No. 150.—HOUSE OF LORDS, MARCH 25TH, 28TH, and 29TH, AND MAY 31ST, 1892.

GRESHAM LIFE ASSURANCE SOCIETY *v.* STYLES (Surveyor of Taxes). (1)

Income Tax.—Deduction from Profits.—Annuities.—Rule 4 of Case I., Schedule D.—A life insurance society in the course of its business sells annuities, covenanting that its capital stock, funds, and property shall be liable in respect of the payment of such annuities.

Held unanimously, reversing the decisions of the Divisional Court and Court of Appeal, *that the annuities are not payable out of the profits and gains of the Society within the meaning of Rule 4 of Case I. of Schedule D., and that the amount of the annuities paid may be taken into account as a disbursement in estimating the balance of profits in respect of which the Society is chargeable with Income Tax under the First Case of Schedule D.*

Alexandria Water Co. *v.* Musgrave (2) *distinguished.*
Mersey Loan and Discount Co. *v.* Wootton (3) *disapproved.*

This was an appeal by the Gresham Life Assurance Society against the decision of the Court of Appeal reported in Volume II. of Tax Cases at p. 633.

March 26.

Sir Horace Davey, Q.C., and *Lumley Smith, Q.C.* (*Fooks* with them) for the Society :—Rule 4 of Case I. of Schedule D. section 100, 5 & 6 Vict. cap. 35., forbids any deduction in respect of any annual interest, annuity, or other annual payment payable out of profits and gains. The case of *Alexandria Water Co.* v. *Musgrave* (2) affords a good illustration of the meaning of the Rule; the Company had issued bonds and debentures, charging the principal and interest on their whole undertaking; and it was held that they were not entitled to deduct the interest from their profits. Of course not, because the annual charge of the interest came against the income of the Company. Although the debenture holders' remedy was against the property of the Company, still in making up the trading balance sheet for the year the interest was primarily chargeable against income. But

(1) Reported L.R. (1892) A.C. 309.
(2) Vol. I., p. 521.
(3) Vol. II., p. 316.

GRESHAM LIFE ASSURANCE SOCIETY v. STYLES.

when we sell annuities, and merely pay them by way of performance of our contract to deliver our goods, these words do not apply at all, for the annuities are not payable out of our profits and gains. Otherwise you would have this fallacy—they say the more annuities you pay the more you diminish your profits and gains; but if we do no annuity business we have no profits and gains at all. It is true in a sense that if we had not so many liabilities, that is to say so many annuities to pay, so many goods to deliver, but had the same property, of course our profits would be larger. But we should not have the same property, because we only get the property by contracting to deliver these goods, or to pay these annuities.

The annuities are not payable out of our profits and gains in any intelligible sense. They are mere payments out of our funds; primarily our annuity fund, and subject to that out of our general funds. Rule 4 contemplates that you should in the first instance ascertain what your profits and gains are, but in an annuity business you cannot find out whether you have any profits until you have taken into account your annuity liabilities. Your very business consists in making profits by your receipts in respect of your annuities exceeding what you have to pay upon your annuities. The annuities are just as much a liability of the business as a coal merchant's or wine merchant's liability to deliver goods which he has contracted to sell.

Then section 102, 5 & 6 Vict. c. 35., is said to touch us. That section says that when annuities are payable out of profits and gains the whole of such profits and gains shall be charged on the person liable to such annual payments, but he may deduct a proportionate amount of duty from the annual payments. That only carries out what was provided by Rule 4 of Case I., section 100; the same question remains, are our annuities payable out of profits? Section 159 really says the same thing, only it is made applicable to all the schedules instead of being confined to Schedule D.

Section 40, 16 & 17 Vict. c. 34., is only optional. It gives the person who pays the annuity power to deduct, if he thinks fit, as against the annuitant, although the annuity may not come within the other clause and be payable out of profits. Since this case has been taken the law has been altered by section 24 51 & 52 Vict. cap. 8., which now makes obligatory that which was left optional by sec. 40, 16 & 17 Vict. cap. 35.

March 28.

Sir E. Clarke, S.G., for the Surveyor:—In *Mersey Loan and Discount Company* v. *Wootton* (1) it was held that the Company was not entitled to deduct interest allowed to depositors because such interest was payable out of its profits and gains. Under the 4th Rule of Case I. the person who is making a return of his profit is not to be allowed in stating the balance upon which he is actually himself to pay to deduct any annual interest, &c., payable out of profits and gains. To deduct from

(1) Vol. II., p. 316.

what? Why from the sums of money which he has received and the balance of which over his expenditure is the amount of the profit upon which *primâ facie* he would be chargeable.

[*Lord Herschell.*—The difficulty is this; you are to say it is payable out of the profits.]

It is payable out of the profits brought into charge.

[*Halsbury, L.C.*—What difference in your view of this Rule would it make if you were to strike out the words "payable " out of profits and gains"?]

I think the construction would be the same. But there is a very great difficulty in the construction of the Rule upon any other principle.

In *Alexandria Water Company* v. *Musgrave*, (1) the judgment was based on the fact that the payment which it was sought to deduct was payable out of profits or gains. The Master of the Rolls said, "Now out of what fund is the interest " paid by the Company? The only fund out of which they " can pay is the money they receive by way of water rents, " which is what the Company gain by their trade; it is not " the net profits, but the gains of the Company."

The statute begins by a charging section upon "profits." That word must be construed to mean what is said in the first Rule of the first Case, the balance of the profits and gains ascertained according to the Rules of the Statute.

March 29.

Danckwerts, for the Surveyor:—Case I. of Schedule D. directs that duty shall be charged on a sum not less than the full amount of the balance of the profits and gains.

Therefore the term "profits and gains" is used in Case I. in the sense of gross profits and gains and not net profits and gains. The first Rule applicable to Cases I. and II. provides that in estimating the "balance" of the profits and gains to be charged no sum shall be set against or deducted from such profits and gains for any disbursements unless they answer to a certain description. So here again the term "profits and gains" is used to designate gross profits.

Lumley Smith, Q.C., in reply:—The contention against us is based upon the assumption that profits and gains really mean gross receipts. If a horse-dealer buys a horse for 80*l.*, and sells him for 100*l.*, his gross receipts would be 100*l.*, but his profits would be only 20*l.*

The Crown gives no meaning to the words "payable out of " profits and gains." We say that means an annuity charged on the profits and gains."

Cur. adv. vult.

JUDGMENT.

Halsbury, L.C.—My Lords, The commercial concern in respect of which the question arises here consists of a business which is

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(1) Vol. I., p. 521.

GRESHAM LIFE ASSURANCE SOCIETY v. STYLES.

carried on by receiving a sum of money as the purchase money for the granting of annual sums. The sum so granted is certainly an annuity and an annual payment, and I believe it is the fortuitous use of those words under circumstances that I shall presently discuss which has given rise to what seems to me an erroneous construction of the Statute.

The question arises under the Income Tax Acts, and the Act itself, like all the Acts of the same class, purports to be "An "Act for granting to Her Majesty duties on profits arising from property, profession, trades, and offices."

Now I leave out for the moment the question of land, and the object being to tax profits, certain Rules have been inserted in the Statute which have become and are made in truth parts of the Act itself. But the Rules are as they themselves import, Rules for ascertaining the duties. "The amount of the profits "and gains" was the expression all through the earlier legislation on the subject down to the Act of 1805. In that year the expression was altered, as is pointed out by Mr. Dowell in his valuable book on the Income Tax Acts, page 114, and the observation appears to be well founded that the alteration of the language pointed rather to a more careful return or statement of income, an account in a debtor and creditor form, and intended to prevent deductions, which possibly had been up to that time claimed, being permitted to reduce the amount of the profit which the debtor and creditor account ought to show. But except as indicating the form rather than the substance of what should be shown in the return as the balance of profits and gains, I am in the condition of Lord Blackburn who said, in the case of the *Coltness Iron Company* v. *Black*, that he had been unable to discover any difference in the meaning of the two phrases.

Now, if I understood the contention before your Lordships aright, it rested on the fourth Rule relating to assessment under Schedule D., which prohibited any deduction being made on account of any annual interest, or any annuity, or any other annual payment, and as those sums were annuities or annual payments, it was said that they were not to be deducted in estimating the amount of the profits and gains arising as aforesaid.

And if the Rule had stopped at the point up to which I have quoted it, I should have concurred with the contention of the surveyor. But the Rule does not stop there. In order to be a prohibited reduction, it must be sought to be made on an annuity or other annual payment payable "out of such profits "or gains."

Now to my mind it is very clear what is the *intuitus* both of the Enactment and of the Rules under which the duties are to be ascertained. The thing to be taxed is the amount of profits and gains. The word "profits" I think is to be understood in its natural and proper sense—in a sense which no commercial man would misunderstand. But when once an individual or a company has in that proper sense ascertained what are the

profits of his business or his trade, the destination of those profits, or the charge which has been made on those profits by previous agreement or otherwise is perfectly immaterial.

The tax is payable upon the profits realised, and the meaning to my mind is rendered plain by the words "payable *out* of profits."

It would be an extraordinary thing to suggest that where a business consists of granting annuities it is to be taxed upon a different principle from any other commercial concern, and no one I suppose could doubt that in any other commercial concern, the cost of the thing sold to the trader is one of the expenses incident to the carrying on of the trade.

If an annuity seller is to be treated differently from a seller of any ordinary article of commerce, coals or corn, or the like, one would have expected to find some words in the Statute rendering him obnoxious to a different system of taxation, and enforcing a different mode of ascertaining profits, whereas it seems to me that the application of the general words "profits and gains," or "balance of profits and gains," are equally applicable whatever the commercial concern carried on may be.

I think one gets a very fair notion of what was in the mind of the Legislature by a variety of cases put in the course of the argument which it is not necessary to repeat here.

The Court of Appeal seems to have been impressed by the decision in the *Alexandria Water Company Limited* v. *Musgrave*. (1). With the decision in that case I am not disposed to disagree, though I am not quite certain I am able to adopt the reasoning, which to some extent appears to depend upon a distinction between the words "gains" and "profits," a distinction which I cannot assent to; but upon the facts I think I should have come to the same conclusion, since, to put it very plainly, in that case it was a claim to deduct the company's debts for borrowed capital and diminish the amount of the profits of the trading.

The whole point seems to me to depend upon the words "out of profits and gains." Profits and gains must be ascertained on ordinary principles of commercial trading, and I cannot think that the framers of the Act could be guilty of such confusion of thought as to assume that the cost of the article sold to the trader, which he in turn makes his profit by selling, was not to be taken into account before you arrived at what was intended to be the taxable profit.

As I have said the confusion has arisen from the use of the words "annuity or annual sums payable" without considering that this particular commercial adventure consists in selling annuities, and that which they pay therefore is to them the cost of the article supplied.

You can no more refuse to take that cost into your consideration when ascertaining the balance of profits and gains than

(1) Vol. I., p. 521.

GRESHAM LIFE ASSURANCE SOCIETY v. STYLES.

you could the cost of the coals or the corn to the coal merchant and to the corn merchant in ascertaining what are the profits from his trade.

I am therefore of opinion that the judgment appealed from ought to be reversed.

Lord Watson.—My Lords, the business carried on by the Appellant Society is that of life insurance; and one branch of it consists in the sale of annuities to the public. The consideration for an immediate annuity is a lump sum instantly paid, and for a deferred or contingent annuity may either be a lump sum or a series of periodical payments. The question raised for decision in this appeal relates to an assessment under Schedule D. in respect of the annual profits and gains arising from the Appella nt's businessfor the fiscal year ending 5th April 1886.

In accordance with the provisions of section 100, Case First, Rule 1, of the Act of 1842, (5 & 6 Vict. cap. 35.), the amount upon which the Appellants became liable to pay Income Tax for the year in question was one-third of the assessable profits or gains which had accrued to them during the three years immediately preceding the 30th June 1885, the date at which their books were last balanced. The Appellants had, in the course of these three years, paid upwards of 250,000*l.* in discharge of their contract obligations to their annuitants. The Respondent, in estimating the triennial average, included all these payments in the balance of assessable profits or gains, disregarding the contention of the Appellants that they ought to be treated as items of debit for the purpose of ascertaining the balance. On appeal the Commissioners for general purposes of the Income Tax Acts for the City of London confirmed the assessment, and stated a special case in terms of 43 & 44 Vict. cap. 19. s. 59. The decision of the Commissioners has been upheld by a Divisional Bench as well as by the Court of Appeal.

Rule 1 of section 100, Case First, prescribes that the duty to be charged shall be computed on a sum not less than " the full " amount of the balance of the profits or gains of such trade, " manufacture, adventure, or concern." It plainly contemplates the preparation of a balance sheet in which proper trading disbursements and liabilities are to be set against trade assets, so that the surplus of the latter, if any, will represent the assessable profits or gains of the concern. All the other rules applicable to Schedule D. are framed upon the same footing. Rule 3 of Case First specifies various items which a trader might naturally enough, for his own private purposes, insert on the debit side of the sheet; and enacts that these shall not be allowed as deductions in estimating his profits for the purposes of the Income Tax. Rule 4 of Case First provides that " in estimating the " amount of the profits and gains arising as aforesaid no deduc- " tion shall be made on account of any annual interest or any " annuity or other annual payment payable out of such profits " or gains."

The first of the rules applicable to Cases 1 and 2 of section 100 provides that, in estimating the balance of the profits or gains to be charged according to either case, no sum shall be set against or deducted from such profits or gains for "any disburse-"ments or expenses whatever, not being money wholly and "exclusively laid out or expended for the purposes of such "trade, manufacture, adventure, or concern." It seems tolerably clear, and it was hardly disputed by the Respondent, that all payments made by the Appellants on account of the annuities which they have contracted to pay are, in the strictest sense of the words, disbursements, made wholly and exclusively for the purposes of their business. The Appellants trade in annuities, and these disbursements are the consideration or part of the consideration which they are bound to give in return for the annuitants' purchase money already received by them, and carried to their credit in the balance sheet. Unless the statute forbids it, the Appellants must have the same right to deduct such payments, in estimating their assessable profits, as a grocer has to deduct the price paid by him for the tea or sugar which he retails. If there be one point free from obscurity in the Act of 1842 it is this, that the Legislature intended all traders, whether in groceries, annuities, or other articles of commerce, to be assessed upon the same footing.

The learned Counsel for the Respondent were constrained to admit that, were it not for the terms of Rule 4 of Case First, the Appellants would be entitled to the deductions which they claim. But they argued that the expression "profits and gains," which occurs twice in that rule, in each instance signifies the gross receipts of the trader, or, in other words, the whole item standing on the credit side of the balance sheet. Upon that construction of the rule, no deduction could be allowed, in estimating profits, of "any annual interest, or any annuity or annual payment;" and one of many startling results would be that the yearly rent and taxes paid by a trader for his business premises, and yearly wages paid to his servants, would not be dealt with as payments out of trading capital, but would be included in the profits upon which he pays income duty.

Although it appears to have been accepted by both courts below, I cannot assent to the construction put upon Rule 4 by the Respondent, which is, in my opinion, at variance with its context. The rule begins thus: "In estimating the amount of "the profits and gains arising as aforesaid." Does that mean "in estimating the amount of the trader's assets?" I venture to think not. I think the words refer, not to total assets, but to the balance of profits and gains to be ascertained by virtue of the preceding rules, for the purpose of being charged with income duty. The Rule then goes on to prescribe that there shall be no deduction made on account of any annual interest, or any annuity or other annual payment, "payable out of "such profits or gains." These last words refer back to profits and gains as described in the commencement of the Rule, and

GRESHAM LIFE ASSURANCE SOCIETY v. STYLES.

must therefore be taken to mean, not gross receipts, but profits and gains, the amount of which is to be estimated for the purposes of the Act. Had it been the intention of the Legislature to enact that no annual interest, annuity, or other annual payment should be inserted on the debit side of the balance sheet it appears to me that Rule 4 would have been expressed in very different terms. The Rule, as it stands, merely enacts that no annual payment, which falls to be paid out of profits, shall be deducted from profits in assessing for income tax.

The Respondent relied in argument upon section 102, which directly charges with duty all annuities, yearly interest of money, or other annual payments, whether such payments shall be payable within or out of Great Britain. That enactment is qualified by the proviso that no charge shall be made upon the person entitled to such payments in the case where the same shall be "payable out of profits or gains brought into charge by this Act." In that case the trader must pay upon the whole profits or gains brought into charge, but is authorised to deduct income tax in settling with the person entitled. These provisions do not appear to me to throw any light upon the question, because, in order to ascertain what profits or gains are brought into charge by the Act, it is necessary to go back to the rules of Case First of section 100.

Section 40 of the Act of 1853 (16th and 17th Victoria chapter 34), which was also referred to in the course of the arguments, has really no bearing upon the present question. It empowers persons who are liable to the payment of any rent, or any yearly interest of money, or any annuity or other annual payment, on making such payment, to deduct and retain thereout the amount of the rate of income duty payable at the time; but it has no application to annual payments, payable out of profits or gains. Section 24 (3) of the Customs and Inland Revenue Act, 1888, for the first time made it compulsory upon the persons liable in payment to retain Income Tax, upon their making payment out of the capital which they employ in trade, of any interest of money or annuities charged with the tax under Schedule D., and not payable or wholly payable out of profits brought into charge to such tax. Had that enactment been in force in the year 1885–6, the present controversy would never have arisen.

The only point which remains for consideration is this, whether the annuities paid by the Appellants are payable, within the meaning of Rule 4 out of profits and gains? In order to bring annuities or other annual payments within the scope of the rule, they must, in my opinion, either be directly charged upon profits, or be in themselves of such a character that they form a proper charge upon profits. Now I cannot understand in what sense the annuities in question can be said to be properly chargeable to profits. An annuity to the widow of a deceased partner, interest on capital advanced by a partner, or upon money borrowed for the purposes of the business, are

truly payable out of profits earned, and therefore ought not to be deducted in estimating the income yielded by the business. On that ground I agree with the decision of the Court of Appeal in *The Alexandria Water Company* v. *Musgrave,* (1) although I am unable to concur in all the reasons which were assigned for it. But the business of the Appellants consists in employing their trading capital to pay annuities, as the counterpart of the consideration given by the annuitant, and the annuities are payable out of stock and not out of business profits.

On these grounds I concur in the Judgment which has been moved by the Lord Chancellor.

Lord Herschell.—My Lords, the Appellant Society, as part of the business which it carries on, sells or grants annuities in consideration of a premium or lump sum paid down in the case of an immediate annuity, and of a similar payment or of periodical premiums in the case of a deferred or contingent annuity. In making up the balance sheet showing the amount of its profits and gains for three years the society put on the one side of the account the consideration money received for annuities granted; on the other side was put the sum paid in discharge of its annuity contracts. The Surveyor of Taxes contended that the latter sum ought not to have entered into the account for the purpose of ascertaining the profits and gains on which Income Tax was to be assessed under Schedule D. of the Income Tax Acts.

This contention was based upon the fourth rule, relating to assessment under Schedule D., which is in the following terms: "In estimating the amount of the profits and gains arising as "aforesaid no deduction shall be made on account of any annual "interest, or any annuity or other annual payment, payable out "of such profits and gains." It was said that this expressly prohibited any deduction in respect of the annuities paid by the society; that the income tax must be paid upon the basis that the entire sum received by the society as the consideration for its undertaking to pay annuities was to be assessed as profits and gains; and that the society would have a right to deduct income tax when paying the annuities to those who had purchased them. The contention of the Surveyor of Taxes has been sustained by the Divisional Court and the Court of Appeal. The learned Judges in the Court of Appeal founded their judgment mainly upon a prior decision of that Court in the case of *The Alexandria Waterworks Company* v. *Musgrave,* (1) which I shall have to consider presently.

It cannot, of course, be denied that, as a matter of business, profits are ascertained by setting against the income earned the cost of earning it, nor that as a general rule, for the purpose of assessment to the income tax, profits are to be ascertained in the same way. "Money wholly and exclusively laid out or "expended for the purpose of a trade, manufacture, adventure,

(1) Vol. I., p. 521.

" or concern " may, by the first of the " rules applying to both " the preceding cases," be taken into account in estimating the balance of profits and gains to be charged. It seems to me beyond question that the payments made by the society to its annuitants are within these words. And those carrying on the business of selling annuities would be assessed on quite a different principle to those carrying on other businesses if their gross receipts were to be treated as profits without regard to the payments to which, in consideration of those receipts, they had bound themselves.

But it is said, and truly, that the Income Tax Acts have laid down certain rules to be applied in determining how the tax is to be assessed, and that, even if the result should be to tax as profits and gains what cannot properly be so called, the requirements of the Acts must nevertheless be complied with. The controversy mainly turns upon the construction to be put upon the fourth rule, which I have already quoted, but the 102nd section of the Act must be read in connexion with it. That section, after enacting that Income Tax shall be charged upon all annuities, yearly interest of money, or other annual payment, provides that, "in every case where the same shall be " payable out of profits or gains brought into charge by virtue " of this Act no assessment shall be made upon the person " entitled to such annuity, interest, or other annual payment, " but the whole of such profits or gains shall be charged with " duty on the person liable to such annual payment without " distinguishing such annual payment, and the person so liable " to make such annual payment out of the profits or gains " charged with duty" shall be entitled to deduct the Income Tax from the annual payment, and the person to whom the payment is made is to allow such deduction.

It was admitted that, reading this enactment in conjunction with the fourth rule, the prohibition contained in that rule only applied when the annuity was payable out of profits and gains brought into charge by virtue of the Act. What is the meaning of " profits and gains " as found in the concluding words of the fourth rule ? Unless the context requires a different meaning, or the words appear to be used throughout the Act in another sense, I think they must be construed according to their ordinary signification. When we speak of the profits and gains of a trader we mean that which he has made by his trading. Whether there be such a thing as profit or gain can only be ascertained by setting against the receipts the expenditure or obligations to which they have given rise.

In the taxing provision of the Income Tax Acts the tax is imposed in respect of the annual profits or gains arising or accruing to any person from any trade, " to be charged for every " twenty shillings of the annual amount of such profits or " gains." Here, it cannot be doubted, I think, the words " profits or gains " are used in the sense I have indicated. There is nothing in any part of the Act to show the contrary.

Indeed when the rules are considered they confirm the view that this meaning is to be attributed to the words. Their general purpose is to prohibit certain matters being taken into account which ought not to be set against the receipts when profits are being ascertained. But the scheme of the Act obviously is to tax, not receipts, but profits properly so called.

The 100th section prescribes that the duties under Schedule D. shall be assessed and charged under certain rules. The first of these is, that the duty shall be computed on a sum not less than the full amount of the balance of the profits or gains of the trade, &c., upon a fair and just average of three years. The expression "balance of the profits or gains" is not a happy one, but the meaning obviously is the balance arrived at by setting against the receipts the expenditure necessary to earn them.

When we come to the third rule, and the first of the rules "applying to both the preceding cases," it must be admitted that the words "profits or gains" are not always used in their proper or ordinary sense. The third rule, for example, provides that, in estimating the balance of profits and gains chargeable under Schedule D., "no sum shall be set against or deducted "from, or allowed to be set against or deducted from, such "profits or gains," on account of any sum expended for the repairs of trade premises, or for the supply, repairs, or alterations of trade implements beyond the sum usually expended for such purposes on an average of three years. Here it is obvious that the "profits or gains" against which the cost of repairs is not to be set, or from which it is not to be deducted, cannot be the profits or gains of the business properly so called. The subject matter necessitates the conclusion that language is being employed loosely and inaccurately. The rule contemplates the making up of a balance sheet and deals with what may be put on the debit side of it. And the first rule "applying to both the preceding cases," which commences with the same words as the rule I have just referred to, evidently requires a similar construction.

But in the fourth rule, which your Lordships have specially to construe, the language employed is very different. I can find nothing to show that the words "profits and gains" were intended to be understood otherwise than in their proper sense. The rule prescribes that in estimating the amount of the profits and gains "arising as aforesaid," no deduction shall be made, &c. This seems to refer back to the charging provision which I have quoted, and I have already pointed out the meaning which must be there attributed to "profits and gains." And when read in connexion with section 102 the rule clearly relates only to annuities payable out of profits and gains "brought into charge," by virtue of the Act, and to cases in which the trader is liable to make the annual payment out of the profits or gains charged with duty.

I have pointed out that in the charging provision it is the profits and gains properly so called, not the gross receipts, which

GRESHAM LIFE ASSURANCE SOCIETY v. STYLES.

are brought into charge. If these do not exceed the expenses nothing is payable by way of income tax. In the fourth rule there is no mention of a balance, nor is it said, as in the other rules, that no sum shall be set against the profits "on account of "any sum expended" in the payment of annuities. I can see no reason why, if the intention was that contended for by the Crown, these words should not have been inserted in the third rule, instead of a fourth rule, with altered language, being added. The expression in this rule is altogether changed; the deduction prohibited is confined to annuities "payable out of" the profits and gains. This implies that the profits and gains out of which the annuity is payable are already ascertained. In the other rule there is no reference to the fund out of which the moneys expended are payable; the only thing regarded is the fact of the expenditure and the purpose for which it has been incurred. It would be a strange use of language to speak of the annuities as "payable out of" the gross receipts of a trader merely because he is under liability to provide for them.

I think the fourth rule was primarily designed to meet such a case as that in which a trader had contracted to make an annual payment out of his profits; as, for example, when he had agreed to make such a payment to a former partner or to a person who had made a loan on the terms of receiving such payment. But for the rule it might plausibly have been contended that in such a case a trader was only to return as his profits what remained after making such payment. It is unnecessary to define the limits within which the rule applies, but I am unable to agree with the Court below that it is applicable to the present case. The annuities are not, in my opinion, payable out of the profits and gains of the Society; until the payments which they necessitate have been taken into account it cannot be ascertained whether there are any profits and gains or not.

I do not think this view conflicts with the decision in the case of the *Alexandria Waterworks* v. *Musgrave*. The payments of interest to the debenture holders were made out of the profits. These were ascertained by deducting from the moneys earned the expenses incurred in earning them, and of these expenses the payments to the debenture holders formed no part. A portion of the capital was raised by shares, and another portion by debentures. There was no more reason why interest on the debenture capital should be deducted from the profits than interest on the share capital. Supposing the whole capital had been raised by shares there would have been no pretence for making any such deduction, and the profits earned by the adventure could not be different, according as the capital was raised wholly by shares, or partly by shares and partly by debentures. It is by no means clear that the case was not within the prohibition of the third rule.

Although it does not appear to me that the view of the present case which I have placed before your Lordships is

inconsistent with the decision in the *Alexandria Waterworks Company* v. *Musgrave*, I think it is in conflict with the *Mersey Loan Company* v. *Wootton*, (1) but the reasoning which has led me to my present conclusion applies equally to the facts of that case.

Lord Field.—My Lords, I have been asked by my noble and learned friend, Lord Morris, to express his entire concurrence in the Judgment which has been moved, and I have no difficulty whatever in adding my own.

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(1) Vol. II., p. 316.