*Privy Council Appeal No. 23 of 1951*

**The Attorney General of Ceylon** - - - - - - *Appellant*

*v.*

**Charles William Mackie (Junior) and another the Executors of the Will of Charles William Mackie, deceased** - - - - - - - *Respondents*

FROM

## THE SUPREME COURT OF CEYLON

# JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL DELIVERED THE 6TH OCTOBER, 1952

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*Present at the Hearing:*

VISCOUNT SIMON
LORD NORMAND
LORD MORTON OF HENRYTON
LORD REID
SIR LIONEL LEACH

[*Delivered by* LORD REID]

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This is an appeal from a decree of the Supreme Court of Ceylon dated 25th May, 1950, which allowed an appeal from an Order of the District Court of Colombo dated 31st August, 1949. The question at issue is the valuation for the purpose of Estate Duty of 5,000 Management Shares of C. W. Mackie & Company Limited (hereinafter called the Company) which belonged to the late Mr. C. W. Mackie (hereinafter called the deceased) at his death on 7th September, 1940. The respondents are his executors. The District Court of Colombo held that the value of these shares at that date was Rs.250 per share. On appeal the Supreme Court reduced that valuation to Rs. 40.6188 per share. The appellant maintains that the valuation of the District Court should be restored.

The deceased had carried on business in Ceylon as a rubber merchant since about 1908 and his business was acquired by the Company as a going concern on its incorporation in Ceylon in 1922. The capital of the Company, which remained unchanged throughout, was Rs.1,000,000 divided into 19,800 8 per cent. Cumulative Preference Shares of Rs.50 each and 5,000 Management Shares of Rs.2 each. The deceased was Life Director of the Company with extensive powers and from the beginning he had held a large part of the share capital and taken the leading part in the management of the Company. He left Ceylon about 1930 but continued thereafter to exercise some supervision. At his death he held 9,201 Preference Shares and all the Management Shares.

The practice of the Company was to buy rubber and grade it for resale. Its graded rubber, known as Mackie standard, had a high reputation in important foreign markets and it appears that some 20 per cent. or 30 per cent. of the whole of the rubber exported from Ceylon was handled by the Company. The policy of the Company was to hold large stocks, and, as the price of rubber has for long been subject to large and rapid fluctuations, the Company's profits varied to an extreme degree. During its first five years very large profits were made amounting

in all to over Rs.3,000,000. During the next six years to 1932 large losses were incurred amounting to over Rs.1,800,000. During the next six years there were profits in four years and losses in two, the figures varying from a profit of Rs.443,161 in 1933 to a loss of Rs.281,907 in 1935. Finally in 1939 and 1940 there were profits of Rs.787,641 and Rs.501,878. No dividend had been paid on the Preference Shares since 1930 and no dividend had been paid on the Management Shares since 1926, the Company having found it necessary to borrow large sums from time to time on overdraft. The leading witness for the appellant admitted that he did not know of a more speculative business in Ceylon.

The Statute in force at the time of the deceased's death was the Estate Duty Ordinance of 1938: by section 20 of that Ordinance it was provided that the value of any property should be estimated to be the price which, in the opinion of an assessor, such property would fetch if sold in the open market at the time of the death of the deceased. Section 20 contains a proviso to the effect that if the value of the property has been depreciated by the death of the deceased such depreciation is to be taken into account. The respondents originally sought to rely on this proviso but they do not now do so. It is now common ground that the shares must be valued at the price which they would have fetched if sold in the open market on 7th September, 1940. The Articles of Association of the Company contained restrictions on transfer of a type often found in private companies, but it is admitted that the decision in *Commissioners of Inland Revenue* v. *Crossman*, 1937, A.C. 26, applies to this case. So the shares must be valued on the footing that the highest bidder in the open market would have been registered as a shareholder but that he would then have become subject to the restrictions in the Articles. In addition to restrictions of a usual character the Articles also contained a provision to the effect that holders of not less than nine-tenths of the share capital could at any time call for a transfer of any other shares at a fair value to be fixed by the auditors of the Company. It was admitted for the appellant that no purchaser would have paid anything like Rs.250 per share for the Management Shares in face of the Company's Articles unless he could buy at the same time a large block of the Preference Shares and so have a majority of votes. But the appellant contends that the respondents must be supposed to have taken the course which would get the largest price for the combined holding of Management and Preference Shares and to have offered for sale together with the Management Shares the whole or at least the greater part of the Preference Shares owned by the deceased. In their Lordships' judgment this contention is correct. But it means that the valuation for which the appellant contends depends on the possibility of having been able to find in September, 1940, a single purchaser prepared to venture a very large sum of money. The agreed valuation of the deceased's Preference Shares is Rs.806,017 and the valuation of the Management Shares for which the appellant now contends is Rs.1,250,000. So a purchaser who wished to acquire a sufficiently large holding to be in a dominant position would have had, on this valuation, to pay some two million rupees in all.

Evidence was given in the District Court as to the value of the shares. The leading witness for the respondents was Mr. Lander, a Chartered Accountant, who had experience of rubber companies. The gist of his evidence was that a buyer would first ask what was the last dividend and when was it paid: but as no dividend had been paid for many years it was impossible to value the shares on a yield basis. He then pointed out that in 1940 the future was unpredictable and it was difficult to find anyone who was willing to invest large sums of money on speculation. He valued the shares on a balance sheet basis because in his view no one would have paid more than that at the time. When asked in cross-examination whether a buyer would not have taken into account the probability that the high profits of 1940 would last for some time, he said that the buyer " would have needed to know precisely what was going to happen in the world which was devastated by war, the length of which could not be guessed by the man in the street. In other words if a

purchaser could have guessed that there was going to be a long war, no Government interference, no form of increased taxation, that he was not going to have competition from others he might take that view. He would be a brave man. It would possibly be a gamble." In his view no good will attached to the business. Similar evidence was given by other witnesses for the respondents.

There was really no contradictory evidence for the appellant on what their Lordships regard as some of the most important points. Neither of the appellant's witnesses professed to have been familiar with the market for shares of rubber companies or to have any direct knowledge about the possibility in 1940 of finding a purchaser for this large block of shares although they admitted that no one would pay the price on their valuation without acquiring such an interest. The respondents' case was that if the shares had been offered at prices corresponding to the value of the tangible assets held by the Company they might have been sold: a purchaser would not then have been gambling on a continuance of the high rate of profit at the beginning of the war. But a purchaser could not have been found to venture two million rupees on a speculation. The appellant's witnesses hardly dealt with these matters. Their approach was more theoretical. They assumed that it was possible to estimate the future average maintainable profit by means of an arithmetical calculation from past profits and losses, and that a purchaser could have been found who would have paid a price for the shares determined by a further arithmetical calculation from that average maintainable profit. One witness said that " a buyer would concentrate on the last five years profits because that is most likely to represent what would happen in the future " ; and the other witness went so far as to say that a prudent buyer would take it for granted that conditions would remain the same.

It may be that these assumptions would be justified in many cases. Where the past history of a business shows consistent results or a steady trend and where there has been no disruption of general business conditions it may well be possible to reach a fair valuation by a theoretical calculation. But in this case neither condition was satisfied. The profits and losses of the Company had fluctuated so violently in the past that, as the second witness for the appellant admitted, it is impossible to choose any five consecutive years in the Company's history the result of which would be reflected in the next years profits. It is therefore in their Lordships' judgment not possible in this case to derive by an arithmetical calculation from past results anything which could properly have been regarded in 1940 as an average maintainable profit, and in addition there were extremely uncertain conditions of 1940. The appellant's witnesses made no allowance for these facts and were not able to give informed evidence on the question whether a purchaser could have been found in 1940 willing to lay out the large sum required on their valuation.

The learned judge of the District Court founded on two lists of rubber companies' shares quoted in 1939 and 1940 as showing that in 1940 the investing public were not pessimistic. Their Lordships are unable to draw any conclusion from these lists. No evidence was given about them by the appellant's witnesses. A few questions about them were put to one of the respondents' witnesses Mr. Cuming in cross examination. He said: " There was business in buying rubber shares in 1940 but not considerable business. There was a feeling that Government was going to take over the buying of rubber and as a result there was a certain amount of business ". As the Company's business depended on its ability to buy rubber, any such feeling could not have helped the sale of its shares. It may be that these share lists show that there were more buyers in the market in 1940 than in 1939 but they do not show whether those buyers were prepared to buy large blocks of shares or whether the prices offered exceeded the break up value of the shares. Their Lordships cannot agree with the District Judge that these lists diminish the value of the evidence of the respondents' witnesses. And there are other matters where

the learned judge appears to have gone beyond the evidence. For example he said that it was quite evident to the other directors at the death of the deceased that large profits were to be made in the near future, and that there is always a goodwill attached to a company of this character.

In their Lordships' judgment the value of these shares at the date of the deceased's death is a question of fact which must be decided on the evidence which was led. That evidence has been very fully considered by the learned judges of the Supreme Court and their Lordships cannot find that these learned judges have in any way misdirected themselves. It was argued for the appellant that the Supreme Court erred in law in accepting the balance sheet method of valuation because that can only give break up value and in this case it is necessary to find the value of the business as a going concern. It is true that a purchaser of the shares held by the deceased could have obtained a controlling interest in the Company as a going concern and in their Lordships' judgment it is right to value these shares by reference to the value of the Company's business as a going concern. No doubt the value of an established business as a going concern generally exceeds and often greatly exceeds the total value of its tangible assets. But that cannot be assumed to be universally true. If it is proved in a particular case that at the relevant date the business could not have been sold for more than the value of its tangible assets then that must be taken to be its value as a going concern. In their Lordships' judgment it has been proved in this case that the deceased's holding could not have been sold in September, 1940, at a price based on any higher figure than the value of the tangible assets of the Company.

Their Lordships will therefore humbly advise Her Majesty that this appeal should be dismissed. The appellant must pay the costs of the appeal.

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In the Privy Council

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THE ATTORNEY GENERAL OF CEYLON

*v.*

CHARLES WILLIAM MACKIE (JUNIOR) AND ANOTHER THE EXECUTORS OF THE WILL OF CHARLES WILLIAM MACKIE, DECEASED

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DELIVERED BY LORD REID

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