Privy Council Appeal No. 100 *of* 1929.

The Commissioner of Taxes - - - - - - *Appellant*

v.

The British Australian Wool Realization Association, Limited (in liquidation) - - - - - - - *Respondents*

FROM

THE SUPREME COURT OF VICTORIA.

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 17TH NOVEMBER, 1930.

Present at the Hearing :

THE LORD CHANCELLOR.
LORD BLANESBURGH.
LORD MERRIVALE.
LORD HANWORTH.
LORD RUSSELL OF KILLOWEN.

[*Delivered by* LORD BLANESBURGH.]

This appeal arises out of assessments to income tax in respect of each of the five financial years beginning on the 1st of July in 1921, 1922, 1923, 1924 and 1925, made upon the Respondent Association by the Commissioner of Taxes for Victoria under the Victorian Income Tax Act 1915. The assessments were all of them notified on, and none of them before, the 21st July, 1926. When so notified the Association, by that time in liquidation, objected to them under Section 56 of the Act ; the Commissioner disallowed the objections and, in pursuance of Section 57 was required by the Association to transmit them to be heard and determined by a Judge of County Courts. The learned Judge of the County Court at Melbourne to whom they were duly transmitted, stated, upon the application of both parties, a special case and referred the whole matter for the opinion of the Supreme Court of Victoria under Section 59 of the Act. The Full Court on the

case so stated decided that certain amounts which for the purposes of the assessments had been included in the taxable income of the Association were not chargeable to income tax and on the 7th May, 1929, ordered the assessments to be remitted to the County Court Judge for amendment accordingly. The present appeal by the Commissioner to His Majesty in Council is an appeal from that order.

Their Lordships have thought it convenient to set forth in some detail the steps by which in accordance with the statute the questions at issue reached the Supreme Court and now come before the Board. They have done so in order that there may at once be made apparent the essential difference between the judicial task under the Victorian statute and that set the Court on a case stated by the Special Commissioners under the British Income Tax Act. The duty of their Lordships, in the present case, as it was the duty of the Supreme Court, is to determine whether on all the facts stated by the learned County Court Judge, as properly appreciated, the Association is assessable to income tax in respect of each or any of the sums still in debate. The question for the Board is not that which in closely analogous circumstances would be submitted to the Court under the British statute which leaves all questions and inferences of fact to the special Commissioners whose decision is conclusive and binding on the Court if there was any evidence to support it. It is important to bear in mind the differing rôles of the Court under the two Acts. It is, for instance, only by doing so that the limits of applicability can definitely be assigned to many of the judicial decisions under the British statute bearing upon questions analogous to those now again in issue.

Of the items originally brought into charge by the Commissioner some are no longer in controversy. In the course of the proceedings they have been either abandoned or conceded. Three, however, presently to be particularised and amounting in the aggregate to a very large sum remain in dispute and must now be dealt with by their Lordships.

The liability, if any, of the Association to Victorian income tax in respect of them arises under Section 35 of the Act of 1915, which, by its terms immediately relevant provides that

> "So far as regards any Company liable to pay tax, the income thereof chargeable with tax shall . . . be the profits earned in or derived in or from Victoria by such company during the year immediately preceding the year of assessment."

Upon this section it is convenient to note in passing that the Association is under it "a company liable to pay tax," not specially because it was a company incorporated in Victoria with its registered office at Melbourne, but because the word "company" as there used is made by Section 4 to include "every corporate company howsoever incorporated and whether under the laws of Victoria or any other country and whether its head or principal office or principal place of business is in Victoria or

elsewhere." It is convenient also to note at once that under the section the income of the Association to be brought into charge must answer the description of being not only " profits earned " but of being " profits earned in or derived in or from Victoria " by the Association. Each of these matters will presently be found to be highly important.

It is not, however, the wording of the section that in this case presents the real difficulty. In themselves its terms are clear enough. One matter upon which there might have been room for discussion must now be taken to be settled, viz., that it is income profits as distinct from an appreciation in value ascertained by the mere realisation of a capital asset that are by the section brought into charge (cf. *Ruhamah Property Company Limited* v. *Federal Commissioner of Taxation,* 41 C.L.R. 148). That difficulty out of the way, the enactment is not in other respects of doubtful import. The trouble is to apply its provisions to the facts of a case so altogether exceptional in its incidents, as is the present. As will immediately appear, it is perhaps not too much to say that the circumstances leading to the formation of the Association were probably without precedent, and its activities while it existed were possibly in extent and certainly in character without parallel. The mere magnitude of its operations, with the attendant organisation to which the Association succeeded, may, if necessary vigilance be not exercised, well result in a misconception of their essential character.

Of the three questions which still remain for decision, the first and most important is whether a sum of approximately £4,101,404 remaining after all share capital has been repaid, and representing for the most part surplus receipts by the Association from the realisation of an immense quantity of wool made in circumstances and under a title later to be stated, is to that extent a capital appreciation of, or is a profit earned by the Association and as to some proportion of it at all events (the Commissioner suggests one-fourth), earned in or derived in or from Victoria. The second question relates to certain sums of commission received by the Association on the realisation by it of wool belonging to the Imperial Government. These commissions were admittedly all of them profits earned by the Association. Were they as to any part of them earned in or derived by it in or from Victoria ? The third question relates to two sums each of £68,848 7s. 9d. and aggregating £137,696 15s. 6d. made over to the Association by the Commonwealth Government in the years 1923 and 1924 respectively and representing a profit realised by that Government from a sale of wool to a company called " The Wool Combing and Spinning Company, Ltd." Was this receipt something which could properly be brought into charge either as a profit earned at all, or as a profit earned in or derived in or from Victoria by the Association ?

The members of the Supreme Court agreed in the conclusion that no one of these three items formed part of the taxable

income of the Association. Even if the third item represented a profit of the Association in any sense—and it was certainly the opinion of MacFarlan J., and possibly of his colleagues also, that it did not—each of them took the view, that neither that item nor, as they held, the commissions referred to in the second question, had been earned in or derived in or from Victoria.

With regard to the main item in dispute—that first above mentioned—the learned Judges also agreed in holding that it formed no part of the taxable income of the Association. But for different reasons. McArthur J. (with whose judgment Wasley J. concurred) was of opinion that the sum in question could not be regarded as in the statutory sense " a profit earned " by the Association. MacFarlan J., on the other hand, held it to represent part of the Association's ordinary trading profit. It was, however, not to be included in its Victorian taxable income because it had not, in his judgment, been earned in or derived in or from Victoria.

The elaborate facts on the true effect of which, of course, everything depends, are set forth in great detail in the special case and in the annexures thereto. They are discussed also in the judgments delivered in the Supreme Court. Those to whom this judgment is primarily addressed are already familiar with them all. Accordingly, in what follows their Lordships will concentrate primarily on the aspects of the case which have most helped them to reach their conclusions upon it, touching only upon such other facts as must be stated to make their judgment self-sufficient.

The transaction leading up to the claim of the Commissioner was an arrangement concluded in 1916 between the Government of the Commonwealth of Australia and the Imperial Government under which for the satisfaction of British and Allied war requirements the Imperial Government acquired through the Commonwealth Government the whole of the Australian Wool Clip for the wool season 1916–1917, upon the terms of paying for it on the basis of a flat rate of 15½ pence per pound greasy wool f.o.b. Australia with a further prescribed sum per pound for handling charges. Before the end of that wool season the arrangement was continued for the wool year 1916–1917. and in June, 1918, was further prolonged, with some slight variation in handling charges, for the duration of the war, and for a further period which, in the event, terminated on the 30th June, 1920—the end of the wool year 1919–1920. Some idea of the magnitude of the transaction and of the payments involved may be gauged from the facts that the suppliers, great and small, numbered approximately 150,000, located all over Australia, and that the total price paid by the Imperial Government for the wool acquired amounted to £153,743,857.

For the purpose of giving effect to the arrangement and of acquiring on behalf of the Commonwealth Government the entire clip from the suppliers, there was constituted by that Govern-

ment a Central Wool Committee with, in each State, a wool committee subordinate to it. To the Central Wool Committee was assigned, in accordance with published statutory Regulations, and subject to the directions of the Prime Minister of the Commonwealth, the entire working out of the arrangement with the Imperial Government. No wool was compulsorily acquired, but as the sale of Australian wool was, by the Regulations, prohibited except through or to or with the consent of the Central Wool Committee, it became possible for that Committee to purchase substantially the whole of the wool of the various clips at prices so adjusted on appraised values that the total sum paid for the clip of the year was equal to a sum arrived at by multiplying the total quantity of pounds supplied by 15½ pence. The price was not inadequate. It represented the average of prices obtained by growers in 1913–14, with an addition of 55 per cent. And it was fixed: so that in the event of the market price falling below it, the burden fell on the Imperial Government. But as between the two Governments it was final, only as regarded the wool used for war purposes. Because the Imperial Government announced that "in the event of profit being realised from the sale of any surplus which might remain over after military requirements of the British and Allied armies had been satisfied His Majesty's Government would propose, after payment of all expenses, to share such profits with the Government of Australia."

And this share that Government in turn publicly declared its intention to allocate amongst the suppliers. "From time to time," says the special case, "between the months of November, 1916, and August, 1919, statements were made in Parliament by different Ministers of State for the Commonwealth of Australia to the effect that the Australian share of any profits made by the Imperial Government by the sale of any wool . . . would not be retained by the Commonwealth Government but would be distributed amongst the suppliers of wool in Australia." The interests in wool certificates and shares of the Association presently to be stated given to the larger suppliers and the substituted sums in cash paid at the time of its formation to the smaller suppliers was the fulfilment by the Commonwealth Government of that promise.

But it must here be noted—the fact becomes very relevant in the sequel—that, as was laid down by the High Court of Australia in *Cooke's* case 31 C.L.R. 394, and in effect affirmed by this Board on appeal, the whole arrangement just summarised was one not cognisable in a Court of Law. As to the Commonwealth Government's share of surplus profits, again the question of its distribution or retention was, as between the two Governments, a matter for the Commonwealth, and its distribution when resolved upon by that Government was in point of law left, by the Regulations, to the wisdom, fairness and discretion of the Central Wool Committee. In other words, no individual supplier, however important, ever had in the eye of the law prior to the formation

of the Association a right to any part of the Commonwealth Government's share of profit.

To some of the suppliers this judicial pronouncement was fundamental. In the case in which it was made, the decision was that the discretion had been legally exercised by the Central Wool Committee when it decided to exclude from participation altogether the suppliers of skin wool during two seasons. For the purposes of the present case, however, the pronouncement is chiefly important in that it emphasises the fact that the Commonwealth Government, or the Central Wool Committee acting on its behalf, was free to prescribe and did prescribe the principles upon which the divisible surplus profit accruing to itself should be apportioned amongst the suppliers throughout all Australia. Difficulties, possibly insuperable, must have arisen if the final division had not been one to be dictated by somebody. To translate either by agreement or judicial decision the necessarily vague Ministerial statements of intention into a definite and detailed scheme of distribution amongst a multitude of participants differently situated might well have proved to be an impossible task. It had not to be attempted. Through the medium of the Association a prescribed apportionment was made by direction of the Central Wool Committee on behalf of the Commonwealth Government. The fact that strictly it was only as a result of his being nominated for benefit by that Committee that any supplier became possessed of or entitled to his certificates and shares in the Association may, as will presently appear, have a bearing on the first and principal question raised on this appeal.

In addition to the Australian clips so purchased, the Imperial Government also acquired the wool grown in other Dominions and Colonies during the same seasons, and at the date of the Treaty of Peace with Germany large quantities of (A) the surplus wool, and (B) the wool acquired from other Dominions and Colonies, the so-called " New Zealand " wool, was in store. Both before and after the Armistice the Imperial Government realised by sales to civilian purchasers very large quantities of surplus wool, and in September, 1920, paid to the credit of the Commonwealth Government the sum of £6,486,992 as a first payment on account of the promised share of profits resulting from these sales. The Central Wool Committee announced its intention to distribute amongst the suppliers in proportion to the originally appraised value of the wool acquired from each that sum, together with a further amount of £1,166,500 held by the Committee and representing receipts over expenses in the handling of the wool, and in October, 1920, the total sum of £7,653,202 was so distributed by the Committee. The Association was not then in existence. It was not the medium of distribution of the first payment, and no question of income tax with reference to it, except in the hands of its Victorian recipients, has ever been raised by the Commissioner.

But great quantities of surplus wool still remained unrealised in the hands of the Imperial Government. On the 31st December,

1920, the amount was not less than 1,836,005 bales. Manufacturers' stocks of raw material had through the sales aforesaid been replenished. Prices were falling. Demand was small. The situation became critical. To throw upon the market this vast quantity of wool when the post-war clips were becoming available for sale must have resulted in the gravest injury to Australian wool-growing, while at the same time the British textile industry was not to be deprived of the opportunity of obtaining ample supplies of wool at the lowest price possible In other words the particular, as distinguished from the Imperial, interests of Great Britain on the one side and of Australia on the other, had in this matter of realisation become divergent. The situation made clear in the annexures thereto is thus described in the special case itself :—

"For some time after November, 1918, no difficulty was experienced in finding a good market for wool, but by the year 1920 woollen manufacturers had replenished their stocks of raw material, and because of the tendency of the market to drop and the uncertainty about future prices were not buying wool freely. Moreover, after the 30th June, 1920, the current clip of Australian wool which had not been acquired by the Imperial Government under the aforesaid arrangements was outside Government control and became available for sale in competition with the surplus wool. Prices for wool began to drop and a danger arose that if both the current clip wool and large quantities of the said surplus wool were put on the market at the same time, the market would collapse, the prices realised for both would be unsatisfactory and the wool industry in Australia would receive a grave set back. On the other hand there were certain interests in England pressing the Imperial Government to place on the market the surplus wool in large quantities in competition with the current clip wool."

Negotiation with a view to meeting the crisis that threatened both in Australia and Great Britain then took place between, on the one side, the Commonwealth Government, and on the other, the Imperial Government acting through the Ministry of Munitions. The incorporation of the Association was one of the results of that negotiation. The objects of attainment on either side, and the manner in which, through the Association, these objects were adjusted, very clearly appear from documents annexed to the special case and, in particular, from two telegrams of the 31st December, 1920, and the 7th January, 1921, which are specially important because as will be seen, their terms became binding contractually upon the Association after it was formed.

Summarised, these documents show that it was, in the view of the Commonwealth Government, of vital importance not only to the wool industry, but to the Commonwealth generally that the realisation of the surplus wool should not be conducted so as to destroy the market for the current clips.

This was recognised by the Imperial Government. For Great Britain, however, it was essential, as Ministers expressed it in their telegram of the 31st December, 1920, that in view of the depressed condition of the textile industry involving much unemployment the operations of realisation should be conducted with due regard to the legitimate interests of the British consumer. The realisation also must be made as promptly as market conditions permitted, and it must be stipulated that His Majesty's Government may revoke the agency agreement at any time if the conduct of the business of the Association gives cause for dissatisfaction.

With this, in turn, the Commonwealth Government agreed. The policy favoured in Australia, it was explained in the cable of the 7th January, 1921, was "to dispose of the surplus or carry-over wool as promptly as market conditions permitted, and the sooner the better. As long as the surplus or carry-over wool remained in a raw condition it was a positive menace to Australian wool-growing."

In the result agreement was reached in terms thus summarised by the Prime Minister of the Commonwealth in the cable of the 7th January, 1921 :—

> "Having accepted the stipulations contained in your telegram [of the 31st December, 1920] it is hereby mutually agreed to liquidate the Australian Section of the Imperial Wool purchase account at the earliest possible date and to hand over half of the surplus assets ascertained and certified to exist on the agreed settling day to Commonwealth Government, which will, in turn, hand it over to the Realization Association on account of Australian wool-growers in final settlement of the reciprocal obligations under the three wool purchase contracts. It is further agreed that subject to an agreement being arrived at between Minister of Munitions and Sir John Higgins, Chairman of the Special Executive Committee appointed by representatives of the Australian Wool Industry with my concurrence, His Majesty's Government assents to the formation of the British Australian Wool Realization Association, Limited. It is also agreed that His Majesty's Government shall sell through the agency of the proposed Association their half of the Australian carry-over wool subject to the before mentioned qualification. Your reference to an arrangement which you hope will shortly be made whereby the New Zealand carry-over wool will be at the disposal of the Association is noted with great interest by Commonwealth Government. It is hardly necessary for me to emphasise the importance of this. I trust that the arrangement may be concluded without delay."

The Association, the British Australian Wool Realization Association, Limited—its primary and in the result its only purpose, is reflected even in its name—was incorporated in Victoria on January 27, 1921, with a nominal capital of £25,000,000, in shares of £1 each. Its constitution was the result, as has been seen, of direct agreement between the two Governments. There was, indeed, no one else to agree anything in relation to it. Except for the five subscribers to its Memorandum of Association, all of them members of the Australian Board appointed by the Articles and subscribing for one share each, the Association had no shareholders for some months, and these were admitted, as will presently

appear, only by the direction of the Commonwealth Government itself. Its Memorandum and Articles of Association, while in many respects in common form, are conveniently effective for every purpose then in view. In its Memorandum of Association reference is specifically made to its primary object, and by Article 62, which names the eleven first Directors—five of them, the British Board, with Sir Arthur Horne Goldfinch, Director General of Raw Materials at the Ministry of Munitions, at their head, and six of them, the Australian Board, with Sir John M. Higgins, Chairman of the Central Wool Committee, at their head, with no share or other qualification required from any one of them—the control of the Association on the lines arranged is obtained at the outset, while by the provision that these first Directors shall hold office until 1924 that control, maintained during realisation, continued undisturbed throughout the existence of the Association.

But the attainment of these governmental purposes as agreed was further assured contractually by the agreements with the two Governments, into which the Association entered some weeks after it had been registered. The first of these in logical order is dated the 1st April, 1921, and is made with the Government of the Commonwealth. It recites the agreement of that Government with the Imperial Government under which the former had become entitled to one-half of the profits of the surplus wool and declares that with the consent of the Imperial Government the Commonwealth Government assigns to the Association all its right title and interest under the agreement to the intent that the Association shall be entitled to the half share of the Commonwealth Government referred to so far as such share has not already been paid to that Government. The consideration for the transfer is expressed to be 12,000,000 shares and £10,000,000 priority wool certificates of the Association, all fully paid up, to be issued to such companies, firms and persons as the Central Wool Committee for and on behalf of the Commonwealth Government may nominate, and there is a provision that these shares and certificates may be reduced in number by payments [in cash] to such companies, firms or persons in lieu of such shares and certificates.

The second agreement, first in point of date, was made with the Imperial Government on the 31st March, 1921. Its terms are summarised in paragraph 9 of the special case. It provided for the entire interest of the Imperial Government in the surplus wool being handed over to the Association for realisation on the terms of its receiving a selling commission of 1 per cent. on the sale price. Clause 9 of the agreement is for present purposes very material :—

> "It is agreed that no physical division of the Australian wool in which the [Association] has a one-half interest shall be made except as provided expressly hereafter, but that one half of every bale of such wool shall become the property of the [Association] and the other half of every such

bale shall remain the property of the [Imperial] Government to be held in trust by the [Association[in trust for the [Imperial] Government and that one half of the proceeds on every bale of such wool sold by the [Association] shall be accounted for to the [Imperial] Government and one half of the proceeds shall be retained by the [Association]."

The Association, by Clause 13, undertook in the management and control of the sales of wool to abide by the conditions laid down in the telegrams, already referred to, of the 31st December, 1920, and the 7th January, 1921, while by Clause 14 the power of revocation reserved to the Imperial Government by the former telegram is confirmed and agreed to and provision is made for a separation of the undivided interests of the Imperial Government and the Association in the surplus wool in the event of that power being exercised.

Finally by Clause 20, it was agreed that if any of the first Directors of the Association ceased to hold office while the selling agency of the Association was in operation, the Imperial Government should have the right of approval of all persons proposed to be appointed in their stead by the Association.

Under these agreements accordingly there passed to the Association the Commonwealth Government interest in the surplus wool still unrealised—an interest now formally recognised by the Imperial Government. There passed to it also a sum of £6,891,295, representing a moiety of the realizations already effected by that government and not, so far, paid over. Further, the Association under the agreements, became the instrument for the conversion of the whole of the surplus wool still unsold into cash, and so far as the Commonwealth moiety of that wool was concerned, it became also the medium for the distribution of the net surplus amongst those to be designated by that government as its recipients—namely, the original suppliers of wool.

And to those who had supplied in large quantities there were issued by official direction and in proportion to the appraised value of the wool they had respectively provided, all the priority certificates and shares of the Association which in the event constituted the scrip consideration for the transfer. For those of the suppliers whose wool had not exceeded £100 in appraised value—some 50,000 in number—a sum of £250,000 was, under the like direction, set aside by the Association. Out of that sum there was made to each of them in accordance with the direction of the Central Wool Committee and in satisfaction of all his claims, a cash payment which, less a substantial discount, represented the equivalent in nominal value of the wool certificates or shares which under the formulated scheme of distribution would otherwise have been his, but which in the event were never issued at all.

If, in its realization of surplus wool, a moderate market price was in the interests of the Australian Growers to be maintained, it was, doubtless, essential that the realisation of the New Zealand wool should also be under the same official control.

It is not surprising, therefore, that the decision of the Imperial Government to entrust this task also to the Association was so warmly welcomed by the Prime Minister of Australia in his cable of the 7th January, 1921. In this, as so frequently throughout the case, is it made apparent, that the realization by the Association was primarily always an affair of state, and never, in essence, commercial.

In the realization the Association was engaged for three years. It never essayed any other activity. The last bale of wool was sold at Hull in March, 1924. It paid no dividends. The net proceeds of realization as they became available were, as to one moiety, accounted for to the Imperial Government, its principal. As to the other moiety, supplemented by the cash proceeds of earlier realizations, received under the contract of 1st April, 1921, as above stated, these were applied, first, in the redemption of the Priority Wool Certificates and next in paying off, under schemes of reduction sanctioned by the Court the capital credited as paid on the shares of the Association. As a result of this procedure—a procedure which it will be seen was the nearest possible approximation, while the Association was still a going concern, to the normal distribution made by a company in liquidation—10s. per share were distributed in April, 1923, and 9s. per share in February, 1924. With 1s. still credited on each of its shares, the Association, its realization completed, went into voluntary liquidation on the 10th July, 1926, and in that liquidation the last remaining shilling has been paid off, leaving in the hands of the liquidators the balance of over £4,100,000. This sum, after all expenses have been met thereout, will become available for distribution as surplus assets, amongst the contributories of the Association, that is to say, amongst the original allottee suppliers or their transferees in accordance with their proportionate rights and interests therein.

The Commissioner, treating the entire amount as profit earned and arising as to some part of it in every one of the five years 1921–1925 has, by assessments for each of these years, charged the Association with income tax in respect of one-fourth of the whole —such being the proportion fixed by himself without, it must be said, any obvious justification—as that earned in or derived in or from Victoria by the Association. The Supreme Court, as already stated, held this assessment to be invalid. The question now to be inquired into and decided—the first of the three already particularised—is whether it is good in whole or in part.

Before embarking on that inquiry it will be convenient to direct attention to an underlying question much discussed in argument—the question, namely, whether the fully paid scrip issued by the Association pursuant to the contract of 1st April, 1921, represented a purchase consideration equivalent to its nominal value. It is only upon the assumption that it did, that

the first head of assessment here can, in point of amount, be justified. Apart, however, from its importance on that head, some attention to this aspect of the case will not be misplaced by reason of the light it throws upon the true rôle played by the Association in this great transaction of State.

Now in the whole record nothing is more striking than the fact that neither for the purpose of fixing the purchase consideration and thus quantifying the extent of Government bounty to the suppliers nor with any other object was it ever attempted to ascertain the real value of the 1,836,005 bales of surplus wool still unrealised with which the Association had to deal. Doubtless the task was one beset with difficulty, but their Lordships cannot doubt that the reason why it was not even essayed was that its result, however reliable, would have served no useful purpose. With the small suppliers provided for by the sum of £250,000 set aside to meet their claims there was nothing to be gained by a valuation made for the purpose of fixing the nominal value of the shares to be issued to the others. The amounts to be ultimately received in respect of these shares in no way resulted from their face value for the reason that, with an exception entirely negligible, the shares represented all the issued shares of the Association, and they were at all times in the hands of the suppliers to whom they were originally issued or of transferees or others deriving title under them. No further shares were ever issued to anybody. The original shares accordingly gave to their holders collectively all there was to be had. The nominal value attached to them, except for the purpose of fixing proportions in distribution, was of no account, and for that effective purpose one set of figures was just as good as another. The circular which accompanied the issue of the shares correctly stated the position. "The value of the shares," it said, "will depend absolutely on the market price of wool current during the realization period and no forecast can be mentioned at the present time as to the duration of such period."

£13,957,105, the sum at which the interest of the Association in the surplus wool was in fact taken into its books, and at which that interest was reflected in the nominal purchase consideration was reached as the result of a calculation described in the case—a calculation so remote from the realities that it could not have been supposed by anyone to have supplied, except by accident, a conclusion of values even approximately reliable. From the beginning it was as a valuation discounted by all previous results of realization, while its inadequacy disclosed in the immediate experience of the Association itself, was by 1922, as is seen by the Report of that year annexed to the special case fully recognised. Yet there was no resulting change in the accounts, and in every year of the realization—four in all—the remaining stock was still brought in at the original figure notwithstanding the surpluses year by year resulting from the realization which was proceeding.

The explanation of all this, their Lordships think, lies in the constitution and working of the Association in which an arbitrary figure to represent its paid up capital was for every effective purpose just as good as any other. If it was convenient, it was preferable to one which, whatever else its merit, was less so. This view is strikingly confirmed by a transaction, the foundation of the third question raised by the appeal—which in that connection must later be particularised. Here it suffices to recall that it concerns the two sums of £68,848 7s. 9d. paid by the Commonwealth Government to the Association in the years 1923 and 1924, sums to which under the contract of the 1st April, 1921, the Association had no claim. There are several corners of the case illuminated by this transaction. It supplies, for instance, one of many indications that for the Commonwealth Government the Association, if it was not always so, certainly became essentially and beyond all else the medium for distribution of the promised bounty to the wool suppliers. For the moment, however, their Lordships point to the transaction as further confirming the conclusion already deduced from so many other converging circumstances that the nominal value of the shares issued under the contract of the 1st April, 1921, was at no time of any effective significance. Even so large an addition to the consideration as that just stated was not allowed to add anything to it. In other words the issue was not based on real values because it never was necessary that it should be.

Their Lordships do not forget the suggestions in a contrary direction made on behalf of the Commissioner. More especially do they bear in mind the arguments based upon the settlement with the small suppliers where, apparently, the nominal value of the Association's issued shares determined the actual cash payments made. But the sum provided for the small suppliers collectively was itself arbitrary in amount. The participants were legion, and while presumably the individual payments made were not on the face of them inappropriate, their Lordships have little doubt that they were fixed by the Committee in the exercise of the power to do what seemed to be called for in the circumstances, a power which they rightly assumed government possessed. Accordingly, even this argument when weighed in the scales is found wanting, and it is their Lordships' considered conclusion on the predominant balance of fact that the figure above stated, while it was never a true index of value, was at no time so regarded. In this aspect of it this case finds its place among the authorities of which *Assets Company* v. *Forbes* 3 Tax Cases 542, and *Rand* v. *Alberni Land Company* 7 Tax Cases 609 may be cited as typical. So much for this question.

And there is another, upon which something must be said before their Lordships proceed further with their inquiry. In certain aspects of it, the description already given of the realization committed to the Association must be supplemented. Much depends upon a true conception being formed of that realization.

As must already have been gathered it was no new thing. Indeed, realization had been proceeding under a Committee of the Ministry of Munitions with Sir Arthur Goldfinch as its chairman since before the Armistice—that is to say for over two years. During that time great quantities of wool had been disposed of to civilian purchasers. As much as 14½ million pounds sterling had already been or were ready to be paid over by the Imperial Government in respect of the Commonwealth's promised half-share of the result. And this figure, large as it is, furnishes no test of the real extent of the realization which produced it. For the Imperial Government treated no proceeds as available for division until its own disbursements in relation to all its surplus wool sold and unsold had been recouped. Accordingly, the proceeds of realization in addition to the surplus divided had sufficed also to reimburse the full price originally paid by Government for all the wool still unrealized. The 1,836,005 bales which on the 31st December, 1920, remained in specie had no charge for purchase price standing against them. That had all been met out of the earlier realizations. The quantity of wool so realized must therefore have been enormous. It may well have exceeded the quantity subsequently disposed of by the Association itself. And these earlier realizations were realizations of the entirety of the wool sold, and it was to such a realization that the Association succeeded. It is not proper to regard its work as having been no more than a realization of its own undivided moiety of surplus wool separated and disconnected from all else, although that is what the Commissioner in justification of this first assessment has striven to do. In real truth notwithstanding variations in the legal title to the second moiety, there was throughout only one realization of the surplus wool and that a realization of the entirety effected by two successive agencies—the Association being the latest—but all of it rendered necessary until completely accomplished, by the fact that the wool having become superfluous for the purpose for which it had originally been acquired and useless in the hands of its owners for any other purpose had either to be realized or wasted. This, their Lordships think, is the outstanding fact. There is in the case no indication that except in one respect the realizations by the Association differed in any way from those to which it succeeded. It is not to be supposed that they would. They continued under the management of the same people. The British Board of the Association which conducted them was, even in its personnel, little more than a continuation of Sir Arthur Goldfinch's Munitions Committee. The organization had now a different name; it was constituted by a different legal authority, but in all essentials it remained as before. The true inference from all the facts stated and appearing is, as their Lordships cannot doubt, that Sir Arthur Goldfinch and his colleagues, continued as a Board, the realization which as a Committee they had inaugurated. Between the actual machinery of realization in use by them as a Committee and that

utilized by them as the Board the case again draws no distinction. It must have seemed to the learned County Court Judge that there was none to be drawn. The clear impression produced and doubtless intended is that the Association and its British Board inherited and utilized the selling organization of the Committee just as it was.

In one respect only, as has already been seen, was there a change—one not externally visible, but of the essence—a change which served to convert the realizations of the Association into something quite *sui generis* so far as the authorities relating to such claims as the present are concerned. Under the Committee the disposal of the surplus wool had been a purely commercial operation, presenting, as has been seen up to 1920, no difficulty. Under the British Board of the Association its realization and that of the New Zealand wool as well became a matter of arranged state policy. The agreement between the two governments, out of which the Association came into being, brought that about, and a realization of surplus wool whose sole or even primary purpose was the acquisition of gain, whether by the Imperial Government in respect of one moiety, or by the Association or its members in respect of the other was never again entertained. "Personal or individual gain is absent in the formation of the Association," was the assurance of the telegram of the 7th January, 1921. And it so remained.

The control, through the Board appointed at the beginning by agreement between the governments continued unbroken. The precautions taken to prevent miscarriage in that matter, already detailed, did not fail of effect. From the first the shareholders in the Association accepted the passive rôle assigned to them, content, as indeed in the circumstances they well might be, to receive in their prescribed proportions as volunteers under government the proceeds accruing from a realization of the government share officially inspired and directed. In all these respects this case, so far as their Lordships' experience goes, stands alone.

Is then this assessment upon the Association in respect of the sum covered by the first question good in whole or in part? To a consideration of that question, their Lordships now proceed. It is with reference to a Company circumstanced as has just been detailed and with reference also to a realization so unprecedented alike in character and extent that the answer must be given, and their Lordships have reached the conclusion that the answer of the majority of the learned Judges of the Supreme Court is the just one. The sums by the assessment brought into charge are not, they think, profits of the Association within the meaning of section 35 of the Act of 1915, and greatly as do the exceptional circumstances of the case point to that conclusion as being alone possible it is not, their Lordships think, strictly necessary to rely upon them in order to reach it. The facts, as detailed in this judgment, cannot upon the authorities

dealing with such questions properly lead to any other. The Association became possessed of its undivided moiety of each bale of surplus wool, for valuable consideration, it must be agreed, but under a binding contract to realize the other moiety expressed in such terms that its performance involved of necessity the simultaneous realization of its own. Moreover, with regard to that moiety the Association was the instrument for the fulfilment of a promise made on behalf of the Commonwealth Government from whom the wool had come that the proceeds of the realization would pass to the shareholders of the Association when available. No doubt the Association had under its memorandum of association full power to treat the proceeds of realization as circulating capital to be embarked and traded with in any business thereby authorised. But the Association could not have exercised that power without breach of a promise made on its behalf when its shares were handed to their original recipients, and there is no suggestion that any authority within the Association ever attempted to do so. It follows if the language of economists may be employed that in truth and in fact the Association's interest in the wool always was fixed capital and never was circulating capital. Its purpose with reference to it was to realize the asset, having done so to distribute the proceeds among those entitled and then itself to disappear. And this is just what in fact it did, and so effectively that if the Association had gone into liquidation so soon as the realization commenced instead of doing so after it was completed, the distribution of the proceeds amongst the contributories could not have been speedier than was the distribution amongst the shareholders. To their Lordships, therefore, there is disclosed, on their view of the facts here a case entirely within the terms of the following words from the judgment in *The California Syndicate* v. *Harris* 5 T.C. 159, which have since been so often cited with approval.

> " It is quite a well settled principle in dealing with questions of income tax that where the owner of an ordinary investment chooses to realise it and obtains a greater price than he originally acquired it at the enhanced price is not profit . . . assessable to income tax."

Equally applicable, in the view of their Lordships, are the words of Lord Dunedin in *The Commissioner of Taxes* v. *The Melbourne Trust* [1914] A.C. 1001, where he says, p. 1009 :—

> " If the liquidator of one of the banks had made an estimate of the various assets held by him for realization and then on realization had obtained more than that estimate such surplus would not have been profit assessable to income tax."

These pronouncements primarily made with reference to the British Income Tax Act are, in view of its judicial interpretation, equally applicable to section 35 of the Victorian statute. And they are, as it seems to their Lordships, sufficient to conclude this part of the case unless their effect can be displaced by either of two qualifying considerations to which attention was directed in the course of the arguments.

The first of these was that while the conclusion might have been inevitable had the realization been one by an individual of his own property, different considerations apply when the realization is that of a Company's property by the Company itself. This distinction is not infrequently drawn in cases upon the subject. Notable instances will be found in the judgment of Rowlatt J. in *Rand* v. *Alberni Land Company* 7 Tax Cases 629, 639, and of Warrington L. J. in *The Westleigh Estates Company's* case [1924] 1 K.B. 390, 417. The distinction, where it exists, arises of course from the fact that whereas the capacities of a natural person have no limitation so that any particular transaction need not be referred to any of them, a company is so bounded by its memorandum that it may be both permissible and essential to consider its authorised objects in connection with the actual transaction in question and even to seek for the principal purpose of its formation. But there is, in their Lordship's judgment no room in the present case for the distinction referred to not only because the business of realization, as might be suspected from its very name, is as has been said, one of the expressed purposes of the Association, but because the realization of this particular asset was a burden imposed upon it by contract, while the distribution of the proceeds resulted from a promise made on its behalf by the Commonwealth Government. If the Association had in either respect acted otherwise than it did it would have failed to fulfil the full purpose which by agreement between the two governments it was formed to achieve.

And the second qualifying consideration flowed from the suggestion that there must have been set up by the Association in connection with this realization a selling organization so extensive that it became a business from which this surplus fund now in question resulted as a trading profit. Reverting to the *Californian Copper Syndicate's* case, the fund, it is suggested, is not the result of such a realization as that envisaged in the passage from the judgment already quoted, but is an "enhanced value" within the meaning of this statement which immediately follows :—

> "But it is equally well established that enhanced values obtained from realization or conversions may be so assessable" (*i.e.*, to income tax) "where what it done is not merely a realization or change of investment but an act done in what is truly the carrying out or carrying on of a business"

—an aspect of the matter well described by Rowlatt J. in his judgment in the case of *The Alabama Company* v. *Mylam* 11 Tax Cases 232 where at p. 252, dealing with a finding there of the Special Commissioners he says :—

> "Merely realizing is not trading. It is no good saying it is a trade of realizing. But, I think, what they mean is : they have taken a process of realizing and embedded it in a trade so that in the course of carrying on a trade they have in fact done some realizing."

Now can it be said that the operations of the Association are aptly described in either of these judicial utterances ? Their

Lordships recognise that it is here that the case of the Association on this first head of claim is most vulnerable, and it is in order that its true position in this connection may not be missed that they have been at pains to emphasise the absence or omission from the special case of any reference, as a relevant factor, to the existence of any trade of the Association in which this realization could be "embedded," and to point to the irresistible inference from the statements in the case that the Association neither invented nor organized any selling organization of its own but merely accepted the machinery it found at hand. All that its British Board did was to utilize on its behalf the organization under which they had acted when, as a Committee of the Ministry of Munitions, they were engaged in the same task of realization. In other words, in their Lordships' judgment there is in the special case neither a finding, nor any statement of facts warranting the conclusion that this Association ever indulged in any activity except that of realization which, as Rowlatt J. has said, "is not a trade." Upon the facts stated, any other conclusion would be tantamount to saying that a realization such as that effected by the Association must be a trade because of the bringing into existence of a selling organization made necessary only by reason of the mere magnitude of the realization—a proposition not to be entertained. It is interesting on this part of the case to contrast the findings and the facts in the case of *Martin* v. *Lowry* [1926] 1 K.B. 550 [1927] A.C. 312, with those detailed in this judgment. It is hardly surprising that at their Lordships' Bar, the appellant, notwithstanding the actual decision there and some encouragement from the judgment of MacFarlan J. here found little in that case to assist him.

The contentions raised by the appellant on this first head of claim did not controvert their Lordships conclusions for the reason that they were conditioned by a view of the facts which the Board is quite unable to accept. They consisted, in the main, in a justification of the judgment of MacFarlan J. who, in the Supreme Court, as has been already stated, alone agreed with the Commisioner that this assessment represented under the Victorian Statute a taxable profit. The inferences which that learned Judge drew from the facts as stated in the Special Case appear from his judgment to have been, first, that the Association was formed by reason of the desire of those interested in the remaining surplus wool to entrust its realization to an organization which would carry on the undertaking of a wool-selling Company on business lines; and secondly, that if the Association was in any sense "machinery" for distribution of the Commonwealth share the machinery chosen was that of a profit earning organization with which those interested in the realization decided to make a fresh start. It was from the trading operations of that organization that the profit in question resulted. These conclusions of the learned Judge were so expressed as to justify the surmise that the facts of the case as he saw them brought it within the

principle of *Martin* v. *Lowry* (*supra*) and within the actual decision in *The Commissioner of Taxes* v. *Melbourne Trust* (*supra*). Their Lordships do not suppose that on the facts as these have been interpreted in this judgment, the learned Judge would have considered either the principle of the one case or the decision in the other to be of any relevance. The truth is that here the true conclusion flows from the view taken of the facts, and the contentions of the Commissioner, as well as the decision on this point of the learned Judge were based upon a reading of these which their Lordships cannot accept.

But while their Lordships have elaborately examined the facts of the case, and in deference to the able arguments addressed to them, have dealt at length with the above aspect of it, they might have been well content to dispose of this first head of appeal on the ground chosen by MacFarlan J. for his decision—namely, that even if this fund was a taxable profit of the Association in the sense of section 35 of the Act it was not brought into charge by reason of the fact that no part of it was earned in or derived in or from Victoria. As this answer applies also to the second head of appeal that, namely, for income tax upon the sums received by way of commission on realization by the Association of the wool belonging to the Imperial Government, the two claims may in what follows be considered together.

Now the facts with reference to this aspect of the case appear to be that no wool at all was sold by the Association in Australia. It was the British Board operating outside Victoria that regulated the quantities of wool to be marketed from time to time and entered into all contracts and made all deliveries. Every payment for wool sold was made out of Australia. Such wool as was stored in Australia at the beginning was from time to time exported upon explicit directions as to quantity and quality from the British Board, and was insured by that Board in transit. All the Australian wool had been acquired by the Imperial Government and paid for by that Government prior to the registration of the Association. The Association was incorporated in Victoria and its registered office was situate in Melbourne, probably because of the fact that Melbourne was the seat of the Central Wool Committee and also of the Commonwealth Government. Certain, in any case it is, that although the fact that the Australian Board of this Victorian Association, presided over by the chairman of the Association, held its meetings at Melbourne was the main ground for the Commissioner's contention that some part, at all events, of the profits of the Association must be taken to have been earned in or derived in or from Victoria, he was unable to point to any action of that Board that could not just as conveniently have been carried out in any other State; nor to any operation of realization for which the Australian Board was really responsible. The activities of that Board mentioned in paras. 35 *et seq.* of the Special Case do not seem to their Lordships to help in this connection, and it

is their view on the facts stated that no part of the profit-earning operations of the Association were carried out in Victoria, and no part of its so-called profits were earned in or derived in or from Victoria. And this their Lordships think was the view of all the Judges of the Supreme Court.

This branch of the case, in the view of the Board, is really covered by the decisions in *Grainger* v. *Gough* [1896] A.C. 325, and *Lovell & Christmas* v. *Commissioner of Taxes* [1908] A.C. 46. They recall the words used in the latter case at p. 51.

> " The rule is easily deducible from the decided cases. The trade or business in question in such cases ordinarily consists in making certain classes of contracts and in carrying these contracts into operation, with a view to profit, and the rule seems to be that where such contracts, forming as they do the essence of the business or trade are habitually made, there a trade or business is carried on within the meaning of the Income Tax Acts so as to render the profits liable to income tax."

It is not without interest to note in this connection that in the *Melbourne Trust* case, of which so much was sought to be made in argument, the only surpluses on realization upon which Victorian Tax was either claimed or allowed were the sum of £104,782 1s. 4d. realized from assets actually situate in Victoria, and £509 1s., representing the difference between prices paid and par for the Company's debenture stock there. See p. 1009 of the Report.

In regard, therefore, both to the first and the second heads of claim, their Lordships are in agreement with the Supreme Court.

The third head already referred to remains to be disposed of. The facts with reference to it are set forth in a supplemental case and so far as material are that on the 12th March, 1924—that is to say, before the incorporation of the Association—the Commonwealth Government allowed the Wool Combing and Spinning Company, Limited, to select for the purposes of its business and at the flat rate acquisition price certain wools acquired for the Imperial Government under the scheme of purchase already described. By the agreement the Spinning Company agreed to account to the Government over and above the flat rate price for a proportion of the profit made by it from its manipulation of the purchased wool. On the 16th April, 1920, in answer to a question in the Commonwealth Parliament, the Prime Minister stated that the Government would allow this profit when received to go to the woolgrowers, as if the wool had been part of that sold to the Imperial Government. But the profit formed no part of the assets included in the Government's contract of the 1st April, 1921, nor was it treated as any part of the assets then taken over by the Association. Nevertheless, when the amount of the profit had been adjusted and ascertained, and was found to be represented by the two sums already referred to, it was to the Association that these were paid by Government with the result that these came to be distributed with the proceeds of realization amongst the original shareholders of the Association or the transferees of their shares exclusively of all other persons. In other words, the

Association in respect of these sums truly became the medium for their distribution amongst those designated by Government to receive them. In no sense were they profits " earned " by the Association, and even more clearly, if that be possible, were they not earned by it " in or derived in or from Victoria." The appeal, therefore, with regard to this sum also fails.

Further objections taken by the Association to the assessments, all minor in character, need not be discussed or further referred to in view of the favourable conclusion reached by the Board on its main contentions.

As a last resort the Commissioner sought to justify his assessment by reference to the amendment following made to the principal Income Tax Act, 1915, by the Income Tax Acts Amendment Act, 1923.

> " 7. (1) The proceeds derived from the sale after the 13th day of June, 1922, whether on the sale of a business as a going concern or in any other manner whatsoever, of the trading stock or part of the trading stock of any business shall be assessable income derived from carrying on a business:"

and in section 5 of the same Act a comprehensive definition of " trading stock " is given.

This section was in no way referred to by the Commissioner in the Court below and Counsel for the Association objected to its being introduced into the discussion now. The objection their Lordships think was well taken. It is only under exceptional circumstances that the Board allows to be raised before it a new issue of this kind upon which it has not the benefit or assistance of the views of the learned Judges who have dealt with the case. And these exceptional circumstances do not exist here. Their Lordships accordingly do not propose to deal with the section in any way. But they must not in saying so much, be supposed to imply that if the section were examined, it would be found to assist the appellant.

Upon a consideration of the whole case Their Lordships will humbly advise His Majesty to dismiss the appeal with costs.

In the Privy Council.

THE COMMISSIONER OF TAXES

v.

THE BRITISH AUSTRALIAN WOOL REALIZATION ASSOCIATION, LIMITED (IN LIQUIDATION).

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