

The Court recalled the interlocutor of the Lord Ordinary and decerned against the defenders for the sum of £3475.

Counsel for the Defenders (Reclaimers)—Sandeman, K.C.—Macquisten. Agents—Alex. Morison & Co., W.S.

Counsel for the Pursuers (Respondents)—Moncrieff, K.C.—Scott. Agents—Kessen & Smith, W.S.

Tuesday, January 7.

SECOND DIVISION.

(EXCHEQUER CAUSE.)

ARCHIBALD THOMSON, BLACK, & COMPANY, LIMITED v. INLAND REVENUE.

Revenue—Income Tax—Profits—Deduction—Expenses Incurred in Reducing Capital of Limited Company—Income Tax Act 1842 (5 and 6 Vict. cap. 35), sec. 100, Schedule D, First Case.

The Income Tax Act 1842, section 100, enacts—“The duties hereby granted, contained in the schedule marked D, shall be assessed and charged under the following rules:— . . . Schedule D, First Case.—*Duties to be Charged in respect of any Trade.*— . . . Rule First—The duty to be charged in respect thereof shall be computed on a sum not less than the full amount of the balance of the profits or gains of such trade. . . . Rule Third—In estimating the balance of profits and gains chargeable under Schedule D . . . no sum shall be set against or deducted from such profits or gains on account of . . . any sum employed or intended to be employed as capital in such trade, and [Rules applying to the First and Second Cases, First Rule] for any disbursements or expenses whatever not being money wholly and exclusively laid out or expended for the purposes of such trade. . . .”

A limited company which had incurred a large debit balance on its profit and loss account applied to the Court to have its capital reduced so as to enable it to resume the payment of dividends out of profits which would otherwise have fallen to be applied in extinguishing the debit balance. Held that the expense of carrying out the reduction was not a proper deduction from the profits for the purpose of assessment to income tax, in respect that it was not made for the purposes of the trade of the company, but for the purpose of distributing the profits of the trade after they had been earned.

Archibald Thomson, Black, & Company, Limited, wire rope manufacturers, Glasgow, appellants, being dissatisfied with an assessment made on them under Schedule D of the Income Tax Acts for the year ending 5th April 1917, amounting to £2089 less depreciation allowance £896, took a Case in which

J. Batty, surveyor of taxes, was respondent. The appellants claimed £300, being the amount expended by them in the year to 31st December 1915 in reducing the capital of the company, as an allowable deduction from their profits for income tax purposes.

The Case stated—“The following facts were admitted or proved:—1. The appellants in the year 1914 reduced their capital from £30,000, divided into 15,000 preference shares of £1 each and 15,000 ordinary shares of £1 each, to £18,829, 16s., divided into 15,000 preference shares of £1 each and 12,766 ordinary shares of 6s. each. 2. The circumstances under which the reduction was effected were that for several years between 1906 and 1912 the company had not been successful, with the result that a balance had accumulated at the debit of profit and loss account until at 31st December 1912 it reached £10,010, 7s. 11d., and at 31st December 1913 it stood at £8397, 11s. 4d. There were also certain assets which were unrepresented by value. 3. The object of the reduction was to enable the company to resume the payment of dividends out of the balance of each year's trading, which would otherwise have fallen to be applied in reducing the debit balance in the profit and loss account until it was extinguished. 4. In reducing their capital as aforesaid the appellants incurred legal expenses consisting of accounts due to solicitors in Glasgow and Edinburgh, counsels' fees, printing, Court dues, and other incidental expenses. No objection was taken to the amount of the said expenses, and it was admitted that they had been incurred.

“The Commissioners, after hearing parties, were of opinion that the legal expenses incurred in reducing the capital of the appellants were not admissible as deductions from profits assessed under Schedule D of the Income Tax Acts, and they dismissed the appeal accordingly.”

Argued for the appellants—The sum in question was a legitimate deduction from profits in respect that it had been incurred not only for the purpose of the trade but in order to earn profits. A company's commercial success was dependent on its reputation, and if it was so encumbered that it could not pay a dividend its reputation and therefore its profits suffered. There was nothing to prevent an item of revenue expenditure being incurred once for all. Profits meant the surplus of the assets at the end of one accounting period over the assets at the preceding, and according to this standard the expenditure in question was a legitimate deduction—*Usher's Wiltshire Brewery, Limited v. Bruce*, [1915] A.C. 433, per Lord Loreburn at p. 443, 52 S.L.R. 894; *Smith v. Lion Brewery Company, Limited*, [1911] A.C. 150, 48 S.L.R. 1083; *in re Spanish Prospecting Company, Limited*, [1911] 1 Ch. 92. The deduction in question did not fall within the express prohibition of the Income Tax Acts—Income Tax Act 1842 (5 and 6 Vict. cap. 35), sections 1 and 159.

Argued for the respondent—The deductions claimed were not allowable under the Income Tax Acts. The profits were in no way

affected by the reduction of capital, which only changed their destination—*Strong & Company, Limited v. Woodfield*, [1906] A.C. 448, 44 S.L.R. 624; *Gresham Life Assurance Society v. Styles*, [1892] A.C. 309; *Granite Supply Association, Limited v. Inland Revenue*, 1905, 8 F. 55, 43 S.L.R. 65; *Anglo-Continental Guano Works v. Bell*, 1894, 3 T.C. 239, 70 L.T. 670; *Texas Land and Mortgage Company v. Holtham*, 1894, 63 L.J., Q.B. 496; *Vallambrosa Rubber Company, Limited v. Inland Revenue*, 1910 S.C. 519, 47 S.L.R. 488; *Coltress Iron Company v. Inland Revenue*, 1881, 8 R. (H.L.) 67, 18 S.L.R. 466. The deduction claimed in the present case had nothing to do with the trade which the company was carrying on.

LORD JUSTICE-CLERK—The point in this case is a very short one, but the findings put forward in the case seem to me to be almost conclusive in the matter. I refer to the third finding, which is—“The object of the reduction was to enable the company to resume the payment of dividends out of the balance of each year’s trading, which would otherwise have fallen to be applied in reducing the debit balance in the profit and loss account until it was extinguished.” That as the other facts show means this, that the company, from circumstances which we need not consider, found that its capital had seriously diminished and there was a debit balance of nearly £9000 on its profit and loss account, so that however successful the trading was in each year up to a certain limit, which seems never to have been passed, the whole profit on the trading account was swallowed up by the necessity of meeting the charge of this debit balance of £9000, and the company thought it would be good finance to take the necessary steps to have its capital reduced so that it could get rid of that debit burden which had lain so long upon it. Accordingly it adopted the necessary procedure by which it reduced its capital and wiped out that debit balance. “The object of the reduction was to enable the company to resume the payment of dividends” (I interpolate here “out of profits”) “of each year’s trading which would otherwise have fallen to be applied in reducing the debit balance in the profit and loss account until it was extinguished.” This expenditure incurred in carrying out the reduction, while it was quite proper expenditure and was properly made in the interests of the company, was made, not for the purposes of the trade but for the purpose of distributing more advantageously the results of that trade, namely, the profit which on a trading account balance would have been available for distribution among the shareholders had it not been for the debit balance to which I have already referred. I do not think that is, in a proper sense of the term, a disbursement made for the purposes of the trade. It is made for the purpose of dealing with the results of that trade after these results have been realised—that is to say, it was made for the purpose of distributing the balance of profit and loss among the shareholders instead of using it to wipe out this debit balance.

I think the sole ground upon which this was said to be a proper deduction fails in respect that it is not a deduction made for the purposes of the trade of this company, but for the purposes of distributing the profits of its trade after these profits have been earned. Accordingly the contention of the appellants fails and the judgment of the Commissioners is right.

LORD DUNDAS—I agree that this appeal fails for the reasons stated by your Lordship in the chair.

LORD SALVESEN—I am of the same opinion.

LORD GUTHRIE concurred.

The Court affirmed the determination of the Commissioners.

Counsel for the Appellants—Constable, K.C.—W. T. Watson. Agents—Whigham & MacLeod, S.S.C.

Counsel for the Respondent—Solicitor-General (Morison, K.C.)—R. C. Henderson. Agent—Sir Philip J. Hamilton Grierson, Solicitor of Inland Revenue.

HOUSE OF LORDS.

Thursday, January 16.

(Before Lord Buckmaster, Lord Finlay, Lord Dunedin, Lord Atkinson, and Lord Shaw.)

CRAIG v. CORPORATION OF GLASGOW.

Reparation—Negligence—Proof—Sufficiency of Evidence—Incuria Dans Locum Injurie.

A farmer brought an action of damages against a corporation for personal injuries alleged to have been caused by the negligent driving of an electrically propelled tramcar belonging to them. He averred that while driving home two cows along a public road about five o’clock on a January afternoon he was run into by the car. It was proved that the car struck the foremost cow, that immediately thereafter and before the car stopped the driver felt a bump, and that the farmer was found lying unconscious on the ground to the rear of the car on the near side. The driver admitted that the car was travelling at the rate of about nine miles an hour, and it was proved that the night though cloudy was not dark, it being within two days of full moon. The farmer was unable to give any evidence as to how the accident happened, having lost his memory in consequence of the injury, and no further evidence was available. In an action of damages at his instance against the tramway company, held (rev. judgment of the Second Division) that the evidence justified the inference that the pursuer’s injuries were due to the fault of the defenders.

Metropolitan Railway Company v.