No. 1130—HIGH COURT OF JUSTICE (KING'S BENCH DIVISION)—6TH AND 7TH APRIL, 1938

COURT OF APPEAL—24TH AND 25TH JANUARY AND 10TH FEBRUARY, 1939

HOUSE OF LORDS—19TH AND 20TH FEBRUARY AND 19TH MARCH, 1940

UNITED STEEL COMPANIES, LTD. *v.* CULLINGTON (H.M. INSPECTOR OF TAXES) (No. 2[1])

Income Tax, Schedule D—Profits of trade—Succession—New company amalgamating two old companies—Whether entitled to carry forward and set off against its profits wear and tear allowances and losses of the old companies.

A new Company was formed to amalgamate, on the terms of a scheme sanctioned by an Order of Court under Sections 153 *and* 154 *of the Companies Act,* 1929, *the undertakings of two existing companies. The businesses carried on by those companies were continued by the new Company.*

On appeal against an assessment to Income Tax under Schedule D the new Company contended that by virtue of the Order of Court it was entitled to any rights which the amalgamated companies had in regard to carry forward of losses and of allowances for wear and tear.

Held, *that the Company was not entitled to carry forward either the losses or the wear and tear allowances of the amalgamated companies.*

CASE

Stated under the Income Tax Act, 1918, Section 149, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the King's Bench Division of the High Court of Justice.

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 25th February, 1937, the United Steel Companies, Ltd. (hereinafter called "the Company")

[1] Reported (K.B.) [1938] 2 K.B. 566; (C.A.) [1939] 1 K.B. 644; (H.L.) [1940] A.C. 812.

appealed against an assessment to Income Tax in the sum of £690,000 less £175,000 wear and tear for the year ending 5th April, 1937.

The said assessment is made under Case I of Schedule D of the Income Tax Act, 1918, and is in respect of the Company's profits as steel manufacturers.

2. The Company was incorporated under the Companies Act, 1929, on 22nd August, 1930, with a capital of £6,650,000 divided into 6,650,000 Ordinary shares of £1 each.

The primary object of the Company was to acquire and amalgamate the undertakings and all or any of the properties, assets, rights, powers, debts, liabilities, and duties of the United Steel Companies, Ltd. (hereinafter called " the 1918 Steel Company ") and United Strip and Bar Mills, Ltd. (hereinafter called " the " Strip Company ") on the terms of a Scheme of Arrangement and Amalgamation dated 20th June, 1930, which was sanctioned by an Order of the High Court of Justice dated 16th August, 1930, and made pursuant to Sections 153 and 154 of the Companies Act, 1929. A copy of the said Order together with details of the said Scheme is attached hereto, marked " A ", and forms part of this Case(1).

3. The 1918 Steel Company was registered on 25th March, 1918.

The Strip Company was registered on 14th February, 1920.

4. In accordance with paragraph 1 of the said Scheme as sanctioned by the Court, the Company was formed on 22nd August, 1930, and thereupon the properties, rights and powers of every description and all the debts liabilities and duties of the 1918 Steel Company and the Strip Company were without further act or deed transferred to and vested in the Company.

5. On 22nd August, 1930, (the date of the incorporation of the Company) there were issued and outstanding the shares and securities of the 1918 Steel Company and the Strip Company which are set out in paragraphs A and C of the third Schedule to the said Scheme of Arrangement and Amalgamation which is included in Exhibit " A " hereto(1).

Shares of the Company were duly issued to the holders of shares and securities of the 1918 Steel Company and the Strip Company in accordance with the said Scheme and Order of the Court.

6. The said Order provided that the 1918 Steel Company and the Strip Company should within seven days after the date of the Order cause office copies of the said Order to be delivered to the

(1) Not included in the present print.

Registrar of Companies and that at the expiration of three months from the date of delivery the Companies should be deemed to be dissolved. Copies of the said Order were duly delivered.

7. The businesses carried on by the 1918 Steel Company and the Strip Company were continued by the Company from the 22nd August, 1930, and the books of account of those Companies were not closed on that date nor were statements of account rendered to their customers or suppliers as on that date. Both manufacture and accounting were carried on throughout the day and subsequently in the name of the Company. The businesses which had, prior to 22nd August, 1930, been carried on by the 1918 Steel Company and the Strip Company were treated as from that date as branches of the Company.

8. In respect of the business carried on by the Strip Company and subsequently by the Company separate books of account were kept from 14th February, 1920, to 30th June, 1932, but without any break at 22nd August, 1930.

9. The Strip Company commenced trading on 1st December, 1921, and the separate accounts (made up to 30th June in each year) showed annual losses from that date until 30th June, 1931. Consequently effect could not be given to the deduction for wear and tear of plant to which the Strip Company was entitled under Rule 6 (1) of the Rules applicable to Cases I and II of Schedule D of the Income Tax Act, 1918.

10. The deductions for wear and tear of plant to which the Strip Company was so entitled under the said Rule 6 (1) but in respect of which relief could not be given are :—

	£
For years ending 5th April, 1923–30	440,199
For period 5th April, 1930, to 22nd August, 1930, being a proportion of the deduction for the year ended 5th April, 1931	15,399
	£455,598
By the Company's method of computation the amount of wear and tear allowances available to the Company to be deducted from the assessment for 1936–37 in respect of assets arising from the 1918 Steel Company is less than is admitted by	6,748
So that the net amount of additional allowances for wear and tear claimed by the Company is	£448,850

11. The trading losses (as computed by the Rules applicable to Cases I and II of Schedule D of the Income Tax Act, 1918, and

reduced to the extent that relief was given under Section 34 of the said Act) of the business carried on by the Strip Company up to 22nd August, 1930, in respect of which relief could not be given to that Company amount to £44,091, and the losses of the 1918 Steel Company for which relief has not been given amount to £90,729, making in all a total sum of £134,820 in respect of which the Company claims relief from the assessment under appeal.

12. On 10th August, 1928, the 1918 Steel Company made with the Board of Inland Revenue an arrangement whereby the liabilities and claims of the 1918 Steel Company in respect of Income Tax, Excess Profits Duty and Corporation Profits Tax subsisting as at 5th April, 1927, were satisfied. Consequently the first year of assessment of the 1918 Steel Company which falls to be considered for the purposes of this Case is the year ended 5th April, 1928.

The 1918 Steel Company's income from its trade for that year is computed by reference to the 1918 Steel Company's accounting year ended 30th June, 1926.

13. The profits and losses (as computed by the Rules applicable to Cases I and II of Schedule D of the Income Tax Act, 1918) of the business carried on without interruption by the 1918 Steel Company and by the Company did not give rise to a charge for tax for the years ended 5th April, 1928 to 1936, either because there were no profits or because the profits were less than the deductions to which the Company was entitled under Rule 6 (1) of the said Rules in respect of wear and tear of plant and machinery.

14. The Company claims that under the circumstances hereinbefore set forth it is entitled to set off against its own profits all the allowances for wear and tear and for losses carried forward which the 1918 Steel Company and the Strip Company would have been entitled to carry forward against future profits if they had continued to carry on trade.

15. It was contended, *inter alia*, on behalf of the Company :—

(*a*) That by virtue of the Order of the Court dated 16th August, 1930, the rights as well as the property of the Strip Company and the 1918 Steel Company were vested in the Company without further act or deed;

(*b*) That the rights conferred by Rule 6 of the Rules applicable to Case I of Schedule D of the Income Tax Act, 1918, and by Section 33 of the Finance Act, 1926, were among the rights so vested in the Company.

(*c*) That in accordance with the said Order the businesses carried on by the 1918 Steel Company and by the Strip Company respectively were not discontinued but were

continued without interruption in the name of the Company, which did not set up a new trade or business.

(*d*) That in these circumstances Rule 11 of the Rules applicable to Cases I and II of Schedule D (as amended by Section 32 of the Finance Act, 1926) is not applicable, and its application would be inconsistent with the intention of Sections 153 and 154 of the Companies Act, 1929, and of the Order of the Court made in pursuance of those Sections;

(*e*) That the liability of the Company to Income Tax for all years should be computed throughout by reference to the profits or losses of the year preceding the year of assessment with the right to set off against the assessment for 1936–37 any losses and wear and tear allowances which become available by that method of computation, whether such losses and allowances arise from the 1918 Steel Company, from the Strip Company or from the Company.

16. It was contended, *inter alia*, on behalf of the Crown that:—

(*a*) The Company on 22nd August, 1930, succeeded to the trades of the 1918 Steel Company and the Strip Company within the meaning of Sub-section (2) of the new Rule 11 substituted by Section 32, Finance Act, 1926:

(*b*) The Company therefore falls to be assessed as if a new trade had been set up or commenced on 22nd August, 1930.

(*c*) The Company is not entitled to set off against its own profits the allowances for wear and tear and losses in respect of which relief could not be given to the 1918 Steel Company and the Strip Company at the date of the incorporation of the Company;

(*d*) The reliefs to which the Company is entitled under the Income Tax Acts are in no way affected by the terms of the Order or the Companies Act, 1929.

17. Having considered the arguments and evidence adduced before us, we found that the Company succeeded on 22nd August, 1930, to the trades previously carried on by the 1918 Steel Company and the Strip Company, and falls to be assessed as if a new trade had been set up or commenced on that date. We held that the Company is not entitled to the wear and tear allowances or losses to which the said 1918 Steel Company and the Strip Company were entitled at the date when the Company was incorporated, *i.e.*, 22nd August, 1930.

18. The Company immediately after the determination of the appeal declared to us its dissatisfaction therewith as being erroneous in point of law and in due course required us to state a Case for the opinion of the High Court pursuant to the Income Tax Act, 1918, Section 149, which Case we have stated and do sign accordingly.

N. ANDERSON,
R. COKE,
} Commissioners for the Special Purposes of the Income Tax Acts.

Turnstile House,
94/99, High Holborn,
London, W.C.1.

28th September, 1937.

The case came before Lawrence, J., in the King's Bench Division on the 6th and 7th April, 1938, and on the latter date judgment was given in favour of the Crown as regards the losses and against the Crown as regards the wear and tear allowances.

Sir William Jowitt, K.C., Mr. Raymond Needham, K.C., Mr. W. G. Brown and Mr. J. S. Scrimgeour appeared as Counsel for the Appellant Company, and the Solicitor-General (Sir Terence O'Connor, K.C.) and Mr. Reginald P. Hills for the Crown.

JUDGMENT

Lawrence, J.—In this case the question is whether the Appellant Company, a new company, which amalgamated under the Companies Act, 1929, the 1918 Steel Company and the Strip Company, is entitled to deduct wear and tear and losses of the constituent companies for the years before the amalgamation. This question turns primarily upon the construction of Rule 11 of the Rules applicable to Cases I and II of Schedule D, which is contained in Section 32 of the Finance Act, 1926.

The two constituent companies of the Appellant Company, that is to say, the 1918 Steel Company and the Strip Company, have had losses in the past and have, I think, never made profits. In those circumstances, wear and tear allowances had accumulated. It is contended on behalf of the Appellant Company that it is entitled to carry forward and to have the benefit of those allowances of its constituent companies for wear and tear and for losses, both under the provisions of Section 32 of the Finance Act, 1926, and also by reason of the provisions of Section 153 and Section 154 of the Companies Act, 1929, under which the Appellant Company was created. The question of losses, whilst not being abandoned, was not pressed by Sir William Jowitt, and I formed the view that that

(Lawrence, J.)

claim could not be substantiated, turning, as it does, upon Section 33 of the Finance Act, 1926, which does not relate in any way to a succession, and seems to confer merely a personal right upon the person who is carrying on the trade.

The main question as to the wear and tear allowances depends upon the construction of Rule 11, and it is important to consider the state of the law before and after 1926. In this connection Sir William Jowitt points out that the Rule which deals with the wear and tear allowances is not a Rule of computation, but is a charging Rule.

Before 1926, when Income Tax was assessed and computed upon the basis of the three preceding years, Rule 6 of the Rules applicable to Cases I and II of Schedule D, provided: "(1) In "charging the profits or gains of a trade under this Schedule, "such deduction may be allowed as the commissioners having "jurisdiction in the matter may consider just and reasonable, as "representing the diminished value by reason of wear and tear "during the year of any machinery or plant used for the purposes "of the trade and belonging to the person by whom it is carried "on". That is a deduction which is to be allowed by the Commissioners during the year of charge and in respect of that year and has no relation to the three preceding years, which are years upon which the computation to tax is based. By Sub-rule (3) of that Rule it was provided that, where the full effect could not be given to such deduction because there were not profits sufficient to permit of the deduction, the deduction might be carried forward. Rule 9 provided that, where there was a succession to a trade, the Commissioners might adjust the assessment by charging the successor with a fair proportion of the assessment from the time of his succeeding to the trade, profession or vocation, and relieving the person originally charged from a like amount. Rule 11 then provided that on changes of proprietorship the tax payable by the person or persons who carry on the trade, profession or vocation after the change should, notwithstanding the change, be computed according to the profits and gains of the trade, profession or vocation during the period prescribed by the Income Tax Acts.

The effect of those Rules before 1926 was, that where there was a change of proprietorship and a succession, the tax would be computed by reference to the three years previous to the year of assessment and would be assessed upon the predecessor, and an adjustment would be made with reference to the time during which the successor continued the trade. In those circumstances, the question was brought before the Courts in Scotland as to whether the carry forward of the wear and tear allowance would apply to a successor, and it was held in the case of *Scottish Shire Line, Ltd.* v. *Lethem*, 6 T.C. 91, that the provisions now contained in Rule 6, Sub-rule (3), did so apply.

(Lawrence, J.)

After 1926, Rule 6 remained in its original form, and Rule 11 was altered, providing in the first Sub-rule for the case of partnerships that, where one or more persons who until the change of partnership have been engaged in the trade continue to be engaged therein, the tax payable by the person or persons who carry on the trade after that time shall, notwithstanding the change, be computed according to the profits and gains of the trade during the period prescribed by the Income Tax Acts ; that is to say, the Rule there uses the same words as the original Rule 11, but the period prescribed by the Act of 1926, instead of being three years previous, was one year previous. The Rule goes on to provide that where all the persons who were engaged in the trade, both before and after the change, wish to do so, they can send the surveyor a notice requiring that the tax payable " shall be computed as if the trade, profession " or vocation had been discontinued at the date of the change, and a " new trade, profession or vocation had been then set up or " commenced, and that the tax so computed for any year shall be " charged on and paid by such of them as would have been charged " if such discontinuance and setting up or commencement had " actually taken place ". That gave to members of a partnership a different option from that which had been given to them by the original Rule 11. Sub-rule (2) of Rule 11 deals with successions other than partnerships where some of the partners remain the same, and provides that if any person succeeds to a trade " which until that time was carried on by another person . . . " the tax payable for all years of assessment by the person " succeeding as aforesaid shall be computed as if he had set " up or commenced the trade, profession or vocation at that " time, and the tax payable for all years of assessment by the " person who until that time carried on the trade, profession or " vocation shall be computed as if it had then been discontinued ".

It is argued for the Crown that the effect of Sub-rule (2) of the present Rule 11 is that on a succession the person who succeeds is to be taxed exactly as if he had not succeeded, but had set up an entirely new business, and that the effect of that is to exclude any right which he would previously have had under Rule 6 (3) to carry forward the wear and tear allowance. As Sir William Jowitt has pointed out, Rule 11 relates to the computation of tax and provides for computation in accordance with the terms of the Act of 1926 and for assessment both upon the predecessor and the successor in case of a succession. He contends that it does not affect in any way Rule 6, which is really a charging Rule entitling the taxpayer to a deduction in respect of wear and tear allowance, by reference not to the year of computation but to the year of assessment ; and he points out that there is a marked contrast between the words of Sub-rule (2) of Rule 11 and the words in the proviso to Sub-rule (1) of Rule 11, for whereas in Sub-rule (2) of Rule 11 the

(Lawrence, J.)

words are: "If at any time . . . any person succeeds to any "trade . . . the tax payable . . . shall be computed as "if he had set up or commenced the trade", the words of the proviso are "that the tax payable . . . shall be computed as if the "trade, profession or vocation had been discontinued at the date of "the change, and a new trade, profession or vocation had been "then set up or commenced".

It is argued that, if the intention had been to do away altogether with the doctrine of succession so as to make a complete division for all purposes at the point where the successor took on the trade it would have been natural and simple to have used the words "as "if he had set up or commenced a new trade", whereas the words used "as if he had set up or commenced the trade" grammatically apply to the trade to which the person has succeeded; and that as there is, according to the contention of the Appellant Company, ample to satisfy the meaning of Sub-rule (2) in that it alters the Rules as to assessment and as to computation in the case with which it is dealing, it is not right to construe that Sub-rule as applying to Rules of charge, such as Rule 6, with results of such very great importance.

In my judgment the argument for the Appellant Company is correct. No meaning has been suggested for the contrast between the words used in the proviso to Rule 11 (1) and the words used in Rule 11 (2), and I cannot think that the Legislature, if it had intended to effect so great a change with reference to the carry forward of the wear and tear allowance, would have effected that change by words which do not expressly refer to the subject at all and which are amply satisfied by the meaning to which I have already alluded.

It was contended for the Crown that Rule 11 (2) refers back to the Rules applicable to Cases I and II. Rule 1 (2) provides that where a trade has been set up and commenced within the year preceding the year of assessment, the computation shall be made on the profits or gains "for one year from the period of the first "setting up of the same, and where it has been set up and commenced "within the year of assessment, the computation shall be made "according to the rules applicable to Case VI", and it is no doubt true that Rule 11 (2) does provide for that method of computation. But that does not, in my opinion, throw any light upon the contrasted words to which I have referred in Rule 11 (2) and Rule 11 (1), and it does not in any way affect the force of the argument that these are Rules of computation, whereas the deduction of wear and tear allowance is a Rule of charge.

The Crown also relied upon the terms of the judgments in the case of *Scottish Shire Line, Ltd.* v. *Lethem*, 6 T.C. 91, at page 98,

(Lawrence, J.)

where Lord Dundas said: "The Crown has treated the Appellant "Company as the Old Company by taking that Company's profits "during the preceding years as the basis for assessing the Appellants' "profits for 1910. I think it would be anomalous if we were to "permit the Crown to treat the Appellants as a new and different "concern when it comes to the matter of the wear and tear deduc-"tion". They referred also to Lord Salvesen's judgment at page 99, where he said: "Even in a taxing statute it is legitimate "to consider which of two possible constructions is most in accordance "with the spirit and intention of the Act. Now the Appellants "admittedly fall to be assessed for Income Tax exactly on the same "footing as the 'Elderslie' Company, to whose concern they "succeeded. If so, can any reason be suggested why they should "not be entitled to the same deductions from those profits as their "predecessors had they remained in business admittedly would have "been?" Those observations were not, I think, the main basis of the judgments and I do not think that they alter in any way the view which I take of the construction of the Act of 1926. In my opinion, as I have said, Rule 11 as amended by Section 32 of that Act was introduced to alter the method of assessment and the periods of computation where there was a succession, and it was not introduced for the purpose of altering the other rights of a successor; and when I read Rule 11 in conjunction with Rule 6, which still stands in the Statute,it appears to me to have no effect upon the right of a successor to carry forward the wear and tear allowance of his predecessor.

The other argument which was addressed to me on behalf of the Appellant Company was that by virtue of the provisions of the Companies Act of 1929, Sections 153 and 154, the amalgamated company really represents the two constituent companies and is entitled to any rights which they may have had under Rule 6 to carry forward of wear and tear allowances. I cannot accede to that argument because I do not think the general terms of the Companies Act, 1929, indicate any intention to vary the terms of the Income Tax Acts relating to succession; and, although a company which amalgamates other companies under the Act of 1929 does in effect fuse them, it is still another legal *persona* and does not, in my judgment, acquire thereby any greater rights than a successor of another type.

I therefore hold that if the construction which I have put upon Rule 11 (2) is incorrect, the Appellant Company would not by virtue of its creation under the Act of 1929 be entitled to the carry forward of this wear and tear allowance.

For these reasons upon the main contention I find myself unable to concur in the judgment of the Commissioners, and the appeal must be allowed with costs.

Mr. Hills.—My Lord, with regard to costs, your Lordship will recollect that the appeal is dismissed with regard to the losses and allowed with regard to the wear and tear allowance.

Lawrence, J.—Perhaps the costs ought to be apportioned.

Mr. Hills.—I should have thought so.

Sir William Jowitt.—I should submit not. The finding of the Commissioners was that we were to be assessed as if a new trade had been set up and commenced, so we had to come to this Court, and I think your Lordship will support me when I say that only a fraction of the time was taken up in regard to the question of losses, and the whole argument has been on the other matter. We had to come here, anyhow. I submit that there ought to be no apportionment. We have succeeded as to £450,000, and the question with regard to £130,000, as to which we fail, has occupied a very slight time of the hearing in the argument. I ask your Lordship to say that the appeal should be allowed with costs.

Mr. Hills.—The decision of the Commissioners is in two parts. The appeal cannot be allowed altogether.

Lawrence, J.—Which is the paragraph ?

Sir William Jowitt.—It is paragraph 17 of the Case. By virtue of that paragraph of the Case their finding is that we have got to be assessed " as if a new trade had been set up or commenced on " that date ", so that we had to come here.

Lawrence, J.—Yes. You had to come here.

Sir William Jowitt.—Having to come here, as we had to come, we have come here with success. It is true that a few moments of time—and that is all it really comes to—were occupied by that matter, but I submit it ought not to affect the costs of the hearing.

Lawrence, J.—What do you say about that, Mr. Hills ? They had to come here.

Mr. Hills.—I say my learned friend's suggestion that the appeal is allowed is plainly erroneous. The appeal is only partially allowed and partially dismissed. As regards the £134,000, he has lost ; as regards the rest, he has won. It is very difficult to apportion the costs. I submit that the best thing would be to say that each party should pay its own costs.

Lawrence, J.—I think perhaps I might make an Order that the Appellant Company should be entitled to three-fourths of the costs and the Crown to one-fourth.

Mr. Hills.—If your Lordship pleases.

Appeals having been entered against the decisions in the King's Bench Division, the case came before the Court of Appeal (Sir Wilfrid Greene, M.R., and Finlay and Luxmoore, L.JJ.) on the 24th and 25th January, 1939, when judgment was reserved. On the 10th February, 1939, judgment was given unanimously in favour of the Crown on both points, with costs, thereby confirming the decision of the Court below as regards the losses and reversing it as regards the wear and tear allowances.

The Solicitor-General (Sir Terence O'Connor, K.C.) and Mr. Reginald P. Hills appeared as Counsel for the Crown, and Sir William Jowitt, K.C., Mr. Raymond Needham, K.C., Mr. W. G. Brown and Mr. J. S. Scrimgeour for the Company.

JUDGMENT

Sir Wilfrid Greene, M.R.—The judgment of the Court will be read by Finlay, L.J.

Finlay, L.J.—The United Steel Companies, Ltd., to which we shall refer as the Amalgamated Company, was incorporated on the 22nd August, 1930, to acquire and amalgamate the undertaking, properties, assets, rights, powers, debts, liabilities and duties of two then existing companies one of which was called the United Steel Companies, Ltd., and the other the United Strip and Bar Mills, Ltd. We shall refer to these two companies as the 1918 Steel Company and the Strip Company respectively. The amalgamation was carried out under a scheme of arrangement and amalgamation dated the 20th June, 1930, which was sanctioned by an Order of Eve, J., dated the 16th August, 1930, and was made pursuant to Sections 153 and 154 of the Companies Act, 1929. The 1918 Steel Company had been registered on 25th March, 1918. The Strip Company had been registered on 14th February, 1920.

Neither of these companies had been successful, and each company had continually made losses in respect of which it had been unable to obtain relief under Section 34 of the Income Tax Act, 1918. The losses in respect of which relief could not be obtained amounted in the case of the Strip Company to £44,091, and in the case of the 1918 Steel Company to £90,729, making in all £134,820. Further, the Strip Company had been unable to give effect to the deductions in respect of wear and tear to machinery which it was entitled to make under the provisions of Rule 6 of the Rules applicable to Cases I and II of Schedule D, Income Tax Act, 1918. The deductions thus carried forward by the Strip Company in the period prior to 1930 and now claimed by the Amalgamated Company totalled £448,850.

(Finlay, L.J.)

The Amalgamated Company was assessed to Income Tax in respect of the year ending 5th April, 1937, in the sum of £690,000 less £175,000 for wear and tear. This assessment was made under Case I, Schedule D, and is in respect of the Amalgamated Company's profits as steel manufacturers.

The Amalgamated Company appealed to the Special Commissioners against this assessment, and claimed to deduct from the £690,000 profits, in addition to £175,000 for wear and tear of its own machinery, the aggregate sum which the 1918 Steel Company and the Strip Company would respectively have been entitled to deduct from profits if each had continued to carry on its trade separately—in respect of losses, that is, the total sum of £134,820 and, further, the sum of £448,850 in respect of allowances for wear and tear to machinery of the Strip Company.

The Commissioners found that the Amalgamated Company succeeded on the 22nd August, 1930, to the trades previously carried on by the 1918 Steel Company and the Strip Company, and fell to be assessed as if a new trade had been set up or commenced on that date. They held that the Amalgamated Company was not entitled to the wear and tear allowances or losses to which the 1918 Steel Company and the Strip Company were entitled at the date when the Amalgamated Company was incorporated, *i.e.*, 22nd August, 1930.

The Amalgamated Company required the Commissioners to state a Case for the opinion of the High Court under Section 149 of the Income Tax Act, 1918. The Case stated in compliance with this requirement came before Lawrence, J., who held that the Commissioners were right in their refusal to allow any deduction in respect of losses made by the 1918 Steel Company and the Strip Company respectively which had not been deducted under Section 34 before the 22nd August, 1930, but were wrong in their refusal to allow any deduction in respect of allowances for wear and tear not deducted by the Strip Company before the 22nd August, 1930.

The Crown has appealed from the decision of Lawrence, J., with regard to the allowance for wear and tear, and the Amalgamated Company has given a cross notice of appeal in respect of the decision as to losses.

The answer to the question whether the Amalgamated Company is entitled to deduct the allowances for wear and tear appears to us to depend upon what is the true construction of Rule 11 of the Rules applicable to Cases I and II of Schedule D. This Rule was substituted by Section 32 of the Finance Act, 1926, for Rule 11 in the Rules applicable to Cases I and II, Schedule D, of the Income Tax Act, 1918. This latter Rule had in turn been substituted for Rule 4, Cases I and II, Schedule D, of the Income Tax Act, 1842.

(Finlay, L.J.)

I will read the Rules. Rule 4, Cases I and II, Section 100, of the Income Tax Act, 1842, is: " If amongst any persons engaged " in any trade, manufacture, adventure, or concern, or in any " profession, in partnership together, any change shall take place " in any such partnership, either by death, or dissolution of partner- " ship as to all or any of the partners, or by admitting any other " partner therein, before the time of making the assessment, or " within the period for which the assessment ought to be made " under this Act, or if any person shall have succeeded to any trade, " manufacture, adventure, or concern, or any profession, within " such respective periods as aforesaid, the duty payable in respect " of such partnership, or any of such partners, or any person " succeeding to such profession, trade, manufacture, adventure, or " concern, shall be computed and ascertained according to the " profits and gains of such business derived during the respective " periods herein mentioned, notwithstanding such change therein " or succession to such business as aforesaid, unless such partners, " or such person succeeding to such business as aforesaid, shall prove, " to the satisfaction of the respective commissioners, that the profits " and gains of such business have fallen short or will fall short " from some specific cause, to be alleged to them, since such change " or succession took place, or by reason thereof ". Rule 11, Cases I and II, Schedule D, of the Income Tax Act, 1918, says: " If " within the year of assessment or the period of average upon which " the assessment is to be based a change occurs in a partnership of " persons engaged in any trade or profession, by reason of death, " or of dissolution of the partnership as to all or any of the partners, " or by the admission of a new partner, or if any person succeeds " to a trade or profession, the tax payable in respect of the partner- " ship, or any of the partners, or of the person so succeeding shall " be computed according to the profits or gains of the trade or " profession during the respective periods prescribed by this Act, " notwithstanding the change or succession, unless the partners or " the person succeeding to the trade or profession prove to the satis- " faction of the commissioners that the profits or gains have fallen " or will fall short from some specific cause, to be alleged to them, " since such change or succession took place, or by reason thereof ". Rule 11, as enacted by Section 32 of the Finance Act, 1926, says: " (1) If at any time after the fifth day of April, nineteen hundred " and twenty-eight, a change occurs in a partnership of persons " engaged in any trade, profession or vocation, by reason of retire- " ment or death, or the dissolution of the partnership as to one or " more of the partners, or the admission of a new partner, in such " circumstances that one or more of the persons who until that time " were engaged in the trade, profession or vocation continue to be " engaged therein, or a person who until that time was engaged in " any trade, profession or vocation on his own account continues

(Finlay, L.J.)

" to be engaged in it, but as a partner in a partnership, the tax " payable by the person or persons who carry on the trade, pro- " fession or vocation after that time shall, notwithstanding the " change, be computed according to the profits or gains of the trade, " profession or vocation during the period prescribed by the Income " Tax Acts :

" Provided that, where all the persons who were engaged in the " trade, profession or vocation both immediately before and imme- " diately after the change require, by notice signed by all of them or, " in the case of a deceased person, by his legal representatives, and " sent to the surveyor within three months after the change took " place, that the tax payable for all years of assessment shall be " computed as if the trade, profession or vocation had been dis- " continued at the date of the change, and a new trade, profession " or vocation had been then set up or commenced, and that the tax " so computed for any year shall be charged on and paid by such " of them as would have been charged if such discontinuance and " setting up or commencement had actually taken place, the tax " shall be computed, charged, collected and paid accordingly.

" (2) If at any time after the said fifth day of April any person " succeeds to any trade, profession or vocation which until that " time was carried on by another person and the case is not one to " which paragraph (1) of this Rule applies, the tax payable for all " years of assessment by the person succeeding as aforesaid shall " be computed as if he had set up or commenced the trade, pro- " fession or vocation at that time, and the tax payable for all years " of assessment by the person who until that time carried on the " trade, profession or vocation shall be computed as if it had then " been discontinued.

" In this paragraph references to a person include references " to a partnership.

" (3) In the case of the death of a person who, if he had not " died, would, under the provisions of this Rule, have become " chargeable to income tax for any year, the tax which would " have been so chargeable shall be assessed and charged upon his " executors or administrators, and shall be a debt due from and " payable out of his estate ".

It is convenient here to refer to Rule 6, Cases I and II, Schedule D, in the Act of 1918, the Rule which now governs allowances for wear and tear. Historically, provision for such allowances was first introduced into the Income Tax law by Section 12 of the Customs and Inland Revenue Act, 1878, which was amended by Section 26 of the Finance Act, 1907. Rule 6 is, so far as is material, in the following terms : " (1) In charging the profits or " gains of a trade under this Schedule, such deduction may be

(Finlay, L.J.)

" allowed as the commissioners having jurisdiction in the matter " may consider just and reasonable, as representing the diminished " value by reason of wear and tear during the year of any machinery " or plant used for the purposes of the trade and belonging to the " person by whom it is carried on.

" (3) Where full effect cannot be given to any such deduction " in any year owing to there being no profits or gains chargeable " for that year, or owing to the profits or gains chargeable being " less than the deduction, the deduction or part of the deduction " to which effect has not been given, as the case may be, shall, " for the purpose of making the assessment for the following year, " be added to the amount of the deduction for wear and tear for " that year, and deemed to be part of that deduction, or, if there " is no such deduction for that year, be deemed to be the deduction " for that year, and so on for succeeding years.

" (4) Any claim in respect of the aforesaid deduction shall be " included in the annual statement required to be delivered under " this Act of the profits or gains of the trade for which the " machinery or plant is used, and the additional commissioners, in " assessing those profits or gains, shall make such allowance in " respect thereof as they think just and reasonable ".

In 1926 the method of computing profits on an average of three years, which had ever since 1842 been a feature of Income Tax law, was abolished, and the profits of the previous year substituted as the measure. It is for this reason, doubtless, that the amended Rule 11 was introduced into the Act of 1926.

In our opinion, this case turns entirely upon the proper construction of this Rule 11. The Rule is divided into two parts. The first part deals with a partnership where a change has occurred in the partnership, and provides that, where such a change has occurred, the tax payable by the person or persons carrying on the trade shall notwithstanding the change be computed by reference to the profits or gains of the trade during the period prescribed by the Income Tax Acts, *i.e.*, the preceding financial year. To this there is a proviso to the effect that where notice is given on behalf of the persons concerned, the tax payable shall be computed as if the trade had been discontinued at the date of the change and a new trade then set up or commenced.

Sir William Jowitt did not raise any question as to the proper construction of this proviso. If the matter is to be treated as if a new trade had been set up at the crucial date, then it is clear that the old partners, and they alone, obtain the benefit of any allowances or deductions available at that date.

It is, however, on the second part of Rule 11 that the present case depends. That deals not with a change in partnership, but

(Finlay, L.J.)

with a succession to a trade by a stranger. The language of the Rule seems to us to negative any suggestion that the tax payable by the successor is to have any reference to what happened when the predecessor was carrying on the trade. The material words are: " the tax payable for all years of assessment by the person succeed- " ing as aforesaid shall be computed as if he had set up or " commenced the trade, profession or vocation at that time ", *i.e.*, the date of succession. The direction to compute the tax payable can only mean that the tax payable has to be ascertained after making all proper allowances on the basis that the trade was set up or commenced on the last mentioned date. This must of necessity exclude any allowances to which the predecessor might be entitled in respect of the period antecedent to the acquisition of the trade by the successor.

Lawrence, J., accepted an argument to the effect that the Legislature cannot be taken to have intended to eliminate what was called the doctrine of succession(1).

We confess that we have some difficulty in understanding this phrase in the context in which it was used, and also in following the argument. It seems to us that, where a trade is referred to as having been set up or commenced at a particular date, it necessarily follows that the trade must be deemed to be a new trade at the particular date, and it is immaterial whether it is referred to in terms as " a new trade " or as " the trade ". The words " set " up or commenced " seem quite inappropriate if it was intended to refer not to the setting up of a new trade, but to the continuation of an old one. We think that on the true construction of Rule 11 (2) the trade is, for the purpose of ascertaining the tax, to be treated as a new trade set up or commenced at the date of its acquisition, and consequently there is no room for any application of Rule 6. In our judgment, the intention of the Legislature has been expressed in plain words, and it is apparent, if the Rule is examined, that the supposed contrast between the " new trade " in the proviso and " the trade " in Rule 11 (2) is without foundation. Both the learned Counsel who argued the case for the Appellant laid stress upon the fact that Rule 6 is entirely distinct from Rule 11. This is, of course, perfectly correct. The two Rules are diverse in their subject-matter, and in their history, but we are unable to understand on what principle of construction it is to be said that the clear words of Rule 11 are to be so read as to bring in allowances for wear and tear to which a predecessor was entitled. It is true, as has been pointed out earlier, that the computation of tax was until 1926 based on the three years' average, and since 1926 has been based on the profits of the previous year,

(1) *See* page 99 *ante*.

(Finlay, L.J.)

while depreciation has, ever since its introduction in 1878, been allowed as a deduction from the profits of the actual year of assessment; but this does not seem to us to affect the matter.

Some reliance was placed, on both sides of the Bar, on *Scottish Shire Line, Ltd.* v. *Lethem*, 6 T.C. 91. That case has, we think, little bearing on the present. It was a decision of the Inner House of the Court of Session in Scotland and had reference to the construction of the Fourth Rule of Cases I and II, Schedule D, in the Act of 1842, Section 12 of the Customs and Inland Revenue Act, 1878, and Section 26 of the Finance Act, 1907. What was there held was that the section in the Finance Act, 1907, upon which the matter there turned, did not, to use the words of Lord Dundas " strike any personal note "[1], and it was accordingly held that the Crown, treating the new company, the successor, as continuing the business of the old company, by taking that old company's profits during the years of average as the basis of assessment, could not be permitted in the matter of wear and tear to treat the new company as a new and different concern. This case, as we have said, has, we think, little bearing upon the present, but the stress which was laid by the Lords of Session there upon the necessity for treating the matter in the same way for depreciation as it was treated for the computation of profits appears to us rather in favour of the Crown's view in the present case.

Then reliance was placed, particularly by Mr. Needham, upon the decision in the case of *Bell* v. *The National Provincial Bank of England, Ltd.*, 5 T.C. 1. That was a case where a large bank having many branches through the country had purchased the business of one of the old county banks, the County of Stafford Bank carrying on business at Wolverhampton. It was held by the Court of Appeal, reversing a decision of Ridley, J., that on the facts of that case the National Provincial Bank had succeeded to the business of the County of Stafford Bank. We have been unable to see either in the conclusion of the Court of Appeal or in the reasoning on which that conclusion was based anything which is of assistance in the present case.

We have, out of respect for the elaborate arguments addressed to us, discussed the matter at some length, but we may repeat that in our opinion the case falls to be decided upon the plain construction of Rule 11.

It remains to deal with the amalgamated company's cross-appeal. This was dealt with by Lawrence, J., in the following words[2]: " The question of losses, whilst not being abandoned, " was not pressed by Sir William Jowitt, and I formed the view " that that claim could not be substantiated, turning, as it does, " upon Section 33 of the Finance Act, 1926, which does not relate

(1) 6 T.C. 91, at p. 98. (2) *See* pages 96/97 *ante*.

(Finlay, L.J.)

" in any way to a succession, and seems to confer merely a personal " right upon the person who is carrying on the trade ".

It is apparent from this passage that the Company, while not abandoning its contention with reference to losses, did not press it. Nevertheless, a cross-appeal has been brought with reference to this point, due perhaps to a feeling that the Company, in affirming its right to deduction in respect of wear and tear, but abandoning its right to deduction in respect of losses, might be in a position of some difficulty.

Section 33 of the Act of 1926 is, so far as is material, in the following terms : " (1) Where a person has in any trade, profession " or vocation carried on by him, either solely or in partnership, " sustained a loss (to be computed in like manner as profits or gains " under the Rules applicable to Cases I and II of Schedule D) in " respect of which relief has not been wholly given under section " thirty-four of the Income Tax Act, 1918 (which relates to relief " in respect of certain losses), or under Rule 13 of the Rules applic- " able to Cases I and II of Schedule D (which provides for the " setting-off of losses against profits or gains in a distinct trade), " or under any other provision of the Income Tax Acts, he may " claim that any portion of the loss for which relief has not been " so given shall be carried forward and, as far as may be, deducted " from or set-off against the amount of profits or gains on which he " is assessed under Schedule D in respect of that trade, profession " or vocation for the six following years of assessment ".

No argument was addressed to us by Sir William Jowitt with reference to this Section. He admitted, in effect, that it conferred a merely personal right, and in these circumstances it is sufficient without more ado to say that we agree with what was said by Lawrence, J., in the passage quoted above. But Sir William Jowitt did argue that he was entitled to succeed in this claim as to losses, and also in this claim as to wear and tear, by virtue of Sections 153 and 154 of the Companies Act, 1929. This is a somewhat startling contention. Both wear and tear and losses are dealt with in appropriate sections in the Income Tax code. It would indeed be surprising if the Legislature in an Act relating entirely to companies and not at all to Income Tax has superseded and rendered of no effect the provisions of the Income Tax Acts with regard to important questions of Income Tax law.

In our opinion, when Section 154 is examined, no such result is produced. The section is, so far as is material, in these terms : " Where an application is made to the court . . . . for the sanction- " ing of a compromise or arrangement . . . . and it is shown to " the court that the compromise or arrangement has been proposed

(Finlay, L.J.)

" for the purposes of or in connection with a scheme for the recon-
" struction of any company or companies or the amalgamation of
" any two or more companies, and that under the scheme the whole
" or any part of the undertaking or the property of any company
" concerned in the scheme (in this section referred to as ' a
" ' transferor company ') is to be transferred to another company
" (in this section referred to as ' the transferee company '), the
" court may, either by the order sanctioning the compromise or
" arrangement or by any subsequent order, make provision for all
" or any of the following matters :—(*a*) the transfer to the
" transferee company of the whole or any part of the under-
" taking and of the property or liabilities of any transferor com-
" pany ". " Property " is defined in the section as including property, rights and powers of every description.

The Order of Eve, J., in the present case directed that the undertaking, properties, rights and powers of every description of the 1918 Steel Company and of the Strip Company should be transferred to and vest in the Amalgamated Company. The argument was that the rights of the 1918 Steel Company and the Strip Company which were transferred include a right to claim for wear and tear and losses.

It seems to us to be clear that this argument must fail. The rights were, on the proper construction of the Income Tax Acts, rights personal to the 1918 Steel Company and the Strip Company. It is impossible to construe Section 154, or the Order of Eve, J., made under it, as referring to rights of that character. The rights were rights of the two old companies to make deductions in respect of losses and wear and tear from their own profits. It is impossible to see how any transfer could transform rights to deduct from the profits of the old companies into a right to deduct from the profits of the new company. Lawrence, J., dealt concisely, but we think conclusively, with this argument where at page 8 of his judgment he says(1) : " I cannot accede to that argument because I do not think
" the general terms of the Companies Act, 1929, indicate any
" intention to vary the terms of the Income Tax Acts relating
" to succession; and, although a company which amalgamates other
" companies under the Act of 1929 does in effect fuse them, it is
" still another legal *persona* and does not, in my judgment, acquire
" thereby any greater rights than a successor of another type ".

In the result we hold that the Crown's appeal succeeds and that that part of the Order of Lawrence, J., which states that the Court is of opinion that the determination of the Commissioners is erroneous so far as they held that the Amalgamated Company was

(1) *See* page 100 *ante*.

(Finlay, L.J.)

not entitled to the wear and tear allowances set forth in paragraph 10 of the Case should be struck out and a declaration in the opposite sense substituted for it.

The cross-appeal must be dismissed.

The Amalgamated Company must pay the costs of both appeals to this Court, and the Order in its favour as to three-fourths of the costs in the Court below must be reversed and the Amalgamated Company ordered to pay to the Appellant the whole of the costs in that Court.

Sir William Jowitt.—My Lords, might I point out that the amount involved in this case is, as your Lordships will appreciate, very considerable indeed. It is the first case of its kind, and there are similar cases rather depending upon this decision. It is a case in which your Lordships have reversed, in the main and more important part, the judgment of a very experienced Judge in these matters. For these reasons I ask your Lordships to say that I may have, if so advised after considering your Lordships' judgment with that care which I cannot pretend to have given it at the moment, leave to appeal to the House of Lords.

Sir Wilfrid Greene, M.R.—All the members of the Court have considered this matter, and we take the view that the case is a proper one for leave to appeal to the House of Lords to be granted. There has been a difference of judicial opinion on a matter which is, in one sense, a novel point, and the sum involved is a large one. We might perhaps have limited the leave to the one matter of wear and tear, but we thought that it would be very inconvenient to do that and probably would effect a very small saving in cost. Therefore, the leave which will be given will be general leave.

Sir William Jowitt.—I am obliged to your Lordships.

An appeal having been entered against the decision in the Court of Appeal, the case came before the House of Lords (Viscount Caldecote, L.C., Viscount Maugham, Lords Russell of Killowen, Wright and Romer) on the 19th and 20th February, 1940, when judgment was reserved. On the 19th March, 1940, judgment was given unanimously in favour of the Crown, with costs, confirming the decision of the Court below.

Mr. Raymond Needham, K.C., Mr. W. G. Brown and Mr. J. S. Scrimgeour appeared as Counsel for the Appellant Company, and the Solicitor-General (Sir Terence O'Connor, K.C.) and Mr. Reginald P. Hills for the Crown.

JUDGMENT

Viscount Caldecote, L.C.—My Lords, the Appellant Company was formed on the 22nd August, 1930. Its primary object was the acquisition on the terms of a Scheme of Arrangement or Amalgamation sanctioned by the High Court of Justice of the undertakings of two companies, which I will call respectively the Steel Company and the Strip Company. The businesses of these two companies were continued by the Appellant Company as from the 22nd August, 1930, the businesses formerly carried on by the two companies being thereafter treated as branches of the Appellant Company. The Steel Company at the date of its acquisition by the Appellant Company had in its books a sum representing trading losses of the Steel Company, in respect of which relief under Section 33 of the Finance Act, 1926, had not been given. The Strip Company had a similar item in its books in respect of which relief had not been given. In addition to this item, the Strip Company was entitled to a deduction for wear and tear of plant, but it had not been possible, owing to the losses incurred by that company, to give effect to this deduction. The Appellant Company claimed the right to set off these three sums against its own profits.

The Special Commissioners found that the Appellant Company succeeded to the trades of the Steel Company and the Strip Company and falls to be assessed as if a new trade had been set up or commenced. They accordingly held that the Appellant Company was not entitled to the deductions claimed. Lawrence J., differed from the Special Commissioners as to the wear and tear claim, but otherwise upheld their decision. The Court of Appeal reversed Lawrence, J., as to the wear and tear item and decided against the contentions of the Appellant Company on all points.

My Lords, the deductions claimed are a form of relief from the liability to pay Income Tax upon profits or gains, and the taxpayer must establish his claim upon a correct interpretation of the language of the material enactments.

The claim to deduct the wear and tear allowance of the Strip Company from the profits of the Appellant Company derives from Rule 6 of the Rules applicable to Cases I and II of Schedule D of the Income Tax Act, 1918, but the decision ultimately depends on the effect to be given to Rule 11 enacted by Section 32 of the Finance Act, 1926. Before the passing of that Act, Rule 11 of the Rules applicable to Cases I and II of Schedule D, which in its turn replaced the fourth Rule of Schedule D as enacted in the Income Tax Act, 1842, provided that the tax payable by a person succeeding to a trade should be computed according to the profits or gains of

(Viscount Caldecote, L.C.)

the trade during the respective periods prescribed by the Act notwithstanding the succession, unless the person succeeding to the trade proved that the profits or gains had fallen or would fall short from some specific cause since the succession took place. If that were the material enactment for your Lordships' consideration, the Appellant Company would clearly be entitled to a deduction of the wear and tear allowance from its profits. The alteration effected by Section 32 of the Finance Act, 1926, was substantial. Paragraph (1) of the new Rule 11 thereby enacted dealt with changes in a partnership, while paragraph (2) dealt with successions to a trade. The difference in the treatment is remarkable. In the first case the computation of tax is to be made notwithstanding the change in the partnership, according to the profits or gains of the trade during the periods prescribed by the Income Tax Acts. In the second case the tax payable by the person succeeding is to be computed as if he had set up or commenced the trade at the time he succeeded, and the tax payable by the person carrying on the trade until that time is to be computed as if the trade had then been discontinued. This direction on the face of it seems to me to conclude this question in favour of the Crown. For if the tax payable by the Appellant Company as successor to the trades of the two former companies is to be computed as if the Company commenced to trade when it succeeded, it would seem impossible to make a deduction in respect of allowances arising in years of assessment before that in which it must be taken that the new trade was set up or commenced.

It was, however, strenuously argued on behalf of the Appellant Company that Rule 11 introduced by Section 32 of the Finance Act, 1926, did not relate to the method of computation of profits, but merely altered the basic year of assessment in cases where there was a succession to a trade. My Lords, I confess I had some difficulty in following the argument. In computing the tax payable upon the profits or gains of the trade, part of the process is the deduction of any allowances permitted by the Income Tax provisions. As long as the profits and gains under Schedule D were computed on the basis of an average of three years, the deduction was made from the figure resulting from the taking of the average, and the balance was the amount of the profits and gains on which tax was charged. When the profits or gains of the year preceding the year of assessment were substituted for the average of the three preceding years, the process was the same so far as a deduction for wear and tear was concerned. The words of the new Rule 11 enacted by Section 32 of the Finance Act, 1926, seem to me imperative and clear, and I see no reason for not giving them their natural meaning.

A further contention which can be dealt with more briefly was made with regard both to the claim in respect of wear and tear and to the claim in respect of losses. Originally the Appellant Company

(Viscount Caldecote, L.C.)

claimed, so far as losses were concerned, to be within Section 33 of the Finance Act, 1926, apart from the effect of the Order of Eve, J. That argument was abandoned in the Court of Appeal and it is now admitted that the relief which Section 33 gives is purely personal to the person sustaining the loss. The claim in respect of losses, therefore, rests solely on the sections of the Companies Act and the Order of Eve, J. The contention now advanced is that the effect of Section 154 and of the Order of Eve, J., transferring the undertakings of the two companies and of their properties was to transfer the right to deductions to the newly formed Appellant Company. This, in my opinion, requires an impossible construction of Section 154 of the Companies Act, 1929, and of the Order of Eve, J.

On both points I agree with the judgment of Finlay, L.J., in delivering the judgment of the Court of Appeal, and I think this appeal should be dismissed with costs.

Viscount Maugham.—My Lords, as appears from the Special Case, the main questions are whether the Appellant Company, a new company amalgamated under Sections 153 and 154 of the Companies Act, 1929, is entitled to deduct wear and tear allowances and losses incurred by the constituent companies for the years before the amalgamation.

The Appellants acquired their business and undertaking on the 22nd August, 1930, under a Scheme of Arrangement sanctioned by the Court pursuant to Sections 153 and 154 of the Companies Act. The two transferor companies were the old United Steel Companies, Ltd., and the United Strip and Bar Mills, Ltd., whom I shall refer to as the 1918 Steel Company and the Strip Company. These companies had not been successful. They had made large losses in respect of which relief could not be obtained under Section 34 of the Income Tax Act, 1918. The Strip Company had also been unable to make the deductions in respect of wear and tear to machinery which it was entitled to make under the provisions of Rule 6 of the Rules applicable to Cases I and II, Schedule D, of the Income Tax Act, 1918 (a Rule which I shall refer to as Rule 6). The Appellants' claim is to carry forward and set off against their own profits the losses incurred by the 1918 Steel Company and the Strip Company before the amalgamation, and also to deduct from their profits the unapplied balances of the wear and tear allowances of the Strip Company. The Court of Appeal have decided both these questions in favour of the Crown, varying an Order of Lawrence, J., who was in favour of the taxpayer with regard to the allowance for wear and tear.

There was a further point suggested, namely, that the Appellants were entitled to succeed by virtue of Sections 153 and

(Viscount Maugham.)

154 of the Companies Act, 1929, a contention which was described by the Court of Appeal as somewhat startling.

My Lords, I am content with the judgment of the Court of Appeal on all points, and shall trouble your Lordships only with a few observations relative to the claim as regards the wear and tear allowance under Rule 6.

I will begin by observing that the right under Rule 6 is not a *chose in action* or an asset of the taxpayer, and that it could not be assigned to the Appellants. It relates only to deductions allowable to a taxpayer in charging the profits or gains of a trade as representing the diminished value by reason of wear and tear of machinery or plant used in the trade by and belonging to the taxpayer. Sub-rule (3) of Rule 6 allows the deduction to be added by the taxpayer to the amount of the deduction in a subsequent year if there has not been a previous opportunity of making the deduction out of profits. It is clear that if the trader goes out of business this right to carry forward a deduction is lost, unless indeed there is a statutory right given to some other trader, presumably a successor, to deduct the diminished value (by wear and tear) of machinery and plant used by the predecessor from the profits or gains of the successor. It will be remarked that the machinery and plant might have been placed on the scrap-heap, or perhaps acquired by the successor for a very small sum. It is a little difficult to see the reason in such a case for giving to the successor the right claimed. But there is always a possibility of finding in the twists and turns of the Income Tax maze some relief or refuge for the harassed taxpayer, and this possibility we must now examine.

My Lords, I agree with the opinion expressed by the Court of Appeal that the point turns upon the proper construction of Rule 11(1), introduced in substitution for an older Rule by Section 32 of the Finance Act, 1926. The new Rule must now be treated as Rule 11 of the Rules applicable to Cases I and II of Schedule D. We were urged to regard this Rule in relation to its history (which is fully stated in the judgment under appeal) and to its context as one of a number of Rules into which it was introduced.

I have carefully borne this precept in mind, but I am nevertheless of opinion that the true construction and effect of the Rule are reasonably clear. There are two parts to the Rule. Reading it shortly, the first Sub-rule deals with partnerships and provides that if a change in the partners has occurred in any way, one or more partners continuing to be engaged in the business, the tax payable by the continuing partners or partner shall, notwithstanding the change, be computed according to the profits or gains of the trade during the period prescribed by the Income Tax Acts.

---

(1) *See* page 106 *ante*.

(Viscount Maugham.)

There is an important proviso to the Sub-rule which gives the continuing partners a right, by a signed notice to the surveyor, to require " that the tax payable for all years of assessment shall be " computed as if the trade, profession or vocation had been dis- " continued at the date of the change, and a new trade, profession " or vocation had been then set up or commenced, and that the " tax so computed for any year shall be charged on and paid by " such of them as would have been charged if such discontinuance " and setting up or commencement had actually taken place ". If such notice is given " the tax shall be computed, charged, " collected and paid accordingly ".

Sub-rule (2) applies to the case of any person (which includes a company) succeeding to any trade previously carried on by another person, and it provides that the tax payable for all years of assessment by the new owner " shall be computed as if he had set up or " commenced the trade, profession or vocation at that time, and " the tax payable for all years of assessment by the person who " until that time carried on the trade, profession or vocation shall " be computed as if it had then been discontinued ".

My Lords, I am clearly of opinion that if the proviso to Sub-rule (1) is brought into operation by an appropriate notice the new partners cannot obtain the benefit of allowances or deductions available prior to the new trade being commenced. It will be noted that the proviso specifies in some detail the notice which must be given and such notice itself states the consequences, namely, that the tax is to be computed for any year and also charged and paid as if there were a *new* trade, profession or vocation. It is stated in the judgment under appeal that Counsel for the present Appellants did not dispute the view of the proviso which I have above stated. This admission was not made before your Lordships, but I heard no argument which led to the belief that the admission was not rendered necessary by the language of the proviso.

If we turn to the second part of Rule 11, which deals with succession to trade by a stranger, the language seems to me almost equally clear. The words " at that time " and " as if it had then " been discontinued " are strong to suggest that the tax payable is to be computed for all purposes as if there were a *new* trade, profession or vocation. To my mind, it is at any rate clear that there is no possibility of reading into the Rule, or any other existing Rule to which we were referred, a right to exercise the remarkable privilege contended for, namely, of deducting from profits made after a previous business has been discontinued the diminished value of plant and machinery which the successor has perhaps never acquired.

For these reasons and for those given by the Court of Appeal, I agree that this appeal must be dismissed.

Lord Russell of Killowen (read by Lord Romer).—My Lords, the claim of the Appellants to be entitled to set off against their own profits allowances for wear and tear which the old companies would have been entitled to carry forward against future profits if they had continued to trade, is a claim which in my opinion could only be acceded to by completely ignoring and proceeding in the teeth of the provisions of the second paragraph of Rule 11 of the Rules applicable to Cases I and II of Schedule D.

It was contended that Rule 11 did not relate to the manner in which the profits of any year were to be computed, but merely prescribed, in the case of a change in the ownership of a trade, the period the profits of which were to be the measure of assessment for the year of assessment. In my opinion, the new Rule introduced by Section 32 of the Finance Act, 1926, goes far beyond that. Under the former Rule 11, as under the Income Tax Act, 1842, the cases of changes in the ownership of a trade within the year of assessment, or within what may be called the basic period, were all treated on the same footing, whether there was any continuity of ownership or not; that is, irrespective of the question whether anyone who was an owner before the change was also an owner after the change. By the new Rule 11 a sharp distinction is drawn between the two cases; paragraph (1) deals with the cases where continuity of ownership exists; paragraph (2) deals with the cases where there is a complete break in the ownership of the trade. In the first case the tax payable by the new owners is computed according to the profits earned during the basic period, that is, earned by the then owners of the trade. The proviso, however, gives an option if all the owners old and new wish it, of dealing with the matter on the footing of the trade having been discontinued and a new trade set up at the date of the change. Paragraph (2) of Rule 11, however, prescribes only one method of computing the tax payable. It postulates that one person has succeeded to a trade " which until that time was carried on by another person ", that is, it postulates a complete break in the ownership. In such a case it provides that the tax payable by the new owner shall be computed as if he had set up the trade when he became owner, and that the tax payable by the old owner shall be computed as if the trade had then been discontinued. In the face of that provision it is impossible to hold that the new owner (whose business is to be treated, for the purpose of computing the tax payable by him, as a brand new business) can have any claim to allowances, in virtue of allowances for wear and tear carried forward by the old owner.

The judgment of Lawrence, J., on this part of the case[1] is largely, if not entirely, based on a contrast of the wording of the proviso to paragraph (1) with the wording of paragraph (2) of Rule 11, emphasis being laid upon the words " new trade " in the

---

[1] *See* page 99 *ante*.

(Lord Russell of Killowen.)

proviso, and the fact that the trade of the new owner in paragraph (2) is not described as a "new" trade. But if it once be appreciated that the proviso is dealing with cases in which there is some continuity of ownership, and that paragraph (2) is dealing with cases in which there is a complete break in ownership, the reason for the difference of wording becomes apparent, and the point disappears. In the proviso it was necessary specifically to require the trade to be treated as if it were a new trade, because the existence of continuing owners might well have prevented it from being considered to be or being treated as a new trade. In the case of a complete break of ownership, the trade in the hands of the new owner, if treated as then set up for the first time, must necessarily be treated as a new trade, and need not be so described.

It was, however, argued that even if the true construction of Rule 11 operated adversely to the contention of the Appellants, they were nevertheless entitled to succeed in their claim and were entitled to exercise the rights which the old companies would have had, had they continued to trade, and this by reason of the Order of Eve, J., made under Section 154 of the Companies Act, 1929. My Lords, I find a difficulty in discovering in that Section any indication that property which the transferor company could not itself have transferred to the transferee company may nevertheless be transferred to that company by the Order of the Court. It is, however, unnecessary to decide this point, because of the particular right here in question. I desire, however, to reserve for future consideration the question whether the case of *Donoghue* v. *Doncaster Amalgamated Collieries, Ltd.*, [1939] 2 K.B. 578, was rightly decided.

The right here claimed is not only personal to the old companies, but is a right which can only be asserted in relation to Income Tax payable by them respectively in respect of the profits of the trades carried on by them respectively : and even assuming that the Order of Eve, J., operated to vest that right in the Appellants, it does not become *in transitu* a right exerciseable in regard to Income Tax payable by the Appellants in respect of the profits of the trade carried on by the Appellants.

There remains the claim for allowances in respect of losses carried forward by the old companies. This was rested solely upon the Order of Eve, J., and Section 154 of the Companies Act, 1929, and must fail with the other claim.

For these reasons I would dismiss the appeal.

Lord Wright.—My Lords, the main argument of the Appellants was as to the true construction of Rule 11 (2) enacted by Section 32 of the Finance Act, 1926. The words are in my opinion quite plain. In the most unequivocal language they sharply divide the trade carried on by the person succeeding, from the trade up to the time

(Lord Wright.)

of the succession carried on by the person to whom the former succeeded. The tax on the former is to be computed as if he had set up or commenced the trade, at the time when he succeeded. The tax on the latter is to be computed on the footing that the trade carried on by him up to the succession had been then discontinued. I cannot better express my reasons for rejecting the Appellants' contention than by quoting the words of Finlay, L.J., in delivering the judgment of the Court of Appeal[1]: "The "direction to compute the tax payable can only mean that the tax "payable has to be ascertained after making all proper allowances "on the basis that the trade was set up or commenced on the last "mentioned date. This must of necessity exclude any allowances "to which the predecessor might be entitled in respect of the period "antecedent to the acquisition of the trade by the successor". I cannot accept the contention on behalf of the Appellants that Rule 11 (2) when it speaks of the computation of the tax is merely concerned with the change in the period of assessment. My view is, I think, fatal to the claim for allowances for wear and tear and *a fortiori* to the claim for losses under Section 33.

But it was sought to support both claims by relying on Section 154 of the Companies Act, 1929, and the Order of Eve, J., made under that Act confirming the deeds of arrangement and amalgamation of the two old companies with the Appellant Company. The Order transferred, so it was contended, to the Appellant Company the right to the allowances claimed because, it was said, they were included in the terms of the Order in that it transferred to the Appellant Company the properties, rights and powers of every description of the old companies. It is, I think, a sufficient answer to this argument that the old companies never had any right to these allowances. I question whether the claim to an allowance under Rule 6 of the Rules applicable to Cases I and II of Schedule D of the Income Tax Act, 1918, can properly come under the description of a property, right or power. But in any case the old companies never had any such right or property or power, however it is described, in respect of these allowances. All they had was a claim to allowances from their own profits in respect of wear and tear or losses. Neither company during its existence ever had profits or gains from which the deductions now claimed in whole or in part could have been made. The Appellant Company has been carrying on its own trade as from 1930 and it is in respect of the profits of that trade that the allowances are claimed. The old companies never had any interest in that trade. Their own trade ceased in 1930.

This, I think, is a sufficient answer. It would however have been a strange result if the Companies Act, 1929, had by a side

---

[1] *See* page 107 *ante*.

(Lord Wright.)

wind amended in a substantial particular the Finance Act, 1926. To effect such an amendment express and apposite words would have been necessary.

The Appellants relied as supporting their construction of the Companies Act, 1929, on the decision in *Donoghue* v. *Doncaster Amalgamated Collieries, Ltd.*, [1939] 2 K.B. 578. That was a decision of the Court of Appeal constituted by the same members as those who gave the judgment under appeal. The powers of Section 154 were there held to extend to dealing with a purely personal right, namely, a contract of employment. If it were material I should desire most carefully to consider what was there decided. But the reasons for which I reject the Appellant Company's contention are sufficient, quite apart from any questions considered in *Donoghue*. Indeed the members of the Court of Appeal when they gave their judgment in *Donoghue* a few months after their judgment now under appeal do not refer to the latter and do not seem to have felt that there was any conflict between their two judgments. I do not here consider it necessary to examine the decision in *Donoghue*.

I concur in the motion proposed.

Lord Romer.—My Lords, it must be conceded that were it not for the change in the law effected by Section 32 of the Finance Act, 1926, the Appellants would have been entitled to deduct from their profits for the year ending the 5th April, 1937, the aggregate of the wear and tear allowances that had been made to the Strip Company up to the 22nd August, 1930. For on this latter date the Appellants succeeded to and continued thereafter to carry on the very same trade that up to then had been carried on by the Strip Company. The allowances would accordingly by reason of the provisions of Sub-rule (3) of Rule 6 of the Rules applicable to Cases I and II of Schedule D, Income Tax Act, 1918, be added to the amount of the deduction for wear and tear for the year of assessment in question and deemed to be part of that deduction. Rule 11 of those Rules would have had nothing to do with the matter. It was in the first place a Rule that dealt only with changes and successions in the persons carrying on a continuous trade or profession occurring within the year of assessment or the period of average upon which the assessment had to be based. In the second place the Rule was solely concerned with the basis on which the profits or gains of the trade or profession were to be computed where such a change had occurred, and was in no way concerned with what deductions could be made from those profits or gains in respect of allowances under Rule 6. But the new Rule 11 substituted for the old one by Section 32 of the Finance Act, 1926, is, so far at any rate as successions are concerned, in very different terms. It now deals with the tax payable for all years of assessment after the succession has taken place,

(Lord Romer.)

and enacts (paragraph (2)) that it shall be computed as if the successor had set up or commenced the trade, profession, or vocation at that time. The Rule no longer seems merely to contemplate, as did the old one, a change in the ownership of a continuous trade, but seems to enact that tax shall be payable as though there had been a change in the trade itself. This was the construction put upon the Rule by the Court of Appeal, and in my opinion it is the only possible construction. I am unable to attach any importance to the fact that in the proviso to paragraph (1) of the Rule the word " new " occurs and that it does not occur in paragraph (2). If the successor is to be treated for Income Tax purposes as if he commenced the trade at the time of the succession, I am unable to see how the trade then commenced can for those purposes be regarded as being other than a new trade. This being so, it is obvious that there can be no deductions allowed in respect of the trade carried on before the succession took place. Such trade has for the purposes of taxation to be treated as though it were a different trade altogether from the trade being carried on by the Appellants.

My Lords, as to the contention of the Appellants based upon Sections 153 and 154 of the Companies Act and the Order of Eve, J., of the 16th August, 1930, a contention that relates to the losses incurred by the Steel Company and the Strip Company as well as to the wear and tear allowances of the latter Company, the decisions of Lawrence, J., and the Court of Appeal rejecting such contention appear to me to be plainly right. The effect of the Order of Eve, J., was that the Appellants succeeded to the trades of the two companies within the meaning of Rule 11 (2); but there is nothing in the two Sections that can possibly be regarded as excluding the Appellants' succession from the operation of that Rule. It is true that by virtue of the Sections and the Order the Appellants succeeded to all the rights possessed by the two companies at the time of the succession, but they did not thereby obtain any right to deduct the losses and wear and tear allowances of the two companies from the profits they might subsequently earn by their own trading; for the two companies had not, and obviously could not have had, any such right themselves.

My Lords, I agree that this appeal should be dismissed with costs.

Questions put:

That the Order appealed from be reversed.

The Not Contents have it.

That the Order appealed from be affirmed and that this appeal be dismissed with costs.

The Contents have it.

[Solicitors:—Johnson, Weatherall, Sturt & Hardy; Solicitor of Inland Revenue.]