

be done in every business, and apply the proper principles of costing in order to find out how he stands in regard to any particular part of his business.

LORD CULLEN—I also agree. I am unable to see how the assessment under Schedule B in respect of the occupation of the lands of Parkieston only can possibly include profit which has been made through the leasing of grazings on different land.

LORD SKERRINGTON was absent.

The Court affirmed the determination of the Commissioners.

Counsel for the Appellant—Hunter. Agents—Simpson & Marwick, W.S.

Counsel for the Respondent—Solicitor-General (Murray, K.C.)—Wark, K.C.—Skelton. Agent—Stair A. Gillon, Solicitor of Inland Revenue.

Thursday, February 16.

## FIRST DIVISION.

[Exchequer Cause.

### SCOTTISH AND CANADIAN GENERAL INVESTMENT COMPANY v. INLAND REVENUE.

*Revenue—Income Tax—Profits—Interest on Colonial Investments—Debentures of Reorganised Company Equivalent to Arrears of Interest—Income Tax Act 1853 (16 and 17 Vict. cap. 34), sec. 2, Schedule D.*

An investment company held as an investment first mortgage bonds in a Canadian company, the coupons attached to which were for interest at 5 per cent. The Canadian company having become embarrassed and made default in payment of interest, a new company was organised on a plan agreed to by the first mortgage bondholders, as the result of which the investment company received in exchange for the original bonds and remaining coupons first mortgage bonds in the new company equivalent in number and face value to the original holding, and bearing interest from a date two years after the last payment by the old company, and in addition debentures of the new company representing in face value 10 per cent. of the surrendered bonds. In arriving at the profits of the investment company for the year in which the debentures were received the assessor for income tax included 75 per cent. of their face value as representing their value when received. *Held* (1) that there was material before the Commissioners upon which they were entitled to conclude that the debentures were issued as payment of the two years' arrears of interest, and (2) that in the absence of evidence that the debentures were not marketable, or that their value was not the value taken, they were properly included in the computation of profits of the investment company.

The Income Tax Act 1853 (16 and 17 Vict. cap. 34) enacts—Section 2—“The said duties shall be deemed to be granted and made payable yearly for and in respect of the several properties, profits, and gains respectively described or comprised in the several schedules contained in this Act . . . and to be charged under such respective schedules (that is to say) . . . Schedule D— . . . For and in respect of the annual profits or gains arising or accruing to any person residing in the United Kingdom from any kind of property whatever, whether situate in the United Kingdom or elsewhere, and for and in respect of the annual profits or gains arising or accruing to any person residing in the United Kingdom from any profession, trade, employment, or vocation, whether the same shall be respectively carried on in the United Kingdom or elsewhere, and to be charged for every twenty shillings of the annual amount of such profits and gains. . . . And for and in respect of all interest of money, annuities, and other annual profits and gains not charged by virtue of any of the other schedules contained in this Act, and to be charged for every twenty shillings of the annual amount thereof.”

The Scottish and Canadian General Investment Company, *appellants*, being dissatisfied with a decision of the Commissioners for the General Purposes of the Income Tax Acts at Edinburgh sustaining an assessment for the year ending 5th April 1919 made upon the company under the Income Tax Acts, appealed by way of Stated Case, in which A. Easson, Surveyor of Taxes, Edinburgh, was *respondent*.

The assessment which was in respect of the profits of the business carried on by the appellants was made under Schedule D of section 2 of the Income Tax Act 1853 (16 and 17 Vict. cap. 34) and section 17 of the Finance Act 1918 (8 and 9 Geo. V, cap. 15). It was objected to on the ground that it took into account a sum of £773 as received by the appellants in respect of interest on certain first mortgage bonds of Western Canada Power Company, Limited, which the appellants maintained they had not received.

The Case set forth, *inter alia*—“The following facts were admitted or proved:— (1) The company was incorporated on 30th December 1910 under the Companies (Consolidation) Act 1908 as a company limited by shares. The authorised share capital of the company is £500,000, of which £250,000 has been issued and fully paid up. The company has in addition £113,192 raised by the issue of debenture stock and terminable debentures. The registered office of the company is in Edinburgh, where the directors and shareholders meet, whence the affairs of the company are managed, and where all the profits of the company are assessable. (2) The principal objects of the company as set forth in the third clause of its memorandum of association are, shortly stated, to carry on the business of an investment, mortgage, and financial company in all its branches, and to invest in or upon securities or investments of all classes and descriptions, including bonds of any company carrying on business in the Dominion

of Canada. A copy of the memorandum of association of the company is attached hereto and forms part of this case. (3) Among the investments made by the company was one of £10,300 first mortgage bonds of Western Canada Power Company, Limited, payable in pounds sterling, forming part of an issue of \$5,000,000 of these bonds, and bearing interest at the rate of 5 per cent. per annum. (4) In 1915 the said Western Canada Power Company, Limited, became embarrassed and was unable to meet its current obligations, including, *inter alia*, the interest coupons of its first mortgage bonds payable on 1st January 1916. (5) In these circumstances a plan and agreement of reorganisation of Western Canada Power Company, Limited, was prepared in June 1916, which provided for the formation of a new company to be organised under the laws of the Dominion of Canada, and contained, *inter alia*, the following:—‘IV—*Provision for First Mortgage Bondholders of Western Canada Power Company, Limited.*—Holders of the first mortgage bonds of Western Canada Power Company, Limited, will surrender their bonds with the January 1, 1916, and all subsequent coupons attached, and receive in exchange an equal principal amount of first mortgage 5 per cent. bonds of the new company bearing interest from July 1, 1917, together with ten-year 7 per cent. debentures of the new company in principal amount equal to 10 per cent. of the face value of the surrendered bonds. Holders of bonds payable in pounds sterling will receive in exchange new bonds and debentures payable in pounds sterling.’ ‘XI—*Underwriting and Disposition of New Cash.*—An underwriting syndicate will be formed by the noteholders’ committee to underwrite the assessments of noteholders and stockholders, and to acquire all of the stock to be presently issued which shall not be distributable under the terms of the plan to noteholders and stockholders. Members of the noteholders’ committee, the bondholders’ committee, the depositary, bankers, counsel, agents, and officials of the committee may personally become subscribers to such an agreement and participants in the syndicate, and in respect to such subscriptions shall be entitled to the same rights and benefits, and subject to the same obligations, as any other subscriber. The amount of the underwriting obligation will be \$644,640, being 15 per cent. of the face amount of notes and stock for which provision is made under this plan. The sum of \$644,640 to be paid in by the noteholders and stockholders as thus underwritten will be applied to payment or adjustment of the existing indebtedness of Western Canada Power Company, Limited, other than principal and interest of its outstanding mortgage bonds, to the acquisition and installation of new property, the expenses of reorganisation, and of the execution of this plan, the provision of working capital for the new company and the other proper corporate purposes of the new company.’ ‘XII—*Means of Effectuating the Plan.*—This plan has been approved and adopted by the protective committee for first mortgage

bondholders of Western Canada Power Company, Limited, sometimes herein referred to as the bondholders’ committee, and upon the approval thereof by the depositing bondholders in the manner provided in the bondholders’ protective agreement, the bondholders’ committee agrees that it will, upon the plan being declared operative by the noteholders’ committee, proceed under the fourth schedule annexed to the deed of trust and mortgage of Western Canada Power Company, Limited, dated June 30th 1909, to cause all the first mortgage bonds secured under said trust deed and all coupons appertaining thereto maturing January 1, 1916, and subsequently to be satisfied and exchanged for the first mortgage bonds and debentures of the new company as the plan provided. Subject, however, to the provisions of article 17 of the plan.’ ‘XIII—*Provision for Outstanding Contracts and Indebtedness of Western Canada Power Company, Limited.*—Such provision shall be made for outstanding contracts and indebtedness of Western Canada Power Company, Limited (other than the principal and interest of the mortgage bonds of that company, for which provision is made in this plan) as the noteholders’ committee in its absolute discretion may determine, and such contracts and indebtedness may be assumed, paid, adjusted, compromised, secured, or rejected as the noteholders’ committee and the new company may in their discretion deem advisable.’ Article 17 of the plan reserved authority to effectuate the plan by readjustment of capitalisation of the existing company, but a new company was formed as provided for by the plan. (6) The Equitable Trust of London, Limited, the depositaries of the bonds in London, under the scheme, by circular letter dated 24th April 1917 intimated to the bondholders that the plan had been approved at a meeting of the bondholders held on 1st February 1917. In this circular they request the depositors who had received advance of the amount of the January 1st, 1916, coupons on their deposited bonds to repay the same to them. Copies of the said plan and agreement of reorganisation and the said circular letter are annexed and form part of this case. (7) The said plan and agreement of reorganisation received the necessary sanction to bring the same into operation, and in accordance with the provision therein above quoted the company in due course received and was obliged to accept in respect of its holding of £10,300 first mortgage bonds of Western Canada Power Company, Limited, (a) \$50,126.66 first mortgage 5 per cent. bonds of Western Power Company of Canada, Limited (the new company), bearing interest from July 1, 1917, and (b) £1030 ten-year 7 per cent. debentures of the said new company. The interest in arrear in respect of the said first mortgage bonds was the same in amount as the face value of the debentures issued. (8) The Stock Exchange Year Book for 1919 shows that the ten-year 7 per cent. debentures were issued on account of the arrears of interest. (9) In arriving at the company’s profits of the year to 31st

March 1918 for computation of average liability for assessment to income tax for the year 1918-19 there was included as being interest received 75 per cent. of the face value of the said ten-year 7 per cent. debentures taken to represent the value of the said debentures when received by the company. . . . 4. The Commissioners after due consideration of the facts and arguments submitted to them were of the opinion that the 7 per cent. ten-year debentures of the Western Power Company of Canada represented two years' arrears of interest on the 5 per cent. mortgage bonds of the Western Canada Power Company, Limited, and that the form of the satisfaction of the arrears by an issue of debentures did not avoid taxability of the arrears so satisfied if the debentures were of saleable value."

The circular letter referred to under head 6 of the Case contained, *inter alia*, the following:—"Under the plan you are to receive in exchange for your holding of bonds of Western Canada Power Company, Limited, a similar amount of 5 per cent. first mortgage bonds of Western Power Company of Canada, Limited, maturing July 1st, 1949, and bearing interest from July 1st, 1917, together with 7 per cent. debentures of the new company maturing October 1st, 1926, and bearing interest from October 1st, 1916, the face value of such debentures representing 10 per cent. of your holding of bonds of the old company. The old bonds must have January 1st, 1916, and all subsequent coupons attached. . . . Depositors who have received an advance of the amount of the January 1st, 1916, coupons on their deposited bonds are requested to repay same to us on or before April 30th. Interest will not be charged in respect of any such advances which may be repaid to us on or before that date."

The questions for the opinion of the Court were—"1. Whether the Commissioners were justified in finding that the ten-year 7 per cent. debentures represented two years' arrears of interest on the 5 per cent. mortgage bonds of the Western Canada Power Company, Limited, and (2) If so, whether the sum £773 was properly included in the computation of profits of the company for the purposes of income tax."

Argued for the appellants—(1) There was no evidence that the debentures represented the arrears of interest. They were not treated as such in the plan and agreement, and the statement in the Stock Exchange Year Book was not evidence. The onus was on the assessor. He was not entitled to make an inference from the face values of the bonds or from the amounts of the arrears of interest and the face value of the debentures. The debentures were explained by the necessity of inducing the bondholders to consent to the plan of reorganisation. (2) The whole transaction was based upon the default of the Canadian company and if the debentures represented the arrears of interest they could only do so in the sense that their acceptance was a postponement of the obligation. In such circumstances the debentures, although they might have a saleable value, were not income—*Scottish*

*Widows' Fund v. Inland Revenue*, 1909 S.C. 1372, 46 S.L.R. 993; *Scottish Provident Institution v. Inland Revenue*, 1912 S.C. 452, 49 S.L.R. 435—and could not be charged for income tax until they matured or were realised. There was no evidence that the bonds had a value. The cases to which the Commissioners had been referred by respondents—*Californian Copper Syndicate v. Harris*, 1904, 6 F. 894, 41 S.L.R. 691; *Tennant v. Smith*, (1892) A.C. 150; *Corke v. Fry*, 1895, 22 R. 422, 32 S.L.R. 341; *Standard Life Assurance Company v. Allan*, 1901, 3 F. 805, 38 S.L.R. 628; and *Royal Insurance Company v. Watson* (1897) A.C. 1—were not in point.

Argued for the respondent—who was called upon to argue the second point only—The debentures had a value, and if they represented arrears of interest fell to be treated as profits for the purposes of income tax—*Tennant v. Smith*, *cit. sup.*, at p. 156. The position was the same as arose in the case of payment in kind—*Corke v. Fry*, *cit. sup.*, was in point. The decision there did not depend on whether or not the manse was let. The question of the saleable value of the bonds had not been raised before the Commissioners.

LORD PRESIDENT—The appellant company were the holders of 10,300 first mortgage bonds of the Western Canada Power Company, the coupons attached to which were for interest at 5 per cent. payable on the 1st of January and 1st of July in each year. On the first of January 1916 default was made by the Power Company in meeting the coupons then due for interest accruing since the preceding 1st of July. As the result of a reorganisation of the finances of the Western Canada Power Company the appellant company received an identical number of first mortgage bonds in the reorganised company of the same face value, the coupons attached to which bore interest as from 1st July 1917, the first of them being payable accordingly on 1st January 1918. In addition they received ten-year 7 per cent. debentures of the new company, the principal amount of which was equal to 10 per cent. of the face value of the surrendered bonds. It follows that the face value of the ten-year 7 per cent. debentures was the precise equivalent of the two years' interest at 5 per cent. on the original holding of bonds in the Power Company for the two years which elapsed between 1st July 1915 and 1st July 1917.

The scheme of reorganisation contains nothing which expressly identifies the debentures as representing the two years' interest. But inasmuch as the form which the reorganisation took was to substitute bonds of the reorganised company for those of the old company—identical as regards face value and otherwise with those of the original company—it is a natural inference that the addition of 10 per cent. represented by the 7 per cent. debentures was the equivalent of the 5 per cent. interest coupons on the original bonds for the two years, which the holders of those bonds surrendered when they surrendered the bonds themselves.

Indeed, the only other explanations of the transaction suggested are—(1) that the 7 per cent. debentures were a bonus or inducement to accept the new bonds; and (2) that the true nature of the transaction was a postponement of the obligation to meet the coupons on the original bonds. I cannot say that I see any bonus or inducement to accept the new bonds in a transaction which had no effect beyond meeting the obligation which the interest coupons themselves represented. And it is difficult, in view of the fact that the interest coupons on the original bonds had to be surrendered, to hold it established that the 7 per cent. debentures represented (not the equivalent of these coupons), but only an arrangement by which these coupons, surrendered as they had been, were to suffer postponement as regards their payment. In short, in the absence of any other evidence of the true character and function of the 7 per cent. debentures, it is impossible to say that the Commissioners did not have material before them upon which they could arrive at the conclusion in fact at which they did arrive, namely, that the 7 per cent. debentures were the *surrogata* of the coupons which were surrendered. That is enough to enable us to answer the first of the two questions in the case in the affirmative.

With regard to the second question—whether the sum of £773 was properly included in the computation of profits of the company for the purposes of income tax—it follows that if the 7 per cent. debenture bonds did represent the interest on the surrendered coupons the value of those debentures must be included in the account of the company's profits, provided that the debentures themselves were saleable and had a value on the market. The question becomes one of ascertaining the amount of the profits and gains of the company. If instead of receiving cash for the coupons on the old bonds, the company got a saleable security, that saleable security is just part and parcel of the company's profits and gains. Its market value must be assessed, and if that is fairly and properly done the amount represents just so much profit or gain to the company. It appears from the proceedings that the question of the saleability and the value on the market of these debentures was the subject of little or no discussion in the appeal before the Commissioners. There is no record in the case that the appellant company raised any contention upon either head, but of course if the appellant company had intended to dispute the surveyor's view that the debentures were marketable, and had a value of about 75 per cent. of their face value, it was their business to do so on appeal before the Commissioners. They did not however dispute it and we have accordingly no material upon which to criticise the finding that 75 per cent. of the value of these debentures was realisable on the market, and therefore fairly represented the profit or gain of the company in the year in question.

The result is to answer the second question also in the affirmative.

LORD MACKENZIE—I am of the same opinion.

The question whether or not the debentures were saleable at 75 per cent. does not seem to have been made the subject of controversy before the Commissioners at all. The only questions which were raised were whether they were entitled to proceed upon a certain principle in dealing with the figure £773, and for the reasons which your Lordship has explained I am of opinion that they were.

LORD CULLEN—I concur.

LORD SKERRINGTON did not hear the case.

The Court answered the questions in the affirmative.

Counsel for the Appellants—Fleming, K.C. — Dykes. Agents—Guild & Shepherd, W.S.

Counsel for the Respondent—Solicitor-General (Murray, K.C.)—Wark, K.C.—Skelton. Agent—Stair A. Gillon, Solicitor of Inland Revenue.

Saturday, February 25.

## FIRST DIVISION.

[Lord Blackburn, Ordinary.]

CLARK v. CLARK.

*Expenses—Husband and Wife—Law Agent—Interim Award—Appropriation—Outlays—Agent's Fees.*

A wife who was pursuer in an action of separation and aliment obtained decree in the usual form for £100 of interim expenses. The money was paid, and she allowed it to remain in the hands of her law agent without giving him any special instructions as to its disposal. Sometime afterwards, while the case was still proceeding, she changed her agent. *Held* (1) that the decree did not imply a special appropriation of the sum to outlays necessary in the cause or create a trust limiting the disposal of the sum to disbursements on that head, and (2) that in the absence of special instructions by the pursuer as to the disposal of the sum, the first law agent was entitled to take payment of his fees, as taxed, *pro tanto* out of the balance of the sum in his hands unexpended on outlays.

Mrs Esther Thomson or Clark, *pursuer*, brought an action of separation and aliment against her husband Donald Clark, M.B., Ch.B., Pollokshields, Glasgow, *defender*.

On 1st March 1921 LORD SALVESEN, for the Lord Ordinary (ANDERSON), closed the record, allowed a proof, and on the motion of the pursuer for an interim award of expenses, decerned against the defender for payment to the pursuer of the sum of £100 in name of expenses.

The sum decerned for was paid by the defender, and was allowed by the pursuer to remain in the hands of Mr John Baird,