South Africanism, with differences of emphasis to take account of local circumstances; the industrial Transvaal, the rural Orange River Colony and the Cape with its already less fiery attitudes. Against this group, and objects of their collective dislike, stood the Progressives of the Transvaal and Cape.

It seemed logical that these loose affiliations of spirit should be formalised against the backdrop of Union, and so it proved to a large extent in 1910. Although disappointed that the most experienced politician in the country and successful Prime Minister of the Cape Colony, John X Merriman, had lost the contest with Botha for the office of Prime Minister, the Afrikaner Bond supported Botha in the first General Election held in September 1910. The result was the formation of the South African Party.

Not all the 'South Africanist' elements joined the new party, however. The strong Afrikaner desire for cultural maintenance led to the rise of 'Hertzogism' and the formation of the National Party in 1914.

In similar vein, the 'British' parties moved towards a logical amalgamation and on the eve of Union the Constitutional, Transvaal Progressive and Cape Progressive Parties merged into

the Unionist Party under the leadership of Jameson. It is scarcely necessary to point out that the party represented industrial interests and British supremacy. Being imperialistic and capitalistic in nature, it was thus the antithesis of its opponents. In later years, Sir Thomas Smartt assumed the reins and took his party into amalgamation with the South African Party in 1921. Smartt did not bear the same opprobrium in Afrikaner eyes as did Jameson, he of the notorious Raid in December 1885/January 1886, (12) and co-operation between the South African Party and him was not unthinkable. Conciliation with Jameson, despite his earnest attempts to further the cause of Union in the post-Anglo-Boer War period, would have been politically disastrous for Botha. Nevertheless, something more than a change of leader was necessary for two parties to merge after so long in opposition to each other.

In fact, throughout the 1914-18 war, the Unionists had supported Botha and Smuts in their prosecution of the conflict. The rebirth of Europe in the post-war period saw Smuts, who assumed the leadership on the death of Botha in 1919, bestride an eminent position on the world political stage. The spirit of the Unionists survived in the South African Party for many years, with far-reaching consequences beyond the scope of this work.

Most of the political parties in the first years of Union were conservative with a liberal element conspicuously absent in the National Party.

The attitudes to financial and related matters may be gleaned from the programmes of the respective parties as published about that time. The following relevant extracts appeared in party publications:

- Unionist Party Programme 1910: (13)

  Agriculture : taxation of unimproved land values

  : provision in any settlement scheme for miners' phthisis sufferers debarred from mining

  Industry : fostering mining in all its branches.

- South African Party Programme - as revised in 1930, but nevertheless reflective of its original principles : (14)

  '(d) The adoption of an equitable and judicious system of taxation, which will have due regard to the development of the natural resources of the country;

  (f) the development of agriculture and stock farming as constituting the permanent resources of the country;

  (g) the promotion of commerce and industries, and of the exploitation of the mineral resources of the country.'

- National Party Programme 1914: (15)

  '(b) By recognising agriculture, stock farming, industry and commerce as the principal sources of the country's permanent material welfare, and their development and encouragement as the best way of promoting the country's durable economic independence.

(2) by a system of taxation in accordance with the paying capacity of the taxpayer and through which the natural sources of the temporary wealth of the country will be sufficiently mobilised in order to promote the country's permanent welfare'.

- S A Labour Party Programme 1910 : (16)

  '3. The promotion of and development of agriculture by the encouragement of co-operative effort and organised research.

  5. Taxing the unimproved value of land and more particularly that in the possession of Land Companies:'

## THE FINANCIAL CONDITIONS IN THE FOUR COLONIES IN THE PERIOD PRECEDING UNION

Any consideration of the financial policies of the Union Government in the initial years of its existence must needs take place in the knowledge of the financial conditions existing in the four colonies before Union and therefore assumed by the fledgling state. Predictably, the war had generated boom conditions in the coastal colonies and in those portions of the inland colonies subjected to permanent British occupation, as the invading forces provided a substantial cash market.

After the war there were great hopes of a boom in the entire country, as the gold mining industry was expected to enjoy tremendous expansion. An increase in building activity touched nearly every town and village in the country and the prices of South African gold shares rose to unprecedented heights on the London Stock Exchange. Unhappily, the expected rapid expansion failed to materialise for two reasons. Firstly, the ready cash market departed with the British forces, and secondly, political uncertainties and the labour shortage on the mines retarded the growth of gold production.

The political uncertainties, according to L M Thompson, (17) flowed from the disparities in economic strength between the colonial governments, disputes about railway revenues, the imminence of self-government in the Transvaal and the Orange River Colony, and the growth of isolationist sentiment in a population still smarting under the pain and ignominy of a totally debilitating defeat. It was feared that the country was drifting into two mutually hostile groups which would destroy any hope of amity and hence unity on the subcontinent. These uncertainties spurred the drive towards Union from as early as 1906.

The fact that the adverse economic effects of the unexpectedly slow growth of gold mining production was felt throughout the country is indicative of the status of South Africa at that stage; as David Yudelman puts it: (18) 'The South African

economy then was almost totally dependent on the mining industry'.

The period from 1903 to 1908 was thus one of depression in the four colonies, although the effects were not equally felt by all. The farming areas were not so much affected as were the towns, and the inland colonies fared better than their coastal counterparts. Two reasons are apparent for this difference: gold mines and railways. Firstly, the gold mining industry did expand, even though its degree of expansion was not as great as had been hoped. Thompson (19) makes this point and reproduces (20) the following table which illustrates the fact.

GOLD OUTPUT OF THE TRANSVAAL

| | Fine ounces | £ | Percentages of world output |
|---|---|---|---|
| 1901 | 258,032 | 1,096,051 | 2.04 |
| 1902 | 1,718,921 | 7,301,501 | 11.97 |
| 1903 | 2,972,897 | 12,628,057 | 18.75 |
| 1904 | 3,773,517 | 16,028,883 | 22,46 |
| 1905 | 4,909,541 | 20,854,440 | 26.69 |
| 1906 | 5,792,823 | 24,606,336 | 29.75 |
| 1907 | 6,450,740 | 27,400,992 | 32.32 |
| 1908 | 7,056,266 | 29,973,115 | 33.01 |
| 1909 | 7,295,108 | 30,987,650 | 33.05 |
| 1910 | 7,531,386 | 31,973,123 | 34.20 |

By 1904, the production figure of some £16 million equalled the pre-war level and had nearly doubled by 1910. Understandably, this was a reasonably effective cushion against the effects of the depression, even though it was the very fact that the mines were not expanding sufficiently quickly which contributed substantially to the general depression. White population in the Transvaal increased in the face of the exodus of disillusioned fortune seekers, from almost 300 000 in 1904 to 420 000 in 1910; other economic indicators reflected a growth tendency, such as savings bank deposits, number of telegrams handled annually and volume of imports. Government revenues totalled some £40,5 million during the period up to Union, of which £13,5 million came from customs and £8,1 million from mines. After a peak of £2,2 million in 1902-3, customs revenue slumped to £1,6 million in 1904-5, before recovering to £1,7 million in 1905-6. A dip to £1,6 million was then followed by a steady improvement to £1,7 million in 1909-10. Mining revenue rose steadily from £500 000 in 1902-3 to £1,2 million in 1906-7 before falling to £1 million the following year. This reduction was more than recovered in the next year when revenue was £1,4 million; but the 1909-10 figure fell to £1,3 million, still a respectable increase in the nine-year period. In summary, the Transvaal showed a surplus of some £5 758 000 for the period from the end of hostilities until Union, together with its share of the £18 million surplus enjoyed by the Central South African Railways (CSAR) during that period. Of the total revenue, 20% came from mines and one-third from customs. (19)

The Orange River Colony operated at a much lower scale, earning revenues of some £6,7 million during the same period together with its share of the CSAR revenue. Some 37% of the revenue other than from railways came from customs, and the net surplus for the entire period, during which only the last two years showed deficits, amounted to £173 000. The white population increased significantly from 143 000 to 175 000, and expenditure was successfully tailored to remain within the falling revenue; contrary to the Transvaal experience, the highest level occurred in 1902-3 at £956 000, after which the revenue fell steadily to £740 000 in 1907-8. It then leapt ahead in the next two years to reach £953 000 in 1909-10. Clearly, then, although there was a general contraction in the economy which was reflected in reduced expenditure by government, at least there was no excess in public spending with a consequent deficit. (19)

Natal, by contrast, suffered mightily under the depressed conditions and its position was aggravated by treasurers who were consistently optimistic in their revenue estimates and caused deficits in most of the financial years during the period. Customs revenue totalled some 16% of all revenue, while the Natal Government Railways produced 57% of the grand total of a little over £30 million for the period. The total receipts in 1909-10 were £4,3 million: considerably more than the £953 000 of the Orange River Colony, but nowhere near the optimistic expectations of the authorities. The accumulated deficit had reached £705 000 by 1910, the result of deficits in no fewer than five of the

eight financial periods. Revenues fell from £4,3 million in 1902-3 to as low as £3,4 million in 1904-5 before subsequently gradually recovering. White population fell from 97 000 in 1904 to 91 400 in 1908 and had reached only 98 000 by 1911. Bank deposits fell by 27% until 1908 and the number of telegrams by one third, while imports tumbled by one half. There was a general recovery after 1908, but the colony was certainly depressed in all sectors. (19)

The Cape Colony experienced the most prolonged depression because a financial crisis in Europe and America severely affected the diamond industry, the most important export commodity of the colony. The following table shows the diamond output of South Africa during the period between war and Union and indicates how this industry was devastated in 1908. (20)

DIAMOND OUTPUT OF SOUTH AFRICA

| | Cape Colony | Transvaal | O.R.C. | Total | |
|---|---|---|---|---|---|
| | £ | £ | £ | Carats | £ |
| 1902 | 4,949,808 | 2,402 | No records | Records incomplete | |
| 1903 | 4,833,040 | 239,752 | | | |
| 1904 | 5,191,661 | 1,150,873 | 866,111 | 3,683,157 | 7,208,645 |
| 1905 | 4,428,383 | 922,330 | 853,834 | 3,368,789 | 6,204,547 |
| 1906 | 6,992,811 | 1,563,141 | 1,040,691 | 4,136,236 | 9,596,643 |
| 1907 | 6,310,796 | 2,268,075 | 1,407,055 | 5,170,812 | 9,985,926 |
| 1908 | 3,085,352 | 1,549,815 | 771,414 | 4,091,121 | 5,406,581 |
| 1909 | 4,690,478 | 1,176,680 | 1,332,201 | 5,169,871 | 7,199,359 |
| 1910 | 5,267,659 | 1,416,464 | 1,505,074 | 5,456,558 | 8,189,197 |

The white population decreased from 580 000 in 1904 before recovering to only 582 000 in 1911. Bank deposits fell by almost one half, as did the number of telegrams. Value of imports in 1908 were £14 million in comparison with £32 in 1902. Optimistic treasurers had an ill effect here too, resulting in deficits in five years of the eight and a net deficit of £3 million by 1910. The Cape relied on customs revenue for 23% of its revenue and on railway receipts for 46%. (19)

In both coastal colonies the share of total customs and railway revenue generated in the sub-continent fell steadily; as those sources were so important, it is clear why they endured so prolonged a period of regression and stagnation. The reasons for the reduced shares were, in the case of customs, beyond the control of the two colonies, as they were part of the Customs Union; and, in the case of railway revenue, the fact that it was cheaper to use the facilities at Lourenco Marques for both import and export to and from the large Transvaal market.

Indeed, the Transvaal authorities had established a modus vivendi with the Portuguese authorities relating railway rates to the employment of mining labour from Portuguese East Africa in 1904. It was, therefore, for several reasons in the interest of the Transvaal to retain this position regardless of its effect on her sister colonies. To make matters worse for Natal, which did not even have the benefit of a diamond mining industry to cushion its losses, new lines between Klerksdorp and Fourteen Streams and between Harrismith and Kroonstad diverted to the Cape much of the

freight which had previously travelled through Durban.

The four members of the Union, then, were a financially disparate group, all only just beginning to emerge from a state of severe depression and all dependent on volatile sources of revenue. Customs comprised, in 1909-10, 36% of the revenue of the Orange River Colony; in the Cape it was 23%, in the Transvaal 34% and 17% in Natal. Customs revenue in turn depends on the general level of trade which is subjected to numerous forces beyond the control of individual governments. Gold mining with all its dependence on labour and international stability, generated almost one quarter of the revenue of the Transvaal in 1910. The diamond mining industry of the Cape was very susceptible to foreign financial conditions.

The net revenues of the respective railway systems in 1909-10 were £3,3 million from the Central South African Railways, £1 million in Natal and £3,1 million in the Cape for a total of £7,4 million. All this revenue was destined to disappear in terms of sections 117 and 127 of the South Africa Act, 1909. (21) Section 117 provided that all revenues derived from the administration of the railways and harbours were to be paid into a railway and harbour fund for railway and harbour purposes, whereas all other revenues would be paid into a consolidated revenue fund. Section 127 stated that the railways and harbours would 'be administered on business principles, due regard being had to agricultural and industrial development within the Union and the promotion, by means of cheap transport, of the

agricultural and industrial development within the Union and the promotion, by means of cheap transport, of the agricultural and industrial population in the inland portions of the Union.'

Railways and harbour earnings were to be 'so far as may be' 'not more than are sufficient' to meet the necessary outlays for working, maintenance, betterment, depreciation, and the payment of interest due on capital.' The Governor-General was to give effect to these provisions within four years after Union. (22) L M Thompson (23) gives as the reasons for this decision the need to reduce railway rates in order to stimulate agriculture and industry in the inland provinces. The result of this change in the rating system also helped to alleviate the growing poor-white problem by subsidising the agricultural sector. Such a decision was politically expedient because of the voting power of the rural whites, but the consequences continue to be felt to this day in the management of the South African Transport Services.

The upshot of this financial situation was that total revenue of the four colonies amounted to £13 million in 1909-10 in addition to net railways revenue of £5,5 million, as against expenditure of £13,6 million. The railways were keeping the colonies solvent and their influence was obliged to disappear over four years. The public debt at the time of Union amounted to £113 million.

Against this background a new state was to come into existence, to generate enough revenue, and to incur expenditure on public works of the correct type and size necessary to establish its credibility and viability.

## BRIEF BIOGRAPHICAL SKETCHES OF THE RESPECTIVE MINISTERS OF FINANCE

1. Mr Henry Charles Hull was Minister of Finance in the first Union Cabinet from 1910 to 21 May 1912, when he resigned from the Government.

   He was born in Caledon, Cape Colony in 1860 and practised as an attorney in Johannesburg. As a member of the Reform Committee, he was imprisoned after the Jameson Raid in 1896 and fined. He was elected to the first Union Parliament in 1910 as Member for Barberton, a safe seat arranged for him after he lost his campaign in Georgetown. He represented Barberton until his retirement from parliamentary politics at the dissolution of the House of Assembly prior to the General Election in 1915.

   In a speech to Parliament on 21 May 1912, Mr Hull gave as his reasons for resigning, the 'policy ......being pursued with regard to the Railways'. (24) He summarised his objections to that policy under two headings: firstly, that Cabinet members in general and he in particular had not been consulted on important matters concerning the Railways; secondly, that the provisions of the South Africa Act

relating to Railways were not being observed.

Apparently the Minister of Railways and Harbours, Mr J W Sauer, was making major capital and fare decisions without submitting them first to the Cabinet, much less Parliament. The principle of collective responsibility was therefore being visited upon Cabinet members ignorant of the very provisions for which they were held responsible. This situation had weighed heavily with Hull as Minister of Finance, and after apparently prolonged discussions with the Prime Minister, he had decided to resign. Mr Sauer defended himself, only for the debate to become quite heated and indeed extended into the next day. In the event, the matter came to rest, the resignation of Hull was accepted and, perhaps significantly, Sauer remained in office, but not for long before giving way to Mr H Burton. This episode could be construed as an example of the general unwillingness of Botha to be firm; he certainly appears to have condoned conduct by Sauer which was less than satisfactory. On the other hand, his appointment of Hull in the first place may well have been forced on Botha by Reformist Transvaal elements despite the philosophical chasm between their policies and those of the broad-thinking Prime Minister. Botha may have greeted the resignation of Hull with a private sigh of relief at having so painlessly been relieved of a potentially prickly political thorn in the side of his Cabinet. The latter explanation gains credence from a letter he wrote to Smuts on 1 February 1915. (25) The

translation of Hancock from the Dutch reads:

'As regards Hull (as a possible addition to the Cabinet to assist with finance portfolio held by Smuts with some difficulty in the midst of his many foreign activities during the War), I feel that to take him into the Cabinet will be the quickest way to break up our party and Cabinet and finish them for a long time, and Jannie, I can stand much, but after what has happened I feel it is impossible for me to sit in the same Cabinet as he; then it would be far better for me to go out of politics altogether.'

2. General J C Smuts succeeded Hull and served until February 1915 when it was clear that he could not simultaneously hold the portfolios of both Finance and Defence, while actively prosecuting his extensive wartime activities. Indeed, the comments of Botha quoted above deal precisely with the means of relieving Smuts of some of his burdens by appointing a new Minister of Finance. A mere fortnight after Botha's letter, he appointed Sir D P de V Graaff to the post, despite the fact that the latter was far from well.

3. Sir D P de Villiers Graaff was the first Baronet in the titled Graaff line, having been so honoured in 1911. He founded the Imperial Cold Storage and Supply Company and pursued a career in politics from as early as 1891, when he was mayor of Cape Town. He supported the Afrikaner Bond and

served in the Cape House of Assembly. Despite poor health, he was apparently always willing to serve and was Minister of Posts and Telegraphs between 1910 and 1912, then Minister without portfolio for a year before leaving the Cabinet and acting as High Commissioner in London. When it became necessary for Smuts to shed some of his duties, Graaff assumed the Finance portfolio in 1915, but served for less than a year and never presented a Budget. Botha described him in the letter to Smuts in which he criticised Hull so heavily as 'upright, loyal and able'. (26)

4. Mr Henry Burton was a controversial figure to whose lot it fell to hold the reins of Finance during both the wartime austerity period of 1916 - 1917 and the painful deflationary time of 1920 - 1924. A product of St Andrew's College, Grahamstown, he practised at the Bar in Kimberley and entered the Cape House of Assembly in 1902 as a supporter of the Afrikaner Bond, where he served in Merriman's Cabinet. He energetically supported the cause of the Cape Afrikaners before the special (treason) court and strongly advocated compensation to farmers for war losses. His urging in the Cape Assembly in 1904 that a special court be convened to review the penalties imposed on Cape rebels brought about the fall of the government of Sir J G Sprigg. Elected unopposed to the House of Assembly in 1910, he held the portfolios of Native Affairs and of Railways and Harbours. Botha replaced him at Native Affairs in 1912, but added to his Railways

position that of Finance in 1916 when Smuts was relieved.

This situation attracted fierce Opposition criticism, to the point where Botha confided to Smuts in a telegram in April 1917: 'The criticism against one Minister holding a Portfolio of Finance and Railways is becoming so strong that I must separate them.'(27) The Prime Minister did so, and Sir Thomas Orr was Minister of Finance until April 1920, when Burton resumed the office; he was relieved of the Railways portfolio less than a year later, but continued in Finance until his election defeat and retirement from politics in 1924.

Burton was clearly the most dominant of the six Ministers of Finance during the first 15 years of Union, if one allows that Havenga qualified for inclusion in this period by a mere year and carved his considerable place in the fiscal political history of South Africa in the period after 1925. In his book 'Some South African Politicians'(28) L E Neame devotes a chapter to Burton and was clearly impressed by the stature of the man.

Burton is described as one who had triumphed in spite of having been cursed by an overbearing and irritating manner which counterbalanced his outstanding ability. His ability at the Bar in Kimberley attracted the patronage of De Beers, and his subsequent adoption of the rights of then Cape Dutch after the Anglo-Dutch War brought him to the notice of the

public in no uncertain terms. Although very young in Parliamentary terms at 38, so much so that Sir Gordon Sprigg referred to him as 'a very, very young member', he managed in his first year in Parliament to overthrow the Sprigg Government by raising the vexed questions of martial law, compensation to farmers for war losses, and fines imposed on rebels. From 1908 he served as Attorney-General in the Merriman administration.

As a member of the Union Cabinet, his tenure as Minister of Native Affairs was undistinguished and all but forgotten. Such was the status of that portfolio in those days that it could easily be given the cavalier treatment Burton accorded it.

His ministry of Railways and Harbours, however, was another matter entirely. He held the position from 1912 until 1921 when his domineering manner had so disaffected the railwaymen that a nervous Government replaced him and left him with only the vitally important Finance portfolio. His great strength lay in his Parliamentary ability to defend an unpopular position with skill, superb debating ability, a caustic wit and untiring resolution. A modicum of tact would have rendered him well nigh perfect, but this he totally lacked.

As Minister of Finance, he was fated to preside over two unpopular eras. The inferior bread introduced during the war as an austerity measure was known as 'Burton loaf' and

tied him, unfairly of course, to the unpleasant economic consequences of wartime living. Far more serious, however, was the fact that he had to preside over the deflation of the early 1920's, having taken over an empty Treasury and mounting deficits. Finance proved his worth and caused his downfall. His 1921 Budget shocked the country with its large deficit and the remedial measures he applied. He displayed what Lloyd George described as the rarest of qualities in public life, moral courage. Secure in his ingrained belief in his rightness, he faced down the increasing hostility caused by retrenchment, increased taxation and reduction in cost of living allowances for public servants. He revived the unpopular patent medicines tax, thus turning every chemist shop in the country into a recruiting office for the Nationalist and Labour parties.

Finally he straightened out the financial situation and handed his successor a far better situation than he had inherited. Unfortunately, his habit of making enemies needlessly with his abrasive manner combined with his being identified with his necessary fiscal measures, and he was rejected by the voters in 1924, to vanish from political life. He certainly seems to have deserved more credit than he received for his contribution to his country in its critical early years.

5. Sir Thomas Orr became Minister of Finance in October 1917 when Botha was obliged to react to growing criticism of the portfolios of both Finance and Railways and Harbours being vested in one man. The choice of Sir Thomas was a logical one, because he had been a valuable financial adviser to the Cabinet throughout his Parliamentary career.

Born in Ireland, Orr had joined the British Civil Service in 1875 at the age of 18. Steady promotions in the Exchequer and Audit Department brought him steadily via Malta to the position of Auditor-General of Natal in 1902. He retired on pension in 1910 and was elected to the Union Parliament in the same year as the Independent member for Pietermaritzburg North. He soon threw his hand in with the governing party, staunchly supporting Botha.

He was Minister of Finance during a difficult period; the war was ending, necessitating tremendous Government expenditure in addition to pensions for the disabled and dependants. In addition, the accounting system was very complicated owing to the financial links between the South African and Imperial governments. Acting on the recommendations of a commission, he prepared a pension scheme for these groups.

No longer young at the time, he felt the strains of office, and these were reflected in a tendency to treat criticism with contemptuous indifference. No doubt a lifetime in service such as his gave him encyclopaedic knowledge of matters fiscal and encouraged resentment of criticism by what were in his eyes lesser financial mortals.

He resigned from the Cabinet in 1920 and did not seek re-election to Parliament in that year. This was perhaps as well, for his age and temperament would surely have militated against his successfully shouldering the enormous burdens of the Minister of Finance in the next four years.

6. Mr N C Havenga was the sixth Minister of Finance during the period covered by this work. He was born in Fauresmith and practised there as an attorney after education at Grey College, Bloemfontein followed by service with General Hertzog in the Anglo-Boer War. He served in the OFS Provincial Council and was a member of the Executive Council between 1910 and 1915, when he became the Member of Parliament for Fauresmith. His interest in Finance made him an expected choice to head that portfolio when Hertzog assumed the reins in 1924.

Havenga was destined to remain in this position until 1939, and to resume it from 1948. He has, then, been the longest-serving Minister of Finance to date.

# CHAPTER TWO

## 1910 TO 1913

GENERAL

The period from Union until 1914 may appropriately be viewed as a unit for the purposes of this work; there was no income tax, the budget being balanced by means of the railway contributions. As has been seen in Chapter 1, these were destined to disappear after 1914 and therefore required the inception of a new fiscal approach.

These first four years are homogeneous in the following respects:

- no income tax
- reliance on railway revenue;
- internal and external peace, tending to be affected only towards the end of the period by strikes on the gold mines and the approach of war in Europe;
- the need for the government to legitimise the existence of the fledgling state by establishing infrastructure and all the other services and financial appurtenances which necessarily accompany and indeed signal the existence of a nation; the kinds of institutions for which potential investors and settlers look; the bureaucratic hierarchies which ensure continuity through changes of government and other variable conditions.

This last-mentioned need is one which is gaining currency in literature. In order to establish its legitimacy, its right to exist and be recognised as an entity, a state must have accumulated wealth to the extent that it is able to provide the

structures necessary for this purpose. In South Africa, the way to accumulation of capital lay via the gold mines. At the same time, without a stable state within which to operate and from which to draw labour and the myriad other services it demanded, the mining industry could scarcely have survived, much less prospered. In South Africa, then, state and mines were enmeshed and utterly interdependent. Marxist theory would characterise this situation as exploitation of the masses via effective control of government by the mines, the milch cow of the fiscus. Yudelman (1) argues rather that the South African political parties represented in Parliament, being fundamentally capitalistic in philosophy, were bound to exist in tandem with the mines. Thus their differences were not 'capitalism' versus 'rural Afrikanerism' but rather a broad South Africanism on the one hand against a desire to establish an exclusive Afrikaner 'volk' on the other, while never seriously upsetting the balance between the state and its capitalistic entrepreneurial partners.

What were these bases of a stable state, and how did the Government finance them? The following tables show the sources of revenue and its destination for the first four years, before introduction of income tax legislation.

| Revenue (£000's) | 10 months ended 31 March 1911 | | 12 months ended 31 March | | |
|---|---|---|---|---|---|
| | Actual | Grossed up to 12 months | 1912 | 1913 | 1914 |
| Customs | 3 758 | 4 384 | 4 302 | 4 405 | 4 630 |
| Excise | 240 | 280 | 295 | 406 | 470 |
| Posts & Telegraphs | 1 128 | 1 316 | 1 385 | 1 498 | 1 679 |
| Mining | 1 531 | 1 786 | 2 243 | 2 261 | 2 457 |
| Licences | 469 | 547 | 541 | 492 | 131 |
| Stamp duties | 436 | 508 | 530 | 544 | 539 |
| Transfer, estate and death duties | 447 | 521 | 506 | 567 | 150 |
| Personal and Native taxes, including poll tax and pass fees | 725 | 846 | 1 197 | 1 145 | 840 |
| Quit rents | 153 | 178 | 160 | 145 | 146 |
| Rental of government property | 195 | 227 | 89 | 90 | 86 |
| Interest | 2 565 | 2 993 | 2 806 | 3 470 | 3 502 |
| Departmental receipts | 440 | 513 | 512 | 466 | 400 |
| Fines and forfeitures | 121 | 141 | 147 | 150 | 160 |
| Sales of government property | 83 | 97 | 100 | 35 | 55 |
| Forest Revenue | | | | 48 | 50 |
| Miscellaneous | 60 | 75 | 80 | 66 | 94 |
| | 12 351 | 14 412 | 14 893 | 15 788 | 15 389 |
| Railways | 1 220 | 1 423 | 1 159 | 500 | - |
| | 13 571 | 15 835 | 16 052 | 16 288 | 15 389 |

| Expenditure (£000's) | 10 months ended 31 March 1911 | | 12 months ended 31 March | | |
|---|---|---|---|---|---|
| | Actual | Grossed up to 12 months | 1912 | 1913 | 1914 |
| Governor-General and Parliament | 98 | 114 | 107 | 110 | 111 |
| Prime Minister | 7 | 8 | 9 | 8 | 8 |
| Agriculture | 587 | 685 | 835 | 502 | 594 |
| Interior | 640 | 746 | 789 | 740 | 754 |
| Defence | 363 | 423 | 440 | 541 | 1 345 |
| Mines | 128 | 150 | 218 | 288 | 204 |
| Justice | 2 150 | 2 510 | 2 544 | 2 580 | 2 443 |
| Education | 158 | 183 | 110 | 124 | 119 |
| Forestry | 94 | 107 | 122 | 123 | 125 |
| Finance | 4 154 | 4 858 | 5 240 | 5 277 | 5 454 |
| Provinces | 2 647 | 3 088 | 3 309 | 3 423 | 2 205 |
| Lands | 240 | 280 | 288 | 293 | 295 |
| Native Affairs | 238 | 277 | 292 | 306 | 310 |
| Commerce and Industries | 147 | 172 | 169 | 151 | - * |
| Public Works | 948 | 1 106 | 936 | 925 | 830 |
| Posts and Telegraphs | 1 203 | 1 403 | 1 485 | 1 539 | 1 622 |
| | 13 802 | 16 110 | 16 893 | 17 130 | 16 419 |
| Surplus/(Deficit) | (231) | (275) | (841) | (842) | (1 030) |

*included in Finance from 1914

It is not the purpose of this work to analyse in depth reasons for changes in expenditure under particular heads; the table is included merely to indicate the kinds of expenditure to which the government committed itself, thus creating the need to generate the revenues. It is interesting to note that the level of expenditure remained virtually constant throughout the period, changes being generally no more than amendments to the distribution order.

Finance drew the largest share, or almost one-third of the total. The reason was simply that the amount needed to manage the public debt formed part of the finance budget, and this comprised the bulk of the budget. For example, in 1913/14, £4 808 000 of the total of £5 454 000 related to the public debt and, of this sum, no less than £4 142 000 was for interest.

Payments to the provinces varied from as much as 20% to as little as 13% of the total, the latter being the figure in 1913/14 when the method of calculating grants was altered; essentially grants for capital expenditure began to be made out of the Loan estimates.

Other pertinent recipients of funds were Justice, Posts and Telegraphs, and Public Works. Defence showed a small but unspectacular growth until 1913/14 when the amount budgeted leapt by about 160% to £1 345 000. Clearly the threat of war had affected the planners, and equally the first round of

disturbances on the mines had shown the need for strengthened forces of law and order.

Most of the other votes show a slightly upward tendency, with the notable exceptions of agriculture (which is precisely the type of area where reductions can be affected in the short term), education (which lends itself to economies in favour of more concrete needs such as defence, communications and interest payments - however reprehensible such a policy might be in terms of the ultimate effect on the nation), the provinces (although this apparent reduction was artificial, as explained above), and public works (once a certain amount of such construction has taken place, further outlays may safely be deferred without too much hardship).

The government, then, was setting up the systems of communication, security and basic infrastructure while at the same time protecting the financial reputation of the country in the outside world.

Its means of filling the state coffers to the requisite level were largely centred around customs, which contributed about 30% of the total; posts and telegraphs 11%; mining 16%; and interest a substantial 23%.

Conspicuous by its absence is any contribution by an income tax. The first Act of Parliament which placed a tax on incomes other than from mining activities in the Union was the Income Tax Act No. 28 of 1914.(2) The only piece of legislation promulgated in 1910 which generated a tax on income was the Mining Taxation Act, (3) providing for an annual tax on mining profits as set out in Appendix 2. As may be seen from the tables in this Chapter, the Budget was balanced each year between 1910 and 1914 by the various sources of indirect taxation together with mining taxation and the contributions from the Railways as discussed in Chapter 1.

Schumann (4) refers to this period as one where gold production was relatively constant, contrasting with a tendency towards decline in diamond mining, while cost production was beginning to increase as a reflection of the incipient economic growth. The agricultural sector was steadily increasing in importance and output, while the manufacturing facet of the body economic was beginning to surge ahead. It is interesting to note that, by the end of the four-year period under review, the gross value of manufacturers was about equal to the values of farming and mining respectively. (This proportion was to alter over the next twenty years to the point where manufacturing output exceeded mineral production by 33% despite a higher gold price, and agricultural production by 100%.) In short, although general expansion was less than dramatic during the period 1910 - 1914, expansion there certainly was, with the fledgling manufacturing

sector preparing for a leap of activity destined to place it in the forefront of expansion.

In considering the annual estimates of revenue and expenditure and the respective budgets, it is important to bear in mind that the Minister, and indeed Parliament, was bound by the provisions of section 5 of the Public Debt Commissioners Act No 18 of 1911. This section provided that, whenever there was a surplus of revenue over expenditure, that surplus was to be paid into the bank account of the Commissioners and used for loan redemption purposes. In other words, any surplus resulting in a particular year was not available to be used to reduce the tax burden in the following year.

BUDGET 1910 - 11

In his budget speech for the ten months ended 31 March 1911 delivered in the House of Assembly on Monday 28 November 1910, (5) the then Minister of Finance, Mr Henry Charles Hull, pointed out that with no direct income tax levied by any Act of the Union Parliament, the Government was obliged to rely on other sources of revenue.

(a) The first of these comprised the bequests from the four provinces in the form of the revenue balances inherited by the central government at the time of Union. Largest provider had been the Transvaal with £1 015 000, followed by the Orange Free State with £577 000; the Cape Province

furnished £421 000, whilst Natal contributed £268 000.

(b) Secondly, the Minister briefly explained the significance of sections 117 and 127 of the South Africa Act (6), pointing out in particular that the Railways were obliged to contribute to the general revenue for four years after Union. He warned members of the House that: (7)

> 'That policy must finally come to an end four years from May 31, 1910, and therefore it will be necessary for this House seriously to consider what other sources of taxation will have to be opened up against the times when the railways will not be able to stand by the general revenue to this extent.'

(c) Thirdly, the Minister mentioned the proposed taxation of mining profits which soon after his Budget speech came to fruition in the Mining Taxation Act.(8)

Mr Hull then referred to the estimates, according to which total expenditure would amount to some £13 802 000, as against revenue of £12 351 000. Agriculture consumed 4% of the budgeted estimates, Interior 4,6% and Public Works 7%. As was to be the case in all future years, Finance received the lion's share at 30%, including as it did the interest due on the public debt. This expense alone amounted to £4 000 000 or a full 29% of

the estimated expenditure. The provinces received 19% and Justice 15,5%, while Posts and Telegraphs, that important economic indicator, was awarded 9%.

This resulted in an estimated deficit of £1 451 000, which the Minister proposed to meet in the following ways:

- appropriation of the sum of £1 220 000 which was to be paid into the consolidated revenue from railway revenues, in terms of section 127 of the South Africa Act, 1909 (9)

- introduction of the Mining Taxation Act referred to above, which would cause the diamond mines of the Cape Province to commence paying profits tax at the same 10% rate as the Transvaal gold mines had for some time been doing and to which the Cape mines had been subject up to the date of Union, and for the Orange Free State diamond mines to pay at an increased rate of 10% instead of the 7% which they had been paying up to that time. At the same time, base metals and minerals would be taxed on a sliding scale. Revenue from this source was estimated at £240 000, thus eliminating the deficit.

BUDGET 1911 - 12

On 10 March 1911 Mr Hull presented the second Union budget. He commenced by reporting that the results of the preceding ten

months had been slightly different from those estimated, and the surplus was £478 000 as against an estimated £9 000. He continued by outlining the financial policy of the Government, which policy was embodied in three objectives in order to eliminate the fiscal inequalities between the four provinces in putting into operation the fiscal revolution demanded by Union (10):

1. Revision and repeal of the different systems of taxation in the provinces and their replacement with a uniform system.

2. Revision and alteration of the differing principles upon which the Central Government gave financial support to the provinces.

3. A radical change in the methods of operating the railways and harbours.

The Minister explained that different systems and levels of taxation existing in each province. Poll tax stood at £2 per head in the Transvaal, £1 in Natal and Orange Free State and did not exist at all in the Cape Province; Natal charged a Hut Tax of 14/- per hut, whereas in the Cape the rate was variable. The Transvaal and Orange Free State did not charge such a tax. Estate duty was subject to wide variations: in the Orange Free State it was nominal, Natal and the Cape used systems of succession duty, while the Transvaal employed a 'scientific system'. Large differences also existed in stamp duty, transfer

duty, licences, mining laws and excise. The subsidies enjoyed by each province varied considerably.

The railways constituted a major source of revenue, especially for the Transvaal and Orange Free State, but this was due to disappear over four years, after which revenue would merely match expenditure.

(It made eminent sense for the government to adopt these objectives, for the alternative would have been that residents would be subject to the vagaries of fiscal inequalities determined by the provinces in which they happened to reside at any time. Such uncertainty was clearly unsuited to development of the Union, whose very existence struck at differences between the provinces. Similarly it was desirable to calculate the subsidies to the provinces on some common base, in the name of sense and equity. The radical change in operating the railways and harbours was perforce an objective of the Government, in terms of the South Africa Act.)

The Minister pointed out that the income tax law of the Cape Colony had lapsed, and that the loss of revenue had not been matched by the proceeds of the Mining Taxation Act. (11) Clearly new sources of revenue in the form of taxation would be needed and these would probably take the form of a general income tax.

In gently preparing the country for the probable introduction of general income tax three years hence, Mr Hull assured members of

the House that there was no need for alarm; the income tax would merely amount to a 'readjustment in the incidence of taxation' (12) in that revenue amounting to £1 500 000 from the Railways would be remitted (and presumably result in that much less being paid by consumers) and a like amount would be garnered from the consumers in the form of income tax. The Minister emphasised, however, that the changes would have to be gradual in order to avoid economic upheaval and in the interests of time.

The view had been expressed that uniformity of taxation should be introduced at once, at the same time allowing for the reduction in the railways contribution. However, Mr Hull rejected this opinion for two reasons. Firstly, it would take some time to prepare the necessary amending legislation, diverse as were the differences. Secondly, a sudden change of so far-reaching a nature would cause a major upheaval in the commercial sector - finance, trade and commerce would be fundamentally affected. The only practical method would be to pass a group of related matters each year for several years until the desired uniformity was a reality.

Turning to the estimates for the current year, Mr Hull mentioned the most prominent sources of revenue, namely customs, posts and telegraphs, mining, stamp duties and interest. These were insufficient to meet the estimated expenditure, and he would appropriate £1 159 000 from railway revenue to help eliminate the shortfall. In addition, the Cape cigarette tax would be extended to the entire Union, bringing in an additional £45 000.

At the same time, of course, this charge was another step in the move towards unifying the tax structures of the various provinces, as was the repeal of the Cape patent medicine tax which would have garnered £11 000. After taking into account certain adjustments, and using the surplus from the previous period, the Minister arrived at a deficit of £148 000 with which he was prepared to live.

(It should be noted that the final result in any year does not accord exactly with the estimates. Matters such as the use to which previous surpluses or deficits are put, and supplementary estimates, tend to change the final result. It is considered, however, that the tables of estimates included in this Chapter are sufficient to indicate trends and the chief heads of revenue and expenditure. More detail would tend to cloud the main issue.)

Compared with the initial fiscal period, expenditure overall was virtually unchanged. An increase in the Interior vote had much to do with the costs of a census and voter registration; the Mines increase resulted largely from the much larger expenditure on the mines school, on district mining development, and particularly on a large grant to the miners' phthisis fund; roads and education were the chief reasons for the increased grants to the provinces. All these expenditures may be seen as part of a concerted effort to establish the young state and aid in its move towards stability and maturity. There is little subtlety in the policy, no vast amounts on scientific research or

esoteric developments related to the comforts of an advanced community. Rather was there an unremitting emphasis on the basics. This point having been made, it must be said that the government could not be quite altruistic in its approach; indeed, public works and education were two votes which suffered in the estimates. However, much of the increases to the provinces was for this type of expenditure.

On the revenue side, the increase in customs receipts reflected the expansion of trade, as did the greater amount received from posts and telegraphs. Mining continued its climb out of the post war depression, while items such as stamp duties, licences and transfer duties all gave evidence of heightened commercial activity. The large increase in interest received was also a healthy sign, as it indicated that the government was involved in fostering commercial activity.

BUDGET 1912 - 13

On 22 March 1912, Mr Hull presented the third Budget of the Union (13) and reported that the estimated deficit had become a surplus of some £855 000 as a result of better trading conditions. Customs revenue had risen by £200 000 or one-half per cent over the estimate; excise by £81 000 or 27%, mainly due to imposition of duty on cigarettes; posts and telegraphs by £79 000 or two-thirds per cent. Although small, this increase was gratifying because changes in revenue from this source were taken as a very good indicator of the general state of business.

An upward trend, therefore, was significant. The labour troubles on the gold mines had reduced revenue by £90 000, but increased income from the diamond mines had resulted in a net increase of £71 000.

For the coming year Mr Hull drew specific attention to anticipated increases in revenue from customs, posts and telegraphs, and interest. Significant changes in expenditure included: agriculture - a reduction of £333 000 or 40%, due mainly to the conclusion of operations against East Coast Fever and the discontinuation of steam ploughing and fencing; [the government had instituted a programme of cattle dipping to eliminate East Coast Fever in Natal, and for the same reason had engaged in fencing to prevent the spread of the disease. Before Union, the Natal government had purchased a number of steam ploughs for hire to farmers; these had never been fully and therefore economically used, and were withdrawn from service to terminate the drain on resources]; interior - a decrease of £93 000 largely due to the completion of the census and parliamentary election and voter registration expenses; defence - additional armaments, stores and the inception of the new Defence scheme of a small Permanent Force, a part-time Active Citizen Force and a General Reserve, together with rifle clubs organised on the basis of the old Boer Commandos accounted for the increase of £100 000; mines - once again a contribution to the Miners' Phthisis Compensation Fund caused this increase; education - generally greater grants to universities and colleges resulted in an additional £14 000 or 13% being spent; posts and

telegraphs - a small increase of only 3%, mainly to employ new staff; and finally the provinces - education and hospitals consumed the increase of some £114 000 from £3 309 000 in the previous year.

By and large the increases and decreases reflected only two significant tendencies: concern with defence, no doubt bearing in mind the first flurry of mining strikes and the tentative signs of unrest in Europe; and, probably allied to the miners' unrest, the contribution to the Phthisis Fund. The latter may be seen as a victory for the miners as well as pragmatic realisation that it behoved the government to care for its 'golden goose', the gold mining industry. In addition, of course, it was tactically sound to show some concern for the supporters of the opposition Labour Party, whose four-year existence had been largely dependent upon white mining support.

The estimated deficit would be more than offset by the surplus from the previous year after taking into account the final contribution of £500 000 from the Railways.

Once again the Minister foreshadowed 'fresh taxation of some description'. (14)

BUDGET 1913 - 14

On 14 March 1913 General Smuts presented the fourth annual Budget. (15) He had assumed the Finance portfolio on the

resignation of Mr Hull on 12 June 1912. As discussed more fully in Chapter 1 at page 23, Mr Hull had resigned in protest against the policy towards the railways: he and other Cabinet members had objected to not having been consulted in regard to what he termed 'important matters affecting the Railways and their administration'. Secondly, he alleged that the provisions of the South Africa Act relating to the railways were not being observed. The railways were being administered, he said, as something apart from the government and towards which the Cabinet had no collective responsibility. Large programmes of extensions had been embarked upon without prior approval of Parliament, and thus the funds of the voters, soon to become direct taxpayers on the recommendation of the Minister of Finance, were being spent before their representatives had considered the proposals for such expenditures. Railway rates had similarly been arbitrarily reduced. Expenditure had taken place beyond that authorised by Parliament. In the circumstances he felt that he had had no option but to resign. Mr J W Sauer, Minister of Railways and Harbours, sought to rebut or excuse aspects of the statement, but if the matter is to be judged on the contents of Hansard, Mr Sauer certainly emerged less than creditably, while Mr Hull displayed a welcome and somewhat rare adherence to principle.

Thus fell to General Smuts the pleasant duty of informing the House that the gloomy predictions of a deficit in the estimates for 1912/13 had proved to be wrong, and there would now be a surplus of £45 000. The road and bridge building programme had been delayed, while customs revenue had increased by £240 000

over the estimates as people bought in advance of expected higher tariffs and as a reflection of general prosperity. The farming community, and in particular that part of it producing wine and grain, was in a healthy state, and imports of agricultural machinery and other requisites had been extensive. Post Office revenue had exceeded the estimates by £156 000, and excise by £80 000. Diamond profits tax had generated £156 000 more than expected while gold profits had remained fairly constant.

For the ensuing year the most significant increase was for defence. There were two reasons for this; firstly, certain police activities had been transferred to the Defence Force; and secondly, there was a need to build up the new Defence Force. Posts and Telegraphs continued to expand, while Public Works continued to fall. In a rapidly expanding economy, roads are perhaps not so vitally necessary (once the basic number has been laid) as are telephones. Grants to the provinces dropped sharply, particularly to the inland provinces. The remaining items in the estimates showed unremarkable changes.

On the revenue side, the loss of the railway subsidy was significant, while increased receipts were expected from those sources which were functions of a buoyant economy: customs, excise, posts and telegraphs. The gold mines were expected to continue their development towards greater yields, while a conservative attitude was taken towards various smaller sources of revenue such as licences, transfer duties and native taxes.

The net result was a deficit of about £1 million. The minister, like his predecessor, warned of the approaching need for income tax by pointing out that it must be clear to members that the process of not imposing additional taxes could not continue indefinitely.

SUMMARY

The four-year period from 1910 to 1913 was one during which the man in the street was free from direct taxation. Only the mines paid direct tax, and the country was able to find its feet and take the first faltering steps towards economic maturity without the psychological disadvantage of direct taxation and without the cumbersome bureaucratic machinery necessary to collect and administer a system of direct universal taxation.

The framers of the South Africa Act never specifically mentioned the possibility that direct taxation would fill the void left by the cessation of the revenue from the railways, but it must surely have occurred to them as a possibility at least. The arguments against only indirect taxation are sufficiently weighty to militate against a continuation of such a system: the authorities are less able to control particular groups in the fiscal area, relying as they must on measures which affect a wider spectrum of persons than might be desirable; and a system which taxes, or is even seen potentially to tax, the wealthy on the same lines as the poor is simply politically suicidal.

Given the huge, impoverished rural White population living in the shadow of the powerful business interests and to a large extent susceptible of unification under an emotional rallying cry to the 'volk', broad taxation measures would be intolerable. Even in a capitalist society, a government does not with impunity take the same proportion of the poor man's bread money as it does of the funds the rich man would otherwise spend on a string of polo ponies. 1914 therefore saw the end of an era of simple, not immediately obvious taxation and presaged the new age of the income tax.

# CHAPTER THREE

## 1914 TO 1916

GENERAL

The three years from 1914 to 1916 may reasonably be viewed as a unit. Historically they include the first general election, the Great War, and gold mining strikes; while in the income tax context the first three Acts were promulgated, each independent of its predecessors. By contrast, the 1917 Act was to be a consolidation measure and would merely be amended each year instead of being replaced by successive Acts.

On the political front, the Rebellion had led to the schism in Afrikaner ranks, and it was a bitter Afrikaner nation whose votes Botha courted in the general election of 1915. The conquest of German South West Africa had added to these factors to alienate those with Afrikaner patriotic feelings. In many areas Botha and Smuts were seen as British Imperialists. Ranged against them were Hertzog, whose narrower Afrikaner vision was spreading into the Transvaal, and Dr D F Malan who was leading the Nationalist movement in the Cape. The election campaign was predictably bitter and especially unpleasant for Botha, whose stature as a folk hero had been affected by his attempts to achieve real national unity and by his acceptance of obligations as the Prime Minister of a member country of the British Empire.

In 1913, the miners of the Witwatersrand had flexed their muscles in the trade unionist arena for the first time since Union. The upheavals, which led to strikes, ranged together the unlikely combination of British skilled artisans, many of them with

Bolshevist tendencies, and Afrikaners who had gravitated to the Rand as a result of the Anglo-Boer War and the subsequent drought and depression.

These strange bedfellows feared the possibility of competition from Black workers, and their resultant alliance had far-reaching effects. Fearing a revolution, Smuts acted with dispatch and deported the ringleaders so quickly that by the time the Mine Workers Union challenged the matter in court, their leaders were already on the high seas. His action outside the law was subsequently ratified by Parliament, but Smuts had given the Afrikaner Nationalist elements another reason for casting him and Botha in the roles of Imperialist supporters of the mining magnates.

The argument that loyalty to Empire was central to Botha's ideal of a greater unity within the country did little to assuage a growing movement towards the exclusivist cry of Hertzog. Moreover, the thesis propounded earlier in this work to explain the alleged control of government by the mining interests in the context of the need to establish the legitimacy of the state cut little ice in the face of Hertzog's oratory. (Subsequent events after 1925 would show that Hertzog courted the mining interests just as strongly and for the same reason - thus giving even more credence to the view of Yudelman (see Chapter 1).) What was more, the ruthlessness of Smuts forged the first links between Nationalists and Labour, a bond which with all its apparent incongruity was to send Smuts into opposition within a decade.

In the event, the South African Party and its independent supporters polled 95 000 votes against the 77 000 for Hertzog and his followers. The government held 59 seats in the new House of Assembly, the Unionists 40, the Nationalists 27 and Labour 4. 40% of the Afrikaners voted against Botha, and he had reluctantly to rely on the support of the Unionists whose policies were distasteful to Botha and anathema to the Nationalists. As explained in the Introduction, this enforced relationship with the Unionists spelt long-term doom for the South African Party.

The estimates of revenue and expenditure for the three years show the effects of the mining troubles and the war.

| Estimates of Revenue (£'000s) | 1914/15 | 1915/16 | 1916/17 |
|---|---|---|---|
| Customs | 4 785 | 4 253 | 4 790 |
| Excise | 627 | 725 | 950 |
| Posts & Telegraphs | 1 867 | 1 620 | 1 791 |
| Mining | 2 357 | 1 846 | 1 924 |
| Licences | 130 | 120 | 111 |
| Stamp duties | 549 | 387 | 452 |
| Transfer, estate and death duties | 165 | 150 | 175 |
| Native taxes, including pass fees | 860 | 860 | 870 |
| Quit rents | 146 | 140 | 145 |
| Rental of government property | 100 | 87 | 105 |
| Interest | 3 680 | 3 759 | 3 840 |
| Departmental receipts | 450 | 400 | 400 |
| Fines and forfeitures | 170 | 170 | 170 |
| Miscellaneous | 153 | 100 | 52 |
| Sales of government property | 50 | 100 | - |
| Forest revenue | - | 42 | 70 |
| Income Tax | 450 | 960 | 1 410 |
| Transfers from sinking funds | | 375 | |
| | 16 539 | 16 094 | 17 255 |

| Estimates of Expenditure (£'000s) | 1914/15 | 1915/16 | 1916/17 |
|---|---|---|---|
| Governor-General and Parliament | 110 | 100 | 105 |
| Prime Minister | 8 | 7 | 8 |
| Agriculture | 566 | 460 | 483 |
| Interior | 750 | 693 | 685 |
| Defence | 1 394 | 1 000 | 1 300 |
| Mines | 202 | 177 | 201 |
| Justice | 2 264 | 2 300 | 2 605 |
| Education | 124 | 112 | 117 |
| Forestry | 129 | 100 | 126 |
| Finance | 5 956 | 6 488 | 7 101 |
| Provinces | 2 320 | 2 120 | 2 349 |
| Lands | 287 | 222 | 275 |
| Native Affairs | 319 | 301 | 302 |
| Public Works | 670 | 593 | 482 |
| Posts and Telegraphs | 1 715 | 1 712 | 1 732 |
| | 16 814 | 16 385 | 17 871 |
| Surplus/(Deficit) | (275) | (291) | (616) |

In each year, the Minister was prepared to live with a small deficit, although this became somewhat high in 1916/17. The overall change in revenue was unremarkable, being of the order of 4,6% over the three-year period. Very few individual components showed any marked change, and on balance the only difference was the substitution of income tax for the reduction in revenue from mining as a result of labour unrest.

On the expenditure side, Finance increased by almost £1,2 million, due mainly to the rising cost of servicing the public debt and to a far lesser extent to the greater cost of manning and running the income tax office. Predictably, the Defence vote was fairly high in 1914 as the nation geared for war; then it reduced in the following year, no doubt while the increases were absorbed and digested, only to rise again in 1916/17 as the war made greater demands upon the public purse. As was the case in the years covered in Chapter 2, agriculture suffered along with public works in favour of the exigencies of wartime expenditure.

Other items of expenditure showed relatively little change, and indeed the estimates of both revenue and expenditure reflect a country recovering from a serious disruption of a major part of its economic fabric, namely the mining industry, while having its general economic development effectively halted by a world war.

BUDGET 1914 - 15

The Budget (1) presented on 24 April 1914 was a landmark in the history of income tax development in South Africa, because it was the first to introduce an Income Tax Act for the newly created Union. The Minister presented estimates which showed a deficit of some £700 000, and informed the House of the proposed means of recouping that shortfall in the following terms (2): 'We have now come to a definite point in our financial history. We have exhausted all the various expedients and devices to which we have resorted since Union for making the revenue and expenditure balance ..... At first we resorted to the railways. The old system of taxation relied very much on the railways.'

Since Union the railways had contributed:

| | |
|---|---|
| £1 520 000 | in 1910/11 |
| £1 159 000 | in 1911/12 |
| £ 500 000 | in 1912/13 |
| Nil | in 1913/14 |

for a grand total of £3 179 000

In terms of the South Africa Act (3), the railways had ceased to be a 'taxing machine'. Indeed, railway rates had decreased to the extent that £1 300 000 less had been recovered than would have been the case had they remained unchanged.

'Nor is that the only change which has taken place. Whilst we have been giving away railway Revenue under the compulsion of the South Africa Act, we have surrendered Revenue also in other directions'. (4) The Minister enumerated the undermentioned reductions in revenue:

| | |
|---|---|
| Cape Income Tax | 280 000 |
| Patent Medicines Tax | 12 000 |
| Natal Poll Tax | 100 000 |
| Reduction of Transfer Duties | 200 000 |
| Surrender of interest | 60 000 |
| | £652 000 |

The total remission of taxation thus amounted to £2 000 000 from both railways and other sources (£1,3 million rates remission plus £,65 million other sources).

Thompson (5) discusses the background to section 129 of the South Africa Act, which provided that the railways be 'administered on business principles, due regard being had to agricultural and industrial development within the Union and the promotion, by means of transport, of the settlement of an agricultural and industrial population in the inland portions of the Union' (6) and points out that as early as the intercolonial conference in 1908, the Transvaal delegates had stated their desire to reduce railway rates. Their reasons were to reduce the cost of living in the Transvaal and to provide lower rates for farm produce in the province.

The policy of reducing the rates, then, seems to have been at least partly motivated by a desire to subsidise the agricultural sector and thus go some way towards alleviating the growing poor white problem reflected in depopulation of the rural areas. The province most concerned with this objective was, of course, the Transvaal, because it had the largest white population and bore the brunt of the flow of Afrikaners to the towns. As Thompson indicates, the Transvalers were by far the most well-organised group at the Union Convention, and 'Transvaal preparations, Transvaal brains, Transvaal teamwork, and Transvaal economic strength prevailed on most issues at the convention'.(7) Small wonder that a measure so eminently desirable to Transvaal interests should have been accepted, particularly in the light of the composition of the government delegates of the Cape and Orange River Colonies; they represented without exception, as did those from the Transvaal, the farming interests of their respective colonies. The lobby for such decisions was therefore strong.

The Minister pointed out (8) that at the same time the Public Debt Commissioners Act provided that any surplus in any year should be used for debt redemption and not be carried forward to the next year. The result was that the public debt was being expunged at an 'extravagent pace' (9) with there being no right to use the surpluses to ease the shortfall in tax revenues.

Returning to the estimated deficit of £700 000, the Minister noted (10) that alterations in the system of tariffs brought about by means of the Customs Tariff Act No. 26 of 1914 would bring in an additional £200 000, leaving £500 000 still in deficit. The problem, then, was how to expunge this?

'We have not had any reason before to go in for any taxing system, but now we are in a position where it is necessary to make new provision. The country is in a sound position, the country is making progress, and it is our duty to make the necessary provision in our financial system in order to make the revenue and expenditure meet. Now we are reaching a very important era in our financial history - now we are coming to new forms of taxation, we have to consider very carefully what is the best policy for this country to pursue. There is no doubt that financial policy is the most important aspect of the State - much more far-reaching is it than the financial policy of any business institution. Now we are changing from one basis to the other, it is necessary for us to consider very carefully what is best in the interests of South Africa in the form of taxation. In the past we have mainly taxed through Customs and Railways. We have mainly taxed on consumption and transportation. Transportation is really a part of consumption, so the policy has been mainly one of taxing consumption through Customs and Railways. It was submitted to the public as being less irksome than the direct form of taxation. But in regard to the railways a great change has been brought about by the South Africa Act, an enormous change, and as regards Customs, the Customs taxation has

its limitations. You can use that source of taxation up to a certain limit, but it is not good policy to use it any further. So far the policy in South Africa has been to have not a protective tariff but a customs tariff. We have taxed people through the Customs, but not from the point of view of erecting a tariff wall round the country, but because we wanted revenue. That has been the policy in the past, and I may at once say it is not the intention of the Government to depart from that sound policy. There is no doubt the circumstances of South Africa are such that a protective wall round the country and a protective tariff as distinct from a revenue tariff would not be in the highest interests of the country.' (11)

The remarks of the Minister on the need to refrain from taxing to any greater extent on the basis of consumption deserve brief comment. It has been argued that indirect taxation is the fairest way to tax people, because they may avoid paying tax merely by refraining from buying goods, or importing, or travelling, or engaging in whatever commercial activity it is that subjects the participant to tax. The counter to this is that people do not always have a choice, and any tax which affects everyone equally must hurt the poor proportionately more than it does the wealthy. In this respect it should be borne in mind that the majority of voters tend to be at the lower end of the economic scale, and this tendency was particularly apparent in South Africa in the years between 1902 and 1914.

Several aspects of Government policy had amongst their aims, reversal of the white denudation of the rural areas: for example, reduction of railway rates. At the same time, the financial needs of the government were more likely to be satisfied by the mines than by agriculture because of the vastly greater incomes generated in the former and its ancillary activities. Both these components of the body economic had therefore to be considered.

An increase in indirect taxation such as customs duties would have resulted in higher costs of importing raw materials and machinery for both mines and industry. The resultant lower profits would have adversely affected the taxes gleaned from the mines and would also have led to general price increases. These would have affected the entire population; the poor whites would have felt the burden at the consumer end of the scale, whereas the industrial sector would have had its potential for expansion inhibited. In one sense this might have had the perceived if not necessarily truly beneficial effect of driving the poor whites back to the land; but in another, it would have choked the very necessary growth of the industrial sector which needed white labour in order to expand. Therefore, at least some flow of labour to the urban areas was necessary.

Direct taxation, on the other hand, if applied skilfully, is far more susceptible of being applied precisely where it is desired, by such methods as rebates, excess profits taxes, progressive

rates and other measures which give the fiscus considerably more flexibility in achieving politically and economically desirable taxing objectives. By introducing a system of direct taxation, the universal impact of indirect taxation could be withheld from the farming community which was struggling anyway, and the golden mining goose could be plucked instead. Of course, the government had to take care not to alienate the voting block representing the mining interests; but the more precise weapon it had via direct taxation allowed it to choose with greater care those feathers it sought from the goose.

The Minister went on to say: (12)
'.....the Government proposed to do the right and wise thing, and to settle the economic policy of this country on a sound footing without delay, and I think the best and fairest thing to do would be to go in for an income tax. Indirect taxation..........bears more heavily on the poor man than on the rich........the sound economic policy is to lay........any fresh burden........on the shoulders best able to carry it, and from the point of view of policy and social justice......we ought to supplement our present Customs policy by an income tax.'

Mr Hull then set out the suggested income tax rates and discussed the proposed unimproved land tax, which would apply to holdings of more than 10 000 morgen or values of more than £10 000. This tax, starting at 1d per £ and increasing to 4d per £ at values of £90 000 and over, would bring in £50 000, leaving £450 000 to be garnered from income tax. The object of this tax was to

discourage the practice of allowing land to lie fallow in anticipation of improvement in value. It was clearly desirable that land be maximally used, both for economic reasons and as an additional means of addressing the poor-white problem. He anticipated the reaction of the public when he remarked: (13)

> 'No doubt these proposals will not be popular in every part of the country, because taxation proposals are never popular, and the form of taxation which is suggested will be very deeply scrutinised in certain quarters.'
>
> 'But', he continued, 'there is no doubt we have come to a point when we must deal with the financial policy wholly and comprehensively, in this country, and I think the proper course is to see the thing through now - to start a taxing machine which will make revenue and expenditure balance, and to lay down a system which will mean a sound policy for the future of the country.'

Sir E H Walton, (14) in a spirited attack on the budget speech, made a prophetic statement about the exemption from tax of incomes up to £1 000 to the effect that one of the very first functions of the Second Union Parliament would be to reduce the exemption. (By 1919 it had disappeared completely).

With reference to the proposed tax on unimproved land, the Land Tax Bill was dropped later in the session. (15)

INCOME TAX ACT 1914

Thus came into being the first Income Tax Act of the Union of South Africa, the Income Tax Act No. 28 of 1914, (16) and from 20 July 1914 the four-year-old country had begun its history of direct income tax legislation. The Act consisted of fifty sections, divided into six chapters.

Chapter I : Administration

The official in charge of the administration of the Act was called the Commissioner of Taxes, who was granted the obviously necessary right to delegate his functions. Section three enshrined a principle without which it is difficult to imagine a piece of legislation of this nature operating effectively : that of secrecy. This requirement was placed upon every person 'appointed or employed in the carrying out of the provisions of this Act,' (17) and could only be breached in performance of duties under the Act or by order of a competent court.

Chapter II : Rate of Income Tax, and Exemptions and Deductions

The Chapter began at sections 4(1) to 4(4) by defining the term 'taxable income' in such a way as to exempt from taxation the first £1 000 of income, leaving a balance, known as the 'taxable amount', to be taxed at the eminently reasonable rate of sixpence plus 1/2000 of a penny per pound up to a total taxable amount of £24 000. A few examples of this method of calculation appear in

Appendix 3. The rate thus began at sixpence per pound, or 2,5%, and increased evenly to a maximum of 7,5% at a taxable amount of £24 000. Taking into account the fact that the first £1 000 was exempt from tax, a taxable income of £2 000 would attract tax at the rate of 1,35%, while a taxable income of £25 000 would be burdened at a real rate of 7,2%. This marked graduation in the rate was a phenomenon destined to remain permanently in South African income tax legislation in one form or another. Given the fact that the White lower income groups made up a large proportion of the voting population, it would be politically naive to expect any other structure.

Section 4(5) likewise introduced a principle which has become enshrined in subsequent legislation, and for good reason. Income was deemed to have accrued to a person even though it had not actually been paid to him but had been otherwise dealt with on his behalf. The consequences of the absence of such a provision are too obvious to discuss.

This section also ensured the inclusion in taxable income of income from two sources which might otherwise have been considered to be outside the Union: income from contracts for sale of goods in the Union, regardless of their destination; and income from the 'carrying on in the Union of any business, trade, profession or occupation', (18) regardless of the residence of the payer or the destination of the payment.

Section 4(6) contained a provision which was destined to change several times even in the short period up to 1925, and to become the source of continued clashes between the South African and Nationalist Parties respectively. In this first reference to farming activities in particular, the values of livestock or produce on hand at both the beginning and end of the year of assessment were not to be brought to account in assessing income, unless the farmer wished otherwise and conveyed this irrevocable wish to the Commissioner in writing. The effect of this provision was that farmers were taxed on the so-called 'cash' basis; that is, they were taxed on the fruits of their labours only when they had turned them into cash or recoverable debts. This concession materially helped the cash flow of a farmer while he was building up his herds or flocks. (Although the phrase 'cash flow' was probably unknown at that time, the principle was certainly familiar.) In the absence of section 4(6) a farmer would be liable for tax on, for example, the value of calves born during a year of assessment even though he had not turned those calves to cash and would consequently need other sources of funds in order to pay the tax. The disadvantage from the point of view of the farmer was that when he finally disposed of the stock he would be taxed on the full proceeds at a relatively high rate. If he chose to bring his stock on hand to account at the beginning and end of every year of assessment, the increases in value of stock would be taxed at a gradual rate each year, and the marginal tax rate would be lower. The farmer would then have to compare the cost of having to find funds for tax on livestock on hand against the lower marginal rate he would enjoy.

Examples of the comparative effects of the two methods appear in Appendix 4.

Section 5 listed the various kinds of income which were exempt from taxation. These included the income of:

- government bodies at all levels down to local authorities;
- building and friendly societies;
- life assurance companies and associations not for gain, except for income from investments;
- ecclesiastical, charitable and educational institutions of a public character;
- income of a non-resident from government stocks : thus came into existence the first incentive via income tax legislation to achieve a benefit not directly related to increased collection of income tax, in this case the inflow of foreign investment funds;
- official income of the Governor-General, his staff, Imperial Government personnel, foreign staff of foreign consulates, and Union Government staff stationed in the United Kingdom;
- dividends paid from income which had already been taxed in the hands of the company concerned;
- income from mining only to the extent that it was taxable under the Mining Taxation Act (see Appendix 2).

Sections 6 to 10 provided for taxation of sales by agents and submarine cable operators. Briefly, tax was levied on a taxable amount deemed to be £5 per £100 of income. Insurance companies were taxed in terms of regulations. In the case of persons or

companies operating both locally and in foreign countries, income was allocated pro rata to assets in use.

Section 11 introduced a principle which has proved to be one of the most contentious in South African income tax legislation : the income of a married woman is deemed to be that of her husband for tax purposes.

Section 12 initiated the principle by which taxpayers acted as unpaid agents for the Commissioner : companies were obliged to remit the tax payable on interest accruing to debenture holders after deducting it from the interest payable.

Section 13 ensured that capitalised profits were subjected to tax.

Section 14 listed allowable deductions from income:

(a) 'losses, outgoings, including interest and expenses actually incurred in the Union by the taxpayer in the production of his taxable income and including also such expenses incurred outside the Union in the production of the taxable income as the Commissioner may allow;'

Subsequent refinements of this section, later known as the 'general deduction formula', will be considered later. As they occurred in its original form, its naivete and vulnerability to interpretation more favourable to the taxpayer than was intended is almost touching; it did not forbid the deduction of capital expenditure, and did not

specify that the expenses incurred outside the Union had also to be incurred by the taxpayer. On such shortcomings do tax consultants thrive.

(b) Expenses incurred on repairs of assets used in the course of trade. For some strange reason, provision was made for the deduction to be the average for the two preceding years, instead of the actual amount incurred during the current year.

(c) A sum deemed reasonable by the Commissioner for wear-and-tear on fixed assets excluding buildings.

Losses in one trade were deductible from the profits of another. Contributions by State employees to public pension or superannuation funds were deductible.

Section 15 indicated those outlays which were not deductible from income. These included private and domestic expenditure, losses recoverable under insurance policies, income carried to reserve fund or otherwise capitalised, and income tax.

Also barred from being deducted were: 'any moneys not wholly or exclusively laid out or expended for the purposes of trade' (14); what is known to economists as 'opportunity cost' or 'opportunity interest'; and any debts owing to the taxpayer, other than those which the Commissioner is satisfied are bad or doubtful.

The portion quoted above and referred to in footnote (19) subsequently became known as the negative aspect of the 'general deduction formula', and was destined to be refined as will be seen in several later Acts. The chapter concluded with section 16, which aimed at defining the word 'trade' as widely as possible, to include 'every profession, trade, employment and calling.'

Chapter III : Returns by Taxpayer and Assessments

This chapter contained the administrative provisions for lodging returns and recording assessments. Of interest is section 20, which provided that if a taxpayer had in the opinion of the Commissioner not been charged with tax when he ought to have been so charged, the Commissioner was empowered to levy the appropriate tax together with a penalty of double tax if the omission had been occasioned by the taxpayer. It is worth noting that this provision was somewhat broadly drawn and required later refinement as will be seen in the discussions on later Acts.

The remaining provisions are of no particular moment within the context of this work.

Chapter IV : Objections and Appeals

The Chapter provided for objections against assessments to be lodged within twenty-one days of their issue, and brought into

existence a Court consisting of three persons to hear appeals against assessments. One of these persons had to be a barrister and another an accountant, each of at least ten years' standing. Appeal from this Court on questions of law was provided for; both the taxpayer and the Commissioner were entitled to initiate such appeals, firstly to the Supreme Court and thence to the Appeal Court.

Chapter V : Payment and Recovery of Tax

The chapter made provision for the administrative machinery for settling tax liability, and established the right of the Commissioner to sue for amounts assessed. It brought the term 'representative taxpayer' into existence, to ensure that there was an identifiable person to whom the Commissioner could turn in the course of recovering taxes from such taxable entities as companies, non-residents, persons under legal disability and receivers.

Chapter VI : General and Supplementary

Section 35 dealt with the appointment of a 'public officer' by every company and the nomination of an address for service of notices or delivery of documents. In effect, the public officer personified the company in the eyes of the Commissioner and the address ensured that the company could be subjected to the operations of legal proceedings.

Whilst Section 35 dealt with companies in particular, Section 36 referred to agents in general and imposed upon this class of person the duties of their principals under the Act.

Section 37 appointed the company as agent for its absent members, and empowered it to deduct a proportionate share of its income tax liability from dividends paid to shareholders. The section was somewhat clumsily worded as regards exceptions to this provision, and would be amended one year later. (Page 80 of this work).

An important principle came into being in Section 39, namely that the burden of proof in the case of any dispute between taxpayer and Commissioner lay squarely with the taxpayer. The future would provide numerous cases where taxpayers lost their appeals through failure to comply with this principle.

Section 40 imposed the duty on persons so required to submit to the Commissioner details of payments made to employees and other persons.

Section 41 placed the liability for taxes payable upon trustees and executors in appropriate circumstances.

Section 42 provided for refunds of taxes overpaid.

Section 43 prescribed the penalties for false statements or evasion, which amounted to fines of up to £100 or imprisonment

for up to 12 months, plus double tax in cases of evasion.

Subsequent sections provided : penalties for obstructing officers and failure to furnish returns; authentication and due service of documents; evidence as to assessments; and empowered the Governor-General to make certain regulations.

The Act concluded with a list of terms used, together with their interpretation within the context of the Act.

Income Tax Cases

Despite the fact that the 1914 Act was an entirely new piece of legislation, and moreover affected virtually every member of the white population in a personal way which would naturally tend to encourage the search for loopholes, no income tax cases were reported immediately on the basis of the provisions of the Act. This was so even in the case of section 14(a), the looseness of whose wording would surely have been pounced upon by the sophisticated income tax advisors of later eras.

However, three cases were heard in later years on the basis of the 1914 Act; one in respect of an appeal against a decision of the Commissioner for the 1915 year of assessment and two for the 1916 year. These cases will be discussed in the chapters dealing with those respective years.

BUDGET 1915 - 16

The Budget Speech of 1915 (20) was delivered on 18 March of that year by the Prime Minister, General J C Smuts. He informed the House that his successor as Minister of Finance, Sir D de Villiers Graaff, had only recently joined the Government and was not yet sufficiently familiar with matters to present the Budget.

The Minister pointed out that there had been a deficit amounting to £ 2 064 000 as a result of the war, which had been declared after Parliament had prorogued. The chief contributors to the Treasury had been customs, the diamond tax and the gold tax. Income tax had produced what had been expected plus £30 000 still to come. It had been decided that the deficit would be met out of loan account.

There was an estimated deficit of £2 702 000 for the 1915/16 fiscal year, and this would be met by taxation, sinking fund balances, and revenue from leases of bewaarplaatsen. (21)

Regarding taxation, three sources of revenue would be called upon to make increased contributions.

Customs duties would be increased on certain necessities and there would be in addition an increase in the general ad valorem rate.

Income tax would be imposed on all incomes greater than £300 and the minimum rate doubled to 1/- per £, rising to a maximum of 2/-. In other words, the minimum rate was increased from 2,5% to 5% and the maximum rate from 7,5% to 10%. To make the burden even more acute, the abatement of £1 000 provided for in the 1914 Act was reduced by £700. The prophecy of Sir E H Walton in 1914 was being fulfilled a mere year after he had uttered it. (22)

The effects of these changes are shown in the examples in Appendix 5. Their result would be to gather an estimated additional £980 000 into the exchequer. The Minister stated that the gold mining industry had remained prosperous throughout years of depression and was capable of contributing to the financial needs of the country. He proposed, therefore, to impose a special war contribution of £500 000 on the industry.

It took therefore just one year before outside events, in this case the advent of the First World War, had a direct effect on income tax legislation. Every 1914 taxpayer would be affected to a greater extent, and a large group of persons who had paid no tax in 1914 because their income had fallen between £300 and £1 000 would now fall into the net of the Commissioner of Taxes.

The Income Tax Act No. 23 of 1915 amended the 1914 definition of 'taxable income' so as to give effect to the reduction of £700 in the amount of income not subjected to taxation. The Act, at section 1, went further and precluded this concession entirely in

respect of taxable incomes in excess of £24 300. As against this, the section introduced abatements related to the personal circumstances of the taxpayer; this principle has since remained in income tax legislation, either in the form of abatements or of rebates. The abatements provided for were as follows:

- amounts of up to £25 paid in premiums in respect of life, accident or sickness insurance policies on the lives of the taxpayer or his wife;
- amounts of up to £10 paid to any friendly or benefit society;
- amounts received from such societies;
- £20 for each child of the taxpayer alive and under sixteen years old on the first day of the fiscal year. 'Child' included 'stepchild' and still does in tax legislation.

Apart from recognising that taxpayers inevitably incur expenditure related to their families, these concessions constituted the first attempt of the legislature to encourage taxpayers to provide for their own fates, rather than to become burdens of the State in their old age. The condition that a child had to be alive on the first day of the year sounds illogical when it is considered that the abatement was granted in respect of expenditure on the child for the year. The age limit of 16 no doubt reflected the social fact that far fewer children matriculated in 1915 than in later years. Both these conditions were destined to have relatively short lives.

Section 2 sustained the provisions of the 1914 Act to the extent that the 1915 Act did not change them. It was thus necessary for taxpayers to read both Acts in order to establish the current law: a clumsy procedure indeed.

Several amendments occurred to the principal Act:

- Section 5 was extended by the addition of another category of exempt income: mining profits already taxable under the Mining Taxation Act No. 6 of 1910, or exempt under the 1908 Transvaal act governing mining. The 1910 Act imposed taxes on mining profits on the following basis:
  Gold and diamond mines : 10% of profits
  Other minerals : on a graduated scale beginning at two and one-half per cent where profits did not exceed 5% of revenue and increasing by one-tenth per cent per 1% of profit. (See Appendix 2).
  Without this exemption, mining companies would have been liable for taxation under both Acts.
- Section 12 was corrected to eliminate an oversight in its original form, which had obliged the company paying interest on debentures to deduct tax from the interest and remit it to the Commissioner. However, in some cases the interest was not deductible by the company as an expense, and this resulted in double taxation - in the hands of the company in that the interest was not deductible, and in the hands of the taxpayer on receipt.

- It took only a short time for one glaring shortcoming in section 14 to be eliminated. The 1915 Act ensured that only losses and outgoings incurred outside the Union by the taxpayer were deductible, thus closing the loophole left in the 1914 Act.
- Section 15 was amended to eliminate the 'value' of repairs as a non-deductible expense, leaving the word 'cost' to convey the meaning.
- Section 29 was amended in a minor fashion regarding the method of payment.
- Section 37 had, as was mentioned on page 74 of this work, been somewhat clumsily worded and was improved upon in 1915. The new wording stated that where there was an express stipulation in a contract debarring a company from doing so, it was not entitled to deduct from dividends paid a pro rata share of its tax liability. This, of course, had no effect on the Commissioner, but merely allowed the company and its taxpayers to decide who should bear the tax payable by the company. One might well rather say that the provision allowed the shareholders to decide how they would settle the tax liability of the company, because whether they paid it directly by deduction from their dividends or indirectly by the company's being able to pay them a smaller dividend after tax, the ultimate liability was theirs as owners of the company.
- The remaining amendments were of no moment to this work.

The contribution of £500 000 by the mining industry was garnered by means of the Mining Taxation Amendment Act No. 24 of 1915, which provided in broad terms that all persons engaged in mining activities would pay a levy of the same proportion of £500 000 as their respective mining profits bore to the total profits from mining.

Income Tax Cases

One reported case based on the Income Tax Act No 24 of 1914 was heard before the Appellate Division in respect of an assessment for the 1915 tax year. This was: Commissioner of Taxes v William Dunn & Co., Limited (23) and was heard before Messrs Justices Innes C J, Solomon J A, C G Maasdorp J A, De Villiers A J A and Juta A J A on 2 and 5 December 1918.

The case was based on the interpretation of sections 4 and 49 of the 1914 Act and resulted from verdicts against the taxpayer in the Special Court and in its favour in the Cape Division of the Supreme Court.

The facts of the case were as follows:
The respondent company was both registered and in business in England. It had partnership agreements with three firms in business in the Union and each agreement provided that the respondent would buy goods overseas on behalf of the South

African firm concerned. The latter in each case would furnish the respondent with lists of goods required, which would then purchase them on its own account and ship them to the Union firm, debiting it with costs and commission. The respondent charged 5% interest on balances outstanding in its accounts with its South African partners.

During the year in question, the respondent had debited its Union counterparts with interest totalling £14 658 and it was this sum which the Commissioner sought to subject to taxation in South Africa.

Counsel for the Commissioner averred that the definition of 'income' in section 49 was relevant, stating as it did that income 'means any gains or profits ...... from any source within the Union, and shall include ...... interest.' Consequently the respondent was taxable in terms of section 4(2), which defined 'taxable income' as : '......income .......from any source whatever in the Union.....' There was no reference as to carrying on business. The test to be applied was where the capital had been employed which produced the profit at issue. This was the same as applying the test: 'where was the business carried on?', which was treated as a question of fact. The sending of goods to the Union was no different from remittance of funds: in essence, loans had taken place and had generated interest whose source was South Africa. The place of contract was irrelevant.

Counsel for the respondent argued that the relationship was one of principal and agent, and the whole transaction was performed in England with English capital under an English contract in the course of an English business. There was no loan and the mere existence of interest did not make it so. When an article was sold on credit, consequent interest was not derived from a loan. If, however, it was found that there was indeed a loan in each case, the interest would still not be taxable because it had been made in England as a banking ancillary to an English business. The respondent neither exercised a trade in the Union, nor had it invested money in this country.

The Court agreed that the test to be applied was where the capital had been employed which produced the profits at issue. In so doing, it established a principle which our courts still apply. It found, however, that the facts indicated a relationship of principal and agent. The respondent was using its capital in its English business and there was no question of the transactions being in the nature of loans. Counsel for the Commissioner had not contended that the mere residence of the debtor in South Africa affected the matter, and he was correct in so refraining. Judgment thus went in favour of the respondent with costs.

This case therefore enunciated two important principles of taxation, namely:

(1) the source of income depends on where the capital was employed which produced the income

(2) the residence of a debtor is of no importance in deciding on the source of interest owing by him.

The importance of this decision may clearly be inferred from the fact that the case is still used as a major reference in discussing the question of the taxability of interest by one of the leading authorities on taxation in South Africa. (24)

BUDGET 1916 - 17

Mr H Burton, having succeeded Sir D P de Villiers Graaff as Minister of Finance in February of that year, presented his maiden Budget Speech on 31 March 1916.(25) In reviewing the position for the past year, the Minister announced that the revised estimates showed a surplus of £363 000, largely as a result of a great improvement in Customs revenue. It had been estimated that revenue from this source would total £4 253 000; in fact, the estimates had now been revised to £4 700 000. The country was prosperous, and there was plenty of money to spend on luxuries. (26)

The estimates for the 1916/17 year showed a deficit of £1 422 000 after revenue of £16 333 000 and expenditure of £17 758 000. The Minister therefore proposed to reimpose increased Customs duties, which would produce £1 000 000, and the special war levy on gold mines, which would generate £320 000. This, together with the

£433 000 Government share from the bewaarplaatsen, would adequately cover the deficit.

So far as income taxes were concerned, Mr Burton stated that he intended to retain the income tax as at present, but to change the insurance abatement so as to make it available on a reduced basis up to £600.

In contrast to this concession, he recognised that businesses were flourishing as a result of the war and he therefore intended to impose a super tax on war profits on income in excess of £2 500.

Although not yet directly affecting income tax legislation, a drought (27) had begun to cause difficulty in the country and its effect would be felt in tax laws within the next few years.

INCOME TAX ACT 1916

The Income Tax Act No 35 of 1916 (28) further refined the tax legislation of the Union, no doubt as the Revenue authorities and taxpayers alike discovered loopholes in drafting.

Section 1(2), which defined 'taxable income' had a proviso added to it in the 1916 Act to the effect that income from 'a native territory bordering on the Union' (29) accruing to a resident of the Union would be deemed to be taxable income from a source within the Union.

Section 1(3) also had a proviso added to it, to the effect that where taxable income exceeded £500, the personal deductions (as the abatements were called at that time) would be deductible, but reduced by the extent to which taxable income was greater than the amount of £500. Examples of the effect of this proviso appear in Appendix 6. Section 1(4) was amended to refer to normal tax; this was made necessary by the advent of supertax. Section 2 provided that the amendments to the provisions of the 1914 Act as amended in 1915 specified in the Schedule to the 1916 Act were of force and effect. These amendments comprised the following:

- Section 6 - Goods sold by agent on behalf of non-resident principal. A proviso was added to the effect that goods were deemed to have been sold in the Union on account of a non-resident, if any resident received a commission on sale or a salary for obtaining orders or for influencing the sale of goods.

  It would appear from this amendment that there had been difficulty, or problems had been foreseen, in defining the process of 'sale or disposal of goods'. Clearly the agent would wish this to be interpreted narrowly, so that principal-agent relationships could be drawn up in order to fall outside the definition. The amendment ensured that this would be as difficult to achieve as possible.
- Section 12 - Company deemed to be agent for debenture holder. The proviso added in 1915, to the effect that interest received which had not been deductible from income in the

hands of the payer would not be subject to income tax in the hands of the recipient, was amended, by substitution of the word 'normal' for the word 'income' as describing 'tax'. This became necessary because of the introduction of supertax in the 1916 Act. It will be seen that such interest was not exempt from supertax.

- Section 13 - What was required to be specified in the returns of certain taxpayers. The amendment merely improved on some clumsy wording.
- Section 15 - Expenses not deductible.
  The section was changed to prohibit the deduction of all taxation levied under the Act. The amendment became necessary because of the imposition of supertax.

Chapter II of the Act introduced the supertax to which the Minister had referred in the Budget Speech. The tax was applicable to individuals whose income from Union sources exceeded £2 500. It is interesting to speculate why companies were not subjected to the tax; perhaps the influence of the mining and commercial interests was apparent here (see Introduction, where the power source of the South African Party is discussed).

Section 4(2) of the Act provided for the calculation of 'supertaxable income' to be the average of the supertaxable incomes of the two years ended 30 June 1916. If this average exceeded £2 500, the taxpayer was liable to supertax on the excess. Consequently, if a taxpayer had begun to enjoy 'super income' only from 1915, his lower income in the first year of war

might save him from supertax liability. The concession was balanced against the fact that in calculating 'supertaxable income' the taxpayer had to bring to account four categories of normally exempt income, namely:

- dividends from any company which had paid Union income tax on the profits from which the dividends were paid;
- dividends from any company taxable under the Mining Taxation Act No. 6 of 1910;
- dividends from any company part or all of whose profits were derived from dividends falling into the two categories mentioned previously;
- profits or income taxable under the Mining Taxation Act No. 6 of 1910.

This provision thus meant that income which was otherwise free of income tax because it had already been subjected elsewhere to tax of some sort or other had now to be subjected to supertax. It would appear that supertax could have been avoided by non-payment of dividends; that is, by simply allowing profits to accumulate in the books of companies in the hope that the supertax would in time disappear. (Companies, of course, were not subject to supertax.) However, this possibility was countered in section 6, which provided in surprisingly vague terms that if the Commissioner was of the opinion that a company permitted profits to accumulate beyond 'the reasonable needs of the business', there would be included in the supertaxable income of each member a pro rata share of undistributed profits.

In addition, taxpayers resident in the Union were obliged to include income from 'native territories bordering on the Union' in their calculations of supertaxable income.

Section 4(3) provided an initial deduction similar to the £300 deductible from normal taxable income: the deduction was £2 500 reduced by 10/- for every pound of supertaxable income in excess of £2 500. Clearly this deduction would fall away completely when supertaxable income reached £7 500. Section 4(4) stated the rates of supertax as follows: up to £48 000 the rate was 1/- and 1/2000d per £ ; thereafter it was 3/- in the £.

Section 5 exempted non-residents from the supertax, no doubt to avoid discouraging foreign investment, provided the shares concerned were not registered in the Union.

Section 7 brought into existence another requirement for taxpayers to act as agents for the Commissioner: companies were obliged to furnish returns of dividends and debenture interest paid, indicating to whom they were paid.

Section 8 required banks to furnish similar information in respect of payments against bearer warrants.

Finally, section 9 obliged the taxpayer himself to make a return.

With reasonably simple provisions, therefore, the Act set about taxing those profits which accrued as a result of the war in

order to meet the costs of that war.

Examples of the effect of the supertax appear in Appendix 7.

INCOME TAX CASES

1. On 25 and 26 April 1917, and again on 3 October 1917, the case of Robinson v Commissioner of Taxes (30) came before the Transvaal Provincial Division of the Supreme Court on the appeal of the taxpayer from a decision in the Income Tax Special Court.
   The case concerned the residence of the taxpayer, who claimed exemption from tax on his large holdings in Cape Government stocks. The grounds for his argument were that, in terms of section 5(f) of the Income Tax Act No. 28 of 1914, (31) the income was exempt because he was a non-resident. Consequently, the case revolved around the question of the residence of the taxpayer.

   The facts of the case were that the taxpayer had lived in South Africa from birth in 1840 until 1899 when, coinciding with the outbreak of the South African war, he moved to England. His substantial interests in the country had necessitated his temporary return on several occasions since 1899 at times of political or financial stress. This he had done in February 1915, no doubt as a result of the political turmoil attending the entry of the Union into the first World War on the side of the Allies and the subsequent

Rebellion.

For the first two years of his stay, when not travelling extensively through the country, he had lived with his daughter in a rented house in Muizenberg. Then he had moved into his own home at Wynberg, which he had bought in 1891 and which had been for sale for some years and had stood vacant since 1907. It was clear that even in 1916 the house was still for sale.

He maintained a rented home in Park Lane, London, which contained his art treasures, and which was considered to be the family home. He intended to return to England as soon as his business interests allowed.

The question at issue was whether the appellant had a second and subsidiary residence in South Africa. The Court was of the opinion that any 'merely casual and temporary abode' (32) did not constitute residence, but that the circumstances had to be considered in each case. English law provided a specific time, namely six months, after which a person was deemed to be in residence, but South African law had no such guideline.

The large business interests of the appellant did not, as suggested by the Government, strengthen the claim that he was a resident, nor did his frequent business visits to these shores.

Despite his avowed intention of returning to England as soon as he could, the fact was that he had been in 'bodily presence' (33) in the Union for 2 1/2 years and moreover had

established a residence here. One of the meanings of residence was that it was the home or one of the homes of a man for the time being. Physical presence for a long period would constitute residence; its entire absence would constitute the opposite. If a man set up a residence in a country and lived there at intervals he was a resident.
If the intention was to prolong a visit beyond 'casual visitation (whatever that might be)'(34), the visit became residence. In the case of the taxpayer, he intended to remain in the Union so long as his business required it. Whatever his anticipation, the fact was that he had been in the country for 2 1/2 years and was still present. There was no legal difference between a decision to live here for a given period, or to do so until the happening of a certain event. The fact was that 2 1/2 years was too long a period to call temporary residence.

This case thus established several principles of residence, namely:

(1) Residence may be inferred from the establishment of a residence in a country which the owner used at intervals.
(2) Casual and temporary abode did not constitute residence.
(3) The existence of large business interests and frequent visits did not of themselves constitute residence.
(4) Physical presence for a long period would of itself constitute residence.

This case continues to be quoted as a reference in discussions on the meaning of 'residence' for the purposes of the Act. (35)

2. On 25 November 1918 and again on 5 December of that year, the Appellate Division heard the case of Commissioner of Taxes v Booysens Estates Ltd, (36) which turned on section 49 of the 1914 Act and revolved around the question as to whether certain receipts were of an income or a capital nature.
   The company had won its case in the Special Court and again on Appeal before the Transvaal Supreme Court. The Commissioner, not yet willing to admit defeat, proceeded to the Appeal Court.
   The Company had been formed in 1899 and its objects were:
   (a) to acquire certain mining claims;
   (b) to acquire appropriate mining assets;
   (c) to mine for gold and other minerals;
   (d) to sell or otherwise dispose of claims and other assets;
   (e) to sell the undertaking.

   In accordance with the articles, the company acquired 239 claims in exchange for 31 000 shares, and then issued 2 000 shares to the vendors for £2 000 to serve as working capital. Another 19 claims were later bought for £30 000, and 2 698 further shares were issued.
   In 1906 the company sold 33 claims of lesser value for £2 050 each. In 1915 it sold the balance to Robinson Deep Limited for 441 000 shares of £1 each, which were distributed to the

vendors on the immediately subsequent liquidation of Booysens Estates Ltd.

The company had never mined the claims, not having enough funds, and in any case the area of the claims was too small. The new company was in a better position because it owned further adjacent claims which made development payable.

The Commissioner sought to tax Booysens Estates Ltd on the difference of £364 402 between the £441 000 value of shares received and the £78 598 present value of the claims sold.

The company objected, was rebuffed and went to the Special Court on the grounds that:

(a) the profit was capital in nature, because its main object was mining for gold and its other objects (particularly (d)) were ancillary to that object, and;
(b) the basis of calculation of the profit had been wrong in principle.

The Commissioner admitted that 'the primary object of the company was that of a gold mining company, its other objects being merely ancillary thereto'. (37)
On this basis he lost in the Special Court and in the Supreme Court, where it was held that there had been no evidence that the company had ever carried on the business of buying and selling mining rights. Consequently, the sale represented a

realisation of capital assets. On appeal, the Commissioner tried to have his admission as to the primary object set aside, and accepted that a change in the calculation of the profit would be needed. The Appellate Division upheld the decision of the lower courts.

The judges in both Supreme and Appeal Courts made several important comments which are still quoted:

Wessels J in the Supreme Court stated: 'Income is, as a rule, revenue derived from capital productively employed. It is true that there is no definite test that can always be applied in order to determine whether a gain or profit is income or not, but it may safely be asserted that the revenue or profit which is derived from a thing without its changing owners is rather to be considered as income than as capital. On the other hand the profit which is derived from a thing when it changes owners is rather of the nature of capital than of income.' (38) He then made the important point that, merely because a company is formed to do business, it does not follow that every transaction entered into by that company is on income account, (39) and followed this with the principle that 'every company that invests in land in order to mine it, must take to itself the right of selling its land in case of need'. (40) This principle was destined to be repeatedly argued in our courts.

The Commissioner had made the point that the Company had never had sufficient capital to mine the property and was therefore speculating in land. The judge rebutted this assertion, but only in the case of a mining company, which sometimes had to wait for shafts on adjoining properties to reach the required level and then to use them. The argument was, in fact, a good one. Gregorowski J, however, compared this case with the English case of California Copper Syndicate v Inland Revenue (41 SLR 691) where only two years elapsed between incorporation and sale of claims, and the present matter with its time span of 17 years and distinguished the cases on these grounds.

In the Appeal Court, Innes C J made the point that: 'in a transaction of this nature, therefore, where profit has undoubtedly resulted from the disposal of the company's assets, we have to enquire whether profit has resulted from the productive use of capital employed to earn it, or whether it has resulted from the realisation of capital at enhanced value'. (41) In the former instance, the profit would be taxable and in the latter not so.

This case was destined to be the forerunner of many cases dealing with the question of income versus capital, the most common grounds by far on which income tax cases are argued. The principles laid down in this case may be summarised as follows:

(1) Income is revenue derived from capital productively employed.

(2) Merely because a company is formed to do business, it does not follow that its every transaction is on income account.

(3) Ancillary rights of a company do not necessarily render the execution of those rights as being on income account.

(4) Whereas lack of capital necessary to carry out the main object weighs against the company, every situation has to be considered on its own facts.

(5) Realisation of productive capital occurs on capital account.

(6) Revenue derived from an asset without its changing owners is rather to be considered as income than as capital.

3. The case of Rex v Bernstein was heard before the Cape Provincial Division of the Supreme Court on 3 May 1920, and referred to the tax years 1916, 1917 and 1918. It constituted an appeal from a conviction in a magistrate's court and added nothing material to the body of income tax law.

# CHAPTER FOUR

## 1917 TO 1925

GENERAL

For three years the legislature had treated each Income Tax Act as a unit separate and distinct from its predecessor. Given the novelty of the concept in the Union and the uncertainty which must surround the ultimate nature of so completely new a piece of legislation, this was understandable. However, this somewhat ad hoc approach had to stop and be replaced by a more permanent approach, particularly in view of the fact that a body of case law would inevitably begin to accumulate. A sense of continuity was therefore both necessary and desirable.

The 1917 Income Tax Act was prepared with the experience of three years as a guide, and served as the basic Act for some eight years. The estimates of revenue and expenditure for the period up to 1925 were as follows:

| Estimates of Revenue (£'000s) | 1917/18 | 1918/19 | 1919/20 | 1920/21 | 1921/22 | 1922/23 | 1923/24 | 1924/25 | 1925/26 |
|---|---|---|---|---|---|---|---|---|---|
| Customs | 4 278 | 4 308 | 5 130 | 6 900 | 6 000 | 5 660 | 6 244 | 7 080 | 8 028 |
| Excise | 950 | 1 150 | 1 483 | 1 680 | 1 400 | 1 919 | 2 089 | 1 936 | 1 686 |
| Posts & Telegraphs | 1 820 | 1 926 | 2 070 | 3 000 | 2 950 | 3 000 | 3 096 | 3 359 | 3 361 |
| Mining | 2 682 | 990 | 1 483 | 2 328 | 710 | 620 | 1 460 | 1 310 | 1 565 |
| Licences | 115 | 114 | 110 | 125 | 130 | 135 | 145 | 120 | 120 |
| Stamp duties | 520 | 570 | 670 | 900 | 900 | 950 | 800 | 820 | 820 |
| Transfer, estate and death duties | 180 | 200 | 240 | 300 | 300 | 450 | 450 | 500 | 525 |
| Native taxes, including pass fees | 880 | 880 | 870 | 870 | 890 | 875 | 855 | 885 | 955 |
| Quit rents | 150 | 150 | 150 | 150 | 150 | 160 | 160 | 160 | 160 |
| Rental of government property | 105 | 110 | 119 | 250 | 230 | 215 | 189 | 183 | 200 |
| Interest | 4 075 | 4 078 | 4 277 | 4 603 | 4 825 | 813 | 952 | 1 086 | 1 145 |
| Departmental receipts | 400 | 450 | 510 | 700 | 750 | 750 | 750 | 625 | 625 |
| Fines and forfeitures | 190 | 200 | 200 | 200 | 200 | 300 | 240 | 240 | 250 |
| Miscellaneous | 55 | 70 | 97 | 100 | 100 | 115 | 125 | 208 | 200 |
| Gold mining leases | | | | | | 475 | 525 | | |
| Forest revenue | 70 | 60 | 109 | 75 | 110 | 85 | 75 | 80 | 80 |
| Income tax | 1 750 | 4 000 | 4 100 | 4 850 | 4 870 | 6 947 | 5 615 | 5 637 | 6 367 |
| Excess profits duty | | | 1 350 | 1 350 | 1 300 | 400 | 100 | 5 | 5 |
| Sundries taken to Loan a/c | | | | | | 165 | | | |
| | 18 220 | 19 256 | 22 968 | 28 381 | 25 815 | 24 034 | 23 870 | 24 234 | 26 092 |

| Estimates of Expenditure (£'000s) | 1917/18 | 1918/19 | 1919/20 | 1920/21 | 1921/22 | 1922/23 | 1923/24 | 1924/25 | 1925/26 |
|---|---|---|---|---|---|---|---|---|---|
| Governor-General and Parliament | 107 | 110 | 115 | 156 | 147 | 144 | 145 | 149 | 159 |
| Prime Minister | 8 | 8 | 8 | 30 | 72 | 34 | 38 | 40 | 42 |
| Agriculture | 500 | 590 | 698 | 1 047 | 1 139 | 1 010 | 1 098 | 1 265 | 1 335 |
| Interior | 819 | 874 | 1 030 | 1 085 | 1 242 | 1 120 | 1 072 | 912 | 955 |
| Defence | 1 300 | 1 300 | 1 575 | 1 267 | 1 340 | 916 | 935 | 982 | 911 |
| Mines | 201 | 221 | 292 | 356 | 633 | 806 | 632 | 323 | 317 |
| Justice | 2 632 | 2 774 | 3 210 | 5 104 | 4 661 | 4 335 | 4 200 | 4 170 | 4 192 |
| Education | 120 | 180 | 251 | 373 | 380 | 442 | 494 | 530 | 762 |
| Forestry | 131 | 144 | 163 | 209 | 207 | 161 | 168 | 168 | 172 |
| Finance | 7 375 | 7 794 | 8 616 | 10 400 | 10 441 | 11 045 | 11 158 | 6 710 | 7 347 |
| Provinces | 2 462 | 2 890 | 3 521 | 4 291 | 4 643 | 4 216 | 4 322 | 4 441 | 5 391 |
| Lands | 254 | 295 | 487 | 206 | 221 | 229 | 229 | 237 | 309 |
| Native Affairs | 294 | 302 | 350 | 444 | 435 | 433 | 376 | 332 | 328 |
| Public Works | 447 | 515 | 614 | 697 | 784 | 811 | 801 | 769 | 781 |
| Posts and Telegraphs | 1 773 | 1 861 | 2 145 | 2 787 | 2 924 | 2 863 | 2 829 | 2 675 | 2 772 |
| Public Health | | | | 260 | 275 | 254 | 259 | 294 | 411 |
| Labour | | | | | | | | 349 | 363 |
| Industrial Disturbances | | | | | | 225 | | | |
| | 18 423 | 19 858 | 23 075 | 28 712 | 29 544 | 29 044 | 28 756 | 24 346 | 26 547 |
| Surplus/(Deficit) | (203) | (602) | (107) | (331) | (3 729) | (5 010) | (4 886) | (112) | (455) |

During this important nine-year period the level of expenditure increased by 68,6%. A considerable proportion of this may be attributed to the rampant inflation experienced at this time throughout the world but, even allowing for this factor, it is clear that the South African state expenditure was growing as the nation evolved and developed, while revenue was keeping pace, with increasing help from income taxes.

Customs and excise, excellent indicators of economic growth, grew steadily and at similar rates. The exception was in 1922/3, when customs revenue fell somewhat as fewer goods and less machinery in particular were imported during the mining strike.

Understandably, mining revenue was the most erratic and indeed comparatively poorest source of revenue during the period. Only once, in 1917/18, did revenue rise to the level it had achieved in 1914 before the earlier troubles. It then plunged in 1918 to one third of the 1917 level, before improving markedly over the next two years, only to be devastated to a mere £710 000 in 1921 and £690 000 in 1922, not much above 25% of the 1917 figure. By 1925 revenue had inched its way to £1 565 000; better, but still only 58% of the 1917 amount. In short, in the twelve years between 1914 and 1925, and in the face of a war and raging inflation, revenue from mines fell to a truly alarming degree.

The most dramatic increase occurred with income tax, which increased from £1 750 000 in 1917/18 to £6 367 000 in 1925/26. As will be seen in this chapter, this increase resulted from

increases in the rates and types of tax as well as from the obvious effect of inflation on incomes.

It is noticeable that, virtually without exception, all sources of revenue leapt ahead in 1920/21 as the post-war inflation took hold. Revenue then fell slightly, as a result of the economic depression but began to climb again after 1923/24. However, by 1925/26 it had still not reached the heights of 1920/21. It is interesting, also, that during this period the revenue from mining was significant only in 1920/21 and made little contribution to the increasing revenues from 1923/24 onwards. The compensating amounts came from income tax and customs, both of which increased by similar proportions. It may justifiably be said, then, that the mining troubles had a direct effect on everyman by the action of the government in compensating for its loss of revenue through increased income tax.

The expenditure side reflects a similar pattern with a substantial increase in 1920/21. One interesting statistic is that expenditure on finance increased less than in proportion to the revenue from income tax, whose collections fell under the control of the Finance Vote. The very marked increase in the Prime Minister's Vote was attributable to the fact that amounts varying between £20 000 and £27 000 were contributed annually to the League of Nations and charged under this Vote. The contribution for 1921/22 was £62 000. The exceptionally large increases under Mining in the years 1921/22 to 1923/24 resulted from special unemployment expenditure of between £250 000 and

£450 000 per year. There was also, as may be seen, a sum of £225 000 voted in respect of industrial disturbances in 1922/23.

In other respects the expenditure followed the general pattern established in earlier years, and calls for no particular further comment.

BUDGET 1917 - 18

The Minister of Finance, Mr H Burton, presented his second Budget on 30 March 1917,(1) and in his review of the current year was able to announce that the bewaarplaatsen moneys had not been needed. This was so despite a reduction in customs revenues during the last six months of the year as a result of the activities of enemy submarines. He announced that the effect that the war had had on the economy had been offset by an increase of £488 000 over the estimated revenue from the diamond tax.

Turning to the coming year, the Minister pointed out that the country was in a state of expansion, with much money being spent on imports. Except for the Gold Mining Profits Tax, practically all sources of revenue showed a tendency to expand. However, estimates of revenue and expenditure were difficult to make, owing to various uncertainties such as sizes of imports and exports in the face of the submarine campaign. After several provisions had been made for contingencies, the estimated shortfall was £500 000.

A change in the method of taxing diamond profits to a flat export duty of 5% would cover £170 000 of this deficit. Up to this time, diamonds had, of course, been taxed on the basis of 10% of profits in terms of the Mining Taxation Act No. 6 of 1910.

Mr Burton then turned to what he termed 'the most important feature of the Budget'.(2) The Government intended to replace the different methods of taxing gold, diamonds, other mines and individuals with a 'better-balanced scheme......on a co-ordinate basis'. (3)

Normal tax would be levied at 5% on the taxable amount (excluding dividends) for companies, 'taxable amount' being the difference between taxable income and relevant abatements. There would be a progressive rate for individuals, which would mean that the rate of tax would rise progressively as taxable income increased. Supertax would remain unchanged, but a dividend tax for companies would be introduced, which would impose levies of 10% on dividends paid by gold mining companies, seven and one-half per cent on those of diamond mining companies, and 5% on those of other companies.

Increases from these sources would leave some £250 000 still unaccounted for. Increasing the rate of supertax was not favoured, because of the difficulty in South Africa of deciding the extent of war profits. Consequently a new tax would be introduced, to be called 'Excess Profits Tax'. This would be imposed on excess profits earned after 1 July 1916 and continue

until six months after the end of the war. Taxpayers would enjoy a £500 abatement on a diminishing scale.

In an explanatory memorandum which appeared in the Cape Times of 21 April 1917, six relevant points were made for information of taxpayers:

1. The imposition of tax on companies at a flat rate on the taxable amount would enable them to recover the tax from shareholders and debenture holders. These investors had up to that time escaped taxation on their dividends and interest respectively to the extent that they held 'bearer' scrip or were non-residents.
2. The division between tax on profits and tax on dividends would enable developing companies (which would presumably pay low or no dividends) to develop at a lower tax level: profits tax was either less than or equal to dividends tax.
3. It would henceforth be possible to carry forward losses incurred in any particular tax year. Under the previous system of annual Acts, this had not been possible. Their replacement with a permanent Act would remedy this defect.
4. Supertax would in future be levied on actual income for the period and not on a two-year average. The latter method was particularly cumbersome, as seen in Appendix 7.
5. Excess profits duty (not 'tax' as it had been called in the Budget speech) was deductible from income in the calculation of taxable income.

6. The dividend tax was payable by companies, which were in turn able to deduct it from their shareholders.

After three successive Income Tax Acts, each independent of its predecessors and valid for only one year, the Revenue authorities had clearly and correctly decided that a permanent Act would far better serve the purpose of tax legislation, with necessary amendments passed each year. Annual Acts suffered from the disadvantages of lack of continuity, one of which was that losses incurred in one year had no status in the next. Therefore a developing business enjoyed no relief for the period during which it was struggling to become established. In addition, the inevitable court cases which would accompany implementation of the legislation would be less effective as precedents if they were based on transient acts which became out of date and irrelevant annually.

## INCOME TAX ACT 1917

Compared with its predecessors, the Income Tax Act No. 41 of 1917 was a veritable tome. The three previous Acts had together stretched over thirty pages and contained a total of 74 sections and a minor schedule. Their successor had no less than 102 sections and was contained in 43 pages,(4) divided into five chapters.

Chapter I : Administration.

The Commissioner of Taxes was renamed the Commissioner for Inland Revenue, thus resulting in a change of name but not in substance of the machinery administering the Act. The remainder of the chapter was unremarkable, merely recording the officers to administer the Act, the right of delegation and the principle of secrecy.

Chapter II : Income Tax.

Part I dealt with normal tax, and commenced in section 5(2) by establishing that this Act would remain in existence in future subject only to amendments by Parliament.

Section 6 defined the terms 'gross income', 'income', 'taxable income' and 'taxable amount'. The definitions were distinct improvements on the corresponding definitions in the 1914 Act and retained in the two succeeding Acts. The latter definitions were vague and altogether too susceptible to argument as to interpretation. For example, the 1914 Act at section 4 had defined 'taxable income' as '....an income.....which has been received by, or accrued to or in favour of ........', without attempting to define income or to exclude capital. The 1917 Act defined 'gross income' as being: 'total amounts received or accrued other than those of a capital nature from sources actually within or deemed to be within the Union.' It went on to illustrate the generality of the definition by specifically

mentioning numerous kinds of receipt from obvious sources such as salaries, wages and stipends; rents as an example of income from sources other than the sweat of one's brow; allowances, board, residence or other benefit granted in respect of employment whether in cash or kind; and pensions, charges or annuities.

The definition included an indication of when income would be deemed to emanate from a source within the Union: when it accrued to a Union resident from a 'native territory bordering on the Union'; and when it accrued to a Union resident or a person carrying on business in the Union and had not been subjected to tax in the country of origin because the recipient was not a resident of the country of source.

On the basis of this definition, a person who, for example, lived in England and was in receipt of rents from the Union (rental income being sufficient to qualify him as being 'in business') while he also earned tax-free income from, say, the United States, would be taxable in the Union on his income from the USA. This was clearly an impractical provision, but strangely enough it survived until 1925 when the Act was largely rewritten.

The 1914 Act defined only 'taxable income' and 'taxable amount'; its 1917 successor split these concepts into four:

- gross income as defined above;
- 'income' was defined as that portion of gross income remaining after deduction of exempt income;

- 'taxable income' was defined as income in excess of £300, after taking off the allowable deductions but before subtracting abatements;
- 'taxable amount' was defined as taxable income less abatements, and was the amount on which tax payable was calculated.

Section 7 introduced the term 'abatements' to describe the deductions of a personal nature first allowed in the 1915 Act. For the first time, consideration was given to the proposition that the mere fact of being married carried with it an inevitable financial burden, as did the duty to maintain children: a taxpayer who was married on the last day of the tax year, or who was widowed, divorced or judicially separated and supported during that period a child or children under seventeen years of age on the last day of the period, was entitled to an abatement of £300. No one could seriously argue with this allowance. The abatements provided for under the 1915 Act were retained in 1917 in broad principle, with some changes of detail and the addition of an abatement of £20 per dependant for whom the taxpayer was 'mainly responsible', provided the taxpayer was not entitled to the £300 abatement.

The child abatement increased to £30 per child, and qualifying children had to be alive at the end of the year and not only at the beginning, and the maximum age was consequently changed from 16 to 17.

In addition, whereas the £300 'primary' abatement remained at that level until the relatively high taxable income of £24 300 was achieved and then disappeared in the case of a person who was married, or widowed, divorced or judicially separated and maintained a qualifying child, a person not so qualifying was entitled to the £300 reduced by £1 for each pound of taxable income in excess of £300.

Under the 1916 Act, the abatements fell £ for £ in respect of incomes in excess of £500; in 1917 this limit in respect only of the corresponding abatements together with the new dependent abatement was extended to £600.

Companies qualified for the £300 abatement with the same income limit.

All abatement limits were reduced in proportion if the period assessed was less than one year. This requirement was absent from the earlier Acts, apparently due to a drafting oversight, because it made nonsense of the concession to allow the same abatements to a person who died after, say, one month of the year as to one who lived for the entire twelve months.

Section 8 dealt with rates of tax and differentiated for the first time between companies and individuals. The former paid tax at a flat rate of 1/- in the £1, whilst the latter were assessed at the same rates obtaining in 1916, namely 1/- plus 1/2000d per £ of taxable amount up to £24 000, and 2/- per £

above that figure. An interesting point is that the differentiation was between companies and individuals; trusts, estates and other artificial persona were thus not provided for. It will be seen that it took until 1919 for this shortcoming to be noticed and corrected. (See page 143 of this work).

Section 9 confirmed the taxability of income accrued but not actually paid to a taxpayer, and repeated the option available to farmers to be taxed on livestock and produce on hand if they so wished.

Section 10 took into account the fact that business transcended national frontiers in a world of expanding trade and improving communications: it provided firstly that any contract made within the Union for the sale of goods would result in the proceeds being deemed to be from a source within the Union; and secondly that income from the carrying on of any 'business, trade, profession or occupation' would attract tax within the Union, regardless of where or by whom payment was made. For example: if a businessman in the Union contracted with a supplier in Australia to deliver goods to a purchaser in Hong Kong, the proceeds would be taxable in the Union if the contract had emanated from this country, regardless of where payment was made.

Section 11 increased the tax payable by foreign charterers of ships to the tax on £10 per £100 of income.

Section 16 covered exemptions and included income of government institutions, building and friendly societies, life assurance companies and associations not for gain, and ecclesiastical, charitable and educational institutions and those Government officials exempted in the 1914 Act. The first new category introduced in 1917 was war pensions, which obviously were no real factor in 1914. The section then created the first incentive for residents to invest in Government stocks by exempting from tax the interest on Local Stock Loans. It also continued the exemption of interest accruing to non-residents from Government Stocks. The remaining changes were made merely to account for certain changes in the Act such as the introduction of the dividend tax.

Section 17 couched the allowable deductions in somewhat improved language, commencing with the 'general deduction formula' : this permitted deduction of losses and outgoings on the same basis as did the 1914 Act, except that it specifically prohibited expenditure of a capital nature, thus eliminating a major flaw in the former Act. Mercifully the section discontinued the requirement that the deduction in respect of repairs be based on the average of the previous two years, and merely required that actual expenditure be deducted.

In respect of wear-and-tear, the Commissioner was required to take into account, in deciding the amount to be allowed, any repairs also allowed on the same assets.

For the first time, the Act addressed the matter of premiums paid at the commencement or renewal of leases. It could have been argued that such payments were in the nature of capital, being moneys expended in order to gain possession of the relevant leases which were assets. However, section 17(1)(e) settled any such argument in favour of the taxpayer.

In deference to the important mining interests, the redemption of capital expenditure was allowed instead of wear-and-tear and lease premiums.

Interestingly, despite the fact that, in general, taxation paid was not allowable as a deduction, the section permitted deduction of excess profits duty paid. Next, the section permitted deduction of donations to ecclesiastical, charitable or educational institutions of a public character within the Union. One can imagine the joy of both the institutions and the taxpayers who were then able to deduct even their church collection and contributions to church bazaars.

More understandably, perhaps, given the state of the world at that time, enmeshed in the second half of an expensive world war, contributions to public funds connected with the war were deductible.

Finally the section put to rights a grave shortcoming in the earlier Acts in that it provided that losses incurred in any year could be carried forward and set off against profits in any

future year, thus giving effect to the third point mentioned in the Explanatory Memorandum and discussed earlier in this Chapter.

Section 19 provided for continuation of the deductibility of contributions by public servants to pension and superannuation funds, but did not extend this concession to members of the general public. There was apparently no perceived need to encourage people to provide for their old age and thus avoid becoming burdens on the State, beyond the minimal incentives contained in the abatement provisions.

Section 21, which listed those matters in respect of which no deductions were permitted, namely domestic expenses, costs recoverable under insurance contracts, income carried to reserves and opportunity costs, was very similar to its predecessor, section 15 of the 1914 Act as amended in minor fashion in 1915 and 1916. The only addition was an important one; the prohibition of the deduction of any expenditure relating to exempt income. Although eminently logical, the absence of this prohibition from the 1914 Act and its two successors reinforces the understandable conclusion that the drafters of the legislation were still very much in the learning stage of the art of closing loopholes to eager taxpayers.

Sections 23 and 24 dealt at length with the calculation of the mining capital redemption allowance. Briefly, the Government Mining Engineer would estimate the life of the mine and

unredeemed capital expenditure brought forward from the previous year would be added to such expenditure incurred in the current year. The resultant total would be divided by the estimated life or thirty years, whichever was the shorter period and the quotient would be the deductible amount. 'Capital expenditure' was appropriately defined.

By means of these two sections, mines were brought under the aegis of the Income Tax Act and away from the Mining Taxation Act.

Part II of Chapter I dealt with supertax, retaining its existence beyond the initial period which was only for 1916. The minimum level of taxable income remained £2 500 including dividend and interest income exempt from normal tax, but an additional and wholly reasonable provision appeared, namely that expenses relating to the dividend and interest income referred to were deductible in the calculation of supertaxable income. The provisions of the 1916 Act had been wholly unfair, no doubt inadvertently so, in not so providing. The abatement remained unchanged, as were the rates. The exemption in respect of non-residents not in business but in receipt of dividends paid outside the Union remained in force as did the duty of companies and banks to furnish adequate returns. As indicated in the Explanatory Memorandum, the tax would be imposed on supertaxable income for the current year.

Chapter III : Dividend Tax.

Section 35 provided that, subject to exemptions, deductions and abatements, all dividends distributed would be subject to a dividend tax, into which was built a 'special war levy'. This levy applied to gold mining companies only, and comprised 6d of the 2/- per £1 dividend tax applicable to them. It was applicable from the first tax period after the year in which the Special War Tax (Gold Mines) Act, 1916 (5) was applied, and would continue until the end of the accounting period falling in the six months following cessation of the war. Diamond mining companies would pay 1/6 in the £ , and other companies 1/-.

An abatement of £2 500 was provided for, diminishing by £1 for every £1 of aggregate dividend in excess of £2 500.

Section 37 introduced for the first time a definition of private companies for tax purposes namely : 'a company whose membership (excluding employees) did not exceed fifty, which restricted transfer rights and which had not invited the general public to subscribe for shares or debentures'. The reason for the inclusion of this definition was that such a company paid dividend tax at a rate which, when added to the normal tax paid, would not exceed the normal tax payable by an individual on an equal amount. For an example of this provision, see Appendix 8.

Section 38 defined 'dividend' for the first time in surprisingly wide terms. In addition to the normally accepted definition of

any sum of money or its equivalent paid, allocated, distributed or credited by the company to or amongst its shareholders or members, the section included in the definition:

- undistributed profits invested outside the principal business of the company; this would include any sums used, for example to purchase share investments not directly related to the business;
- undistributed profits applied to redemption of capital liabilities (a quaint phrase) or reduction of the capital value of assets; this provision was destined to remain more or less in the successors to the 1917 Act;
- undistributed profits which had been allowed to accumulate beyond what the Commissioner deemed reasonable: mining companies could avoid this situation by investing such funds in capital expenditure ranking for the redemption allowance;
- interest paid beyond six percent on debentures;
- excessive directors' fees.

Section 40 provided that the source of dividends paid by a company operating to a material degree outside the Union would be deemed to be from Union and foreign sources in the same ratio as profits earned. The definition of the word 'material' invited argument from alert taxpayers. An alternative apportionment based on assets was provided for.

Section 41 somewhat surprisingly allowed taxpayers to deduct assessed losses brought forward from dividends before calculating the tax. This would clearly benefit mining companies, which

paid a higher rate of dividend tax than normal tax. If a company chose to deduct its assessed loss in terms of section 41, it could not deduct the amount once more under section 17.

Section 42 offered the first definition of the term 'subsidiary company', describing it as a company wholly owned by another or one in which another held as many shares as were legally possible. The section made a concession in favour of such groups inasmuch as dividend tax was payable only on the dividends distributed by the principal company, and by any dividends distributed by the subsidiary company to outside shareholders.

Sections 43 and 44 contained administrative provisions, after which section 45 listed those dividends which were exempt from dividend tax. These comprised dividends distributed:

- by building or friendly societies;
- out of dividends already subjected to the dividend tax;
- out of profits taxed under the Mining Taxation Act or any previous Income Tax Act;
- out of profits exempted from tax under the 1908 Transvaal Mining Act; such dividends were subject to the special war levy, however;
- on liquidation, to the extent that they represented distribution of capital.

Also exempt were the profit distributions of mutual life assurance companies.

Chapter IV : Excess Profits Duty.

In deciding to impose a tax on the excess profits earned as a result of the war, the authorities had the problem of establishing what constituted 'normal' profits as opposed to 'excess' profits. The means of solving this problem appeared in sections 49 to 64, comprising Chapter IV of the Act. Section 49 provided that there would be levied until six months after the end of the war, for the benefit of meeting war expenditure, a duty of 5/- per £1 of excess profits as defined.

Section 50 furnished the necessary definitions for the Chapter. The starting point on which the duty would be based was the taxable income for the 1914 year of assessment, calculated in terms of the provisions of the 1917 Act. This was known as the 'pre-war standard'.

The section then defined the term 'statutory percentage' as being 8% in the case of companies and 10% in the case of individuals, applied to the 'capital employed'. The latter phrase was defined as being:
gross assets - (assets whose income is not subject to excess profits duty + liabilities + investments except where principal business is making or dealing in investments).

Section 51 declared liable to the duty all profits subject to normal or dividend tax, but excluding the profits of:

- gold mining operations - once again the shadow of the mining interests loomed;
- non-company diamond mining operations;
- life assurance;
- employees, but excluding earners of commission;
- Union Government securities;
- investments, unless the business was making or dealing in investments;
- professional practices.

Section 52 described how excess profits were to be determined, which was basically to begin with taxable income before deduction of excess profits duty, plus any adjustment in respect of decreased capital (see section 57), and to deduct debenture interest payments, excess profits duty imposed outside the Union, and an abatement of £500. The amount by which the resultant figure exceeded the pre-war standard would be subject to excess profits duty.

Section 53 provided for the duty to be paid on profits, realised or unrealised on investments held or dealt in by taxpayers whose business consisted of such activities.

Section 54 entitled taxpayers to carry forward shortfalls between the pre-war standard and profits subject to the duty.

Sections 55 and 56 provided that the statutory percentage would be applicable in calculating the basic comparable amount where

taxpayers had not been in business on 30 June 1914, and also in cases where the pre-war standard was less than the statutory percentage.

Section 57 made provision for charges against or additions to profits to take account of alterations in capital employed, and the following section allowed for some flexibility on the part of the Commissioner in cases where a taxpayer had been affected by economic depression during the 1914 tax year. To qualify for this concession, profits for the 1914 year had to be lower by at least 25% than the average profit for the 1912, 1913 and 1914 years.

Section 60 guarded against the obvious ploy of paying excessive remuneration to management - who, especially in the case of private companies, might well have been the effective owners - by freezing such remuneration at the 1914 level, subject to adjustment at the behest of the Commissioner.

Section 61 provided that groups would be levied as if they were one company, in similar vein to the provisions of the dividend tax.

The remaining sections dealt with penalties for fictitious transactions, and administrative matters.

For an example of the operation of this Chapter, see Appendix 9.

Chapter V : General Provisions

Most of the sections in this chapter were of no particular moment as regards innovation or development of the legislation. However, section 66 improved upon its counterpart in the 1914 Act relating to the taxation of income of married women by specifically providing that from the date of death of a husband the wife became a taxable entity in her own right. This situation was implied in the 1914 Act, but clearly spelled out in 1917. A rather surprising change, however, was that the wife became a separate taxable entity on the insolvency of the husband. This provision was destined to disappear on the next major revision, never to reappear.

Section 84 dealt with the courts for hearing appeals. It specified that the courts should each consist of an advocate of the Supreme Court, an accountant of not less than ten years' standing and a representative of the business community. A further requirement showed again, as was apparent in several places in the 1918 Act, the effect of the mining interests - although in this case a very sensible one: in cases involving mining, the third member had to be a qualified mining engineer.

By contrast, section 24 of the 1914 Act provided for a three-person court consisting of a barrister (with no instruction as to the bar or bars of which he should be a member), an accountant of not less than ten years' standing, and gave no guide as to the type of person who should fill the third position. Perhaps

fortunately, few cases were heard under the 1914 Act.

Finally, section 100 reflected a number of new terms which required interpretation: the most surprising of these was that of 'dependant' which restricted the definition to aged or indigent persons or children related to the taxpayer 'within the second degree', thus excluding from these relief provisions a potentially vast number of genuine dependants.

The 1914 Act briefly stated in section 10(1) that the proportion of the income of insurance companies which was taxable in the Union would be determined by regulations, and section 10(4) provided that the taxable income of life insurance companies would be the income from their investments, wherever made, of the funds received from Union residents. This commendable brevity was inadequate for the purpose of regulating so complicated a sector of the economy, and the 1917 Act introduced, in the first Schedule, specific means of computing the taxable income of insurance business; indeed, section 15 had referred to the Schedule as being the source of the method of making this calculation.

Mutual companies were exempt in terms of section 16(d) and (e). Non-mutual companies were taxable on their income by various methods described in the Schedule, depending on the type of Company. These methods were relatively simple and somewhat specialised and of no great moment within the context of this work.

The Second Schedule described the method of computing the value for redemption in respect of mines.

In general, the Act could at least be described as not unfavourable to the various components of the taxpaying public : mining, agriculture, commerce, manufacturing and individuals. Abatements were increased, and the tax rate applicable to companies was fixed at the previously minimum level. The effects of unprofitable years could be used to offset profits in subsequent periods, and taxpayers were able to enjoy a tax benefit from the inevitable costs of starting a business. Experience was assisting in the steady improvement of the operating efficiency of the Act, to the general benefit of all concerned.

Income Tax Cases

1. On 10 December 1918 and 14 January 1919 the case of Stephan v Commissioner for Inland Revenue (6) was heard before the Witwatersrand Local Division of the Supreme Court as an appeal against a decision of the Special Court.
   The appellant had for many years carried on business as a general, produce, fish and soft goods merchant. He also owned a fleet of small coasting vessels, all but two of which he had disposed of by 1916. In 1910, 1913 and 1916 he had salvaged wrecks near Cape Town, using hired equipment but his own employees and vessels. In 1916 he had salvaged the cargo of a wreck on Dassen Island and realised a profit of

£41 736, which the Commissioner sought to tax.
The appellant claimed that the profits were earned outside the normal scope of his business and thus did not fall for taxation as income from trade in terms of sections 6 and 51 of the 1917 Act.

The court was unimpressed with this argument, holding that as the Act made no provision for the exemption of profits from isolated transactions, and further because these profits had resulted from productive use of capital and not realisation of capital, they were taxable. It held further that the venture itself was a business transaction, being a special transaction of the business of the appellant.

Mason J referred to the Booysens case (7) and in particular to the definition of income given by Wessels J and approved by Innes C J : 'revenue derived from capital productively employed'.(8) He averred that this was indeed the nature of the profit of £41 736 in the present case and not 'the realisation of capital at an enhanced value'.(9)

The learned judge pointed out that the salvage operations necessitated so many business acts such as management, engaging the services of men, hiring apparatus, purchasing equipment and transport of the cargo that they of themselves became a business or trade. Thus the resultant profits were from the use of capital productively employed, and taxable.

Principle established in this case

This case therefore produced a principle which is still very much alive and frequently argued:

An isolated transaction, outside the ordinary course of business, may result in taxable profits if it constitutes productive use of capital and not mere realisation of capital.

So important, indeed, is this principle that the case has been directly quoted in at least two subsequent judgments:

- Commissioner for Inland Revenue v George Forest Timber Co Ltd (10)
- Commissioner for Inland Revenue v Stott (11)

These judgements themselves, based partly on Stephan's case, have been widely used ever since, even as recently as 1975 in the celebrated case of Natal Estates Ltd v Secretary for Inland Revenue,(12) and even more recently in 1981 in Income Tax Case 1343 (13).

2. On 21 and 28 June and again on 29 July 1920, the matter of Deary v Deputy Commissioner of Inland Revenue (14) was heard before the Cape Provincial Division of the Supreme Court on appeal from the Special Court. The case revolved around whether certain receipts were of an income or a capital nature.

The appellant, having been in trade for some years as a general dealer, had sold his business to three of his employees in partnership. The terms of payment were that the purchasers would pass a bond for £10 000 in favour of the seller; interest was payable at 7% per annum, and capital reductions would occur at the rate of £500 per annum; this amount could be increased or decreased at the behest of the seller, depending on the condition of the business. He also had the power to call up the bond at one month's notice.
In addition, for so long as any portion of the bond was outstanding, the seller was entitled to 25% of the annual profits as consideration for goodwill. He had wide powers of control over the business, but it was specifically stated that he was not in partnership with the other three persons.
For the 1917 tax year, the appellant received £516 in respect of his 25% share of profits. The Commissioner sought to tax this amount and the taxpayer appealed to the Special Court. Having lost, he appealed to the Cape Provincial Division. He argued that the receipt was of a capital nature, being part of the proceeds of the sale of his goodwill, and therefore not taxable. The Commissioner maintained that the terms of the agreement made the appellant a partner and thus the amount was a share of profits.

Benjamin J made the point that the price for the goodwill was not fixed, but was totally controlled by the appellant inasmuch as he had the power to decide for how long it would remain payable : 'but it is clear that there cannot be a

contract of sale where the price is left to the discretion of one party.'(15) He rejected the proposition that the share of profits was the price or capital value of the goodwill, and quoted extensively from the English case of Jones v Commissioner of Inland Revenue (121 LT 611) to make the point that a person could in any case sell an asset for an amount which would be taxable : this would be achieved by converting or exchanging the asset into an annuity, which would surely attract tax.

Gardiner J considered three ways in which the seller could have established the value of the goodwill. Two of these would have resulted in tax being payable: increased price paid for stock; increased rent for the premises. The third would not have done so: stipulation of a definite sum.
Under the present agreement, the appellant was effectively receiving an annual share of profits in return for the use of the goodwill; this was analogous to the receipt of rental for his asset.

The appellant thus lost his case, having failed to discharge the burden of proof as required under section 83 that the amount received was not income in terms of section 6.

Principles established in this case (and very relevant even today)

(1) Where a price for goodwill is specified, the terms of repayment cannot render the repayments income in nature. Any vagueness in the exact indebtedness, however, place the payments under suspicion.

(2) A person may be in receipt of a share of profits of a business and yet not be a partner in the business. (16)

3. In Platt v Commissioner for Inland Revenue (17) the Appeal Court had to decide whether the finding by the Special Court that a taxpayer was engaged in a business was one of fact or of law; if the former, superior courts had no right to upset such a finding. If it found that it was a question of law, it had to decide on the facts whether the taxpayer was indeed in business or not.

The appellant was a sugar manufacturer and farmer who had guaranteed the debts of a company in which he was a shareholder, although not of a major number of shares. The company had incurred huge losses and the appellant had had to pay the bank a sum in terms of his guarantee exceeding the profits of his other enterprises. He sought to set off the amounts so paid against his profits from other sources on the grounds that his issuing of guarantees constituted a business of financing the company. His argument was upheld in the

Special Court and the Commissioner appealed to the Natal Provincial Division of the Supreme Court.

That court reversed the decision, finding that financing the company did not constitute carrying on a business and further that the loss was of a capital nature.

The taxpayer then appealed to the Appeal Court on the following basis:

(a) that in terms of section 22 of the 1917 Act, he was in trade, a word which included every profession trade, business, employment or calling;

(b) that in terms of section 18 of the same Act, he was entitled to set off his loss from the financing business against profits from his other activities;

(c) that in terms of section 86 of the same Act, the Commissioner was precluded from appealing against what the taxpayer contended was a finding of fact by the Special Court, namely that he had been in business in financing the company.

Juta J A dealt with these matters as follows:

Dealing first with (c) above, he found that the facts found by the Special Court were not that the taxpayer was in the business of financing the company, but rather that the taxpayer had financed a company, of which he was a

shareholder, by means of issuing guarantees to a bank. The question as to whether these facts meant that the taxpayer was in business or not was one of interpretation of sections 22 and 18 of the 1917 Act, and this was a question of law and consequently open to appeal.

Regarding part (a) above, the Court found that one of the factors in deciding whether a person was carrying on business or not was the possibility of the acquisition of gain. Was the taxpayer putting his capital to productive use? The Court answered in the negative, on the grounds that the only chance for gain were his possible enhancement by means of dividends if the company prospered. This was essentially no different from an ordinary investment. He could not be said to have carried on the business of financing the enterprise, as he received nothing for it. He was not a moneylender, but merely the giver of security.

In the circumstances, the appellant was not carrying on a business in this respect, and his losses consequently did not fall for deduction under section 18. It was therefore unnecessary to decide whether the losses were of a capital nature or not.

<u>Principles established in this case</u>

(1) The decision as to whether or not a given set of facts falls within the ambit of a section of the Act or not is

one of law;

(2) One relevant factor in deciding whether a person is carrying on business or not is the possibility of the acquisition of gain;

(3) The issuing of guarantees does not in itself constitute carrying on a business.

(4) The test of continuity as an indication as to whether a taxpayer is carrying on business or not differs between individuals and companies. There is less need for continuity in the case of companies than there is for individuals, there being a stronger presumption by the courts that anything a company does is for reasons of of profit. (18)

4. The case of Crown Mines Ltd v Commissioner for Inland Revenue (19) came before the Appellate Division on 11 November and 19 December 1921, and referred to the tax years 1917 and 1918. The appellant had made certain payments to the Commissioner under sections 46(2) and 47, in terms of which a company was obliged within thirty days of distribution of a dividend to remit the dividend tax to the Commissioner. Considering that it was so liable in respect of redemption of debentures in the relevant years, the company remitted tax in respect of redemptions of debentures redeemed. It subsequently claimed a refund of these amounts on the grounds that the tax had not been duly payable. Its grounds were that the proviso to subsection (d) of section 38, exempting from the tax undistributed profits which have accumulated

beyond the needs of the company but which in the case of a mining company have been reinvested in the business, applied also to subsection (c) which taxed debenture redemptions.

The learned judge conceded that this might be true, but pointed out that this interpretation had been pointedly suggested to the Commissioner and there was no suggestion that he had disregarded it. Therefore, even if he had misinterpreted the section, which was by no means certain, he had applied his discretion in terms of section 95 and no court could interfere. Section 95 gave the Commissioner the right to authorise a refund of tax paid if it was proved to his satisfaction that the amount paid was in excess of the amount properly chargeable.

If the facts had been so clear that no reasonable man could doubt that there had been an overpayment of tax, then the Court could find that the Commissioner had not applied his mind to the matter. However, that would be on the assumption that the proviso to subsection (d) applied also to subsection (c) of section 38; and on this point there was dispute. The Commissioner had considered both sides of the matter and came to a decision in terms of section 95. Accordingly the Court upheld the decision of the trial Court.

Principle established in this case

The principle arising from this case is that if the

Commissioner had a discretionary power under the Act and exercises it having acted in bona fides and having applied his mind to the relevant sections of the Act, the Courts have no right to interfere.

BUDGET 1918 - 19

The new Minister of Finance, Sir Thomas Orr, who had succeeded Mr H Burton during October of the previous year when growing opposition to the same minister holding simultaneously the portfolios of both Finance and Railways and Harbours had forced the Prime Minister to remove the former portfolio from Mr Burton addressed the House of Assembly on 15 February 1918 to present his first budget.(20) He reported that the estimates for the current year had changed to the extent that a surplus of £464 000 was now expected. As Mr Burton had pointed out in the Budget speech the previous year, estimating the size of imports and exports in the face of the submarine campaign had been almost impossible, and the estimates finally made had been well below the actual figures. Consequent increases in customs duties together with an increase of £510 000 from income tax had combined to produce this change for the better.

The revised estimate of revenue from income tax was £3 700 000 (compared with the estimate £500 000 a mere four years earlier). The same amount was estimated for the coming year, the sources being approximately as follows:

| | | |
|---|---|---|
| Gold mines : | normal tax | 423 000 |
| | dividend tax | 640 000 |
| Diamond mines : | normal tax | 163 000 |
| | dividend tax | 213 000 |
| Other normal tax | | 1 600 000 |
| Supertax | | 423 000 |
| Dividend tax | | 238 000 |
| | | £3 700 000 |

INCOME TAX ACT 1918

The Act itself was not changed at all in 1918, and the Income Tax Act No. 26 of 1918 (21) merely stated that the rates of tax specified in the 1917 Act would be applied in 1918.

Income Tax Cases

1. The first reported case heard in respect of the 1918 year of assessment was Commissioner for Inland Revenue v Delagoa Cigarette Co Ltd (22) relating to sections 17(1), 65(2) and 70 of the 1917 Act.
   The respondent company had embarked on a scheme under which it sold 6d packets of cigarettes for 10/- per packet. Each packet contained a numbered coupon entitling the holder to take part in a monthly lottery, for which purpose two-thirds of the proceeds of the sales would be set aside.

The scheme was about to be attacked by means of criminal proceedings on the grounds that lotteries were illegal, and the Commissioner feared that a conviction would place the company in a financial situation so hazardous that it might not be able to meet its income tax obligations. He had decided that the payment of the monthly prizes constituted a distribution of profits and that the moneys involved were therefore taxable before payment. In this regard he held the view that they were not deductible under section 17(1). Wishing to hasten the receipt of the tax so that it would be paid before the next batch of prizes was distributed, the Commissioner issued an interim assessment, claiming to act in terms of sections 65(2) and 70.

The company predictably indicated its intention of objecting to this assessment, whereupon the Commissioner sought an interdict restraining the company from paying out the next round of prizes. This action, of course, rendered the case very unusual within the context of income tax case law.

The company opposed the application on three grounds:

(a) that the payments were incurred in the production of income and were therefore deductible from income;

(b) that the Commissioner had had no right in terms of section 65(2) to act as he had done in issuing an estimated assessment and demanding immediate payment;

(c) that the profits, being illegal, were not taxable.

Bristowe J found firstly that the legality or otherwise of income was immaterial to its taxability, thus rejecting the third submission of the company. By the same token, he stated that the expenditure attendant upon such income was deductible (provided, of course, it was not capital in nature). In the second place, he found that, since section 65(2) provided for the Commissioner to demand interim accounts, it would be strange if he did not have the right to issue assessments and demand payment. Therefore, it was his opinion that the matter fell under section 70, which enabled tax to be assessed and levied whenever there was a default in furnishing a return. Given the circumstances, the brief period of time was not unreasonable. He therefore recognised the right of the Commissioner to demand immediate payment of an interim assessment if he considered such action necessary to ensure payment of the tax due.

There remained the crucial question of the deductibility or otherwise of the prizes paid. The learned judge wasted little time in deciding that there was no question of the payments' being classified as capital. He then proceeded to argue and find that the payments were sufficiently allied to the amounts received for sales of the cigarettes to enjoy the description 'outgoing necessarily incurred in producing the profit'. (23)

Gregorowski J concurred, describing the prize money as trust money held by the company on behalf of as-yet unknown

prizewinners.

Principle established in this case.

The important principle to emerge from this case is that all income is subject to tax, and its related non-capital expenditure deductible, regardless of its legality or otherwise.

2. On 24 and 25 October and again on 1 November 1921 the case of Lockie Bros Ltd v Commissioner for Inland Revenue (24) was heard by the Transvaal Provincial Division. The case revolved around the interpretation of section 17(1)(a) of the 1917 Act in relation to the income of the appellant for the 1918 year of assessment. This section allowed losses and outgoings actually incurred in the Union in the production of income, provided such losses and outgoings are not of a capital nature'. (25)

The appellant company carried on business in the Union via an office in the Transvaal; it was incorporated in England. During the 1918 tax year, the manager of the South African office embezzled a total of £11 365 following an embezzlement of £1 260 in the preceding year.

The company sought to claim as a deduction the whole sum of £12 625 on the grounds that it was 'an ordinary trading loss incidental to the actual carrying on of the business'. (26)

The Commissioner refused the claim and his decision was upheld in the Special Court; hence the appeal to the Transvaal Provincial Division.

Mason J interpreted the words of section 17(1)(a) as meaning 'losses or outgoings actually incurred in the course of and by reason of the ordinary operations undertaken for the purpose of conducting the business, not being losses or outgoings of a capital nature'. (27)

Whilst the embezzlement had clearly been committed in the course of the business operations, and whilst the presence of the manager was necessary for the conduct of the operations of the company, it could not be said to have been undertaken for the purposes of the business and was accordingly not admissable as a deduction.

De Waal J placed upon the words 'losses and outgoings incurred in the production of income' (28) the meaning 'expenses necessarily incidental to the production of income'. (29) The nature and scope of the manager's employment were to manage the business of the company and not to steal its funds. Once assets are converted into cash, it becomes capital liable for reinvestment and its theft is the theft of capital.

This case has enjoyed extensive use in subsequent cases, being the major reference in all cases involving the

deductibility of losses through dishonesty, the most recent case reported being in 1978 in Income Tax Case 1383. (30)

Consequent changes in legislation

Although, as explained above, Bristowe J had found for the Commissioner in the Delagoa Bay Cigarette Co case as regards his right to issue assessments on the basis of interim accounts, the legislature seems to have moved quickly to eliminate any doubt in this regard. In the Income Tax Act No 39 of 1919, section 65(2) was amended to read:

'....the Commissioner .... may .... require any person by notice in writing to render interim accounts for any period he may designate in such notice and shall make an assessment in respect of that period'. (31) The portion underlined was that added in the 1919 Act.

In this way the lawmakers removed this aspect of the interpretation of this section from the vagaries of the courts; this was the first recorded response to legal interpretation of the Act by changing the Act.

For a discussion of two Southern Rhodesian cases from this time, see Appendix 10.

BUDGET 1919 - 20

Sir Thomas Orr presented the Budget on 19 February 1919 (32) in a speech, the records of which are unusually brief. He indicated that there would perhaps be a small surplus in the current year, the actual amounts of tax received having been of the order of:

| | |
|---|---|
| Normal tax | £12 500 000 |
| Super tax - gold mines | £ 850 000 |
| - diamond mines | £ 370 000 |
| - other | £ 2 655 000 |

The income from these sources for the coming year was estimated at £12 360 000 from normal tax and £3 850 000 from supertax.

INCOME TAX ACT 1919

The Income Tax Act No 39 of 1919 (33) commenced by providing that the rates of both normal and super tax would remain unchanged. It then proceeded to change the principal Act (No. 41 of 1917) in several respects.

Section 7 was amended to increase from 17 to 18 the maximum age a child could be in order that its parent qualified as married; the wording was also improved in subsection (a). Subsection (b) was amended to correct a shortcoming in drafting, so that it ensured that the £300 abatement for persons other than those qualifying under subsection (a) would be reduced pro rata if the

period assessed was less than twelve months.

The insurance abatement was doubled to £50; the abatement of amounts received from friendly or benefit societies was removed; the maximum age for children to qualify in calculating the child abatement was raised to 18; a new subsection, (4), ensured that 'children' always included 'step-children'; the actual wording was in fact ambiguous, stating that 'the words child or children wheresoever used in this section shall include the step-child or step-children of the tax-payer'. (34) Although the intention was surely otherwise, the wording did not exclude children who were not children or step-children of the taxpayer, but merely included those who were; the dependant abatement was increased from £20 to £30.

Section 17(h) was reworded in a more orderly fashion and amended so as to include any contribution to ecclesiastical, charitable or educational institutions and not merely those in excess of £20. In addition, the deduction in respect of contributions to war funds was scheduled to end at 30 June 1920.

A new section 17(i) was introduced, permitting the deduction of compulsory contributions by employees to superannuation, pension, widowers' or orphans' funds, thus continuing the practice of encouraging people to provide for their own old age.

Section 49 doubled the excess profits duty to 10/- in the £. The excess profits duty was then perpetuated beyond the war

period by the declaration that the words in Chapter IV, 'for the benefit of loan account towards meeting war expenditure chargeable thereon' would thenceforth be ineffective. Thus was the practice established of imposing a tax to meet a particular set of circumstances and then retaining the tax when the circumstances had ceased to exist.

Section 53 was repealed, so removing the special conditions of applying the excess profits duty to investment businesses.

Section 6 was amended to eliminate the provision in terms of which the first £300 of income was tax-free. Thus was the prophetic remark of Sir E H Walton during the budget debate of 1914 proved true within a few short years. (See discussion of the Budget in 1914 on page 65 of this work).

Section 8 was amended to refer to 'persons other than companies' instead of 'individuals'. Clearly the fiscal authorities had realised that a large number of taxpayers fell outside the descriptions 'individual' and 'company'.

Section 16 was amended to reflect the tax-free status of income from Union Loan Certificates.

Section 19 was amended to ensure that public servants were taxed on allowances.

Section 23 was amended to oblige mining enterprises to take into account recoupments of capital expenditure. As the Act had read previously, such recoupments were not taxable, which clearly operated to the benefit of the taxpayer.

The amendment to section 26 perpetuated the existence of the supertax. Inclusions in the meaning of 'dividend distributed' were changed to include amounts applied to redeem debentures or mortgages or to reduce the capital value of assets; this section did not, however, cover wear-and-tear, lease premiums, or mining capital redemption allowances.

Obviously as a result of the case of Commissioner v Delagoa Bay Cigarette Co Ltd discussed in the consideration of the 1918 Act in this chapter, the Act was changed to ensure that there was no doubt at all about the power of the Commissioner to issue assessments on the basis of interim accounts. Thus, despite having won the case involved, the Commissioner for the first time moved to consolidate the provisions of a section of the Act in his favour; in this case, section 65(2).

Section 65(12) did not specifically spell out the liability for submission of the joint return in the case of partnerships until the 1919 Act amended the section to provide clearly that partners were jointly and severally so liable.

The realities of marital dissension as well as the existence of women in receipt of substantial earnings doubtless gave rise to

the amendment to section 66, which was to the effect that married couples could request separate assessments provided the total amount of tax was not less than it would have been under joint assessments.

Sections 67 and 68 were changed in minor respects.

Section 71, dealing with penalties for default or omissions, was more clearly drafted.

Section 81 was amended to correct an omission in drafting and provided that every company maintain a place for delivery of notices.

Income Tax Cases

1. The case of Modderfontein B Gold Mining Company Limited v CIR (35) appeared before the Appellate Division on 23 July and 16 October 1922. The appellant had won its case in the Special Court and lost on appeal to the Transvaal Provincial Division of the Supreme Court; as a result, it resorted to the Appeal Court. The essence of the case was that the appellant owned a certain bewaarplaats in the Transvaal. Only the Government was entitled to mine such areas; but it could lease them to mining companies, in which case the rentals, being a percentage of the mining profits, were shared between the Crown and the owner of the bewaarplaats. Precisely this had happened in the matter before the Court, and the taxpayer

contended that the proceeds were not taxable, being either:

(a) capital in nature, being the proceeds of the owner in return for parting with its asset; or

(b) capital in nature, being a debt owing by the Government; or

(c) if income in nature, then exempt as being mining profits exempt under section 46 of Act No 35 of 1908, such profits being exempt from taxation under section 16(1)(p) of the 1917 Income Tax Act.(36)

The Court rejected the proposition that the payment was capital in nature, being a share of rental earned by leasing the asset. It further decided that the income was not a share of mining profits between partners, but rather the result of an agreement between lessor and lessee and therefore rental.

Principles established in this case

1. The nature of business of the lessee does not change the nature of the rental.
2. An annual payment is not necessarily an annuity.

2. In the case of CIR v Collins (37), a company had large accumulated profits but insufficient cash to declare dividends. It therefore changed its articles to permit it to convert these profits to bonus shares in satisfaction of a bonus dividend. Seizing upon section 27(b) of the 1917

Income Tax Act, (38) the Commissioner deemed that the bonus shares were 'dividends......which.....were excluded in the computation of taxable income' and consequently to be included in the calculation of income of the shareholders subject to supertax. The taxpayer appealed to the Special Court and won, whereupon the Commissioner appealed to the Transvaal Provincial Division of the Supreme Court and lost. He proceeded to the Appeal Court, where the case was heard on 7 November 1922 and 28 February 1923.

The Court found that the operation of capitalising the profits and adding them to share capital was allowed by the Companies Act and the articles of the company. In the act of being capitalised, the profits had assumed the nature of capital.

Consequent change in legislation

Section 29(c) of Act 40 of 1925 included in the definition of income subject to supertax: 'an amount equal to the nominal value of bonus shares ...... awarded to the taxpayer by way of capitalising the profits of the company.' (39)

BUDGET 1920 - 21

Mr H Burton, having resumed his position as Minister of Finance after a two-year tenure by Mr Orr, presented his Budget speech on 30 April 1920. (40) His message was a buoyant one : revenues for

the current year had increased by £3 771 000; all sources had contributed to this, except the excess profits duty, which was £134 000 below the budgeted figure, and a few other small sources. The chief contributors to the increase had been customs : £1 158 000; and income taxes, all of whose components (with the exception of excess profits duty) had risen by a total of £702 000.

Actual expenditure of £24 468 000 had resulted in a surplus of £2 271 000. Mr Burton ascribed the satisfactory position to the buoyant trade conditions, in which wool had played a major role. Indeed, since 1910, production had increased by 52% and prices by 207%. In the industrial sector, production had increased by £20 000 000 since 1915 to its present total of £61 000 000. (It must be remembered, of course, that these figures were affected by the high rate of inflation being experienced during this period.)

Referring to the coming year, the Minister estimated revenue at £27 381 000. The taxes on gold mines would increase by £60 000 to £1 480 000, and those on diamond mines by £175 000 to £1 250 000. Normal income tax receipts would increase by £163 000 to £1 900 000, and supertax by £50 000 to £750 000. Excess profits would garner an additional £284 000 and the total customs revenues would be £6 900 000.

During the debate on 7 May 1920, Mr G Hills, Labour, made a few remarks which illustrated aspects of the philosophy of his party;

(41) namely, taxing of profits and relief for the individual.

He expressed a preference for retention of the excess profits duty and the wish of his party for the amount of income exempt from tax to be £750 in the case of individuals, thus shifting the burden towards the larger income earner. He bewailed the differentiation between married and single men in the form of abatements, declaring that they revealed a desire by the Government to condemn single men to a perpetual state of celibacy.

INCOME TAX ACT 1920

The Income Tax Act No 45 of 1920 (42) devoted a fair proportion of its attention to the excess profits duty, and made several further amendments to other sections. After leaving the rates of normal and super tax unchanged, the 1920 Act amended section 7 in four respects, despite the attention this section had received in 1919. Firstly, the abatement for married persons (or those taxed at the married rates) was increased to £500 from £300, thus occasioning the remarks of Mr Hills mentioned in the previous paragraph.

Secondly, the wording of the paragraph providing for the dependant abatement was simplified.

Thirdly, the poor drafting of subsection (4) in the 1919 Act (43) was improved by changing the wording to read 'child .......shall

mean and include only the child.....of the taxpayer concerned.'(44)

Fourthly, a new subsection, (5) was introduced which stated that for the purposes of this section of the Act, taxable income included the dividends and debenture interest exempt from tax under section 16(1)(n) and (o); these subsections referred to amounts received from companies subjected to the dividend tax. As a result, taxpayers were obliged to take into account in calculating their abatements more than merely taxable income. This amendment certainly made sense, because the essence of the abatement concession was to recognise the effect of personal circumstances on taxpayers whose incomes were relatively low. It was illogical, therefore, to make these concessions available to persons who in fact enjoyed the income but were not taxed on it for reasons of equity provided for in the Act.

Section 10 was increased by the addition of a subsection deeming the source of any pension or annuity to be within the Union, unless the services relating to the pension or annuity had been rendered entirely outside the Union. Previously section 10 had referred only to contracts and services rendered. No doubt experience in the intervening years had revealed that there was no such deeming provision in respect of pensions, thus leaving a loophole for such payments to be made free of tax.

Section 5 of the 1920 Act continued the existence of excess profits duty into the 1920 tax year, in respect of excess profits

earned up to 30 June 1919, and for as long thereafter as it was leviable, at the present rate. The duty was due to cease six months after the declaration of peace, which would have been 10 July 1920. The Minister had announced in his Budget speech that for the sake of convenience the duty would end ten days earlier to coincide with the end of the fiscal year. (45)

Section 52 was amended to make the logical provision that assessed losses could not be deducted from taxable income in arriving at the figure of income subject to excess profits duty.

Section 8 of the 1920 Act empowered the Commissioner to take account of reductions in the value of trading in establishing the amount of income subject to excess profits duty. It was strange that no such provision existed in respect of normal tax; this omission therefore forced the taxpayer to calculate his normal tax using cost price of stock on hand, regardless of the current value.

Section 10 of the 1920 Act was an example of the use of the Income Tax Act to achieve objectives other than the garnering of income. Investments in Union Government securities were deemed to be capital employed in the hands of investment dealing business, thus making them more attractive and therefore encouraging investment in such securities.

The definition of 'dependant' in section 100 was broadened to include any person incapacitated from maintaining himself, or any

child under 18 years old (on the last day of the financial year) other than the child of the taxpayer and who had been maintained by the taxpayer throughout the year. The original definition had been hopelessly insufficient, being any aged, infirm or indigent person or any child under sixteen years old, provided the person or child was related to the taxpayer within the second degree. In the first place this had meant that the aged person could have been capable of working but not willing to do so, and in the second place foster children were excluded from the definition. The 1920 definition eliminated these problems.

Income Tax Cases

The case of Union-Castle Mail Steamship Company Ltd v Commissioner for Inland Revenue (46) was heard before the Appellate Division on 2 October 1923 and 16 January 1924 in respect of the 1920 year of assessment.

The company had elected, under section 11 of the 1917 Act, to be taxed on the basis that its shipping profits amounted to 10% of gross amounts received in respect of passengers and cargo within the Union. In 1918 its fleet was taken over by the Imperial Government and its shipping activities therefore ceased. In 1919 some of its ships were returned and business commenced anew. As the taxable income, on the 10% basis, fell short of the pre-war standard, no assessment was issued.

However, in 1920 the taxable income so calculated was high enough to justify an assessment, and one was duly issued after allowing a deficit of £83 122 for 1919.

The company objected on the grounds that a deficit of £112 543 ought to have been allowed for 1918. On consequently reconsidering the matter, the Commissioner concluded that in fact there had been a withdrawal of capital inasmuch as the tonnage employed was less than that used in the year in which the pre-war standard has been set. He recalculated the taxes owing on this basis and issued an amended assessment for 1919 on the basis of which excess profits duty was payable. He then also amended the 1920 assessment, taking into account no deficit at all, of course.

The company objected once more on the grounds that:

(a) the Commissioner had no right in terms of section 82 to issue an amended assessment in respect of 1919;

(b) section 57 had no reference to the case and thus the Commissioner had been incorrect in treating the reduction in tonnage as a withdrawal of capital;

(c) the Commissioner had no grounds for acting under section 70, which empowered the Commissioner to issue an estimated assessment if he ..... 'is not satisfied with the return furnished by any taxpayer', (47)

(d) the assessment was wrong in that it did not take into account the 1918 deficit of £112 543.

The case went in favour of the Commissioner before the Special Court, and again on appeal to the Cape Provincial Division of the Supreme Court. The company then appealed to the Appellate Division which in finding for the Commissioner, held:

(a) that the Commissioner was indeed entitled to act in this matter under section 70 and that the basis he had used was fair and reasonable;
(b) that the deficit ceased to exist in a year during which the company had not traded - in this case, 1918;
(c) that a matter which had not been the subject of objection in the first instance could not be considered in a case stated to the Supreme Court.

Principle established in this case

The principle arising from this case is contained in that portion of the Appeal Court finding described in paragraph (c) above. This principle is still very much in operation and the case is quoted in its support.(48)

BUDGET 1921 - 22

The Minister of Finance, Mr H Burton, presented his Budget (49) for the 1921 session on 15 April 1921 and reported that the current year would show a deficit of £250 000 instead of the estimated surplus of some £570 000. South Africa was in an

unfavourable position in world trade: there had been an efflux of capital from the country during the early part of the previous year, causing an increase in interest rates. Imports had risen by nearly 100% to a figure of £93 405 000. The wool and diamond markets were stagnant, and in fact the latter had been a chief contributor to the deficit in the 1920 financial year. Fortunately, gold was holding its own in economic conditions which the Minister described in the following terms: 'We are in the midst of the process of deflation'. (50)

The estimates for the coming year made grave reading. Revenue was expected to be £25 815 000, to which significant contributors would be:

| | |
|---|---|
| Customs | £6 000 000 |
| Diamond duty | £ 300 000 |
| Gold mining tax | £ 995 000 |
| Normal tax | £2 500 000 |
| Dividend tax | £ 300 000 |
| Super tax | £ 775 000 |
| Excess profits duty | £1 300 000 |

As against that, estimated expenditure was £32 271 000 which, together with the £250 000 deficit from 1920, would result in a deficit of some £6 000 000.

How was this deficit to be met? In the first place, it was proposed to reduce the cost of living allowance for public

servants by 25% in each of the next three years. This would achieve a saving of £2 000 000. Mr T Boydell (Labour) interjected: 'Why did you not say that before the election?'(51) The answer to that was, of course, simple if not stated in the House : governments do not hit voters in the pocket shortly before election time.

Secondly, luxuries such as films, beer and tobacco would be taxed, while postage and stamp duties would be increased.

Then farmers would be obliged to be taxed on the stock basis, thus having to reflect opening and closing values of livestock on hand. No longer would they have the option of deciding whether to be taxed on the stock or cash basis.

It was further proposed to limit the £300 abatement for individuals, while increasing the child abatement from £30 to £50; abatements would fall in concert with increases in income. The abatement in respect of super tax would diminish.

The Minister then acknowledged for the first time that private companies were being used as a tax-saving measure, to the chagrin of the authorities: 'The business still belongs really to the former owner, but for taxation purposes it ranks as a company, and I am afraid a good deal of abuse has been made of this condition of the law. The private owner contents himself with a small salary and small dividends of profit, the bulk of them remaining in the business. As they belonged to the company they

are charged at the flat rate, and the dividend tax payable being limited, the company becomes entitled to a rebate. The company becomes entitled to an abatement, which is additional to the abatement enjoyed by the proprietary shareholder. We propose now to tax the private proprietary companies at the progressive rate, repeal this section, and abolish the abatement to which I have referred, and we hope to get from that for the full year £80 000 and for the present year £60 000'. (52)

The company rate of normal tax would be increased by 6d to 1/6 in the £. The Minister pointed out that with the disappearance of the excess profits duty and the special war levy, there would be only a minimal extra burden. The exemption in respect of gifts, contained in section 17(1)(h) of the 1917 Act, had been introduced to encourage contributions to war funds, according to Mr Burton. Instead, taxpayers had extended it to 'all sorts of things - ecclesiastical, educational and charitable - and I am told that there are even taxpayers who total up how much they have given to the Church plate on Sundays, and deduct that amount from their taxable income'. (53) This had never been intended, and the section would be scrapped, resulting in additional taxes of £30 000 per annum.

Nationalist and Labour members, he said, had complained that the tax burden of the 'mining magnates' had not been increased in order to avoid the taxes proposed. This would hurt the man in the street, who would have to be taxed correspondingly more severely. In particular the reduction of the war bonus would

have this effect. In fact, the Minister pointed out, the 'mining magnates' were being substantially taxed inasmuch as company tax was to be increased to 1/6 in the £ and the same profits would be taxed in the hands of the individuals on declaration of dividends.(54) The alternative to reduction of the war bonus (COLA) was the dismissal of many civil servants. (55) The tax on private companies was being introduced to prevent evasion of super tax - henceforth private companies would pay at the rates applicable to individuals. (56)

During the subsequent debate, Mr M Alexander (Constitutional Democrat) pleaded for separate taxation for married women. (57) He failed to gain a response from the Minister on this, the first attempt to raise a topic destined to remain an unresolved source of controversy. Other topics around which there was considerable debate were: taxation of farmers, private companies, and mines.

After consideration of the Bill by the House Ways and Means Committee, it was decided to tax private companies at the progressive rate, which would replace the former normal and dividend taxes. (58) At the same time the Commissioner would be empowered to 'hand back to shareholders for supertax such proportion of the undistributed profits of the company as he might consider reasonable'. (59) By this means the Commissioner would be enabled to differentiate between private companies whose existence was genuinely commercially desirable, and those whose

only reason for existence was the reduction of the income tax burdens of their shareholders.

In addition the Bill was altered to account for another criticism, namely, that the amendment would result in the taxation at individual rates of private companies which were the subsidiaries of public companies and therefore obviously not in existence for the sake of savings in individual taxes. In terms of the change, there would be excluded from the definition of 'private company' any company at least 90% of whose shares were held by a public company.

The next subject of debate was the taxation of farmers, and the remarks of some of the speakers reflect the open championing of the farmers by the Nationalists and the attitude of the Government that farmers were essentially no different from other taxpayers. The Minister pointed out that all other taxpayers were subject to the stock basis, and that this was the only method which ensured uniformity of the tax burden throughout the community. 'The agrarian community throughout the world has always been rather marked by its unwillingness to be taxed according to its full capacity'. (60) There was some peculiar quality in the agricultural community which appeared to resist taxation perhaps more than 'the humbler and more brow-beaten residents of the urban areas appeared to do'. (61) This system was far from being some nefarious scheme introduced by the Government: it had been introduced by the present Prime Minister in 1914 and then partly withdrawn to the extent that farmers were

given a choice of which basis they wished to use. In 1919 it had been proposed once more, but withdrawn under Nationalist pressure. The problem with the cash basis, according to Mr Burton, was that it created a 'tremendous loophole' for the evasion of taxation because the farmer could escape tax by re-investing in new stock the proceeds of any stock sold. (Apart from the income tax point of view, it encouraged overstocking of land, which was a severe problem in any case at the time.) The present system resulted in people occasionally paying very large sums in income tax at intervals of five to seven years (when they sold a portion of their stock and did not re-invest the proceeds in new stock), but there could be no doubt that the farming community as a whole did not produce a uniform fair return of tax. To this, Mr C T M Wilcocks (Nationalist) replied 'Tommy rot'. (62)

(With respect, the use of the word 'evasion' was inaccurate and unreasonable. Evasion implies dishonesty and this was not the case at all. Farmers were able to postpone the payment of tax (hence the remark of the Minister about large sums being paid every five or seven years), but sooner or later it became necessary to reduce the amount of stock and then tax would be paid. In fact, on a progressive tax scale, a farmer could pay more in the long run under the cash system.)

Mr Burton stated that the proposal would be reasonable at the present time, when the whole community was under pressure, so

that farmers would help to share the tax burden on a continuing basis.

In order to take into account the problem of stock mortality, which was unique to farmers, the Government was considering the introduction of a mortality allowance, and this would be introduced while the Bill was in Committee.

Gen. Hertzog (Nationalist) complained that the income tax form was too complex for farmers and required simplification and explanatory notes. (63) He criticised the stock basis of valuing stock, because increases in value would be taxed before they were turned into cash. He apparently did not understand the explanation of the Minister that this would not be so if the farmer elected to use standard values for livestock.

Mr A P J Fourie (Nationalist) maintained that the farmer was now being burdened with increased taxes of £55 000 in order to compensate for the reduction of £1 618 000 in the amount the fiscus would receive from the mines, whose owners had good cause to be satisfied because their 'cause was safe with the Minister'. (64) To this Sir David Harris (SAP) (65) replied that the diamond mines had lost money during the past year, but had nevertheless been obliged to pay huge sums in export duty. Farmers could sell their produce or stock in order to raise funds for tax, whereas the mines were unable to sell as many diamonds as they wished. This exchange typifies the basic contrast

between the perceived interests of Government and Opposition respectively.

Sir David, representing Kimberley and a tireless champion of the mines, bewailed the fact that industrial companies paid a maximum of 2/- in the £ whereas the mining companies paid 1/6 normal tax and 1/6 dividend tax, in addition to the economically nonsensical export duty.

Mr N C Havenga (Nationalist) blamed the farming provisions of the Act on the amalgamation of the South African Party and the Unionists. (66) The latter had achieved the victory they had long sought and which their partners had previously managed to avoid. The power of the Unionists had now prevailed, and would surely be followed by a land tax. Not only were the farmers now the sole section of the community which had to pay tax on unrealised profit, but the real injustice was that the tax was not even necessary.

Mr C T M Wilcocks (Nationalist) (67) maintained that the rate of advance of the country as a whole had surely been less than the 79% by which taxes had increased. (He omitted to state over what period this increase had occurred.) In addition, few public works of a permanent nature were in evidence as the result of these taxes. In fact, the taxes were hindering the economic development of the country.

Mr T Boydell (Labour) reflected the interests of his party in calling for the return of the £500 exemption from tax for the sake of the working man. He pleaded for abatements in respect of rent and trade union contributions. He then expressed his wonder at the way the farmers were 'crying out about this tiny tax' which the Government had finally brought into existence in response to public opinion. (68)

(It is ironic that four years later Mr Boydell and his party were sharing the Government benches with the Nationalists.)

Mr J H H De Waal (Nationalist) simply stated that the Government had gone out of its way to exempt the mining magnates from taxation and tax the farmers in every possible way. (69)

Mr H W Sampson (Labour) reflected the interests of his party in calling for the exemption from taxation of moneys paid under the Compensation Act to injured workers, and of similar payments to phthisis sufferers. (70)

Finally Gen. C H Muller (Nationalist) blamed the 'Imperial connection' and the 'see-the-war-through' policy of the Government for the need to impose further taxes. (71)

Perhaps some comments on this debate would be appropriate at this point. The Government was clearly confident that it could rely on the civil service as a source of support despite the somewhat draconion treatment it received. In any case, having only

recently won an election, Smuts had another four years in which to re-establish, if that were necessary, the loyalty of the civil service by whatever means he could; the party in power always has access to ways and means of satisfying sectional interests as short term means of attracting votes. In any event, it was more than likely that the civil service would at that stage still have been largely populated with the remnants of the colonial administrations whose affiliations would surely have been anti-Nationalist almost as an article of faith, even if not always pro-Government when the government hurt their pockets.

Regarding the imposition of the stock system of livestock valuation for farmers, this was not the huge burden which the Nationalists sought to project it to be. Standard values were always lower than market value, and in any case the equalisation of the tax liability from year to year can never be a bad thing. (Indeed, now in 1984, suggestions are being made to amend the Act so as to eliminate provisions which encourage farmers to spend mightily in good years in order to reduce their tax burdens, resulting in their having no funds in reserve in lean times. The solution is to intoduce a system of equalising tax from year to year). In addition, the fact that the system tended to discourage overgrazing could only benefit the country in general. The Government was probably hoping that the adverse feelings about this measure would have dissipated by the next election; there was, at least, some breathing space during which the farmers could be pacified in the interim. In fact, the suspicion arises that the Nationalist obsession with this

provision was partly to gain favour with the agricultural community and more largely because philosophically there was little difference between the income tax policies of two essentially capitalistic parties reliant, whichever happened to be in power, on the same limited sources of income to the same degree; consequently, where a small difference occurred, it was avidly exploited.

The same could probably not be said for the Labour Party, which might well have tried to establish a more socialistic system of taxation had it ever come to power. It is submitted, however, that the realities of South African economic life would have affected even the Labour Party. The plea of Mr Boydell for alleviation of the lot of the working man may have been a test to establish the attitude of the Government towards labour; more likely, it was a harmless way of posturing before his constituency.

So far as the anti-Imperialist and anti-war remarks of Gen. Muller were concerned, they appeared to have no significance beyond being a rather typical knee-jerk reaction to an opportunity to launch a barb at the Government for the benefit of the anti-British voters of the National Party. In short, it was probably the sort of almost meaningless, typically shallow remark which backbenchers have been making since parliaments came into being.

INCOME TAX ACT 1921

The Income Tax (Consolidation) Act further Amendment Act No 29 of 1921 (72) was assented to on 28 June 1921, and amended the principal Act in several respects.

Section 8 was amended to reflect the new rates of normal tax applicable to companies, namely an increase of 50% in the rate for companies, from 1/- to 1/6 in the £. At the same time, privately-owned companies were to be taxed at the rates applicable to individuals, and for this purpose the section contained a proviso which defined private companies in the following terms:

(i) not more than 10% of the shareholders held 90% of the shares;
(ii) restrictions existed as to transferability of shares;
(iii) no invitation had been issued to the public to subscribe for shares or debentures in the company or in at least 90% of its shareholders if these were companies.

Requirement (i) of the proviso was badly phrased in that it spoke of '90% of the shares' when it surely meant 'at least 90% of the shares'. Such literal interpretations of the Act are grist to the mill of the tax avoider and planner.

The rates of normal tax applicable to taxpayers other than companies were unchanged. The rate of super tax, however, was

set at 1/- and 1/500d per £ of the amount subject to super tax up to £24 000, and 5/- per £ above that figure. The effect of this change is illustrated in Appendix 11.

The provision of section 6 deeming income from 'a native territory bordering on the Union' to be part of gross income was deleted, thus removing what had really been an illogical decision in the first place.

Section 7 was amended yet again; indeed only in 1918 had it not undergone some sort of change. This time, however, the lawmakers appear to have found a satisfactory combination, as the section remained intact until the new Income Tax Act of 1925 came into being. The 'primary' abatement was reduced to £300 from £500, whilst provision was made for its reduction at the rate of £1 for every £10 by which taxable income exceeded £600 in the case of persons taxed as married and £300 in other cases. The child abatement was substantially increased from £30 to £50, but the dependant rebate remained unchanged at £30. In addition, the child abatement became applicable only where the taxpayer had maintained the children during the year. Previously this proviso had unaccountably been absent. Finally, premiums on the lives of minor children were also made subject to the insurance abatement.

Appendix 12 illustrates the effects of the development of this section in the years 1917 to 1921.

The amendment to section 9(2) was the one which caused so much distress to the Nationalists and their power base, the farmers. After a few improvements to the wording of section 9(1), the amendment to section 9(2) followed, providing that farmers bring to account the opening and closing values of livestock on hand. Section 9(3) stated the means of arriving at those values. These were:

(a) for purchased stock : purchase price or standard value;

(b) for stock acquired other than by purchase : standard value.

Section 9(4) then defined 'standard value' as either:

(a) standard value fixed by regulation; or

(b) standard value adopted by the taxpayer.

While the taxpayer had the option as to which value to adopt, his decision was binding for the future, except with consent of the Commissioner.

Section 9(6) provided that purchase price would be used for stud stock. Finally Section 9(7) stated that the value of produce on hand would be one which the Commissioner deemed fair and reasonable.

Section 17 was amended to give effect to the unhappiness expressed by the Minister in the Budget speech concerning abuse of the deductibility of gifts to ecclesiastical, charitable or educational institutions, or to any war fund; paragraph (h) was deleted.

Section 19(2) was amended to make it clear that losses deductible referred to those of previous years.

The 1921 Act at section 6 empowered the Commissioner to allocate to the incomes of shareholders subject to supertax their proportionate share of distributable profits to the extent that the Commissioner deemed the dividends declared to have been inadequate or unreasonably non-existent. This addition was obviously aimed at eliminating a means of avoiding supertax by leaving profits in the companies concerned instead of distributing them to the shareholders where they were subject to the supertax. Section 29 of the principal Act was then amended by reducing the abatement from income subject to supertax. The details and effects of this change are illustrated in Appendix 13.

As a result of the new method of taxing private companies, section 37 was repealed. This section had provided that the total of normal tax and dividend tax payable by a company would not exceed the tax which would have been payable by a taxpayer other than a company on the same amount of income. Finally, section 91 was amended in respect of a minor administrative matter.

Income Tax Cases

1. In CIR v Lydenburg Estates Limited, (73) heard in the Transvaal Provincial Division of the Supreme Court on 2 August 1923, Messrs Justices Curlewis and Stratford heard the appeal of the Commissioner against the decision of the Special Court in favour of the taxpayer. The company was the owner of certain properties whose value fell. As a result, the capital was reduced by 75%. Subsequently some of the properties were sold for a price in excess of the written-down value, and the surplus was distributed as a return of reduced capital. The Commissioner taxed this sum as a dividend under section 38(a) of the 1917 Act, which read: 'any sum of money.....paid.....to.....its shareholders or members as such'. (74)

   The Court held that these amounts were indeed dividends and therefore subject to section 38(a).

   Principle established in this case.

   This case established the principle, also enunciated in City & Suburban Gold Mining & Estate Company,Limited (75) and still in force, that all distributions of either capital or revenue profits are dividends in the hands of shareholders (except on winding up, where different rules apply).

2. Income Tax Case No 23 (76) was heard in the Cape during September and November 1924 and revolved around section 6 of the 1921 Act. The appellant had been assessed to supertax on income including dividends from a private company; these dividends had amounted to a little less than 10% of the accumulated profits, but more than the profits for the current year. This being the first year that section 6 was in operation, the Commissioner sought to construe the words 'profits available' in the section as 'accumulated profits available'. He added a proportion (40%) of the accumulated profits to the income of the taxpayer subject to supertax. The taxpayer took the matter to the Special Court, which decided that to find in favour of the Commissioner would amount to retrospective legislation. The word 'profits' clearly referred to profits for the current year, that is, 1921.

Consequent changes in legislation

Section 32 of Act 40 of 1925, the successor of section 6 of Act 29 of 1921, referred to 'accumulated profits available'. (77)

BUDGET 1922 -23

On 6 May 1922 Mr Burton, still Minister of Finance, presented a somewhat uneventful Budget. (78) Revenue from customs had been less by £1m than the estimates, excise less by £450 000 and posts by £310 000, while diamond export duty had produced £155 000 less than anticipated. As against that, revenue under the Income Tax Act had produced nearly £1,5 million more than estimated : normal and dividend tax revenue had been £600 000 more than estimated, supertax £390 000 more and excess profits duty £500 000 more. Overall the results for the year were down by £286 000 on the estimates.

Estimates for the coming year showed modest increases in most items, with the exception of diamond export duties and, understandably, excess profits duty whose revenue was only in respect of a few taxpayers whose assessments were several years in arrears. Normal tax was also expected to be slightly lower at £5,3 million, while supertax was budgeted at £2,6 million above the figure for the previous year.

The Minister announced that the miners' strikes on the Reef had cost £445 000. He had resolved to adopt the European method of containing expenditure rather than increasing the tax burden in order to balance the Budget. This would involve retrenchments from the Public Service. In addition he would use revenue from land sales and mining leases. (Some £1 000 000 was saved through abolition of cost of living allowances and retrenchments.

Public works and posts and telegraphs suffered the largest retrenchments, while chief contributors via actual remuneration adjustments were Defence and printing and stationery. These decisions accorded with the logical areas in which to seek reductions at such a stage.)
The net result was expected to be a deficit of £349 000.

INCOME TAX ACT 1922

The Income Tax Act No. 23 of 1922 (79) was assented to on 10 July 1922 and merely confirmed the rates of income tax and supertax as unchanged for the coming year.

Income Tax Cases

1. The case of Rex v Assiazsky, Sher and Levin (80) came before Mr Justice Benjamin in the Cape Provincial Division of the Supreme Court on 5 and 19 March 1923. The defendant partners were charged under section 96 of the 1917 Act with having falsified their tax returns. Section 90(1) stated that any person who:

   (a) knowingly or wilfully made a false statement in any returns, or;
   (b) by falsehood, wilful neglect, fraud, and or contrivance whatever, evaded or attempted to evade assessment or taxation;

   would be guilty of an offence and liable to a fine of £100.

In addition, a conviction under (b) could be punished by the imposition of double tax.

In the Magistrate's Court, the partners were found guilty under section 96(1)(b) and held liable to the double tax.

On appeal, the Supreme Court held that the offence of falsifying returns fell under section 96(1)(a), which did not carry with it the penalty of double tax. Section 96(1)(b) related to other offences, such as falsifying books, to evade tax. Consequently the taxpayers were not liable to double tax.

Consequent change in legislation

Section 44 of Act 40 of 1925 (81) made provision that a person who defaulted in rendering a return would be liable to treble tax, and one who 'omits from his return any amount which should have been included therein' would be subject to double tax on the amount so omitted. This wording effectively eliminated the loophole exploited by Assiazsky, Sher and Levin.

Section 69 of the 1925 Act (82) provided that any person who with intent to evade tax or to assist another to evade tax:

(a) falsified a return, or;

(b) gave a false answer to the Commissioner, or;

(c) prepared false books, or;

(d) made use of any fraud, act or contrivance whatsoever;

would be guilty of an offence and liable on conviction to a £500 fine or 2 years' imprisonment or both.

Thus was the loophole doubly closed.

2. Income Tax Case No. 6 (83) was heard by the Special Court in the Cape Province on 18 June 1923. The appellant had received a sum of money in commutation of a service agreement and commission when the company employing him went into liquidation. He claimed that this sum was capital in nature, but the Commissioner disagreed and the taxpayer appealed to the Special Court.
After a most interesting discussion on the subject of capital and revenue, the Court found that the payment was properly deductible by the payer as being in the nature of a business expense and was therefore duly taxable in the hands of the recipient. A sum received or paid was not necessarily capital merely because it was a lump sum.

<u>Consequent change in legislation</u>

The Income Tax Act No. 40 of 1925 (84) ensured that such an argument would not reach the courts again by providing in the definition of 'gross income' at paragraph (c): 'any

amount so received or accrued in commutation of amounts due under any contract of employment or service'.

3. Income Tax Case No. 7 (85) took place before the Special Court in the Cape Province on 26 June 1923. The appellant had earned substantial dividends, but at the same time had sustained trading losses. He sought to reduce the former by the latter in arriving at the amount subject to supertax.

In other words, he treated 'taxable income' as a negative figure. The Commissioner disagreed and the case commenced.

The Court held that 'taxable income' in section 6 of the 1917 Act was defined as an 'amount remaining', which phrase implied a positive figure. Further, section 27, in describing the method of arriving at the amount of income subject to supertax, spoke of 'the aggregate of .....' thus implying a positive amount. In neither case was there any suggestion of negative amounts entering the calculations, and judgment went accordingly against the taxpayer.

Consequent change in legislation

In a rare instance of the Act changing in favour of the taxpayer after the Commissioner had won a case, section 30 of Act 40 of 1925 (86) provided for assessed losses to be deducted in calculating income subject to supertax.

4. Income Tax Case No.10 (87) was heard before the Special Court in the Cape Province on 22 June 1923 and raised the question of trusts for the first time. The taxpayer had created a trust in favour of his minor children, reserving the right to revoke wholly or partially and to alter the terms relating to his wife or children. He was never allowed to benefit from the trust, and neither was anyone else other than his wife and children. However, he administered the trust. The Commissioner taxed the income of the trust in the hands of the taxpayer, who appealed on the grounds that the trust was a separate taxable persona. The Court held that an irrevocable trust had been created and therefore the taxpayer was taxable only in a representative capacity.

   (Note: Although the findings in this case were not countered in the 1925 Act, under present legislation the income of the trust would be taxable in the hands of the taxpayer. Indeed, this provision was already apparent in the Income Tax Act No.31 of 1941 (88) at sections 9(3) and (4)).

5. On 18 June 1923, the case of City & Suburban Gold Mining and Estate Company Limited v CIR (89) came before the Natal Provincial Division of the Supreme Court. The case related to sections 38(a) and 45(f) of the 1917 Act and the facts were as follows: the company had ceased its gold mining operations and sold most of its assets, receiving shares in return for these. It intended to sell its remaining assets

piecemeal and then to go into liquidation. Accordingly the shares received as proceeds for sale of assets were distributed to the shareholders. The Commissioner treated these as dividends in the hands of the shareholders in terms of section 38(a) of the 1917 Act which included in the definition of 'dividend': 'any sum of money or the equivalent of money.....distributed......to its shareholders'. (90) The company objected, claiming firstly that the distribution was of capital, as the profits were capital in nature; and secondly that it was made in the course of winding-up and was thus exempt from tax in terms of section 45(f) of the 1917 Act, which exempted from the dividend tax 'any dividend distributed on the winding-up of a company, in so far as such dividend represents the distribution of capital assets'. (91)

The Court held that such distributions, whether capital or revenue in nature, fell into the definition in section 38(a); and further that, as no attempt had yet been made to place the company in liquidation, the provisions of section 45(f) could not protect the distribution.

Principles established in this case

These two aspects of the treatment of distributions by companies still exist and form part of subsequent legislation.

6. The case of CIR v Lunnon (92) was heard by the Appellate Division on 16 and 17 October 1923, on appeal from a decision in the Transvaal Provincial Division of the Supreme Court. The taxpayer had been obliged to resign as director of a company after a period of 20 years' service, when it moved its activities from Pretoria to Johannesburg. His emoluments had been paid to the date of his departure. At the annual general meeting following his resignation, he was voted a sum in recognition of his services during his years with the company. The Commissioner sought to tax the amount as being for services rendered, but the taxpayer claimed that it was a capital receipt. Having lost in the Supreme Court, which had described the payment as a non-obligatory, non-recurring payment, not arrear salary or fees and not in respect of any claim by the taxpayer, the Commissioner had recourse to the Appellate Division. The Appeal Court held that the payment was a donation and not taxable, being in the nature of capital.

In the course of his judgement, Innes C J, who certainly contributed mightily to the development of tax principles in South African case law, said that income resulted from the product of capital invested or from the use of labour and wits. This payment had been neither; the element of annuality, although not decisive, had to be considered and was absent in this case. The words: 'any other benefit or advantage of any kind granted in respect of employment' (93)

in section 6 definition of 'gross income' did not refer to voluntary gifts.

Principles established in this case

1. Income results from the product of capital invested or from the use of labour or wits.
2. Annuality is an element of income, albeit not a decisive one.

Consequent change in legislation

Section 7 of Act No. 40 of 1925 (94) included in the definition of 'gross income' amounts received:

(b) for services rendered whether due and payable under a contract or not.

It is not clear whether or not this was an attempt to avoid a repetition of the defeat in Lunnon's case. In any event, Lunnon would probably still have won, because the payment had been found to be capital, and was therefore not susceptible of taxation.

BUDGET 1923 - 24

Mr Burton presented his Budget (95) for the 1923/4 fiscal year on 28 March 1923, and commenced with bad news in respect of the current year. The estimated deficit of £349 000 had grown, first to £900 000 and then to £1 350 000 after taking to revenue account a sum of £800 000 which properly belonged in the loan fund. He proceeded to paint an even blacker picture of the true position.

On 1 April 1922 there had been a deficit of £1 149 000 which, together with the current deficit gave a total shortfall for the last two years of £2 499 000. In fact, he went on, the position was even worse if one went back three years and took account of certain figures which had been credited to revenue account instead of to loan account.

The 1919/20 surplus of £460 000 had been so dealt with, as had loan receipts of £934 000 in 1921/22 and £800 000 in 1922/23. Taking these figure into account, the real shortfall for the last three years had been no less than £4 693 000. Chief contributors to the deficit in the current year were the various Inland Revenue receipts: income tax had generated £1 742 000 less than expected; stamp duties £800 000 less; excess profits £30 000 less; and death duties £180 000 less. As against this, customs receipts had risen by £100 000 and expenditure fallen by £713 000. The Minister explained that the disturbances on the Witwatersrand had reduced exports: gold exports had fallen by

£5 140 000 and coal by £880 000. In addition, the severe drought had decimated agricultural exports to the extent of a £1 240 000 reduction in maize meal and £65 000 000 in sugar. Appendix 14 discusses the findings of the Drought Investigation Commission published in October 1923.

For the current year, expenditure was expected to be £28 561 000, down by £552 000 in comparison with the previous Budget but £161 000 more than the revised estimates for the current year. Revenue was expected to be £27 755 000, an increase of £1 508 000 on the revised estimates for the current year. Thanks to improvements in trade and a good agricultural season, customs revenue was expected to increase by £3 544 000. Inland revenue receipts were expected to rise by £878 000 to £16 586 000, with gold and diamonds contributing increases of £571 000 and £437 000 respectively, income tax £345 000 and death duties £235 000. Diamond export would also increase by £190 000. Total revenue was estimated at £27 755 000, leaving a deficit of £896 000. Accumulated with the deficits for the previous two years, this meant that the shortfall over the last three years stood at some £3 400 000.

Clearly, this deficit would have to be met, at least in some degree. The Minister proposed increases in various duties, mostly on patent medicines and protective clothes, to produce £260 000, and a lower scale of pay in the public service which would save £200 000. The balance of £436 000 would be more than covered by his proposal to take £1 065 000 from loan receipts

into revenue account.

## INCOME TAX ACT 1923

The Income Tax Act No.19 of 1923 (96) contained only two sections which retained the rates of income tax and supertax in force in 1922.

## Income Tax Cases

1. Income Tax Case No. 11 (97) was heard before C J Ingram in the Cape Province on 9 June 1924. The taxpayer had contributed £36 towards the maintenance of his indigent mother, and he claimed the abatement for dependants in terms of section 7 of the 1917 Act, as amended by Section 3 of Act 29 of 1921. (98) The Commissioner disallowed the claim, contending that the abatement was available only if the recipient was wholly dependent on the taxpayer; in this case the brother of the taxpayer also contributed towards the maintenance of his mother.

   The Court held that Section 7(1)(c)(v) of the 1917 Act used the phrase 'mainly responsible' (99) in respect of the financial relationship between taxpayer and recipient; the taxpayer would probably have qualified as being 'mainly responsible' in this case. However, Section 11 of Act No. 45 of 1920 had redefined 'dependant' in the following terms: 'such person.....has been maintained throughout the year of assessment at the expense of the taxpayer.' (100) This

revised definition led the Court to conclude that the intention had been that the taxpayer should be the sole contributor to the dependant in order to claim the abatement, and judgment went accordingly against the taxpayer.

Consequent change in legislation

Section 72 of Act 40 of 1925 defined 'dependant' in terms of the amount spent on an otherwise qualifying person, and not in terms of the extent of responsibility of the taxpayer towards the recipient. The taxpayer was obliged to spend not less than £30 per annum in order to be able to claim the abatement.

2. Income Tax Case No. 14 (101) was heard in the Northern Areas Special Court during July 1924 before Mr G T Morice K C. The taxpayer in this case sought in terms of section 66(2) of the 1917 Act as amended in the schedule to the 1919 Act to claim the deduction of alimony paid to his former wife. The relevant section read: 'Any amount payable by way of alimony to one spouse......under any judicial order....of separation......shall be assessable only in the hands of (the) spouse (to whom the payment is made)'. (102) The Commissioner disallowed the claim on the grounds that the section did not apply to divorced persons, but only to judicially separated spouses, and the taxpayer appealed to the Special Court.

The Court held that it did not appear reasonable to exclude payments by divorced persons in respect of judicial orders of divorce, and judgment went in favour of the taxpayer.

Consequent change in legislation

Section 39(3) of Act No. 40 of 1925 specifically mentioned both divorce and separation. (103)

## BUDGET 1924-25

The Budget for the 1924/25 fiscal year was the first of many to be delivered by Mr N C Havenga, Minister of Finance in the newly elected 'Pact' Government. This administration had come to power in the General Election of 1924 and was made up of the combined forces of the National and Labour parties. Traditionally, elections in South Africa have been fought on political issues, and the 1924 contest was no exception: financial issues have tended to play a secondary role, although any government would be at some disadvantage, whatever its political stance, if it had presided over a period of depression and high unemployment. Such was the case in 1924; the country had been through four years of depression accompanied by stringent fiscal policies so unpopular that they effectively ended the political career of their architect, Henry Burton. In his book (104) L E Neame says of Burton in a passage which eloquently reflects both the financial state of the country and the mood of the voters in the

years leading to the 1924 election:

"....from the outset his task had been an impossible one. He took over a bankrupt Treasury in 1920. He was like the Chancellor whom Peel described as "seated on an empty chest by the side of bottomless deficiencies, fishing for a Budget."

Revenue fell so fast that increasing taxation could not keep pace with it. "I am afraid the Budget will shock the country" he remarked ruefully when introducing his 1921 financial statement. It did. But the shock of the deficit was slight compared with the shock of Burton's subsequent remedial measures.
"Of all the qualities in public life, courage is the rarest" is one of Lloyd George's favourite sayings. There was the highest moral courage in Burton's handling of finance between 1921 and 1924. Even his ingrained belief that he is always right could hardly have closed his eyes and ears to the ever-growing hostility he was creating in the outer world. But he strode on. And not apologetically. He fought for his policy as though he gloried in it, and defended it with all the fire of the fanatic and the skill of the trained legal mind.

'He lived through a nightmare of retrenchment and increased taxation. He cut loan estimates - and departmental expenditure - and cost of living allowances - and income-tax exemption - and public service salaries. He doubled postage rates and match duties; thrust extra taxation on spirits, beer, estates and all manner of things; put an excise on tobacco; and enforced all

over the Union a patent medicine tax which Mr Hull had swept away in 1911 because it was irritating. Somebody said that the art of taxation lies in plucking the feathers from the goose with as little squealing as possible. Burton had no time to pick and choose. He tore out feathers by the handful. The squealing was deafening. To an Opposition long hungry in the wilderness it was as though political manna fell from Heaven. Every chemist's shop became a recruiting station for Hertzogites and Labourites.

'But Burton set his teeth and stuck to his rough task. In the end he straightened out finance. But neither he, nor the Government of which he was a member, survived to reap the benefit of his work. He was the Great Disillusionist. And the public hated to be disillusioned.

'His fate was that of the scapegoat mentioned in the sacrificial rites laid down in Leviticus. Like the goat Aaron was instructed to select by lot to bear all the iniquities of the people, Burton was sent away "into a land not inhabited .....into the wilderness." The reward of his labours was rejection by Ladismith. No other constituency appeared to desire to be represented by him in Parliament. He vanished from political life, and for a long time never even made a political speech. Perhaps he was wise, "For silence after grievous things is good."'

Clearly the unpleasant, if necessary, fiscal measures of the past few years had an effect and contributed towards bringing down a Smuts Government tainted by Unionist membership and increasingly alienated from the grassroots Afrikaner voting public.

In his speech, delivered on 30 July 1924, (105) Mr Havenga announced that the revenue for the year just past had been £24 253 000, about £2 500 000 less than had been estimated. However, actual expenditure had been only £24 028 000, a reduction of £3 500 000 in comparison with the estimates. As a result, the country had enjoyed a surplus of £225 000, reducing the accumulated deficit to £1 919 000.

Sources of increases in revenue had included customs, postage, telephones and receipts from Government-owned mines, while reductions had been experienced in excise, telegraphs , licences, income and supertax, excess profits duty and the diamond export duty. The taxes on gold mines had increased by £328 000 (income and dividend tax), but those from diamond and other mines were lower by £116 000. General income and supertax had decreased by £224 000 and £194 000 respectively.

Estimates for the current year were £24 346 000 for expenditure and revenue of £24 234 000. The small deficit of £112 000 would be covered by strict economies, thus ensuring that there would be no need to increase the rates of taxation. An anticipated general improvement in the economy was expected, and this would result in increased imports, mining revenues and postal and

telephone income, as well as increases in income taxes amounting to £265 000.

Coming, as it did, less than one year after issue of the Report of the Drought Investigation Commission (106), the debate provided the first opportunity for representatives of the rural community to address their appeals for concessions to farmers with the support of the recommendations of the Commission. Four members did this, and their proposals were obviously based on those recommendations.

First, Mr G C van Heerden, (Nationalist) moved an amendment in the following terms to Act No. 25 of 1924, which went no further than to maintain the rates of tax in force in 1923:

'Provided that section seventeen of the Income Tax (Consolidation) Act, 1917, be amended so as to allow the deduction, from the income of a person carrying on pastoral operations, of such expenditure as has been incurred by him for the purpose of watering stock, in sinking boreholes and erecting the necessary machinery for the extraction of water therefrom.'(107)

Sir Thomas Smartt (SAP) supported the proposal of Mr van Heerden, and made the point that the tax lost initially would be recouped by the subsequent increased tax the farmer would pay. (108)

Brig-General W Arnott (SAP) then proposed that the cost of fencing be allowed as a deduction from taxable income, as an encouragement to farmers 'to do their duty and erect more fences'. (109)

Finally Mr C J Krige (SAP) endorsed the remarks about fencing. (110)

Mr Havenga replied in terms which indicated that his Government had not yet had time to react fully to its victory and introduce the agricultural measures for which it had striven from the Opposition benches in previous Budget debates. He appealed to Mr van Heerden not to press the amendment as it would lead to a discussion of the whole field of income tax and numerous proposed amendments. The proposal would 'receive due consideration next year.' (111)

## INCOME TAX ACT 1924

The Income Tax Act No 25 of 1924 (112) merely provided for retention of the rates of taxation in force in 1923.

### Income Tax Cases

1. L Berman + Others v Rex (113) was heard on 6 March 1925 in the Cape Provincial Division of the Supreme Court before Searle J and Watermeyer J. The appellants in the case were virtually illiterate and employed a bookkeeper to maintain

their records. They signed their income tax returns in blank and relied on the bookkeeper to complete and submit them. He falsified the figures in the returns and the appellants were subsequently charged under section 96(a) of the 1917 Act, on the grounds that they had 'knowingly and wilfully made a false statement.' (114) They were found guilty in the Magistrate's Court and appealed to the Cape Provincial Division.

The Court held that it was unable to find that knowingness and wilfulness had been proved. It was unfortunate, in the opinion of Searle J, that the section was phrased as it was.

Comment

Act 40 of 1925 (115) stated at section 69: 'any person who with intent to evade......taxation, makes any false statement or entry in any return rendered in terms of this Act; or signs any statement or return so rendered without reasonable grounds for believing the same to be true.' Strangely enough, this section was not extended to include negligence, which would probably have resulted in a finding of guilty in this case.

2. On 11 and 16 March 1925, Mr G T Morise K C presided in the Northern Special Court in Income Tax Case No. 17. (116) The Appellant company had sold most of its assets in exchange for shares in another company. A third company then made an

offer for much of this parcel of shares at a substantial profit. The offer was made to four individuals; three directors and a substantial shareholder. The board of directors then decided to sell the shares to the four individuals at a nominal value; the latter sold them to the purchasing company and distributed the profit pro rata to all the shareholders. The stated intention of this series of transactions was to avoid the payment of dividend tax. The Commissioner contended that:

(i) the distribution was in reality a distribution by the company;
(ii) the whole transaction was a process of evasion and therefore null and void.

The Court held that:

(i) on the facts, the distribution had not been made by the company;
(ii) because there had been no attempt at concealment, there could not be said to have been fraud or deception. It had been a legitimate scheme to avoid tax.

(Comment: Under Section 103(1) of Act 58 of 1962,(117) the taxpayer would have some difficulty in winning today.)

BUDGET 1925 - 26

On 8 April 1925, Mr N C Havenga presented his second Budget as Minister of Finance. (118) In so doing, he was able to indicate for the first time the thinking of his fledgling Government in matters financial, and particularly relating to income tax. Instead of once again amending the 1917 Act, the Minister introduced an entirely new Bill, which came to be the Income Tax Act No. 40 of 1925. (119)

Mr Havenga reported that revenue for the current year had exceeded the estimates by some £1 100 000, chief contributors having been customs, posts and telegraphs, diamond export duty and income tax. These increases reflected a general improvement in the business climate and higher dividends paid. Expenditure had exceeded the estimates by very little, about £200 000 in fact, and as a result the country had enjoyed a surplus of £800 000.

For the coming year, a deficit of £457 000 was anticipated on revenues of £25 822 000. Diamond mines were expected to produce £307 000 more than in the previous year from the three sources of revenue which they provided: Government-owned mines, export duty and income taxes. General income tax would continue its trend of generating increased revenues to the extent of £145 000, while the gold mines would produce £1 570 000 with the disappearance of the premium. (120)

The Minister announced the repeal of the Dividend chapter of the Income Tax Act, (121) stating that it had originally been introduced to tax companies on two bases; firstly on assessed profits and secondly on dividends distributed. Together these taxes would yield an amount approximating the previous level of company taxation. Unfortunately, this aim had not been realised, because of 'well thought out, organized methods of avoiding the payment of dividend tax, which are becoming more widespread every day, either by withholding distribution of profits or by distributing them disguised in a form that lays the onus on the revenue department of establishing that there has been a distribution of profits and not of capital.' (122) Clearly the Minister was echoing the frustration of the Department of Inland Revenue at the findings of the Court in ITC 17 (second case discussed in 1924 above) and, no doubt, similar situations. (123)

'What is said above', he continued, '......applies equally to supertax......'. (124) '.....the Commissioner's powers (to counteract these methods) have proved to be quite illusory in effect'. (125)

It had therefore been decided to revert to a single flat rate of tax on profits. Gold and diamond mining companies would pay 3/- in the £, and other companies 2/6d in the £. The £300 abatement would be introduced, sliding off at the rate of £ for £.

On the subject of farming, it was hardly surprising that he announced the re-introduction of the right of farmers to choose whether they wished to be taxed on the stock basis or the cash basis. In addition, there was to be an amortisation allowance in respect of the cost of boreholes and windmills incurred by farmers.

In a clear indication that the tax avoidance industry was beginning to come into its own, the Minister stated: 'There are other minor amendments for tightening up the provisions of the Act so as to prevent leakages that experience of the administration of the Act has brought to light'. (126)

As finally promulgated, the taxation proposals were as follows:

- gold and diamond companies : 3/- in the £, compared with 1/6 in the £ plus 1/6 dividend tax;
- other companies : 2/6 as compared with 1/6 and 1/-;
- insurance companies : 1/6 in the £;
- individuals, societies, trusts and similar classes of taxpayer : 1/- plus 1/2000d per £, up to a maximum rate of 2/- per £;
- private companies, previously taxed at the individual rate, would henceforth be taxed as companies;
- supertax, previously applicable only to individuals, would in future be payable by all taxpayers other than companies;
- abolition of the dividend tax, which had required 'complex provision to guard against evasion', resulting in 'much litigation and difficulties in administration'. (127)

Mr P Duncan (SAP) criticised the fact that companies were more heavily taxed than individuals. He maintained that it was wrong to talk of companies as if they were 'some sort of creature'; (128) effectively it was the shareholders who were being taxed. This meant that a person would be penalised for investing his money in a company instead of into Government stock. The country needed foreign investment in order to develop its resources. The most obvious way to attract capital was through industrial and commercial companies and it seemed illogical to discourage such investment through a tax system which was punitive to companies.

Mr J J M van Zyl (Nationalist) pleaded for tariffs to protect the wine farmer in the same way as grain and cattle farmers had been provided for. (129)

Mr R Stuttaford (SAP) took the Minister to task at some length about the inequity of taxing income earned via companies more heavily than that earned in the hands of individuals. He took the argument of Mr Duncan further by quoting examples of what he felt was the unfair way in which investors in private companies were penalised. (130)

Mr J P Louw (SAP) appealed for an increase in the excise tax on whisky and the elimination of the tax on mutual life assurance societies. This would encourage people to take out life assurance and so provide for their old age. (131)

Mr J G Keyter (Nationalist) spoke against the Estate Duty Act, calling it the 'robbery and plunder Act', (132) an appellation he attributed to the farming community.

Col. Sir David Harris (SAP) criticised the large tax burden borne by the diamond mines, much of which was in order to compensate for the number of industrial companies which had 'been dodging the present Income Tax Act. If they have been dodging it, get at them, but don't punish me and the concerns I am interested in which are practically taxed to the hilt, because they know industrialists and merchants have been clever enough to circumvent - I won't say evade - the present Income Tax Act. Now I am quite positive that there is not a greater factor in causing unemployment than heavy taxation'. (133)

Later in Committee, the Minister drew attention to abuses employed by persons operating via companies and against which abuses the decision to tax all companies on a uniform basis was arrived. A man would form a company or a trust and divide the profit between himself and his five sons, thus avoiding the payment of supertax. In addition, exorbitant salaries would be paid to reduce the profits of companies. It was these abuses which he wished to eliminate by the proposed legislation. (134)

Clearly the new Government was not departing radically from the established legislation. The fact that both main parties differed to no great extent in their respective fiscal philosophies has already been canvassed (see comment on the

Budget debate in 1921; the 1925 Act bears this out.)

## INCOME TAX ACT 1925

The Income Tax Act No. 40 of 1925 (135) covered 40 pages divided into three chapters. It clearly drew heavily upon the experience of the fiscus in administering its predecessor over the years 1917 to 1924.

Chapter I was virtually the same, merely streamlining the wording without substantially altering the meaning or intention.

Chapter II dealt with Income Tax, and Part I with Normal Tax, as was the case in the 1917 Act. The 1925 Act alleviated the need formally to confirm the rates of tax each year by stating at section 5(2) that the rate in force at any time would continue if no rate was passed by Parliament in respect of any particular year. (136)

Section 6 stated the rates applicable to the 1925/6 fiscal year, which were as indicated in the Budget speech namely, in respect of each £1 of taxable amount:

- gold or diamond mining companies : 3/-;
- life assurance companies : 1/6;
- other companies : 2/6;
- persons other than companies : 1/- + 1/2000d per £ , up to a maximum of 2/-.

Section 7, the equivalent of section 6 in the 1917 Act, defined various terms used in the Act, beginning with 'gross income'. While still cast in deliberately broad terms to include receipts and accruals from actual or deemed sources within the Union, the definition specifically included certain items whose nature could have rendered their inclusion in gross income arguable. Indeed, two of them had been the subject of court cases, as discussed earlier in this Chapter at the 1922 tax year (CIR v Lunnon and Income Tax Case No. 6.) These were: amounts received or accrued in respect of services rendered, whether in terms of a contract or not; and amounts received or accrued in commutation of amounts due under service contracts. The remaining items specifically mentioned were: annuities more clearly mentioned than in 1917; premiums for use of assets (not mentioned in 1917); remuneration in kind (more tidily described than in 1917); and recoupments of capital expenditure on mining operations in excess of the redemption allowances (although no case had been fought on this point, the fiscus apparently wished to forestall any claim that such an accrual was in the nature of capital).

Whereas the 1917 Act included its description of deemed sources of Union income in its definition of 'gross income', the 1925 Act accorded this important topic a section on its own; section 9.

Finally in section 7 the 1925 Act deemed it necessary to include an enlarged definition of 'trade'. It included 'every

profession, trade, business, employment, calling, occupation or venture including the letting of any property.' (137) Section 16 of the 1914 Act (138) had provided a brief definition of 'trade' which had been repeated in the 1917 Act.

Section 8 sustained the provision that income reinvested or otherwise accumulated on behalf of a taxpayer nevertheless accrued to him, but relocated the pastoral provisions which had somewhat inappropriately been included in the corresponding section of the 1917 Act. (139) The provisions of section 9 deeming certain income to be from sources within the Union was similar to its corresponding section in the 1917 Act, with the addition of a subsection deeming income from employment from a Government body also to be from a Union source. Then in addition to sustaining the method of taxing the income of married women, the section deemed that the income of any minor child, which was derived either directly or indirectly from its parent, was income of the parent.

Section 10 dealt with exempt income and to a large extent merely improved the wording of the corresponding section of the 1917 Act. For example, 'receipts' in the latter was described as 'receipts and accruals' in the former. One substantive addition was the exemption of awards made to persons under the miners' phthisis laws.

Section 11 dealt with allowable deductions and was similar to its predecessor, with the addition of paragraph (g) permitting the deduction of bad debts incurred in the course of trade. The section also described 'assessed loss' as such for the first time; the 1917 Act had used somewhat clumsy wording.

Sections 12 and 13 listed the prohibited deductions in similar terms to the corresponding sections of the 1917 Act.

Section 14 listed the abatements deductible from taxable income. These varied in only one respect from those provided for in the 1917 Act as amended; the child abatement was increased from £50 to £60.

Section 15 gave farmers the right to decide whether they wished to include their opening and closing values of livestock on hand, or whether they wished to exclude these values and be taxed only on proceeds of livestock sold. In addition, the section permitted persons carrying on pastoral operations to deduct from their income from that source any expenditure on boreholes or pumping plant.

Section 16 dealt with the assessment of foreign shipowners, in terms similar to those in the preceding Act.

Section 17 taxed submarine cable or wireless business on the same bases as did the 1917 Act.

Section 18 provided for the taxation of goods sold by South African resident agents on behalf of foreign principals at the rate of 5%.

Section 19 taxed persons whose businesses extended beyond the borders of the Union on the same basis as did Section 14 of the 1917 Act.

Section 20 made familiar provisions for taxation of insurance businesses.

The taxation of the income of public servants was provided for in section 21 on the same basis as in the 1917 Act.

Section 22 empowered companies to deduct from debenture interest paid the corresponding amount of normal tax which they had paid on such interest. Section 20 of the 1917 Act had made a similar provision.

Sections 23 and 24 whose predecessors had also borne the numbers 23 and 24, provided similarly for calculation of the redemption allowance in mining operations.

Part II of Chapter II dealt with super tax (previously known as supertax). The rate began at 1/- in the £ and increased by 1/500d per £ up to a maximum of 5/- in the £. In other words, the maximum rate was reached at an income of £24 000. In comparison, the 1917 Act had a limit of 3/- in the £, and this

was reached at an income of £48 000.

In most other respects, the provisions of the two Acts were similar. The 1925 Act, however, incorporated the three amendments necessitated by the findings in CIR v Collins (discussed in this Chapter at the 1919 tax year), Income Tax Case No. 23 (discussed in this Chapter at the 1921 tax year) and Income Tax Case No. 7 (discussed in this Chapter at the 1922 tax year) respectively.

It will be recalled that in CIR v Collins, the Court was unable to fault the act of capitalising profits by the issue of bonus shares, thus avoiding the distribution of dividends which would have been subject to supertax. Section 29(c) of the 1925 Act prevented repetition of this ploy by providing that there should be included in the income subject to super tax an amount equal to the nominal value of such bonus shares issued.

Section 32 was worded in such a way as to give the Commissioner the right to include in income subject to super tax such amount as he deemed fair and reasonable, if in his opinion the dividends distributed were insufficient in relation to the accumulated profits available. In Income Tax Case No. 23, the Commissioner had sought unsuccessfully to persuade the Court to interpret the phrase 'profits available' in section 6 of the 1917 Act to mean 'accumulated profits available'.

The wording of section 30 ensured that the Commissioner would not win again as he had in ITC 7, by providing that any balance of assessed loss for normal tax purposes would be deductible in calculating the amount of income subject to super tax.

Chaper III dealt with general provisions and was largely unremarkable, except for a few changes in comparison with the 1917 Act to take into account the findings in several court cases. Further, such differences as there were reflected a desire to phrase sections better or to improve administration. The first section to include a substantial change was section 39(3), which ensured that alimony paid would be deductible in the hands of the payer and taxable in the hands of the recipient, regardless of whether it was paid in terms of a divorce order or an order of judicial separation. This provision enshrined in legislation the findings of the Court in Income Tax Case No. 14 (discussed in this Chapter at the 1923 tax year).

Sections 44 and 69 ensured that the findings of the Court in Rex v Assiazsky, Sher and Levin (discussed in this Chapter at the 1922 tax year) would not be repeated. Section 44 provided that omission from a return of any amount which should have been included would result in a penalty amounting to double the tax involved, and section 69 provided that any fraudulent activity relating to tax evasion was punishable with a fine of £500 or two years' imprisonment or both.

# CHAPTER FIVE

# CONCLUSION

POLITICAL AND SOCIO-ECONOMIC INFLUENCES

By its very name, an Income Tax Act may be expected to provide the means of garnering for the fiscus sufficient funds from the private sector to meet the difference between revenue from other sources and expenditure by government. Incentives and disincentives to various sectors of the economy, and the achievement of particular political or socio-economic objectives are not by their nature obviously at home in income tax legislation.

This idealistic view is gainsaid in the very first Income Tax Act, No. 28 of 1914, albeit on a small scale. Section 5 exempted non-residents from tax on income from government stocks. By no stretch of the imagination can such a provision be seen as part of the tax-gathering machinery; the only reason for its existence can have been to encourage foreign investment in government stock at a time when the country was in the process of becoming established and every source of foreign exchange was welcome. The 1915 Act introduced the first incentives to people to provide for their own old age, by means of the abatements in respect of premiums on life insurance policies and contributions to friendly or benefit societies. Of course, it could be argued that such concessions are closely related to income and therefore are at home in income tax legislation; however, they substantially result from socio-economic needs - it is clearly socially, economically and indeed psychologically bad to have

large numbers of elderly people dependent for their livelihood, after a lifetime of toil, on charitable and insufficient handouts from the State.

The 1916 Act provided that the newly-introduced abatements would be reduced to the extent that taxable income exceeded £500. There seems to be no logical reason for this from the tax-gathering point of view; the greater amount of tax received by the fiscus as a result of this proviso can surely not have been so material as to constitute a major source of revenue. Rather this proviso may be seen as a gesture to the largest group of voters: the poorer, working class. These people might then see the government as being concerned for their welfare and expressing this by shifting some of their tax burden to the rich. At the same time so small an additional burden would not gravely alienate the feelings of the wealthy. In this way the tax law was used to score a political point in an inexpensive and painless fashion.

The imposition of supertax in 1916 was a far more material change and certainly more justifiable from every point of view. Provided the additional burden does not become so great that entrepreneurs, the lifeblood of any developing capitalistic economy, are discouraged altogether, it is eminently sensible to tax those who can afford it more severely than those who exist close to the starvation line.

The 1917 Act recognised that churches, charities and educational institutions deserved support as members of the social community. There was probably no more obvious way of rewarding contributions to these institutions than via the Income Tax Act : but the fact remains that provision for their support by the public has no direct relevance to the gathering of taxes.

The 1919 Act continued the theme of encouraging people to provide for their own retirement by allowing employers to deduct contributions to various funds. This concession was far more attractive than merely permitting an abatement for such payments.

The 1920 Act added to the incentives to foreigners to invest in government stocks by providing in section 10 an incentive to residents to make such investments. Such investments were deemed to be capital employed in the hands of investment dealing businesses. Were it not for this provision, profits on sale of such investments would have been taxed. In addition, section 100 broadened the definition of 'dependant'; this encouraged, if only to a small degree, the relief to the State of the burden of helpless people or children. Here again, a socially desirable objective was sought to be achieved via income tax legislation.

It may be seen, therefore, that from its very inception the income tax legislation of South Africa has gone beyond the function of merely balancing the revenue and expenditure account of the State and has been a vehicle by which the government has tried to achieve socially and economically desirable objectives.

It is predictable that the effect on income tax legislation of events on the national or international stages derives from any loss of State revenue which such events may cause. In consequence, rates of tax must be adjusted accordingly. Often such events affect sources of revenue other than income taxes, such as customs revenue.

The very first income tax legislation in the Union came into being as a result of outside factors: the South Africa Act, as mentioned in several budget speeches and discussed in chapters 2 and 3 of this work, provided that revenue from the railways would cease to be a source of revenue to the Treasury by not later than four years after Union. This imposition in the founding Act of the Union certainly forced the introduction of the Income Tax Act.

The 1915 Act placed upon taxpayers the burden of the first World War; the deficit of more than £2 million caused by the cost of entering the conflict, and the expected increased rate of expenditure, resulted in a reduction of the tax-free portion of income and an increase of between 33 1/3% and 100% in the rate of tax. In addition, the gold mines were required to pay a special war levy.

The 1916 Act contained the next really major change to tax legislation as a result of the war. Despite an increase of some £2 million in customs revenue as the inevitable result of buoyant trading accompanying the war economy, the cost of prosecuting the war was outstripping the current level of revenue. This

situation led to the introduction of the supertax, as discussed in chapter 8 of this work.

The effect of the war was clearly evident in the Budget speech : customs revenues had fallen as a result of the pressure of shipping brought about by the submarine threat; estimates were difficult because of the uncertainty caused by this campaign; and all sources of revenue were tending to expand. As an additional means of meeting wartime expenditure, the dividend tax was imposed on companies. In addition, the excess profits duty came into being, which clearly derived its revenue base from the improved trading conditions engendered by the war.

The excess profits duty was doubled in 1919 as the country continued to need revenue for war expenses.

The 1920 Act was affected by a more peaceful outside source, namely the increase in both the price and production level of wool. Largely as a result of this improvement, allied to the growth of the industrial sector during the war, the existing sources and rates of revenue were filling the State coffers sufficiently to avoid any need for new or increased taxes.

By contrast, the wool and diamond markets had become stagnant by 1921, as the post-war recession struck the country simultaneously with the drought which had begun in 1919 and was reaching serious proportions. The 1921 Act was then used to bridge the gap between revenue and expenditure. Farmers were obliged to

include values of livestock on hand, a particularly heavy blow in the short term while they were assailed by drought and a reduction in demand for the wool clip. The rate of company tax was trebled to 1/6 in the £, alleviated by the disappearance of the excess profits duty and special war levy. It is questionable whether, in times of financial hardship, shortfalls in revenue should be covered by taxing more heavily the very groups affected by the adverse circumstances.

The miners' strikes of 1922 did not have any direct effect on the Act for that year, despite the reduction in revenue resulting from the smaller gold production. The shortfall was met by containing expenditure.

In the 1923 Budget speech the loss of exports resulting from the strikes was stated to be £5 140 000 for gold and £880 000 for coal. The effects of the drought on exports of farm products was also devastating. Fortunately, the improvement in weather conditions and trade in general had had the effect of enabling the tax rates to be maintained at their previous levels.

In 1924, rates were maintained in anticipation of a continuation of the economic improvements. The 1925 Budget speech confirmed that the improvement had indeed occurred.

It is fair comment, then, to conclude that outside events, sometimes not directly part of the economic fabric of society,

had a material effect on the development of income tax legislation in South Africa.

It is at the same time only fair to point out that it is totally idealistic to expect income tax legislation to retain a pristine purity unsullied by outside influences. It has never been suggested in this work that tax laws should operate in a vacuum; indeed, they respond to economic realities, and this response is a world wide phenomenon. The conclusion that outside events have had a material effect on the legislation is therefore not a criticism, but the identification of one of the sources of development of the legislation.

One could argue that the Government ought rather to have filled the gap between revenue and expenditure by means of loan finance. However, the South African fiscal approach has always been conservative and justifiably so. A realm of annual deficits met by money printing presses working overtime is a recipe for disaster, as witness numerous experiences in both the developed and particularly developing worlds. Let it be borne in mind that South Africa is a developing country which in 1910 to 1925 had far less sophisticated infrastructure than it now has. Improvident forays into fiscal irresponsibility would have been devastating to a country trying to establish its viability in the early years of its existence.

It is submitted that the fiscal measures adopted during the period were basically sound; unpopular, but sound. It is

beyond the scope of this work to delve into the exact cost of the drought; suffice it to say that agriculture was then, perhaps even more than now, a critically important part of the economy. The drought must have had very serious consequences at this stage in the development of the country, coupled with the world depression. During any prolonged drought, not only is revenue lost, but other revenue must be used to import food, sustain needy farmers, cater for reductions in commercial turnover as a result of reduced buying power of the farmers, and take care of the inevitable costs, both social and financial, of processing dispossessed farmers entering urban areas.

Any one of drought, international recession, or internal trade slumps occasioned by reductions in mining production, is likely to make things difficult for an economy; all three occurring simultaneously is a dreadful burden.

In such a situation, where can a Government turn, but to its people? Of the several ways of so turning to the population, direct taxation is an obvious one : easy to apply, flexible if it needs to be selectively applied, and proceeds easily calculated. In short, there can be no real argument against the tax policies of the time insofar as they were affected by outside events.

The unfortunate aspect, however, is that later Governments never knew when to stop tinkering with tax legislation in order to achieve other ends. This argument is beyond the scope of this work, but it may be briefly pointed out that the current Income

Tax Act has become so laden with incentives that the legislature is now in the process of dismantling them in favour of cash incentives. The Income Tax Act has evolved into a huge, cumbersome machine for redistributing income in the process of encouraging such aims as: investment in capital equipment, increasing exports, moving to economic development areas. It has become totally unwieldy, in fact; and this is a pity, because fundamentally it is a sound piece of legislation.

Now, as far back as the period covered by this work, the lawmakers saw fit to use the tax law in this way. No one could seriously fault this, particularly since it was done to a relatively miniscule degree. However, with the benefit of hindsight, perhaps the tax legislation of the country would have been better today had not the legislators in the second decade of the century driven in the thin edge of the wedge which today is so firmly embedded that it might require the dismantling of the entire edifice in order to retrieve it.

Nevertheless, given that this process began in the period under discussion, it was not then an evil nor would it ever be an evil if Governments did not allow it to mushroom out of all proportion. The fiscus was acting quite correctly at the time in responding to what this work has shown is a perfectly understandable influence on tax legislation.

ELIMINATION OF SHORTCOMINGS IN THE LEGISLATION

The process of recognising loopholes in the legislation by means of which taxpayers may pay less tax than might otherwise be the case is a logical part of the development process of the Income Tax Act. An example of such a loophole has been given in chapter 3 of this work in respect of section 14(a) of the 1914 Act, which was hastily corrected in 1915. In the same chapter, the clumsy or generalised wording of certain sections was mentioned. These instances all presented potential loopholes and were improved upon during the ensuing years. For example, section 6 was amended in 1916, as discussed in chapter 3 of this work, to ensure that carefully worded agent-principal contracts would not escape tax on the resultant commissions. As another example, the so-called 'general deduction formula' was reworded in the 1917 Act to eliminate shortcomings.

This aspect of the development of tax legislation, then, was an ongoing process which commenced from 1914 and continued independently of loopholes discovered by taxpayers and fought for in the courts before being plugged by legislative procedures.

Before one considers criticising the drafters of the laws for the need to tinker with the Act at such regular intervals, it is necessary to remember that this legislation was very new in concept and, even overseas, there was little in the way of previous example on which to draw. In any event, the legislation had to reflect local circumstances. Some of the

loopholes or errors in drafting were discovered by officials as part of the process of dealing with the Act on a daily basis, while others came to light by means of the acts and claims of taxpayers. The process was, therefore, carried out by a combination of systematic study of the legislation and arbitrary reaction to discovered shortcomings.

DEVELOPMENT BY REACTION TO JUDICIAL INTERPRETATION

The loopholes so won by taxpayers were of a different ilk and less glaringly obvious than the type discussed above. It has been shown that this process of the discovery by taxpayers of ways of reducing their tax burden by interpreting sections of the Act in a particular way and then of sustaining those interpretations in Court, only to have the Commissioner change the Act accordingly soon after, was from the beginning a major part of the development process. The cases concerned have been fully discussed earlier in this work in chapter 4 and are only listed here, in this context:

- CIR v Delagoa Bay Cigarette Co Ltd discussed at tax year 1918
- CIR v Collins, discussed at tax year 1919
- Income Tax Case No. 23, discussed at tax year 1921
- Rex v Assiazsky, Sher and Levin, discussed at tax year 1922
- Income Tax Case No. 6, discussed at tax year 1922
- Income Tax Case No. 7, discussed at tax year 1922
- CIR v Lunnon, discussed at tax year 1922
- Income Tax Case No. 11, discussed at tax year 1923
- Income Tax Case No. 14, discussed at tax year 1923.

The abovementioned nine cases set the pattern for an important and integral part of the development of tax legislation.

In commenting on the relative importance of this aspect of the development of tax legislation, it is necessary to bear in mind that these shortcomings would sooner or later have come to light in any case. For example, the fiscus could scarcely have left open the loophole discovered by Lunnon; the result would have been a flood of instances where employees took large lump sums 'in recognition of services' declared after their retirement and entirely tax free. This would seriously have warped the tax-gathering process as well as the normal commercial practices. The findings of the courts, then, while important, are not as far-reaching as is the other aspect of judicial activity.

This other aspect of the influence of court cases on development of the law is the extent to which they establish principles. In legislation of this type, where there is no common law and the law is exclusively the result of legislation, the courts are very important in establishing principles based on their interpretation of the statutes. The period under consideration in this work saw this leg of the development process operate in earnest from the very earliest cases. It will be recalled that the following cases established principles during the period up to 1925:

- COT v William Dunn & Co Ltd, discussed in chapter 3 at tax year 1915, which is still quoted today as a major source of the principles relating to source of income.
- Robinson v COT, discussed in chapter 3, at tax year 1916 relating to place of residence
- COT v Booysens Estates Ltd, discussed in chapter 3 at tax year 1916 whose principles regarding capital and revenue are still extensively used together with quoted extracts from the judgment of Innes C J.
- Stephan v CIR, discussed in chapter 4 at tax year 1917 established a principle of taxability of isolated transactions and has since been quoted with approval in several cases.
- Deary v Deputy CIR, discussed in chapter 4 at tax year 1917 established the principles used in deciding whether the proceeds of the sale of a business were in the nature of goodwill (and therefore capital) or not. The case continues to enjoy use as a major reference in this respect as well as the taxation of partnerships.
- Platt v CIR, discussed in chapter 4, at tax year 1917 established principles guiding decisions as to whether a person was carrying on business or not, and also established that they differed as between companies and individuals. It, too, enjoys current use in matters where these principles require consideration.
- Crown Mines Ltd v CIR, discussed in chapter 4 at tax year 1917 established that the Courts have no right to interfere with the exercise of the discretionary power of the

Commissioner, provided he has acted in good faith and applied his mind to the matter.

- CIR v Delagoa Cigarette Co. Ltd, discussed in chapter 4 at tax year 1918 established that all income is subject to tax, and its related expenditure deductible, regardless of whether it is legal or not.
- Lockie Bros v CIR, discussed in chapter 4 at tax year 1918 established that thefts by the manager of a business were not deductible in terms of the general deduction formula. This case is still in use as a source of the principle in cases of this nature.
- Modderfontein B Gold Mining Co. Ltd v CIR, discussed in Chapter 4 at tax year 1919 established that the nature of rental does not depend on the business of the lessee, and also that an annual payment is not necessarily an annuity. The case is still used in the context of these principles.
- Union-Castle Mail Steamship Co. Ltd v CIR, discussed in chapter 4, at tax year 1920 established that where a matter had not been the subject of objection in the first instance, it could not be raised in a case pleaded in the Court.
- City & Suburban Gold Mining & Estate Co. Ltd v CIR, discussed in chapter 4, at tax year 1922 established that distribution of capital profits were taxable as dividends in the hands of shareholders except in the course of liquidation.
- CIR v Lunnon, discussed in chapter 4 at tax year 1922 established another of several principles used in deciding whether particular receipts were capital or revenue in nature: income is the product of capital invested, or the product of

labour or wits; further that annuality is an element of income.

Clearly, even in these early years of the development of income tax legislation, the courts were actively responding to the need to interpret the statutes and establish principles for their application, and this function was a major part of the development as a whole.

Indeed, as pointed out at the discussion of each case, several of the principles are still used extensively today - for example, the means of deciding the residence of a person is still based on the dictum in Robinson's case. Perhaps more important are the principles found in Booysens Estates case; by far the most common subject of income tax cases is capital versus revenue, and the Booysens Estates case is invariably quoted. In similar vein, Stephan's case continues to enjoy frequent use, because taxpayers tend to try to regard occasional transactions as being on capital account. This is particularly relevant in the share market, and Stephan's case is very much a live matter. Wherever people deal with money, there will be theft, and for this reason the Lockie Bros. case is very important. It is quoted every time a taxpayer seeks to claim losses by theft or embezzlement.

These are perhaps the four most important cases in the era under discussion from the point of view of producing lasting relevant principles. Having said this, however, it must be stated that the other cases are of scarcely lesser importance. The four

cases concerned merely enjoy a greater usage on account of their more general applicability.

## INFLUENCE OF DIFFERENT POLITICAL PHILOSOPHIES

The final factor influencing the development of income tax legislation is differences between political philosophies of the parties in Parliament. During the period covered by this work, the two main political parties displayed differences of approach in two areas: mines and farmers. Predictably, the governing party maintained that its motives were even-handed and favoured no particular group. Equally predictably, the opposition National Party proclaimed that this was not so, and that the Government was favouring the mining interests over the struggling farmers.

The 1914 Act made only one specific reference to farmers and this would hardly have been described as against their interests. Farmers were taxed on the so-called 'cash basis' unless they elected to be taxed on the 'stock basis'. The Act referred to mining interests only insofar as it exempted from tax any profits from mining activities which had already been taxed under the Mining Taxation Act. This meant that mining companies paid tax at 10% in the case of gold and diamonds and between 2 1/2% and 6% in the case of other minerals, increasing in the latter case if profit exceeded 40% of the gross revenue. These rates were certainly not favourable in comparison with the rates payable by

other taxpayers, which varied between 2 1/2% and 7 1/2% after an abatement of the first £1 000.

The 1915 Act added to the burden of gold mines by imposing a special war levy of £500 000. Personal abatements came into existence, which did not apply to companies at all.

As against this, in 1916 individuals became subject to the supertax. Although the mining companies, like all other companies, were not affected by this tax, the 'mining magnates' most certainly were.

The 1917 Act placed the burden of dividend tax upon all companies, but gold mines paid twice as much as non-mining companies and diamond mines half again as much as companies not engaged in mining. Even allowing for the fact that the dividend tax could be passed on to shareholders, gold mining profits were taxed at 3/- in the £ and diamond mines at 2/6 and other companies at 2/-. These rates included the 5% payable by all companies instead of the rates formerly payable under the Mining Taxation Act of 1910. Diamond profits also bore an export duty of 5% on exports. All taxpayers were equally charged with the 25% excess profits duty. Mining companies became entitled to a capital redemption allowance in recognition of the fact that they were dealing with wasting assets.

In 1919 all taxpayers were saddled with a doubled supertax.

Up to this point, the mining companies were certainly not favoured over the general body of taxpayers; it is clear that quite the contrary was the case.

In 1921 farmers were singled out for the second time when they became obliged to calculate their taxable incomes on the 'stock basis'. As has been discussed in chapter 3 of this work at tax year 1914 this was not really a disadvantage in the sense that farmers paid more tax than before; it merely meant that they would pay the same amount of tax a little earlier. However, coming as it did at a time when drought and a substantial fall in demand for wool and sugar had placed the farmers in a poor position, it seems to have been a badly-timed decision upon which the Nationalists predictably pounced. At the same time, though, the rate applicable to all companies was increased by 50% to 1/6 in the £, while the excess profits duty and the special war levy disappeared. Although the latter concession benefitted the gold mines, they still were not better off than other taxpayers were; in fact, they still paid more than other taxpayers did. One must with respect pay more heed to the remarks of Sir Davis Harris, as recorded in chapter 4 of this work at tax year 1921, than the frankly electioneering rhetoric of Mr N C Havenga on the same page.

The 1925 Act reflected the first opportunity of the Nationalists to heed the pleas of their rural constituents. Predictably, farmers were once more allowed to elect the 'cash basis' in preference to the 'stock basis'. This was a purely political

ploy which, as indicated earlier, merely deferred the payment of tax. A more soundly-based decision was the one allowing farmers to amortise the costs of boreholes and windmills. This last-mentioned concession represented in itself the start of a lasting principle in South African tax law: the right of farmers to claim as deductible capital expenditure incurred in improving their land. Such a policy is difficult to fault in principle. The corollary, namely that on subsequent sale of improved land this expenditure is not taxable as a recoupment, is certainly open to attack in principle.

While making these concessions to farmers, the new Government did not then move to bleed the 'mining magnates' after their years of alleged cossetting at the hands of the Smuts government; indeed, the rate remained at 3/- for mining companies, being in effect a consolidation of the previous normal rate of 1/6 and the dividend tax of 1/6 in the £, while the rate applicable to other companies rose to 2/6 in the £.

The conclusion to which these factors lead is that neither of the main parties in the South African political arena was really in the thrall of any particular special interest group; neither dared to tax the mines beyond reason, while the Nationalists were more sensitive to both the political power and the very legitimate needs of the farming community. It is submitted that both parties had essentially similar economic philosophies, and their differences and preferences reflected nuances in emphasis rather than any deepseated divergencies in ideology. The South

African Party taxed the mines more heavily than it did any other category of taxpayer; it was not as sensitive to the plight or the influence of the farmers as it might have been. The National Party was not so foolish as to cripple the mines, and made concessions to farmers which were by no means radical and were at least partly justifiable in simple economic terms.

This analysis of the development of tax legislation tends therefore to bear out the thesis of Yudelman as discussed in the introduction. In fact, it is submitted that even had the Labour Party itself come to power, the harsh realities of life would have precluded it from bleeding the mines to the point where the source of expansion for the young country was seriously affected. The yoke joining business and government, particularly in a developing country, is so integral to the very existence of the nation that it must inevitably transcend ideology.

## SUMMARY

It is perhaps fair to submit, then, that this work has illustrated that in the period from Union to the victory of the Pact Government, the elements of the development of South African income tax legislation were established. These were:

1. the use of the Act to provide incentives not directly related to attracting taxes into the State coffers. This element was at first apparent on a small scale only; the future would show that it became a major factor, especially after 1959. The large scale use of the Act to achieve these ends, mentioned earlier in this conclusion, began in 1959 with the introduction of incentives for investment in industrial buildings, followed soon after by similar incentives in respect of plant and machinery, and then grew completely out of control until it is now in the process of being dismantled;

2. outside events of a political or natural kind. This element would always be present, because of the effect of such events on the economy and thus on State revenues;

3. shortcomings in drafting of statutes and their consequent exploitation by taxpayers. This element was an inevitable concomitant of drafting by fallible human beings and of the parallel search by taxpayers for ways and means of reducing the tax burden;

4. the interpretation of statutes by the Courts, leading to two equally very important results:

   (a) the alteration of statutes to prevent the exploitation by taxpayers of loopholes discovered in them; and

(b) the establishment of a body of principles for the future guidance of taxpayers, legislators and the Courts;

5. the desire to make political capital and express political philosophies. In the South African context this element is of limited importance.

Of these elements, the most important, because the most continually operating and most durable, is undoubtedly the influence of the Courts. It is here that the principles of interpretation are established which endure in perpetuity. Indeed, they outlast even changes to the Act, because every such change potentially begs judicial interpretation. In addition, the vast complexity of commercial activity means that no Act of Parliament can possibly cater for every eventuality; consequently, the Courts will always have to interpret legislation and enunciate principles or apply existing principles to new situations.

# APPENDICES

# APPENDIX 1

## Extracts from the South Africa Act, 1909

## PART VII

## Finance and Railways

Constitution of Consolidated Revenue Fund and Railway and Harbour Fund.

117. All revenues, from whatever source arising, over which the several Colonies have at the establishment of the Union power of appropriation, shall vest in the Governor-General-in-Council. There shall be formed a Railway and Harbour Fund, into which shall be paid all revenues raised or received by the Governor-General-in-Council from the administration of the railways, ports, and harbours, and such fund shall be appropriated by Parliament to the purposes of the railways, ports, and harbours in the manner prescribed by this Act. There shall also be formed a Consolidated Revenue Fund, into which shall be paid all other revenues raised or received by the Governor-General-in-Council, and such fund shall be appropriated by Parliament for the purposes of the Union in the manner prescribed by this Act, and subject to the charges imposed thereby.

Administration of railways, ports, and harbours

127. The railways, ports, and harbours of the Union shall be administered on business principles, due regard being had to agricultural and industrial development within the Union and promotion, by means of cheap transport, of the settlement of an agricultural and industrial population in the inland portions of all provinces of the Union. So far as may be, the total earnings shall be not more than are sufficient to meet the necessary outlays for working, maintenance, betterment, depreciation, and the payment of interest due on capital not being capital contributed out of railway or harbour revenue, and not including any sums payable out of the Consolidated Revenue Fund in accordance with the provisions of sections one hundred and thirty and one hundred and thirty-one. The amount of interest due on such capital invested shall be paid over from the Railway and Harbour Fund into the Consolidated Revenue Fund. The Governor-General-in-Council shall give effect to the provisions of this section as soon as and at such time as the necessary administrative and financial arrangements can be made, but in any case shall give full effect to them before the expiration of four years from the establishment of the Union. During such period, if the revenues accruing to the Consolidated Revenue Fund are insufficient to provide for the general service of the Union, and if the earnings accruing to the Railway and Harbour Fund are in excess of the outlays specified herein, Parliament may by law appropriate such excess or any part thereof towards the general expenditure of the Union, and all sums so appropriated shall be paid over to the Consolidated Revenue Fund.

# APPENDIX 2

## Extract from Mining Taxation Act No. 6 of 1910

## TAXATION ON PROFITS OF MINING

Annual tax on the profits of mining

3. There shall be levied annually a tax, -

(a) on the profits of mining for diamonds, ten per cent.;
(b) on the profits of mining for gold, ten per cent.;
(c) on the profits of mining for other minerals, according to the following scale, that it to say:-

| Scale | Rate of tax |
|---|---|
| If the amount of profit do not exceed 5 per cent. of the gross revenue derived...... | 2 1/2 per cent of the profits |
| If the amount of profit exceed 5 per cent., but do not exceed 10 per cent. of the gross revenue derived............... | 3 per cent of the profits |
| If the amount of profit exceed 10 per cent., but do not exceed 15 per cent. of the gross revenue derived ............... | 3 1/2 per cent of the profits |
| If the amount of profit exceed 15 per cent., but no not exceed 20 per cent. of the gross revenue derived................ | 3 1/2 per cent of the profits |
| If the amount of profit exceed 15 per cent., but do not exceed 20 per cent. of the gross revenue derived................ | 4 per cent of the profits |
| If the amount of profit exceed 20 per cent., but do not exceed 30 per cent. of the gross revenue derived................ | 5 per cent. of the profits |
| If the amount of profit exceed 30 per cent., but do not exceed 40 per cent. of the gross revenue derived................ | 6 per cent of the profits. |

and thereafter for every additional one per cent of profit an addition of one-tenth per cent. to the rate of the tax.

## APPENDIX 3

### Examples of calculation of income tax payable under section 4(4) of the Income Tax Act No. 28 of 1914

| | | £ | |
|---|---|---|---|
| 1. | Taxable income | 500 | |
| | Less: Amount deductible in terms of section 4(3) | 1 000 | |
| | Taxable amount | NIL | |
| 2. | Taxable income | 1 000 | |
| | Less: deduction in terms of section 4(3) | 1 000 | |
| | Taxable amount | NIL | |
| 3. | Taxable income | 1 001 | |
| | Less: deduction in terms of section 4(3) | 1 000 | |
| | Taxable amount | 1 | |
| | Tax payable in terms of section 4(4)(a) | | 6d |
| | | | 6d |
| 4. | Taxable income | 2 000 | |
| | Less: deduction in terms of section 4(3) | 1 000 | |
| | Taxable amount | 1 000 | |

Tax payable in terms of section 4(4)(b):

$6 \frac{1000}{2000}$ d x £1 000 — £27/1/8

| | | £ |
|---|---|---|
| 5. | Taxable income | 13 000 |
| | Less: deduction in terms of section 4(3) | 1 000 |
| | Taxable amount | 12 000 |

Tax payable in terms of section 4(4)(b)

$6 \frac{12000}{2000}$ d x £12 000

i.e. 1/- x £12 000 — £600/0/0

| | | £ |
|---|---|---|
| 6. | Taxable income | 21 000 |
| | Less: deduction in terms of section 4(3) | 1 000 |
| | Taxable amount | 20 000 |

Tax payable in terms of section 4(4)(b)

$6 \frac{20000}{2000}$ d x £20 000

i.e. 1/4 x £20 000 — £1 333/13/4

APPENDIX 3 (Continued)

| | | £ | |
|---|---|---|---|
| 7. | Taxable income | 25 000 | |
| | Less: deduction in terms of section 4(3) | 1 000 | |
| | Taxable amount | 24 000 | |

Tax payable in terms of section 4(4)(b)

$$6 \frac{24\ 000}{2\ 000} d \times £24\ 000$$

| | |
|---|---|
| 1/6 x £24 000 | £1 800/0/0 |

| | | | |
|---|---|---|---|
| 8. | Taxable income | 31 000 | |
| | Less: deduction in terms of section 4(3) | 1 000 | |
| | Taxable amount | 30 000 | |

Tax payable in terms of section 4(4)(c)

| | |
|---|---|
| 1/6 x £30 000 | £2 250/0/0 |

The maximum rate of tax was thus 7,5%

## APPENDIX 4

### Comparison of the effect of taxing a farmer on the 'cash basis' and 'stock' basis respectively

ASSUMPTIONS

1. Other farming income is £2 000 per year.
2. Number of adult cattle unchanged at 100.
3. 40 calves are born during year 1.
4. Any subsequent births are ignored for this purpose.
5. All 40 calves are sold in year 5 for £15 each.
6. Livestock values for income tax purposes are:

| | | |
|---|---|---|
| Calves | | £1 |
| Tollies + Heifers: | 1 - 2 years | £2 |
| | 2 - 3 years | £3 |
| Cows | | £5 |

'CASH' BASIS

| | | £ | |
|---|---|---|---|
| YEAR 1 | Other income | 2 000 | |
| | 100 Adult cattle - no effect | | |
| | Calves - no effect | | |
| | TAXABLE INCOME | 2 000 | |
| | Less: s4(3) DEDUCTION | 1 000 | |
| | TAXABLE AMOUNT | 1 000 | |
| | TAX PAYABLE $6 \frac{1000}{2000}$ d x £1 000 | | 27/1/8 |
| YEARS 2, 3, 4 | UNCHANGED i.e. £27/1/8 x 3 | | 81/5/0 |
| YEAR 5 | Other income | 2 000 | |
| | 100 adult cattle - as above | - | |
| | 40 adult cattle sold for 40 x £15 | 600 | |
| | Taxable income | 2 600 | |
| | Less: s4(3) deduction | 1 000 | |
| | Taxable amount | 1 600 | |
| | Tax payable $6 \frac{1600}{2000}$ d x £1 600 | | 45/6/8 |
| Total tax liability for the 5-year period | | | £153/13/4 |

APPENDIX 4 (Continued)

'STOCK' BASIS

| | | £ | |
|---|---|---|---|
| YEAR 1 | Other income | 2 000 | |
| | Adult cattle : closing stock 100 x £5 | 500 | |
| | : opening stock 100 x £5 | (500) | |
| | Calves : births 40 R1 | 40 | |
| | Taxable income | 2 040 | |
| | Less: s4(3) deduction | 1 000 | |
| | Taxable amount | 1 040 | |
| | Tax payable $6\frac{1040}{2000}$ d x £1 040 | | 28/5/1 |
| YEAR 2 | Other income | 2 000 | |
| | 100 adult cattle : as above | - | |
| | Tollies & Heifers 1 - 2 years : closing stock 40 x £2 | 80 | |
| | Calves : opening stock from closing stock year 1 | (40) | |
| | Taxable income | 2 040 | |
| | Less: s4(3) deduction | 1 000 | |
| | Taxable amount | 1 040 | |
| | Tax payable $6\frac{1040}{2000}$ d x £1 040 | | 28/5/1 |
| YEAR 3 | Other income | 2 000 | |
| | 100 adult cattle : as above | - | |
| | Tollies & heifers 2-3 years : closing stock 40 x £3 | 120 | |
| | Tollies & heifers 1-2 years : opening stock from closing stock year 2 | (80) | |
| | Taxable income | 2 040 | |
| | Less: s4(3) deduction | 1 000 | |
| | Taxable amount | 1 040 | |
| | Tax payable $6\frac{1040}{2000}$ d x £1 040 | | 28/5/1 |
| YEAR 4 | Other income | 2 000 | |
| | 100 adult cattle : as above | - | |
| | 40 adult cattle : closing stock 40 x £5 | 200 | |
| | Tollies & heifers 2-3 years : opening stock from closing stock year 3 | (120) | |
| | Taxable income | 2 080 | |
| | Less: s4(3) deduction | 1 000 | |
| | Taxable amount | 1 080 | |
| | Tax payable $6\frac{1080}{2000}$ d x £1080 | | 28/8/8 |

APPENDIX 4 (Continued)

| | | £ | |
|---|---|---|---|
| YEAR 5 | Other income | 2 000 | |
| | 100 adult cattle : as above | - | |
| | Sales : 40 adult cattle x £15 | 600 | |
| | 40 adult cattle : opening stock from closing stock year 4 | (200) | |
| | Taxable income | 2 400 | |
| | Less: s4(3) deduction | 1 000 | |
| | Taxable amount | 1 400 | |
| | Tax payable $6 \frac{1400}{2000}$ d x £1 400 | | 39/1/8 |
| Total tax liability for 5 - year period | | | £152/5/7 |

The difference in total tax paid under each system is small in this example; however, it would become more marked with births every year and at higher levels of income.

## APPENDIX 5

### Comparison of the change in tax rates from 1914 to 1915

The first 1915 example in each case shows the position of a taxpayer entitled only to £300 deduction, whereas the second is for a taxpayer entitled to all abatements and with two qualifying children

| | | £<br>1914 | £<br>1915 | | £<br>1915 |
|---|---|---|---|---|---|
| 1. | Taxable income | 500 | 500 | | 500 |
| | Less: exempt portion | 500 | 300 | | 300 |
| | | – | 200 | | 200 |
| | Abatements: insurance | | | 25 | |
| | societies | | | 10 | |
| | children | | | 40 | 75 |
| | Taxable amount | - | 200 | | 125 |
| | Tax payable : | | | | |
| | 6d $\frac{0}{2000}$ d x NIL | - | | | |
| | : 1/- $\frac{200}{2000}$ d x 200 | | 1/0/0 | | |
| | : 1/- $\frac{125}{2000}$ d x 125 | | | | 7/9 |
| 2. | Taxable income | 1 000 | 1 000 | | 1 000 |
| | Less: exempt portion | 1 000 | 300 | | 300 |
| | | - | 700 | | 700 |
| | Abatements (as above) | | | | 75 |
| | Taxable amount | - | 700 | | 625 |
| | Tax payable : 6d $\frac{0}{2\ 000}$ d x NIL | - | | | |
| | : 1/- $\frac{700}{2\ 000}$ d x 700 | | 12/5/0 | | |
| | : 1/- $\frac{625}{2\ 000}$ d x 625 | | | | 9/15/2 |
| 3. | Taxable income | 24 300 | 24 300 | | 24 300 |
| | Less: exempt portion | 1 000 | 300 | | 300 |
| | | 23 300 | 24 000 | | 24 000 |
| | Abatements (as above) | | | | 75 |
| | Taxable amount | 23 300 | 24 000 | | 23 925 |
| | Tax payable : 1/6 x 23 300 | 1747/10/0 | | | |
| | : 1/- $\frac{24\ 000}{2\ 000}$ x 24 000 | | 2400/0/0 | | |
| | : 1/- $\frac{23\ 925}{2\ 000}$ x 23 925 | | | | 2388/15/2 |

APPENDIX 5 (Continued)

| | £ 1914 | £ 1915 | £ 1915 |
|---|---|---|---|
| 4. Taxable income | 25 000 | 25 000 | 25 000 |
| Less: exempt portion | 1 000 | - | - |
| | 24 000 | 25 000 | 25 000 |
| Abatements (as above) | | | 75 |
| Taxable amount | 24 000 | 25 000 | 24 925 |
| Tax payable : 1/6 x 24 000 | 1800/0/0 | | |
| : 2/- x 25 000 | | 2500/0/0 | |
| : 2/- x 24 925 | | | 2492/10/0 |

It is clear that the abatements became progressively less useful as income increased, but this is a perfectly understandable situation, as the cost of keeping a child need not necessarily increase in proportion to the increased income of the parent, and neither is it necessary to increase life assurance cover in proportion to income.

# APPENDIX 6

## Illustrations of the effect of the second proviso to Section 1(3) of the 1916 Act

Assume in each case that the taxpayer enjoys deductions under the section amounting to £75 before applying the conditions of the proviso.

| EXAMPLE | 1<br>£ | 2<br>£ | 3<br>£ | 4<br>£ | 5<br>£ |
|---|---|---|---|---|---|
| Taxable income | 200 | 375 | 500 | 540 | 575 |
| Less: exempt portion | 300 | 300 | 300 | 300 | 300 |
| | - | 75 | 200 | 240 | 275 |
| Less section 1(3) deduction: | | | | | |
| : not applicable | - | | | | |
| : in full | | 75 | | | |
| : in full | | | 75 | | |
| : reduced by excess of taxable income over £500 i.e. £540 - £500 .˙. £75 - £40 | | | | 35 | |
| : reduced by excess of taxable income over £500 i.e. £575 - £500 .˙. £75 - £75 | | | | | - |
| Taxable amount | - | - | 125 | 205 | 275 |

From these examples it is clear that the benefits of the deductions were rapidly lost as taxable income increased beyond £500 until they disappeared entirely at a taxable income of £575.

## APPENDIX 7

### Illustrations of the provisions for supertax in the 1916 Act

1. Taxpayer entitled to deductions totalling £75 in terms of section 1(3) enjoys the following items of income:

| | £ | £ |
|---|---|---|
| Year ended 30 June | 1915 | 1916 |
| Income from business in Union | 4 000 | 7 000 |
| Income from business in Basutoland | 1 000 | 2 000 |
| Dividends from Union registered company | 50 | 70 |
| Dividends from gold mining company | 20 | 42 |
| Dividends from Union registered company, 40% of whose profits accrue from dividends from gold mining companies | 100 | 120 |

The Commissioner has decided that the company which paid the dividends of £50 and £70 respectively had accumulated funds surplus to its reasonable needs, and that it should have doubled its dividends paid, in terms of section 6 of the 1916 Act.

Calculation of taxable income:

| | | |
|---|---|---|
| Income from Union business | 4 000 | 7 000 |
| Income from Basutoland business | 1 000 | 2 000 |
| Taxable income: | 5 000 | 9 000 |
| Dividends: Union registered company | 50 | 70 |
| : gold mining company | 20 | 52 |
| : Union registered dividend-earning company 40% | 40 | 48 |
| Deemed income in terms of section 6 | 50 | 70 |
| Total income | 5 160 | 9 240 |

Average $\frac{5\ 160 + 9\ 240}{2}$ $\frac{14\ 400}{2}$

Supertaxable income 7 200

Deduction in terms of section 4(3):

2 500 - [(7 200 - 2 500) x 10/-]

2 500 - 2 350 150

Supertaxable amount 7 050

Supertax payable : 1s $\frac{7\ 050}{2\ 000}$ d x 7 050 £456/-/9

APPENDIX 7 (Continued)

2. Same taxpayer, but income from Union business is £4 200 and £7 400 in 1915 and 1916 respectively.

| | | |
|---|---|---|
| Taxable income | 5 200 | 9 400 |
| Total income | 5 360 | 9 640 |
| Average $\frac{5\ 360 + 9\ 640}{2}$ | $\frac{15\ 000}{2}$ | |
| Supertaxable income | 7 500 | |
| Deduction in terms of section 4(3): 2 500 - [(7 500 - 2 500) x 10/-] | - | |
| Supertaxable amount | 7 500 | |
| Supertax payable: 1s $\frac{7\ 500}{2\ 000}$d x 7 500 | £492/3/9 | |

3. Same taxpayer, but supertaxable amount is £50 000

Supertax payable: 3/- x 50 000 — £7 500/0/0

APPENDIX 8

Examples of the taxation of a private company as defined in Section 35 of Act 41 of 1917

1. 'A' Limited earned a taxable income of £6 300 for the 1917/18 tax year. It declared dividends totalling £3 000 during the same period. The company qualifies as private in terms of section 35 of the Income Tax Act 1917.

| | £ |
|---|---|
| Taxable income | 6 300 |
| Less: Abatement | 300 |
| Taxable amount | 6 000 |
| Normal tax payable : 1/- x 6 000 | 300 |
| Dividend tax : 1/- x 3 000 | 150 |
| Total tax liability | 450 |

But in terms of section 35, an individual would pay tax as follows on a taxable amount of £6 000:

| | |
|---|---|
| 1s $\frac{6\ 000}{2\ 000}$ d x 6 000 | 375 |

.˙. Dividend tax payable by the company may not exceed 75 i.e. 3d per £.

2. Same comany, but with a taxable amount of £12 000 and dividends paid totalling £6 000.

| | |
|---|---|
| Normal tax payable : 1/- x 12 000 | 600 |
| Dividend tax : 1/- x 6 000 | 300 |
| Total tax liability | 900 |
| An individual would pay 1s $\frac{12\ 000}{2\ 000}$ x 12 000 | 900 |

.˙. No change in dividend tax payable.

3. Same company, but with a taxable amount of £20 000 and dividends paid totalling £10 000.

| | |
|---|---|
| Normal tax payable : 1/- x 20 000 | 1 000 |
| Dividend tax : 1/- x 10 000 | 500 |
| | 1 500 |
| An individual would pay 1s $\frac{20\ 000}{2\ 000}$ x 20 000 | 833/6/7 |

.˙. No change in dividend tax payable.

# APPENDIX 9

In his book Income Tax Simplified, (1) Walter J Barnes gives the following illustrations of the operation of Chapter IV of the Act on Excess Profits Duty. Slight adjustments have been made to the original text.

## 1. Calculation of capital employed

J Brown - General Dealer

Balance Sheet at 30 June 1918

| Liabilities | £ | Assets | | | £ |
|---|---|---|---|---|---|
| | | Fixed Assets | | | |
| Capital Account | 24 300 | Goodwill - cost price | | | 500 |
| Loan : T Robinson | 400 | Property investment | | | 1 200 |
| Trade creditors | 5 000 | Buildings | | | |
| Bank overdraft | 500 | - cost price | | 13 900 | |
| | | - depreciation | | 900 | 13 000 |
| | | Machinery | | | |
| | | - cost price | | 2 160 | |
| | | - depreciation | | 660 | 1 500 |
| | | Furniture | | | |
| | | - cost price | | 600 | |
| | | - depreciation | | 100 | 500 |
| | | | | | 16 700 |
| | | Current Assets | | | |
| | | Trade debtors | 4 000 | | |
| | | Less: provision for doubtful debts | 1 000 | 3 000 | |
| | | Stock in trade | | 10 000 | |
| | | Cash on hand | | 500 | 13 500 |
| | 30 200 | | | | 30 200 |

Depreciation on machinery is £220 greater than the amount allowed by the Commissioner in calculating taxable income.

### Computation of Capital Employed

| | | | |
|---|---|---|---|
| Total assets | | | 30 200 |
| Less: | Property investment (profits not liable to e.p.d. per section 51) | 1 200 | |
| | Loan (per section 50) | 400 | |
| | Bank overdraft (per section 50) | 500 | |
| | Trade creditors (per section 50) | 5 000 | 7 100 |
| | forward...... | | 23 100 |

APPENDIX 9 (Continued)

| | | | |
|---|---|---|---|
| | forward...... | | 23 100 |
| Add: | Provision for doubtful debts (not recognised by Commissioner) | 1 000 | |
| | Excess depreciation (section 50 refers to taxable income i.e. after providing depreciation at Commissioner's rate only) | 220 | |
| | Depreciation on buildings (not allowed for tax purposes) | 900 | 2 120 |
| Capital Employed | | | £25 220 |

2. Calculation of excess profits where deficits arise

Year ended 30 June 1914 : Capital employed £25 220
Profit £ 2 774/4/0
Percentage 11%

| Year ended 30 June | Capital employed | Profit |
|---|---|---|
| 1918 | £20 000 | £2 000 |
| 1919 | £21 000 | £1 500 |
| 1920 | £21 500 | £5 000 |

| | | | |
|---|---|---|---|
| Assessment 1918 : | Profit | | £2 000 |
| | Less: pre-war standard, 11% of capital R20 000 | 2 200 | |
| | : abatement | 500 | 2 700 |
| | Deficit carried forward | | £ 700 |
| Assessment 1919 : | Profit | | £1 500 |
| | Less: pre-war standard, 11% of capital £21 000 | 2 310 | |
| | : abatement | 500 | |
| | : deficit from 1918 | 700 | 3 510 |
| | Deficit carried forward | | £2 010 |
| Assessment 1920 : | Profit | | £5 000 |
| | Less: pre-war standard, 11% of capital £21 500 | 2 365 | |
| | : abatement | 500 | |
| | : deficit from 1919 | 2 010 | 4 875 |
| | Excess profit | | £ 125 |
| | Duty at 10/- per £1 | | £62/10/0 |

## APPENDIX 10

Two cases heard in Southern Rhodesia under Ordinance 20 of 1918, although not subject to the South African Acts, bear consideration for two reasons. Firstly, they serve as an illustration of the principle that South Africa and the then Rhodesia have always had similar income tax legislation in common and their respective decisions, although not binding on one another, certainly have persuasive effect.

Secondly, they also illustrate the fact that income tax cases with similar facts can have virtually opposite results.

In L v Commissioner of Taxes 1 SATC 75, the appellant had sold a branch of his business, including trading stocks at cost plus 15%. When the Commissioner taxed the proceeds the taxpayer appealed on the grounds that the sale was part of the shutting of the branch and therefore not a normal sale, but rather the realisation of an investment. This case was heard in March 1920 and the taxpayer won.

One year later the case of A B v Commissioner of Taxes 1 SATC 77 appeared before the High Court. The appellant had sold a cattle ranch lock, stock and barrel and the Commissioner had taxed that portion of the proceeds as related to the cattle. The taxpayer contended that these proceeds were part of the realisation of his investment. The court held that the surplus had been earned in a business where the object was to make a profit on selling livestock and therefore the amount in question fell within the definition of gross income.

# APPENDIX 11

## ILLUSTRATIONS OF THE EFFECT OF THE CHANGE IN RATES OF SUPERTAX IN THE 1921 ACT

| | £ | £ | £ | £ | £ |
|---|---|---|---|---|---|
| Income subject to super tax | 10 000 | 24 000 | 30 000 | 48 000 | 60 000 |
| Tax payable under 1917 Act: | | | | | |
| 1/- + $\frac{1}{2000}$ d per £ up to taxable income of £48 000, and 3/- per £ on amounts exceeding £48 000 | 500/-/5 | 1200/1/- | 1500/1/3 | 2400/2/- | 2400/2/- |
| | | | | | 1800/-/- |
| | 500/-/5 | 1200/1/- | 1500/1/3 | 2400/2/- | 4200/2/- |
| Tax payable under 1921 Act: | | | | | |
| 1/- + $\frac{1}{500}$ d per £ up to taxable income of £24 000 | 500/1/8 | 1200/4/- | 1200/4/- | 1200/4/- | 1200/4/- |
| and 5/- per £ on amounts exceeding £24 000 | | | 1500/-/- | 6000/-/- | 9000/-/- |
| | 500/1/8 | 1200/4/- | 2700/4/- | 7200/4/- | 10200/4/- |
| Increase under 1921 Act | 1/3 | 3/- | 1200/2/9 | 4800/2/- | 6000/2/- |

Clearly the 1921 rates were extremely severe on taxable incomes in excess of £24 000.

# APPENDIX 12

## EFFECTS OF THE DEVELOPMENT OF SECTION 7 OF ACT 41 of 1917 AS AMENDED UP TO AND INCLUDING 1921

1. Example of a married man with : children aged 4, 8, 12, 16, 17, 18; two dependants; life or sickness insurance premiums totalling £60 per year; contributions to friendly societies amounting to £15 per year; receipts from sick benefits of £12 per year; at various levels of income.

| Abatement | 1917 | 1918 | 1919 | 1920 |
|---|---|---|---|---|
| 'Primary' | 300 | 300 | 300 | 300 |
| Amount allowed at taxable income of: | | | | |
| £200 | 200 | 200 | 200 | 200 |
| 300 | 300 | 300 | 300 | 300 |
| 500 | 300 | 300 | 300 | 300 |
| 600 | 300 | 300 | 300 | 300 |
| 700 | 300 | 300 | 300 | 300 |
| 1000 | 300 | 300 | 300 | 300 |
| 3000 | 300 | 300 | 300 | 300 |
| 24000 | 300 | 300 | 300 | 300 |
| 24300 | 300 | 300 | 300 | 300 |
| 24301 | - | - | - | - |
| 'Secondary' | | | | |
| Life or sickness insurance (maximum) | 25 | 25 | 50 | 50 |
| Friendly societies (maximum) | 10 | 10 | 10 | 10 |
| Sick benefits | 12 | - | - | - |
| Children | 150 | 150 | 180 | 180 |
| Dependant | 40 | 40 | 60 | 60 |
| | 237 | 225 | 300 | 300 |
| Amount allowed at taxable income of: | | | | |
| £600 | 237 | 225 | 300 | 300 |
| 800 | 37 | 25 | 100 | 100 |
| 837 | - | - | 63 | 63 |
| 890 | - | - | 10 | 10 |
| 900 | - | - | - | - |

APPENDIX 12 (Continued)

2. Example of an unmarried man with : children aged 4, 8, 12, 16, 17, 18 not maintained by him; two dependants; life or sickness insurance premiums totalling £60 per year; contributions to friendly societies amounting to £15 per year; receipts from sick benefits of £12 per year; at various levels of income.

| Abatement | 1917 | 1918 | 1919 | 1920 |
|---|---|---|---|---|
| 'Primary' | 300 | 300 | 300 | 300 |
| Amount allowed at taxable income of: | | | | |
| £200 | 200 | 200 | 200 | 200 |
| 300 | 300 | 300 | 300 | 300 |
| 500 | 100 | 100 | 100 | 100 |
| 600 | - | - | - | - |
| 2000 | - | - | - | - |
| 3000 | - | - | - | - |
| 'Secondary' | | | | |
| Life or sickness insurance (maximum) | 25 | 25 | 50 | 50 |
| Friendly Societies (maximum) | 10 | 10 | 10 | 10 |
| Sick benefits | 12 | - | - | - |
| Children | 150 | 150 | 180 | 180 |
| Dependant | 40 | 40 | 60 | 60 |
| | 237 | 225 | 300 | 300 |
| Amount allowed at taxable incomes of: | | | | |
| £600 | 237 | 225 | 300 | 300 |
| 800 | 37 | 25 | 100 | 100 |
| 837 | - | - | 63 | 63 |
| 890 | - | - | 10 | 10 |
| 900 | - | - | - | - |

3. The same married person described in example 1, in the 1921 tax year

| | |
|---|---|
| 'Primary' | 300 |
| 'Secondary' | 120 |
| | 420 |
| Amount allowed at taxable incomes of: | |
| £ 500 | 420 |
| 600 | 420 |
| 4000 | 20 |
| 4200 | - |

APPENDIX 12 (Continued)

4. The same unmarried person described in example 2, in the 1921 tax year.

| | |
|---|---|
| 'Primary' | 300 |
| 'Secondary' | 120 |
| | 420 |

Amount allowed at taxable incomes of:

| | |
|---|---|
| £300 | 420 |
| 500 | 400 |
| 600 | 390 |
| 4000 | 20 |
| 4200 | - |

It may be seen that from 1917 to 1920 married persons enjoyed the benefit of the 'primary' abatement while they earned up to £23 700 more than unmarried persons. The 'secondary' abatements were the same for each category.

In 1921, with the abatements combined, unmarried persons lost their abatements at a faster rate than did married persons, but the difference was far less marked.

# APPENDIX 13

## EFFECT OF THE CHANGES TO SECTION 29 OF ACT 41 OF 1917, AS PROMULGATED IN SECTION 7 OF ACT 29 OF 1921.

Section 29 of the principal Act (41 of 1917) provided that where income subject to supertax did not exceed £7 500, there would be an abatement of £2 500 reduced by 10/- for every £1 by which the income exceeded £2 500.

The section was then amended to the effect that only where the income did not exceed £5 000 would the £2 500 abatement be available, reduced by £1 for every £1 by which the income exceeded £2 500.

### Illustration of the effect of these changes

| | Abatement | |
|---|---|---|
| Income subject to supertax | 1917 Act | 1921 Act |
| £2 000 | 2 000 | 2 000 |
| 2 500 | 2 500 | 2 500 |
| 4 000 | 1 750 | 1 000 |
| 5 000 | 1 250 | - |
| 6 000 | 750 | - |
| 7 500 | - | - |

# APPENDIX 14

## SUMMARY OF THE FINAL REPORT OF THE DROUGHT INVESTIGATION COMMISSION : OCTOBER 1923

The Commission investigated the 1919 drought, whose effects were felt as late as 1923, when the Minister of Finance referred to the huge losses suffered as a result of the fall in agricultural exports (see page 182 of this work). The Commission estimated that the direct losses to farmers as a result of the drought were not less than £16 000 000. The indirect losses were impossible to calculate, but 'affected every profession, business and trade'. (1)

The Commission made the following findings of interest from the point of view of the subsequent development of the Income Tax Act:

1. Overstocking was found to be very prevalent and largely responsible for losses during the drought. (2)
2. 'Government should encourage farmers in every way possible to improve the water resources of the farm'. (3)
3. 'Prompt action (in combating soil erosion)..is imperative'.(4)
4. Improvement of farming methods and conditions : one of the findings in this category was that the very unsatisfactory system of 'kraaling' was adhered to because of the unavailability of sufficient capital for jackal and other fencing. (5)

The Commission made several recommendations, three of which in particular were to have a bearing on future tax legislation.

1. '....The Government should do its utmost to abolish the kraaling system and make it as easy as possible for the farmer to put the paddock system into effect.' (6)
2. 'In order to make this change possible, it will be necessary, as has been shown, to exterminate the jackal, to provide fencing on easy terms and to facilitate the provision of drinking water for stock'. (7)
3. 'It has also been shown that the deterioration of the veld and soil erosion are national dangers, and that the State must assume its responsibilities in connection therewith'. (8)

The Commission summarised its findings in respect of taxation in the farming context as follows: (9)

'The income tax in the past had the effect of encouraging overstocking, and thereby increasing drought losses. Fortunately this defect has been removed in the new law. The question of eliminating the disabilities under which the energetic farmer works as compared with the unprogressive man - that is, the old question of taxation of unimproved values still remains. This question must again be thrashed out with particular reference to the encouraging of improvements designed to prevent drought losses, and erosion - such as irrigation works, damming of sloots, fencing etc. In addition arises the question as to whether the funds required for State action in minimising drought losses should be drawn from the country as a whole, or from the farming community only.'

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18. Op cit at note 8, at p.4.
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20. Op cit, at p. 497.
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13. Union of South Africa. House of Assembly Debates 1912, pp. 1335 et seq.

14. Op cit, at p. 1341.

15. Union of South Africa. House of Assembly Debates 1913, pp. 880 et seq.

CHAPTER THREE

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12. Op cit, at p. 1936.
13. Op cit, at p. 1939.
14. Op cit, at p. 2193.
15. Op cit, at p. 4312.
16. Statutes of the Union of South Africa 1914, pp. 260 - 304.
17. Op cit, section 3(1).
18. Op cit, section 4(5).
19. Op cit, section 15(2)(a).
20. Union of South Africa. House of Assembly Debates 1915, pages 473 et seq.

21. Bewaarplaatsen was the name given to ground assigned to the south of the Reef outcrops for mine dumps, tailings sites or machine stands and subsequently found to be gold-bearing. This property was often privately owned. There was considerable dispute as to who held the mining rights to these properties, and in 1896 the Volksraad of the ZAR resolved that the rights belonged partially to the holders of the surface rights and partly to the Government. The mining companies then bought out the freeholders shortly before war intervened. When peace returned, the new Government resumed negotiations which continued until well after Union. Finally in 1917 the Government agreed to allocate to the holders of surface rights 19/40 of the accumulated mining profits and 18/40 of future profits. It was the 21/40 and 22/40 share enjoyed by the Government which comprised the share of revenue referred to in the Budget each year.

22. See note 14.

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33. Op cit, at p. 45.

34. Op cit, at p. 46.

35. Op cit at note 24, at p. 984.

36. South African Tax Cases. Volume 32, p. 10.

37. Op cit, at p. 15.

38. Op cit, at p. 15 - 16.

39. Op cit, at p. 17.

40. Op cit, at p. 17.

41. Op cit, at p. 25.

CHAPTER FOUR


1. Union of South Africa. House of Assembly Debates 1917, pp. 129 et seq.
2. Op cit, at p. 130.
3. Op cit, at p. 130 By 'co-ordinate basis', the Minister presumably meant that the methods of taxation would be decided with a view to each other and on consideration of the effects of each on the various classes of taxpayer.
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11. South African Tax Cases : Volume 3, p. 253.
12. South African Tax Cases : Volume 37, p. 193.
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43. See discussion in this chapter at 'Income Tax Act 1919'.

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117. Statutes of the Union of South Africa 1962, p. 879.

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119. Op cit at note 39.

120. The gold premium was the result of the inflation which ravaged paper currencies in the years after the War. Up to 1914, gold mines had sold their gold at par value in British currency, which was based on the gold standard prevailing at the time. In 1919, however, this agreement was terminated because of the decline in sterling in relation to the U S dollar. The difference served as a reliable indicator of the depreciation of paper sterling against the gold dollar. The mines wished to reap the fruits of this premium and made representations for the establishment of a free market for gold in London. In terms of the subsequent agreement, gold shipped to London as from July 1919 was then sold by the agents of the mines at the best market price obtainable. In this way the mines enjoyed the benefit of the devaluation of sterling as against the US dollar. For example, while the price per fine ounce had been 85s when sterling was representative of gold, under the new arrangement the price went as high as 127s 4d in 1920. The average price in 1921 was 103s 1d as sterling improved; eventually the premium disappeared as sterling strengthened with the general world economic improvement, until in July 1924 the price was 95s per fine ounce.

     As an aside, as the premium declined, the mines sought to compensate for the lost revenue by reducing costs. Wages were a prime target, and this policy had much to do with the industrial unrest and miners' strike in 1922, as a result of which 3 000 white mine workers lost their jobs and the cost of living allowance disappeared entirely.

121. Op cit at note 118, at p. 2019.

122. Op cit, at p.2019.

123. See note 116.

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126. Op cit, at p. 2020.

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128. Op cit, at p. 4774.

129. Op cit, at p. 4816.

130. Op cit, at p. 4817.

131. Op cit, at p. 4839.

132. Op cit, at p. 4838.

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