IN THE SUPREME COURT OF ZAMBIA **Appeal No. 39/2017**
HOLDEN AT NDOLA **SCZ/8/013/2017**
(Civil Jurisdiction)

B E T W E E N :

AFRICAN LIFE FINANCIAL SERVICES LIMITED **APPELLANT**

AND

ZAMBIA REVENUE AUTHORITY **RESPONDENT**

Coram: **Hamaundu, Malila, and Kabuka, JJS**
On 4th June, 2019 and 23rd July, 2019

For the Appellant: Mr. M. Chiteba of Messrs Mulenga Mundashi Kasonde Legal Practitioners

For the Respondent: Mrs. S. Mulwanda-Chanda, in-house Legal Counsel, Zambia Revenue Authority

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J U D G M E N T

Malila, JS delivered the judgment of the court.

Case referred to:

1. *Hallstroms Pty Ltd v. Federal Commissioner of Taxation (1964) 72 CLR 634 p. 648*
2. *Tyco Australia Pty Ltd v. Federal Commissioner of Taxation (2007) FCA 1055*
3. *British Insulated and Helsby Cables Ltd v. Atherton (1920) AC 205*
4. *Heather (Inspector of Taxes) v. P.E. Consulting Group (1922) 2ALL ER 107*

5. *Odeon Associated Theatres Ltd v. Jones (Inspector of Taxes) (1971) 1WLR 454*
6. *British Insulated and Helsby Cables Limited v. Atherton (1926) AC 205*

Legislation referred to:

1. *Income Tax Act, chapter 323 of the laws of Zambia*
2. *Companies Act, chapter 388 of the laws of Zambia*
3. *Pensions Scheme Regulations Amendment Act No. 27 of 2006 (the PSRA)*
4. *Halsbury's Laws of England Vol. 24, 4th ed. para. 8*
5. *Income Tax Assessment Acts, 1936-1941*

The appellant was aggrieved by a decision of the Tax Appeals Tribunal (the Tribunal) given in September 2017, whereby the Tribunal upheld the respondent's refusal to grant the appellant tax relief under section 91 of the Income Tax Act, chapter 323 of the laws of Zambia.

The background facts are plain. The appellant is an incorporated entity under the Companies Act, chapter 388 of the laws of Zambia. It was owned by Botswana Insurance Fund Managers (BIFM) and MENEL Management Services (MANEL) in the ratio of 70% and 30% respectively. It carried on business as a provider of pension fund management services, which is a regulated business under the superintendence of the Pensions and Insurance Authority (PIA). Alongside that regulated business, the appellant carried on non-regulated business ventures in the nature of asset management.

The passage of the Pensions Scheme Regulations Amendment Act No. 27 of 2006 (the PSRA) changed the regulatory framework in regard to PIA regulated business. By section 17 of the PSRA, it was a requirement that at least 51% of the shares in any pension fund managers' equity should be owned by Zambian citizens.

In its quest to comply with the new legal requirement, the appellant decided to restructure its operations by separating those of its activities that fell under the supervisory mandate of the PIA and those that did not. In the restructured set up, the ownership of the appellant was to be refashioned around this consideration.

To attain that end, the appellant incorporated a company called Quantum Assets Zambia Limited (Quantum) in the same shareholding proportions as in the appellant, the purpose of which was to assume the non-regulated business hitherto undertaken by the appellant. The incorporation of Quantum having been done, the non-regulated business of the appellant was then transferred to Quantum following a special dividend declared by the appellant in favour of its shareholders.

On advice from a firm of tax consultants, and in the belief at that time that the special dividend declared consummating the transfer of the unregulated business from the appellant to Quantum represented a taxable dividend in the hands of the shareholders, the appellant paid K5,999,018.12 to the respondent, being 15% withholding tax on that dividend.

Further advice was received by the appellant from its auditors, cum tax advisors – Deloitte & Touche. This was to the effect that the Income Tax Act, chapter 323 of the laws of Zambia, does not, after all, require the payment of withholding tax on dividends in the case of a restructuring in the manner done by the appellant.

The appellant was then enlivened to the possibility of recovering, by way of tax relief, the payment of withholding tax which it now believed was not payable at all on the restructuring exercise it had undertaken.

The appellant instructed Messrs Deloitte & Touche to pursue the recovery, by way of tax relief, from the respondent, of the moneys paid as withholding tax. The latter wrote, in August 2012, a suitably worded letter to the respondent, applying for a refund, in the form of tax relief, of the withholding tax paid by the appellant on the special dividend.

The respondent's response was perhaps predictably less than enthusiastic. It rejected the appellant's request, insisting that the withholding tax on the special dividend was correctly and properly paid. The appellant then appealed to the Tax Appeals Tribunal on one ground, namely that:

> **The respondent erred in law in refusing to grant the appellant error tax relief under section 91 of the Income Tax Act because the income Tax Act does not require payment of withholding tax in the case of a restructuring by operation of law...**

After considering the submissions of the advocates for the respective parties, the Tribunal dismissed the appeal, holding that there was no error or mistake in the payment of the withholding tax by the appellant to warrant any relief under section 91 of the Income Tax Act. It is that decision of the Tribunal that has prompted the appellant to launch the present appeal, fronting three grounds formulated as follows:

1. **The Tax Appeals Tribunal misdirected itself in law and fact when it held that the test of whether a dividend is capital or revenue by nature is to be determined based on the source of the dividend and not the manner in which it is applied;**

2. **The Tax Appeals Tribunal misdirected itself in law when it held that the special dividend paid by the appellant was revenue by nature because it was paid out of company profits or earnings;**

3. **The Tax Appeals Tribunal erred in law and in fact when it held that there was no error in the payment of withholding tax by the appellant for it to qualify for relief under section 91 of the Income Tax Act.**

Heads of argument were filed on behalf of the respective parties. At the hearing of the appeal, the learned counsel for the parties were present. Both Mr. Chiteba, for the appellant, and Mrs. Mulwanda-Chanda, for the respondent, adopted and placed reliance on their heads of argument.

In respect of ground one, Mr. Chiteba contended that the appellant's restructuring exercise undertaken with a view to reorganising its business, did not attract 15% withholding tax which was in fact paid by the appellant in error and, therefore, that the Tribunal was wrong to have endorsed the decision of the respondent in this regard. He specifically took issue with the following passage from the ruling of the Tribunal:

> **We therefore have to agree with the respondent that the test is the source of the dividend and not its treatment thereafter or whether or not certain cash has accrued to the investor or shareholder.**

The learned counsel submitted that in terms of section 17 of the Income Tax Act, 'income' includes dividends. Withholding tax is payable on dividends for a company in the same way that the company is obliged to account for pay-as-you-earn (PAYE). It follows, according to counsel, that withholding tax is a tax on the recipient of income.

Counsel adverted to **Halsbury's Laws of England** (Vol. 24, 4th ed. paragraph 8) and submitted that there is no comprehensive definition of the term income. However, in **Halsbury's Laws of England** it is said to be:

> **...the quality of the receipt in the recipient's hands, not the fund or pool of money out of which it is paid, which is to be regarded in determining whether it ranks as income.**

Counsel also quoted two more passages. The first was from the case of *Hallstroms Pty Ltd v. Federal Commissioner of Taxation*[1] which reads as follows:

> **What is an outgoing of capital and what is an outgoing on account of revenue depends on what the expenditure is calculated to effect from a practical and business point of view, rather than upon the juristic classification of the legal rights, if any, employed or exhausted in the process.**

The other was from *Tyco Australia Pty Ltd v. Federal Commissioner of Taxation*[2] reading as follows:

> **The enquiry as to whether an outgoing is on capital or revenue account looks to the business and practical effects and advantages sought in the whole context.**

He submitted that flowing from the foregoing, dividends can either be categorised as capital or revenue in nature, depending on the manner in which the dividend in question is effected or the quality of receipt in the recipient's hands, and not the source. In the present case, according to Mr. Chiteba, the shareholders of the appellant resolved to restructure the appellant in order to achieve compliance with the amended PSRA. The value of the non-regulated business in the appellant was transferred from the revenue reserves of the appellant to a share premium account, which is not distributable.

We were referred to a copy of the letter from the respondent to the appellant's agent, Messrs Deloitte & Touche, in the record of appeal, where the respondent communicated its decision that the dividend was revenue in nature because the said dividend was paid from the retained earnings and not from the shareholder's equity.

The relevant portion of that letter dated 4th April 2013, reads as follows:

> **Our view is that the dividend paid to the shareholders was not a capital dividend as claimed in your letter dated 3rd August 2012. A review of the records which were provided to us indicate that the dividend was paid from retained earnings and not from shareholders equity, hence qualifies to be treated as a distribution of revenue profits.**

Counsel maintained that the source of the dividend is irrelevant in determining whether or not a dividend is capital or revenue in nature. It is the manner in which it is applied that should matter.

The learned counsel for the appellant ended his submission on ground one by reiterating that the dividends in question were transferred from the revenue reserves of the appellant in order to achieve compliance with the amended law. There was, according to counsel, a misdirection on the part of the Tribunal with regard to the test to be employed in determining whether a dividend is revenue or capital in nature.

Turning to ground two of the appeal, Mr. Chiteba referred us to the definition of 'dividend' in section 2 of the Income Tax Act. That section defines a dividend broadly as 'any amount distributed or credited' to the shareholders. However, subsection 3 states that a dividend in relation to a company that is not being wound up or liquidated includes:

> **Any profits distributed, whether in cash or otherwise, other than those of a capital nature, including the value of that element of any shares awarded to its shareholders which is redeemable or capable of redemption by conversion and any debentures or securities awarded to its shareholders by a company.** (underlining ours for emphasis)

The learned counsel interpreted this provision to mean that for a company not being wound up or liquidated, a dividend relates to any profits distributed, but excludes profits or distributions of a capital nature so that where profit distribution is revenue in nature, it should attract withholding tax. On the other hand, if the distribution is capital in nature, it should not attract withholding tax. The distribution in the present situation was capital in nature.

The learned counsel accordingly submitted that it was a misdirection for the Tribunal to have held that the 'special dividend' paid by the appellant was revenue in nature because it was paid out of the company's profits. This is because the definition of a dividend presupposes that a capital distribution (excluded from the definition of a dividend) will be derived from profits. This position, according to the learned counsel, is reinforced by the holding in the case of *British Insulated and Helsby Cables Ltd v. Atherton*[3] where it was stated as follows:

> **When expenditure is made not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, there is very good reason...for treating such an expenditure as properly attributable not to revenue, but to capital.**

In regard to ground three, it was submitted that the appellant had declared what it erroneously called a 'special dividend' of K39,993 million which resulted in a payment of withholding tax on it in error. In terms of section 91(1) of the Income Tax Act, the appellant was entitled to claim relief. That section provides that:

> **If any person alleges that an assessment is excessive by reason of some error or mistake in the return or statement made by him for the purpose of the assessment, he may, at any time, not later than six years after the end of the charge year in respect of which the assessment was made, make an application in writing to the Commissioner General for relief.**

Counsel prayed that we uphold the appeal.

The respondent, for its part, stoutly opposed the appeal on all grounds. In supporting the holding of the Tribunal in respect of ground one of the appeal, it was submitted by Mrs. Mulwanda-

Chanda that the appellant made reference to foreign case law and a selective reference to **Halsbury's Laws of England** but has made no reference to Zambian statutory authority to support the argument.

Mrs. Mulwanda-Chanda also submitted that the Income Tax Act does not support the argument made on behalf of the appellant under this ground of appeal. To the contrary, it reinforces the position taken by the Tribunal that the test to use in determining whether a dividend is capital or revenue in nature is to consider its source.

According to the respondent, the Income Tax Act imposes a withholding tax on dividends on the basis that it is paid out of the income of a company. The income in this case represents the revenues of the company and, therefore, the dividend is paid out of the revenue account of a company.

It was further contended that by virtue of the dividends being paid out of the revenue/income account, it is a dividend of a revenue nature. The Income Tax Act only imposes a withholding tax on dividends when it is established that the dividend is paid out of the income/revenue of the company, and this points to the source of the dividend.

The learned counsel quoted section 17 of the Income Tax Act which identifies 'income' sources for any charge year to include dividends. She then turned to section 81 of the Income Tax Act, which she quoted. That section obliges every company incorporated in Zambia to deduct from every payment of dividend, a tax at the rate specified in the Charging Schedule. Part I, 6(1) of the Charging Schedule reads as follows:

> **Tax required to be deducted from any payment made under section eighty-two and section eighty-one shall be deducted at:**
>
> **(a) The rate of fifteen percent for dividends...**

Mrs. Mulwanda-Chanda then took us into a meticulous analysis of the situation, viewed from the appellant's perspective. She did this through a series of factual questions which she answered by reference to the evidence on record. The first of these questions was whether the appellant had declared and paid any dividend? Her answer to this question was in the affirmative, adding that the appellant had throughout admitted that a dividend in the sum of K39,993 million had been declared.

The second question counsel posed was whether the dividend was paid out of income/revenue of the appellant? Again, by reference to specific evidence in the record of appeal, the answer she gave was, 'yes'.

Counsel then asked the third question as to whether withholding tax was paid on the dividend declared and paid out by the appellant. To this, she explained that following the declaration and payment of the dividend into the appellant's revenue reserve account, the appellant proceeded to make a payment of the withholding tax in the sum of K5,999,016.12, being 15% of the dividend declared and paid. The payment of this sum is, likewise, not in dispute. The learned counsel referred us to portions of the record where that is confirmed.

She then turned to the crucial question whether the dividends were paid out of either one of the share capital account or the share premium account. To this she gave an emphatic 'no' as the answer. The dividends, according to counsel, came neither from the share capital account nor the share premium account. She referred us to the record of appeal, and more specifically to the columns titled 'share capital' and 'share premium,' neither of which contains any deduction for a dividend, let alone reference to the figure K39,993 million.

The learned counsel pointed out that the record clearly showed that it was the appellant's own witness, Mr. Muhundika, who testified that the dividends were paid from the revenue reserve account of the appellant. According to counsel, the Tribunal subsequently confirmed that the dividend in the sum of K39,993 million was not paid out of either the share capital account or the share premium account.

Counsel for the respondent then referred us to the testimony of the respondent's Expert Witness, a Mr. Stephen Chulu, the gist of which was that the dividend of K39,993 million, having been paid out of the revenue reserves, cannot be said to be a dividend of a capital nature as revenue reserves are a representation of accumulation of yearly profits over a period of time. According to the same witness, dividends declared out of the share capital or share premium account qualify to be called dividends of a capital nature, but having been paid out of the revenue reserves, those dividends cannot be called dividends of a capital nature.

From the foregoing two significant conclusions were made and stressed by the learned counsel for the respondent, namely: first, that there was confirmation that the Tribunal was in essence right to hold that the test of whether a dividend is capital or revenue in nature is to be determined on the basis of the sources of the dividend. Second, the fact that the respondent's Expert Witness' evidence was not challenged and remained unshaken in cross-examination rendered credence to the respondent's position.

Counsel contended that the case of *Hallstroms Pty Ltd v. Federal Commissioner of Taxation*[(1)] cited by counsel for the appellant, was distinguishable and thus inapplicable to the present situation. That case did not deal with dividends but allowable deductions from assessable income under the Income Tax Assessment Acts 1936-1941. We were accordingly urged to dismiss ground one of the appeal.

With regard to ground two of the appeal, the response of the learned counsel for the respondent was to reiterate the arguments she made in respect of ground one of the appeal, and more especially those surrounding the evidence of the respondent's Expert Witness.

Counsel argued that although the appellant's learned counsel has correctly quoted section 2 of the Income Tax Act, the same has been misunderstood and wrongly applied. According to Mrs. Mulwanda-Chanda, the import of subsection 3 of that section is that in the context of dividends, any profits which are distributed other than profits of a capital nature, shall be considered as dividends. It also means that any profits distributed and are of a capital nature such as profits distributed from a share capital or share premium account, shall not be considered as a dividend and, therefore, not liable to payment of withholding tax. The dividends paid and distributed by the appellant were made out of the revenue reserves account.

Counsel also dismissed as misplaced the appellant's reliance on the case of *British Insulated and Helsby Cables Ltd. v. Atherton*(3), as in *Heather (Inspector of Taxes) v. P.E. Consulting Group*(4), Goulding J dispelled the notion in the *British Insulated*[3] case in the following terms:

> **The general principle seem, on the contrary, to be that in determining what is capital expenditure and what is revenue expenditure in order to ascertain profits for tax purpose, the court must follow ordinary principles of commercial accountancy, save so far as modified by express statutory direction.**

This position, according to Mrs. Mulwanda-Chanda, was echoed in *Odeon Associated Theatres Ltd v. Jones (Inspector of Taxes)*[5].

We were urged to dismiss ground two of the appeal as well.

The reaction of counsel for the respondent to ground three was fairly short. She submitted that ground three is dependent on grounds one and two. From her arguments under grounds one and two, it should follow, according to Mrs. Mulwanda-Chanda, that the payment of K5,999,016.12 as withholding tax was correctly done. There being no error, the claim for relief under section 91 of the Income Tax Act must, according to counsel, fail.

Counsel submitted that as the appellant had failed to prove that there was an error or mistake in the payment of withholding tax. Ground three should equally be dismissed.

We have considered, with immense interest, the rival arguments so ably addressed to us by the learned counsel for the respective parties. The material facts are themselves not in contention. It seems to us that the main dispute between the parties is entirely interpretational. Although there is a proliferation in the use of technical, fiscal and accounting terms, the overarching question is whether the special dividend declared in the context of the reorganization undertaken by the appellant is one that attracts withholding tax.

To answer this question, it is imperative to determine the subsidiary question whether the special dividend declared was one of a capital nature, or one of a revenue nature or indeed one of a totally different species. Our view is that the three grounds of appeal are cross-cutting in substance. We shall, therefore, consider them compositely.

The first grievance of the appellant is with regard to the Tribunal's holding that the determinative test as to whether the dividend declared attracted withholding tax or not, is the source of the dividend rather than the purpose to which it was applied. As we shall establish later on in this judgment, we believe that unduly heavy premium has been placed on the issue of the source rather than the application.

The difference in positions between the appellant and the respondent stems largely from the interpretation that they each place on section 2(3) of the Income Tax Act. In effect, the argument boils down to whether or not the special dividend declared by the appellant was one of a capital nature within the intendment of that section. The appellant believes it was while the respondent argues it was not. The Tribunal held that it was of a revenue nature.

We have already quoted the relevant parts of section 2(3) earlier in this judgment on the definition of a dividend. It includes any profit distributed <u>whether in cash or otherwise, other than those of a capital nature</u> (emphasis added).

Mr. Chiteba contended that the dividend declared was capital in nature because it was declared from the retained earnings of the company and not from the shareholders' equity. In another breath, however, he had argued that it does not matter what the source of the dividend is; it is the application that does.

The appellant's expert witness, Mr. Muhundika, had also told the Tribunal during the hearing in re-examination that the special dividend was declared from the retained earnings of the company and not the capital account.

We find the responses by the appellant's expert witness before the Tribunal usefully revealing when in cross-examination he read out section 2(3) of the Income Tax Act. To recap, the witness stated that:

> **The Act itself recognizes that a profit distribution can be capital in nature. So, the contention in that letter [from the respondent] that because this profit distribution, or distribution is coming from the retained earnings, it has to be revenue in nature, already, it is being challenged by that provision which makes an exception of distribution of profits of the capital nature...I explained earlier our position is that this distribution is capital in nature and is actually captured by that exception.**

Elsewhere in his evidence, the expert witness stated that:

> **There is nothing that accrued to the shareholders as a result of this restructuring. The position as far as the shareholders are concerned before and immediately after this incident, in terms of the assets they hold in the business is exactly the same. There was no accrued of income, there was accrual of assets to the individual shareholders that they could dispose of, there was nothing that happened other than splitting their business into two. It is like a man who owns cattle. You have ten animals then you decide to split the ten into two**

kraals. One kraal here with 5, the other kraal 5 here. Nothing has happened, its exactly the same thing.

In responding to the Tribunal's question whether the dividend that moved to holding the equity in Quantum was distributable, the expert witness answered that it was not distributable as it moved into a share premium account – which is more permanent than retained earnings. To appreciate these submissions, one has to understand what retained earnings of a company are and what they are ordinarily used for.

Mr. Chiteba did not end at the point he made about the dividend being from retained earnings. He submitted that the dividends in question were transferred from the revenue reserves to the share premium account of the appellant to attain compliance with the amended law. This is a point also made by the appellant's expert witness. Again, it is significant to appreciate the terminology used.

Our understanding of the term 'retained earnings' of a company is that these comprise the net of income left over from the business after the company has paid out dividends to its shareholders. The earnings of a company, if positive in the sense that the company did not operate at a loss, could be used in a variety of ways. As intimated already, often the profit is paid out to shareholders as dividends. A company does not have to pay tax on its retained earnings since those earning represent some or all of the company's after-tax profit. The money not paid to the shareholders that is to say, retained earnings, may be invested for purposes of expanding the existing business operation or other investment that may improve the business prospects of the company. It may also be used for share buy-backs or indeed to pay any outstanding loans the business may have.

We apprehend revenue reserves of the company as comprising money retained in the business of a company so as to meet future obligations. Capital reserves, on the other hand, refers to a fund that is created to finance long term projects or to write off expenses. The revenue reserve account is thus available for distribution of dividends, while the capital reserve account is not.

What about the share premium account which Mr. Chiteba referred to as having been credited for the value of the non-regulated business and was transferred from the revenue reserves of the appellant to a share premium account? We are aware that the share premium account or the capital surplus account ordinarily appears on the company's balance sheet as a component of shareholders' equity and is not, as the appellant's expert witness correctly told the Tribunal, distributable.

A capital dividend is a form of dividend declared by a company to its shareholders that is drawn from the company's paid in capital or shareholders' equity rather than from the company's earnings. A capital dividend is typically not taxable for shareholders as it is viewed as a return of the capital the investor paid in.

The letter from the respondent declining to grant the appellant the tax respite sought by the appellant intimated that the respondent based its decision on the fact that the dividend was revenue in nature because it was paid from the retained earnings. In other words, because of the source, rather than its application.

A traditional or ordinary dividend, when declared, is taxable since it represents a cash outflow from a company's earnings. It may be issued in the form of cash payment, shares of stock or any other form.

Section 145 of the Companies Act No. 10 of 2017 provides that the share premium account may be applied by the company:

(a) In paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares;

(b) In writing off

(i) the preliminary expenses of the company; or

(ii) the expenses of, the commission paid or the discount allowed on any issue of shares or debentures of the company; or

(c) In providing for the premiums payable on redemption of any redeemable preference shares or of any debenture of the company.

It does not seem to us that if indeed, as argued by the learned counsel for the appellant, the special dividend was paid into a share premium account, the use to which that money was applied, i.e. as the share capital for Quantum, can be located into any of the uses specified in section 145 of the Companies Act detailing the uses to which such an account could be resorted.

There appears to be a sense in which retained earnings could be used for profit distribution which could be capital in nature. It seems to us, therefore, that section 2(3) of the Income Tax Act was fully cognizant of this fact for it clearly states, as the appellant's expert witness testified, that distributable profits could be both revenue or capital in nature.

We do not agree, therefore, with the Tribunal that the sole test *to* be used in determining whether a dividend is capital or revenue in nature is considering the source rather than the manner in which it is applied. Our view is that a characterization of a dividend as either revenue or capital premised only on the source of the dividend is erroneous. We agree with the appellant that rather, it is the application of the distributed profits that will determine its characterization into revenue or capital. Ground one as structured is bound to succeed and we uphold it accordingly.

Expressed in non-technical and non-elevated language, our understanding of the position here is simply this, that, a special dividend was declared. This was a one off, non-recurring distribution of the company's assets to shareholders – tied to a specific event, that is to say, the restructuring of the company. As defined by the Companies Act, section 2 and the equivalent section in the Income Tax Act, a dividend is money to be dividend and distributed or credited to the shareholders out of the profits arising or accumulating from the appellant company's business.

The special dividend did not, however, result in money getting into the pockets of the shareholders. It was immediately transferred to the books of Quantum and instantly reflected that each of the shareholders (i.e. BIFM and MENEL) held equity or value in Quantum.

The transaction that occurred in the present situation was not one of the company offering shares in lieu of cash dividends, in terms of section 160 of the Companies Act.

It is, of course, significant to understand why distribution of dividends of a capital nature is exempt from suffering withholding tax. Our view is that the underlying policy is to encourage investment rather than consumption. A dividend paid out in the form of cash to a shareholder is money in the hands of the recipient and thus liable to be taxed. A special dividend paid out in the form of an allotment of shares, on the other hand, signifies investment and growth which can only result in more value to the company and enhanced taxable income.

In our considered view, section 2(3)(a)(ii) in its exemption of dividends of a capital nature should be understood in context. It refers to dividends of a capital nature declared by a company to its shareholders, that is to say the shareholders of the very company declaring the dividends.

The contemplation of section 2(3)(a)(1) in exempting payment of withholding tax on dividends of a capital nature, is that such dividends would go to enhancing the capital value of the company which would invariably result in greater profitability for the company with the enhancement of its taxable income-generation capacity. It does not appear to us to have been intended that exempted dividends of a capital nature would go to the acquisition of shares in a separate, albeit related company.

As regards ground two of the appeal, we have already shown that in terms of section 145 of the Companies Act, a share premium account is to be applied for very limited specified purposes. Having regard to that section, paying for unissued shares, or for shares to be issues as fully paid bonus shares is what comes close to the purpose to which the special dividend in the present case was used for. However, our reading of that section does indeed suggest that any such payment for shares to be issued must be to the existing members of the company from whose premium account the payment is made. This was clearly not the case here where there are two different companies, albeit related through shareholding.

We accept the position taken by the English Court of appeal in *British Insulated and Helsby Cables Limited v. Atherton*[(6)] that:

> **When expenditure is made not only once and for all, but with a view to bring into existence an asset or an advantage for the enduring benefit of a trade, there is very good reason...for treating such an expenditure as properly attributable not to revenue, but to capital.**

Our considered view however is that the dividend declared in this particular case came from the appellant's profits or earnings. The Tribunal did not, therefore, misdirect itself as alleged in ground two of the appeal. As we have explained however, this is inconsequential.

It follows from our reflection that there was no error in the payment of withholding tax by the appellant as contended by the appellant's learned counsel under ground three of the appeal. That ground is bound to fail.

The net result is that the appeal, is on the whole, without merit and is dismissed. Costs shall follow the event.

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E. M. Hamaundu
SUPREME COURT JUDGE

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M. Malila
SUPREME COURT JUDGE

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J. K. Kabuka
SUPREME COURT JUDGE