No. 541.—High Court of Justice (King's Bench Division).—24th and 25th June, 1924.

Court of Appeal.—6th and 7th November, 1924.

House of Lords.—22nd, 23rd and 26th October and 11th December, 1925.

Atherton (H.M. Inspector of Taxes) *v.* British Insulated and Helsby Cables, Limited.[1]

Income Tax, Schedule D—Profits of trade—Deduction—Income Tax Act, 1842 (5 & 6 *Vict.*, *c.* 35), *Section* 100, *Schedule D*, *Case* I, *Rule* 3, *and Cases* I *and* II, *Rule* 1, *and Section* 159.

The Respondent Company claimed as a deduction in computing its profits for Income Tax purposes a lump sum of £31,784 *which it had contributed irrevocably as the nucleus of a Pension Fund established by trust deed for the benefit of its clerical and*

[1] Reported K.B.D. and C.A., [1925] 1 K.B. 421, and H.L., [1926] A.C. 205.

technical salaried staff, that being the sum actuarially ascertained to be necessary to enable past years of service of the then existing staff to rank for pension.

Held (*Lords Carson and Blanesburgh dissenting*), *that the sum in question was not an admissible deduction in arriving at the Company's profits for Income Tax purposes.*

CASE

Stated under the Taxes Management Act, 1880, Section 59, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the King's Bench Division of the High Court of Justice.

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1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on the 24th February, 1922, for the purpose of hearing appeals, British Insulated and Helsby Cables, Ltd. (hereinafter called " the Company ") appealed against an assessment to Income Tax in the sum of £250,000 for the year ending 5th April, 1918, made upon it under the Income Tax Acts, in respect of the profits of its business.

2. The sole question which was before us on the appeal, and on which the opinion of the Court is sought, is whether a contribution of £31,784 made by the Company in the circumstances detailed below to a Pension Fund established for the benefit of its clerical and technical salaried staff is an admissible deduction in computing its profits for the purpose of assessment to Income Tax for the year in question.

3. The Company carries on business as manufacturers of insulated cables. Its issued capital at 31st December, 1916, consisted of 500,000 £1 Ordinary Shares and 500,000 £1 Preference Shares, and in addition it had issued £750,000 Debenture Stock. The profits of the Company for the 5 years to the 31st December, 1920, as shown on the respective balance sheets, have been approximately as follows :—

	£
For the year to the 31st December, 1916 ...	306,000
,, ,, ,, 1917 ...	363,000
,, ,, ,, 1918 ...	288,000
,, ,, ,, 1919 ...	328,000
,, ,, ,, 1920 ...	340,000

4. In addition to its wages staff the Company had a clerical and technical salaried staff of about 500, of whom approximately 300 were eligible to participate in the Fund. Prior to the year 1916 the Company had not paid pensions to employees retiring on account of old age. It found, however, that it frequently lost

experienced members of its salaried staff, who left to take up appointments elsewhere and that the absence of a regular system of pensions was injurious to its business in other respects. It was therefore decided to establish under the powers given to the Company by its Memorandum of Association a Pension Fund for its clerical and technical salaried staff, in the hope that the benefits to be derived from the Fund would induce the members of its staff to remain in its service, and otherwise increase the efficiency of the Company's staff.

5. A Pension Fund was accordingly constituted by a Trust Deed, dated 8th August, 1916, a copy of which marked "A" is annexed and may be referred to for the purpose of this Case. The Deed contains the following provisions, *inter alia* :—

Contributions by the Staff.—Each member of the existing staff who elected to join the Fund undertook to contribute 5 per cent. of his salary to the Fund as from 31st March, 1916. The older members of the staff were not called upon to pay any higher rate of contribution on account of their age.

Persons joining the staff after the commencement of the Fund were also to contribute at the rate of 5 per cent. of their salary, if not above the age of 40 at the time of joining the Fund. If above the age of 40, the rate of contribution was increased according to the age at the time of joining.

Contribution by the Company.—The Company undertook to contribute to the Fund an amount equivalent to one-half of the contributions of the members. In addition it undertook to pay the sum of £31,784 (the item giving rise to the appeal in this case) to form the nucleus of the Fund, and to provide the capital sum necessary in order that past years of service of the then existing staff should rank for pension. A copy of the report, marked "B", of the Actuary consulted by the Company showing how the sum of £31,784 is arrived at is annexed, and may be referred to for the purpose of this Case. The Company also undertook to make up the income from the invested funds to a net income equal to the rate of 4 per cent. per annum free of tax on the amount of the accumulated funds.

Investment of Pension Fund.—All money in the hands of the Trustees and the income thereof not for the time being required for making of the payments specified in the said Trust Deed were to be invested upon such securities and in such manner as the Trustees should think fit.

Benefits and Application of Fund.—The benefits take the form (*a*) in the event of retirement at the age of 65 and in certain other circumstances, of a pension depending on the length of service, and (*b*) in other cases, of a return of the member's contributions with interest.

The Trustees of the Fund have power to apply the income and also as far as necessary the capital of the Fund in payment of the benefits provided.

Appointment of Trustees.—Two of the Trustees of the Fund are appointed by the Directors of the Company while the three other Trustees (called " Staff Trustees ") must be contributing members of the Fund and are appointed by the remaining or continuing Staff Trustees. The majority therefore of the Trustees, with whom the administration of the Fund rests, are representatives of the members of the Fund, and the actual management of the Fund is left to the Staff Trustees, the Directors' Trustees advising only with regard to investments.

Disposition of Fund on Winding-up.—In the event of the winding-up of the Fund the whole of the amount is to be divided among the Members, and the Company will not recover any part of the contributions which it has paid.

6. On behalf of the Company it was contended :—

(1) That the payment of pensions by the Company to its employees is an ordinary business expense and a continuous business demand.

(2) That in determining the admissibility of the deduction it is immaterial whether payment of a pension is made to the pensioner as it falls due, or whether a payment is made in a lump sum to relieve the employer of a future liability on a pension already payable as in the case of *Hancock* v. *General Reversionary and Investment Co., Ltd.*(1), [1919] 1 K.B. 25, or whether payment is made irrevocably by the employer to Trustees to meet the liability for pensions which will only commence at a future date.

(3) That the Company parted with the sum of £31,784 irrevocably and this sum was not represented by any asset of the Company, and

(4) That this sum should be allowed as a deduction in computing the Company's profits for the purpose of Income Tax.

The following cases were also referred to :—

Usher's Wiltshire Brewery v. *Bruce*(2), [1915] A.C. 433.
Smith v. *Incorporated Council of Law Reporting*(3), [1914] 3 K.B. 674.
Ounsworth v. *Vickers*(4), [1915] 3 K.B. 267.

7. On behalf of the Crown it was contended (*inter alia*) :—

(1) That the sum of £31,784 was not money wholly and exclusively laid out for the purposes of the trade under

(1) 7 T.C. 358. (2) 6 T.C. 399. (3) 6 T.C. 477. (4) 6 T.C. 671.

Rule (3) (*a*) of the Rules applicable to Cases I and II of Schedule D(1) and therefore was not an admissible deduction from the profits for the purposes of Income Tax.

(2) That the said sum was capital withdrawn from the trade and therefore not deductible from profits under Rule 3 (*f*) of the Rules applicable to Cases I and II of Schedule D(1).

8. Having taken time to consider our determination we held that in view of the decision in the case of *General Reversionary and Investment Co., Ltd.* v. *Hancock*(2) the contribution of £31,784 was an admissible deduction in computing the profits of the Company for the purposes of the Income Tax Acts, and the figures having been agreed between the parties we reduced the assessment to the sum of £275,736, less £33,210 wear and tear allowance.

9. The Appellant immediately upon the determination of the appeal declared to us his dissatisfaction therewith as being erroneous in point of law and in due course required us to state a Case for the opinion of the High Court pursuant to the Taxes Management Act, 1880, Section 59, which Case we have stated and do sign accordingly.

J. JACOB,
H. M. SANDERS,

Commissioners for the Special Purposes of the Income Tax Acts.

York House,
23, Kingsway, London, W.C.2.
9th April, 1924.

Stamp 10*s*.

"A"

TRUST DEED OF 8TH AUGUST, 1916.

THIS INDENTURE made the Eighth day of August One thousand nine hundred and sixteen between BRITISH INSULATED AND HELSBY CABLES LIMITED whose Registered Office is situate at Prescot in the County of Lancaster (hereinafter called "the Company") of the first part SIR JOHN SUTHERLAND HARMOOD BANNER Knight Member of Parliament of 24 North John Street Liverpool in the County of Lancaster and JAMES TAYLOR Justice

(1) The references are to the Income Tax Act, 1918. (2) 7 T.C. 358.

of the Peace of " Heathercliffe " Helsby in the County of Chester of the second part and DANIEL SINCLAIR of " The Grange " Huyton in the County of Lancaster JOHN BROTHERTON of " Elm Cottage " Helsby in the County of Chester and WILLIAM KERFOOT of " Prescot Hall " Prescot in the County of Lancaster of the third part.

WHEREAS it has been determined to create an insurance and pension fund for the benefit of persons now or hereafter employed on the permanent staff of the Company (hereinafter referred to as " Staff Employees ") and the Company are willing to contribute to the said fund in manner hereinafter expressed AND WHEREAS the parties hereto of the second and third parts have consented to act as Trustees of the said fund and of these presents NOW IT IS HEREBY AGREED as follows :—

1. CONTRIBUTIONS BY THE STAFF.

(*a*) The Company shall obtain from each of its present staff employees receiving a salary of £100 per annum and upwards who may elect within 3 months from the date hereof to join the said fund and from each of its present staff employees whose salary was on the 31st of March 1916 less than £100 per annum but whose salary has since been raised to £100 per annum or upwards who may elect to join the said fund within three months from the date hereof or in the case of any present staff employee whose salary may be hereafter raised to £100 per annum or upwards as aforesaid before he has attained the age of 40 years who may elect to join the said fund from the date on which his salary is so raised an authority to deduct and pay to the parties hereto of the second and third parts or other the Trustees or Trustee for the time being of these presents (hereinafter called " the Trustees ") an amount equivalent to 5 per cent. of every sum payable to such employee by way of salary but not including payments for staff bonus overtime or other special payments.

(*b*) Every staff employee who elects to join the said fund and who was on the 31st of March 1916 in receipt of a salary of £100 per annum or upwards shall forthwith pay to the Trustees an amount equivalent to 5 per cent. of all sums paid to such employee between the 31st of March 1916 and the day on which he may give the authority hereinbefore mentioned by way of salary but not including payments for staff bonus overtime or other special payments and every other staff employee whose salary may hereafter be raised to £100 per annum or more before reaching the age of 40 years who elects to join the said fund shall in like manner pay to the Trustees an amount equivalent to 5 per cent. of all sums paid to him by way of salary but not including payments for staff bonus overtime or other special payments from the date on which his salary may be raised to £100 per annum or upwards to the day on which he may give the authority hereinbefore mentioned.

(*c*) The Company will make it one of the terms of employment of every person engaged on the permanent staff after the date hereof (except in the case of persons above the age of 40 years and excepting persons who fail to pass the medical examination to the satisfaction of the Trustees) that if his salary shall then amount to £100 per annum then as from the commencement of his engagement (or if his salary shall upon his engagement be less than but shall afterwards be raised to £100 per annum before he has attained the age of 40 years then as from his salary being so raised) there shall be deducted by the Company from every payment on account of salary (but not including payments for staff bonus overtime or other special payments) and paid to the Trustees the equivalent of 5 per cent. thereof.

(*d*) The Company shall make it a condition of increasing the salary of an existing staff employee who has joined the said fund that a sum equal to 5 per cent. of all payments on account of his salary as so increased shall be deducted by the Company and paid to the Trustees.

(*e*) No deduction shall be made from any staff employee's salary after he has attained the age of 65 years.

(*f*) All sums which the Company may be authorised to deduct as aforesaid shall be duly deducted and paid over to the Trustees monthly in the first week of each month.

(*g*) Any employee who after the date hereof and after attaining the age of 40 years joins the permanent staff of the Company at a salary of £100 per annum or more or any staff employee whose salary may hereafter be raised to £100 per annum after attaining the age of 40 years may at the discretion of the Trustees be given the option of joining the fund and the contributions to the fund of any such employee shall be according to the following rates :—

Age over	40	years but not exceeding			41	years	$5\frac{1}{4}$	per cent.
,,	41	,,	,,	,,	42	,,	$5\frac{1}{2}$	,,
,,	42	,,	,,	,,	43	,,	$5\frac{3}{4}$	,,
,,	43	,,	,,	,,	44	,,	6	,,
,,	44	,,	,,	,,	45	,,	$6\frac{1}{4}$	,,
,,	45	,,	,,	,,	46	,,	$6\frac{1}{2}$	,,
,,	46	,,	,,	,,	47	,,	$6\frac{3}{4}$	,,
,,	47	,,	,,	,,	48	,,	7	,,
,,	48	,,	,,	,,	49	,,	$7\frac{1}{4}$	,,
,,	49	,,	,,	,,	50	,,	$7\frac{1}{2}$	,,

(*h*) Any staff employee who is a subscriber to the fund shall not be permitted to withdraw and shall continue to contribute to the fund so long as he remains on the permanent staff of the Company at a salary of £100 per annum or over except as provided in Clause 1 (*e*) hereof.

2. MEDICAL EXAMINATION.

All employees joining the permanent staff of the Company after the 31st March 1916 and any present staff employee whose salary may hereafter be increased to £100 per annum shall be required to pass a medical examination to the satisfaction of the Trustees before being admitted as subscribers to the fund.

3. CONTRIBUTIONS BY THE COMPANY.

The Company shall in addition to the sums to be deducted and paid over as aforesaid make out of its own money the following payments to the Trustees :—

(*a*) The Company shall pay to the Trustees at a date to be hereafter agreed upon the sum of £31,784 to form the nucleus of the fund and in order to provide the capital sum necessary in order that past years of service of the present permanent staff since they received a salary of £100 per annum or more shall rank for pension. Until the date the said sum of £31,784 is paid over to the Trustees the Company shall pay the Trustees as from the 1st January 1916 a subscription to the fund at the rate of £1,300 per annum free of deduction for Income Tax.

(*b*) The Company shall in the first week of every month commencing with the month of May 1916 pay to the Trustees an amount equivalent to one half of the aggregate of the sums deducted from salaries during the month then last past.

(*c*) If in any year ending the 31st December the funds in the hands of the Trustees under the Trusts hereof have not as a whole produced a net income equal to the rate of 4 per cent. per annum free of income tax on the mean of the accumulated funds of the Trust at the beginning and end of the year then the difference between the interest produced and 4 per cent. free of income tax shall be made good by the Company.

4. INVESTMENT OF PENSION FUND.

The Trustees shall from time to time invest all money in their hands and the income thereof not for the time being required for making any payments hereunder in or upon such securities and in such manner as they think fit including securities to bearer and securities transferable by mere delivery and the purchase of or lending upon the security of the shares or obligations of the Company or any other Joint Stock Company. All registered investments shall be made in the names of at least three of the Trustees or in the name of a Bank or Trust Company approved by the Trustees. In the case of investments in securities to bearer or transferable by mere delivery such securities shall be deposited in a Bank approved by the Trustees for safe custody in the names of at least three Trustees.

5. BENEFITS.

The Trustees shall stand possessed of the monies coming into their hands for the purposes of these presents and of the investments representing the same and the income thereof (hereinafter called " the fund ") upon trust out of the income thereof and so far as necessary out of capital to pay the pensions allowances and other sums hereinafter mentioned to the staff employees of the Company who have joined the fund and their legal personal representatives respectively that is to say :—

(*a*) To every staff employee who having attained the age of 65 years while in the service of the Company shall retire or be retired otherwise than on account of conduct entitling the Company to dismiss him without notice a life pension at the rate per annum to which he shall be entitled calculated on the basis of one-sixtieth of the average salary from the date the said employee received a salary at the rate of £100 per annum or over multiplied by the number of years' service during which the said average salary was paid excluding years of service if any after the age of 65 years to commence from the date of his leaving such service.

(*b*) To every staff employee who after 20 years' service or upwards ranking for pension shall before attaining the age of 65 years and while in the Company's service become totally incapacitated for work solely by reason of permanent breakdown of health blindness paralysis or lunacy not in the opinion of the Trustees occasioned by his own fault or misconduct a life pension at the rate per annum to which he shall be entitled calculated on the basis of one-sixtieth of the average salary from the date the said employee received a salary at the rate of £100 per annum or over multiplied by the number of years' service during which the said average salary was paid. The decision of the Trustees as to whether a staff employee is or is not obliged to retire from total incapacity under this Clause shall be final and any staff employee alleging that he is obliged to retire from either cause shall furnish to the Trustees all such information and shall submit to such medical examination as they may require.

(*c*) To every staff employee who shall be discharged merely for the purpose of reducing the staff not being entitled to a pension under (*a*) or (*b*) the equivalent of all sums actually contributed by him to the fund out of his salary with compound interest thereon at the rate of 4 per cent. per annum.

(*d*) To every staff employee of the Company leaving its service except as hereinafter provided before attaining the age of 65 years the equivalent of all sums actually contributed by him to the fund out of his salary with simple interest at the rate of 4 per cent. per annum.

(*e*) To the legal personal representatives of any staff employee who shall die in the service of the Company before attaining the

age of 65 years one year's full salary at time of death or alternatively the equivalent of the sums actually contributed by him to the fund out of his salary with simple interest thereon at the rate of 4 per cent. per annum whichever may be the greater sum.

(*f*) If on the death of any staff employee in receipt of a pension under (*a*) or (*b*) the amounts received by him by way of pension with simple interest thereon at the rate of 4 per cent. per annum shall be less than the amounts actually contributed by him to the fund out of his salary with simple interest thereon at the rate of 4 per cent. per annum or alternatively if the amounts received by way of pension shall be less than one year's salary at time of retirement whichever may be the greater sum then to the legal personal representatives of such employee a sum equal to the difference.

(*g*) Whenever under these rules a staff employee or his personal representatives is or are entitled to receive back the amount of his contributions with interest such interest shall be calculated on the amounts contributed by such employee in each year from the end of the year in which the same were deducted by the Company.

(*h*) No person shall under any circumstances be entitled to receive a pension whilst still in the employment of the Company.

6. EMPLOYEES SERVING WITH H.M. FORCES.

(*a*) Any staff employee serving with His Majesty's Forces who was employed by the Company before the 31st March 1916 at a salary of £100 per annum or more shall be eligible to become a subscriber to the fund on returning to the Company's service on the same conditions as present staff employees, and all time with the Forces up to the 31st March 1916 shall rank for pension at the ordinary rate of salary but no employee whilst serving with the Forces shall be entitled to any benefit under clause 5.

(*b*) Any such staff employee may at his option elect to pay arrears of contributions to cover the period with the Forces from the 1st April 1916 in order that such time shall count for pension or failing payment of contributions time served with the Forces from the 1st April 1916 to the date on which contributions are commenced shall not count for pension.

(*c*) Any staff employee who is a subscriber to the fund joining the Forces after the 1st April 1916 shall thereupon cease to be a subscriber or to have any interest in the fund whilst serving with the Forces. Such employee shall be entitled on request being made to have his own contributions refunded on joining the Forces and shall on returning to the Company's service be eligible to rejoin the fund on the terms and conditions hereinbefore mentioned.

7. PAYMENT IN THE EVENT OF DISMISSAL.

Any staff employee dismissed from the service of the Company for fraud or dishonesty or conduct justifying immediate dismissal or retiring or resigning in order to escape dismissal shall at the discretion of the Trustees and with the approval of the Directors of the Company forfeit all or any part of his contributions and lose all benefit from the funds except such return (if any) as may at such discretion and with such approval as aforesaid be made to him out of his own contributions.

8. QUINQUENNIAL VALUATIONS.

At the expiration of every 5 years from 1st January 1916 or at any other period that the Trustees may determine the position of the funds shall be submitted to actuarial investigation and for that purpose all necessary accounts and information shall be furnished to an Actuary to be appointed by them. If as the result of the Actuary's Report it shall appear that there is a surplus beyond the requirements of the fund such surplus or any part thereof may be set aside and separately invested by the Trustees as a reserve fund to meet any subsequent loss or deficiency or may be applied in such a manner as to enable the Trustees to increase the amounts of benefits or to reduce the limit of age for retirement. If as the result of such report it shall appear that there is a deficiency in the amount of the fund the same shall be made good in such manner as the Trustees may determine either by alteration or modification of this Deed or by such other means as may seem best regard being had to all circumstances of the case and the report and recommendation of the Actuary.

9. PAYMENTS TO LEGAL PERSONAL REPRESENTATIVES AND OTHERS.

Whenever any sum is payable to the legal personal representatives of a staff employee the same shall be paid to his executors or administrators if Probate of his Will or Letters of Administration to his estate shall be produced to the Trustees within six months from the date of his death but if such Probate or Letters of Administration shall not be so produced within the time aforesaid then the Trustees may at their absolute discretion pay such sum or sums to any person being a widow child father mother brother or sister of the deceased or to any two or more such persons jointly and the receipts of any such person or persons shall be good and valid discharges to the Trustees for the sum or sums so paid.

10. BANKRUPTCY, ETC.

If any staff employee shall after he shall have become entitled to receive a pension under the provisions of these presents be adjudged a bankrupt or take proceedings for liquidation in bankruptcy or make any arrangement or composition with his creditors

having the effect of a charge upon or alienation of his said pension or any part thereof or if he shall attempt to alienate charge or anticipate the same or any part thereof or if he shall do or attempt to do or suffer any act or thing or if any event shall happen whereby if the same were payable to him absolutely for his life he would be deprived of the right to receive the same or any part thereof it shall be in the option of the Trustees (whose decision shall for this purpose be final and unquestionable) (*a*) either to continue to pay the said retiring pension to such staff employee or the Trustee in bankruptcy of such staff employee or other the person or persons claiming in right of such staff employee to receive the same or (*b*) in lieu thereof to repay to such staff employee or such Trustee in bankruptcy or other person or persons as aforesaid the aggregate amount of such staff employee's own contributions to the fund with simple interest thereon at the rate of 4 per cent. per annum computed as hereinafter provided up to the date when his contributions ceased after deducting therefrom the amount of the payments (if any) then already made to such staff employee in respect of his pension.

11. PENSIONS TO BE PAID MONTHLY.

Every pension payable under this Deed shall be paid monthly on the last day of each month in every year.

12. EMPLOYEES OF TELEGRAPH MANUFACTURING CO. (COLONIAL) LTD. AND OTHER COMPANIES MAY BE ADMITTED.

(*a*) Employees engaged on the permanent staff of the Telegraph Manufacturing Company (Colonial) Limited whose registered office is situate at Helsby in the County of Chester or of any other Company controlled by British Insulated and Helsby Cables Limited as shall be approved by the Trustees shall be eligible to join the fund on the same terms and conditions in every respect as staff employees of British Insulated and Helsby Cables Limited upon the said Telegraph Manufacturing Company (Colonial) Limited and such other Company and their respective staff employees undertaking to subscribe to the fund in accordance with the conditions of this Trust Deed excepting that they shall not contribute any part of the capital sum under Clause 3(*a*).

(*b*) If the said Telegraph Manufacturing Company (Colonial) Limited or any other Company who with their employees have been admitted as subscribers to the fund shall be wound up (except for the purpose of reconstruction) or shall cease to be controlled by British Insulated and Helsby Cables Limited any subscriber of less than 10 years' service who is in the employment of such Company shall be entitled to a refund of his own contributions with compound interest at the rate of 4 per cent. per annum but any subscriber of 10 years' service or more shall in addition be entitled to a proportionate part of the Company's contribution and interest thereon at the rate aforesaid.

13. TERMINATING EMPLOYMENT.

Nothing in this Trust Deed shall in any way restrict the rights of the Directors of the Company by whom a subscriber to the fund is employed to determine such employment and the Directors of the Company by whom a subscriber is employed shall be the sole judges of the cause of his dismissal or if he resigns as to whether or not he resigns in order to escape dismissal and their decision shall be absolutely final and conclusive upon all parties and the Trust Deed shall not be used as an aggravation of damages in any action brought by any subscriber against the Company in respect of his dismissal.

14. MAJORITY OF TRUSTEES MAY ACT.

The business of the Trust hereby created shall be managed by the Trustees or a majority of such of them as may be present at the Trustees' Meetings hereinafter mentioned and all powers expressly or by implication given to the Trustees may be exercised by such majority.

15. MEETING OF TRUSTEES, ETC.

There shall be meetings of Trustees for transaction of business at such times and places as the Trustees may from time to time determine. Any two Trustees may convene a Special Meeting. One clear day's notice in writing of every Special Meeting stating in general terms the object of the Meeting shall be given to each Trustee. Every such notice may be given by posting the same under cover addressed to such address as the Trustee may give for the purpose in writing to the person for the time being acting as their Secretary or if no such address be given by leaving the same addressed to the Trustee in the room appointed for the meetings. Every notice posted shall be deemed to have been received at the latest on the day following that on which it shall have been posted.

16. TRUSTEES TO ELECT CHAIRMAN.

The Trustees may from time to time elect a Chairman of their meetings and may determine the period for which he shall hold office. If the Chairman is not present at the time appointed for holding the meeting the Trustees present shall elect one of their number to be Chairman.

17. QUORUM AT TRUSTEES' MEETINGS, ETC.

The Trustees may adjourn and otherwise regulate their meetings as they may think fit and determine the quorum necessary for the transaction of the business. Until otherwise determined the quorum necessary for the transaction of business shall be three of whom one shall be a " Directors' Trustee " and one a " Staff's Trustee " as hereinafter respectively defined.

18. CHAIRMAN OF TRUSTEES TO HAVE CASTING VOTE.

Questions arising at a Trustees' Meeting shall be decided by a majority of votes. In case of an equality of votes the Chairman shall have a second or casting vote.

19. REMOVAL OF TRUSTEES.

A Trustee may be removed by a resolution passed by the votes of all the Trustees other than the Trustee to be removed.

20. QUESTIONS TO BE DETERMINED BY TRUSTEES OR ARBITRATOR.

All questions as to whether any staff employee is or is not entitled to contribute to the fund under the provisions herein contained or as to whether a staff employee of the Company is entitled to any and if any to what payment out of the fund shall be determined by the Trustees in the same manner as other questions arising in the management of the fund. Provided that if a question as to whether a staff employee is entitled to any and what payment out of the fund be decided adversely to the employee by the casting vote of the Chairman and such Chairman shall be a Directors' Trustee then the minority may within three days by writing under their hands delivered to the Trustees' Secretary require the question to be referred to arbitration under the Arbitration Act, 1889. The award of such Arbitrator shall be binding upon all persons interested in the fund.

21. COMPANY TO PROVIDE PLACE OF MEETING, SECRETARY AND CLERICAL STAFF.

British Insulated and Helsby Cables Limited shall provide for the Trustees some convenient place for their meetings and proper minute books and books of account and also a Secretary who may be one of the Trustees or any competent employee of the Company and shall also arrange for the performance by the staff or otherwise of all clerical work in connection with the Trust hereby created and subject as aforesaid all proper costs and expenses of the Trustees in the execution of the Trusts of these presents shall be borne by the Company.

22. APPOINTMENT OF NEW TRUSTEES.

(*a*) The parties hereto of the second part being members of the Board of Directors of the Company they and their successors

are herein referred to as " Directors' Trustees " and the parties hereto of the third part being staff employees of the Company they and their successors are herein referred to as " Staff's Trustees."

(*b*) The power of appointing a new Trustee in the place of a Directors' Trustee or of any person appointed under this first power shall be exercised by the Board of Directors of the Company and the power of appointing a new Trustee in place of a Staff's Trustee or of any person appointed under this second power shall be exercised by the remaining or continuing Staff's Trustees or Trustee and in each case the power to appoint a new Trustee shall extend to the filling of a vacancy caused by the removal of a Trustee and any Directors' Trustee ceasing to be a Director and any Staff's Trustee ceasing to be a contributing member of the staff shall be deemed desirous of retiring from the Trusts so that a new Trustee may be appointed in his place. No person shall be appointed a Directors' Trustee other than a Director of the Company so long as a Director be willing to act and no person shall be appointed a Staff's Trustee other than an employee of the Company contributing to the fund so long as an employee contributing is willing to act.

23. DISPOSITION OF FUND ON WINDING UP.

If an effective resolution shall be passed or an Order be made for winding up the Company and neither the Government nor any Company or body shall within six months from the date of such resolution or Order undertake the obligations of the Company hereunder then it shall forthwith be referred to two Actuaries one to be appointed by the Directors' Trustees and the other by the Staff's Trustees to decide in what manner the fund shall be apportioned and divided among the members of the fund or such of them as shall be living or in receipt of retiring pensions the first charge upon the fund being the return to the said members of all sums actually contributed by them to the fund with simple interest thereon at the rate of 4 per cent. per annum and the decision of such Actuaries shall be final and binding on all parties and the employees to whom such decision and apportionment and division shall relate shall accept the amount (if any) which shall be allotted to them respectively thereunder in full discharge of all claims in respect of the Pension Fund and shall have no further claim whatsoever in respect of any rights to a retiring

pension or otherwise under these presents. Any difference between the Consulting Actuaries shall be determined by a third Actuary of their selection or in such other way as they think fit.

24. TRUSTEES' INDEMNITY.

No Trustee shall be responsible for the acts or defaults of any other Trustee whether such act or default may be attributable to his having allowed Trust property to remain in the hands or under the control of such other Trustee or not nor for any act or default of any company or person with whom securities may be lodged for safe custody nor for any banker broker or other person or company employed by the Trustees nor for any error in judgment mistake or unintentional omission and any Trustee shall be entitled to indemnity out of the funds for any liability incurred by him in the execution of the Trusts hereof by reason of his being a Trustee.

25. TRUSTEES TO KEEP PROPER REGISTERS AND ACCOUNTS.

The Trustees shall keep a register of the employees who join the fund and of the rate of mortality and withdrawal and all necessary and proper accounts to show the position of and all dealings with the fund and the income thereof. The said accounts shall be made up to the 31st December in each year and shall be audited by a Chartered Accountant to be appointed by the Trustees—such Chartered Accountant shall have access to all books papers vouchers accounts and documents connected with the fund and shall certify the result of his yearly audit in writing. Each subscriber to the fund shall on application be entitled to inspect such certificate.

26. PROVISIONS FOR VARIATION OF THESE PRESENTS BY SUPPLEMENTAL DEED.

The provisions of this Deed including any of the provisions relating to benefits to employees or to contributions by the Company or out of the employees' salaries may by Supplemental Deed executed by all the then existing Trustees be varied in any way provided such alterations be approved by a resolution of the Trustees by a resolution of the Board of the Company and be assented to in writing by a majority in number of the staff employees of the Company for the time being contributing to the fund out of their salaries provided that no such alteration shall have the effect of reducing any pension or other sum which may then have become payable to an employee.

IN WITNESS WHEREOF the Company of the first part has caused its Common Seal to be hereunto affixed and the Trustees of the second and third parts have hereunto respectively set their hands and seals the day and year first before written.

The Common Seal of British Insulated and Helsby Cables Limited was hereunto affixed in the presence of

J. CARLTON STITT, } *Two*
G. CROSSLAND TAYLOR. } *Directors.*

W. KERFOOT, *Secretary.*

SEAL OF BRITISH INSULATED & HELSBY CABLES LIMITED.

Signed sealed and delivered by the within-named Sir John Sutherland Harmood Banner M.P. in the presence of
WM. L. HODGES,
56, Moorgate Street, E.C.
Clerk.
} J. S. HARMOOD BANNER L.S.

Signed sealed and delivered by the within-named James Taylor J.P. in the presence of
JOHN BROTHERTON,
"Elm Cottage," Helsby,
Manager.
} JAMES TAYLOR L.S.

Signed sealed and delivered by the within-named Daniel Sinclair in the presence of
GEO. E. ROBERTS,
"Lydford," Whiston Lane, Prescot,
Accounts-Clerk.
} D. SINCLAIR L. S.

Signed sealed and delivered by the within-named John Brotherton in the presence of
JAMES TAYLOR,
"Heathercliffe," Helsby,
Manufacturer.
} J. BROTHERTON L.S.

Signed sealed and delivered by the within-named William Kerfoot in the presence of
GEO. E. ROBERTS,
"Lydford," Whiston Lane, Prescot,
Accounts-Clerk.
} W. KERFOOT L. S.

ALTERATION OF TRUST DEED.

By a Supplemental Deed dated 11th October 1916 executed by the Company and all the Trustees, Clause No. 7 of the Principal Trust Deed dated 8th August 1916 has been cancelled and the following substituted therefor :—

7. PAYMENT IN THE EVENT OF DISMISSAL.

Any staff employee dismissed from the service of the Company for fraud or dishonesty or retiring or resigning in order to escape dismissal for fraud or dishonesty shall at the discretion of the Trustees and with the approval of the Directors of the Company forfeit all or any part of his contributions and lose all benefit from the funds except such return (if any) as may at such discretion and with such approval as aforesaid be made to him out of his own contributions.

Prescot, 11*th October* 1916.

ALTERATION OF TRUST DEED.

By a Supplemental Deed dated 12th July 1917 executed by the Company and all the Trustees, Sub-Clauses 5 (*e*) and 5 (*f*) of the Principal Trust Deed dated 8th August 1916 have been modified as follow :—

Clause 5 (*e*) of the Principal Trust Deed shall as from the twenty-sixth day of March one thousand nine hundred and seventeen be read and construed as if the words " two years' full salary " had been originally inserted instead of " one year's full salary " at the beginning of the third line thereof.

Clause 5 (*f*) of the Principal Trust Deed shall as from the twenty-sixth day of March one thousand nine hundred and seventeen be read and construed as if the words " two years' full salary " had been originally inserted instead of the words " one year's salary " at the end of the sixth and the commencement of the seventh lines thereof.

Prescot, 12*th July*, 1917.

"B"

ACTUARY'S REPORT

BRITISH INSULATED AND HELSBY CABLES, LIMITED.

PENSION SCHEME.

Particulars have been furnished to me of 300 men, it being supposed that this is the utmost likely number to join the Pension Scheme. In the case of 238 men employed on the Prescot and Agency staffs, information was given as to the age, salary and length of service of each man, the average salary being about £220, and the average length of service about 11 years. In the case of 62 men on the Helsby staff particulars of the age and length of service only were given for each man, the average length of service being over 17 years. For the purpose of my

calculations the average salary of the Helsby staff has been taken as £200. No person has been included in any of the lists whose salary is under £100.

I have made calculations with the view of determining what capital sum ought to be provided to start a Pension Scheme, on lines indicated in the following Abstract, for the 300 men above referred to :—

It is understood that joining the Scheme would be optional as regards the present staff, but would be compulsory for new additions to the service, and that those of the present staff who join the Scheme from its commencement are to receive the benefit of the capital sum provided by the Company, by counting towards pension years of service with the Company prior to the Scheme as well as the years during which they pay contributions.

ABSTRACT OF PENSION SCHEME.

The Scheme provides the following benefits :—

1. *On leaving the service at the age of* 65 *or after* a pension will be granted for an amount depending on the number of years' service with the Company, and on the average salary paid during such service. The annual pension will be 1/60th of the average salary multiplied by the number of years service. A guarantee is given that if death should occur before the pension payments come up to the amount of the man's own contributions with 4 per cent. simple interest added, the difference shall be paid over to his representatives.

2. *In case of death before being granted a pension* one year's salary will be paid to the man's representatives, at the rate of salary which is being paid when death occurs.

3. *On resignation or dismissal* the whole of the man's own contributions will be returned with the addition of 4 per cent. simple interest. If dismissal should occur on account of reduction of staff, compound interest will be added at the rate of 4 per cent. instead of simple interest.

4. *In case of permanent breakdown of health* after 20 years' service and before the age of 65, the Directors would have power to grant a pension depending on the number of years' service and on the average salary during service, in the same way as for a man who retires at 65.

The arrangements secure that in every possible event, a man's own contributions with interest shall be paid back to him or to his representatives, and in the case of those who continue in the service and do not leave by resignation or dismissal, the payment will in most cases be more.

The contributions to the Scheme would be as follows :—

1. *From employees* who join the Scheme, 5 per cent. on their salaries and on any future increase of salaries.

2. *From the Company*, 2½ per cent. on the salaries of employees who join the Scheme, and on any future increases of the salaries of those employees.

3. *The Company* also makes a grant, in addition to its contributions of 2½ per cent., with the object of providing the cost of bringing in years of service before the introduction of the Scheme in reckoning the amount of pensions.

I have made some provision for cases of permanent breakdown of health, so that when a man is incapacitated in such a way that it is quite impossible for him to continue his occupation and yet has the prospect of living for some years, the Directors may in their discretion, grant him a pension out of the Fund. But I have assumed that in all ordinary cases the men will not be put on pension before the age of 65. If, for example, the Directors should some time in the future decide that men of a certain class or classes should be pensioned at 62, this would throw a burden on the Fund which has not been provided for, and a further capital sum would have to be found.

It is pointed out in the abstract of the Scheme, that every man who joins the Fund is secured the return of his own contributions at least, with interest, in every possible event. I may add here, that no man who leaves the Company by resignation or dismissal, receives any part of the contributions of the Company. The capital sum provided by the Company, and the contributions of 2½ per cent., are reserved entirely for the benefit of men who remain in the service until death, or until 65, with some provision for exceptional cases of breakdown before 65.

In making my calculations, I have made allowance in a reasonable way for future increases of salary, being guided by my experiences of other commercial concerns, and by the consideration that promotions must take place as vacancies occur, in the natural course of things, by death, and by retirement on pension. I have also allowed for resignations and dismissals among the younger men.

As regards interest, my calculations are based on the supposition that the Fund will obtain at least 4 per cent. per annum net, on the balances which will be available for investment from time to time.

Reducing everything to capital sums, the result of my calculations is as follows :—

	£		£
Value of Company's contributions of 2½ per cent.	21,269	Value of payments at death	9,637
Value of employees' contribution of 5 per cent.	42,539	Value of payments on resignation and dismissal	575
Deficiency	31,784	Value of pensions ...	85,380
	£95,592		£95,592

There is therefore a deficiency of £31,784 to be made up. As the calculations are made on a 4 per cent. basis, this means that an annual income of £1,271 has to be found for the Fund. I understand that a sum of £25,000 was set aside a year ago which with one year's interest at 5 per cent. amounts to £26,250. If this sum can be invested so as to obtain 5 per cent. interest, free of tax, the necessary annual sum will be provided.

If the interest income of the Fund is liable to deduction on account of Income Tax, this will be a serious burden in view of the high rate of tax now prevailing. I make the suggestion, therefore, that instead of handing the sum of £26,250 to the Fund for investment, the Company should retain this sum, and make an annual grant to the Fund of £1,300, which would not be subject to tax, because it would not be interest on an investment.

My calculations have been made on the basis of a net yield of 4 per cent. on the future investments made by the Fund, and if the effect of Income Tax should be to reduce the net yield below 4 per cent. it would be necessary to give the Fund some temporary help until the normal rate of 4 per cent. is attained.

(Signed) DUNCAN C. FRASER, M.A., F.I.A.

1, North John Street, Liverpool.

31*st January*, 1916.

The case came before Rowlatt, *J.*, in the King's Bench Division on the 24th and 25th June, 1924, when the Attorney-General (Sir Patrick Hastings, K.C., M.P.) and Mr. R. P. Hills appeared as Counsel for the Crown, and Mr. A. M. Latter, K.C., and Mr. A. Hildesley for the Respondent Company.

On the latter day judgment was given against the Crown, with costs.

JUDGMENT.

Rowlatt, J.—In this case the Respondent Company thought it wise, in order to attract and retain a good class of servant, to inaugurate a system of pensions. The scheme was, in principle, that the necessary Fund should be created by a payment of 5 per cent. on their wages by the employees and half that amount by the Company, and I understand that, if the scheme could have commenced with new and young employees, those sums would be sufficient to maintain the Fund in a solvent condition when it had got established in the future and these sums had been paid in respect of everybody throughout their employment. But there was this difficulty. It was desired that this system of pensions should start at once. That meant that there would be

(Rowlatt, J.)

a claim upon the Fund in respect of people who had already been long in the employment of the Company and in respect of whom no payments had been made. Therefore a lump sum had to be found to initiate the Fund and make it solvent in respect of that source of deficiency, and that sum, £31,000 odd, was found by the Respondent Company, and it is that sum which they seek to deduct against the profits of the year in which they found it. That sum was not a sum which would produce by way of interest enough to make good the deficiency of income of the Fund owing to the claims upon it of these older employees, but it was an actuarial sum which, taking the principal and the interest together, would cover the claims in question and redeem them in advance, to use a short expression. When these older employees had all drawn their pensions and died, according to the actuarial calculation, if it proved to be exactly borne out by the facts, this sum would have disappeared, capital and income.

If the Company had started to pay these pensions and had paid them year by year, I understand it is not disputed that those payments would be a business expense, sums laid out for the purposes of the business, according to the Act, and year by year those annual sums would be deductible. The question is whether a lump sum of the kind which I have described, paid at the beginning to prevent these sums having to be paid later, can be deducted.

It is clear that expenditure, which in its nature is a revenue expenditure, does not cease to be deductible because it is not made strictly annually. In the course of the argument reference was made by way of illustration to the facts of a case(1) which is reported, which happened to come before me—I forget whether it went further—namely, the case of dredging a water passage, and it was conceded that dredging a water passage which is continually silting up is an income expense to be faced by the people who own the passage, and it does not cease to be deductible because, instead of continuously dredging, or dredging, say, every year, you may dredge very efficiently in one year and thereby save yourself from having to dredge in the next two years. It still is an income charge. On the other hand, I suppose, if the undertakers in possession of a channel of that kind were minded, by concreting the bottom of their water passage, to make it a channel which never required dredging, and so saved themselves from that expense until the concreting wore out, as it would in time, I apprehend it would not be argued that that was an income expenditure. I gather it would be said that that was providing yourself, by a capital expenditure, with a better sort of channel that had not the disadvantage that it required dredging.

(1) Ounsworth v. Vickers, Ltd., 6 T.C. 671.

(Rowlatt, J.)

The question in this case is whether when, in order to get rid of sums like pensions, you invest an actuarial sum to free your undertaking from that liability, which is a liability for a term of years uncertain, that can be treated as a payment in one year on the same footing as the annual payments would have stood if they had been made annually. I confess that I think that is a matter of very considerable difficulty, and had it not been for the case of *Hancock*(1), the principle of which was accepted apparently without misgiving in the Court of Appeal, I do not know whether I should have been able to come to that decision. But it seems to me that *Hancock's* case governs the present one when once you realise that this is an actuarial sum preventing the arising of those payments, and when you once realise that those payments are payments which themselves would have been deductible.

But the Attorney-General did seek to distinguish *Hancock's* case in this respect. He said that in *Hancock's* case the pension was already *de facto* being paid, and this was redeeming it, whereas in the present case the pension scheme was still *in futuro*, and this payment was made to prevent the annual payments having to be made in the future. I do not think I ought to apply a distinction of that kind, because it does not seem to me to be a distinction of principle. If they had gone into this pension scheme for a year or two on the principle of making payments and then had changed their minds and had said : " Well, now, " we will buy from a life assurance company an indemnity " against these payments for the future, or we will put up the " money into the Fund ourselves on an actuarial basis," which is the same thing, if they had done that, I do not see how it would have been possible to distinguish *Hancock's* case. I think if I distinguished *Hancock's* case merely upon the ground that they adopted this policy from the beginning instead of at a time after the beginning of the scheme, I should be giving effect to a distinction without a difference.

Under these circumstances I think this appeal fails and must be dismissed with costs.

The Crown having appealed against this decision, the case came on for hearing in the Court of Appeal (Pollock, *M.R.*, and Warrington and Scrutton, *L.JJ.*) on the 6th November, 1924, when the case was adjourned. On the following day judgment was given unanimously in favour of the Crown, with costs, reversing the decision of the Court below.

The Attorney-General (Sir Patrick Hastings, K.C., M.P.) and Mr. R. P. Hills appeared as Counsel for the Crown, and Mr. A. M. Latter, K.C., and Mr. A. Hildesley for the Respondent Company.

(1) Hancock *v.* General Reversionary and Investment Co., Ltd., 7 T.C. 358.

JUDGMENT.

Pollock, M.R.—We need not trouble you, Mr. Attorney. This is an appeal from a decision of Mr. Justice Rowlatt, who gave judgment for the Company on the 25th June, 1924. From that decision the Crown appeals and claims that a certain sum, namely, £31,784, is a sum which ought not to be deducted by the Company as a part of the cost of the carrying on of their business for the purpose of ascertaining what are their profits and gains subject to Income Tax.

Now the facts may be recapitulated quite shortly. This British Insulated & Helsby Cables Company is a large and important company carrying on a large business and having in addition to a working staff what is called a clerical and technical salaried staff. They were minded, I think in the year 1916 or 1917, to establish a Pension Fund. The Pension Fund was started on this principle, that the staff were to contribute a certain amount, and the Company were to contribute one-half of the amount contributed by the employees. It is stated in paragraph 5 of the Case that each member of the existing staff who elected to join the Fund undertook to contribute 5 per cent. of his salary to the Fund as from the 31st March, 1916, and that the older members of the staff were not called upon to pay any higher rate of contribution on account of their age. Then persons joining the staff after the commencement of the Fund were also to contribute at the rate of 5 per cent. of their salary, if not above the age of 40 at the time of joining the Fund; if they joined above the age of 40 the rate was increased. That system obviously entailed this difficulty, that, inasmuch as the existing members of the staff, whatever might be their ages, were not required to contribute any larger sums than the incoming and presumably younger members, it would not be possible actuarially to give so great a benefit in the matter of pensions to the older members of the staff as it would be to the younger members of the staff; or, putting it in other words, it was quite obvious that the older members of the staff, contributing the same as the younger members, would necessarily have to be content with decreased benefits. The Company thought that would be unfortunate; they were afraid that if that were so the older staff might, if they could, seek to get employment elsewhere, and they were minded to put the whole staff on the same footing whether they were older or whether they were younger; in other words, they wanted to see that the benefits, whatever be the age of those who were contributing to the Fund, should be the same. They thereupon had the matter calculated out by an actuary, and it was ascertained that the deficiency as shown on the existing system, if you were to give all the employees, whatever their age, similar benefits, would be £31,784. They have contributed that sum

(Pollock, M.R.)

to the Pension Fund, and they now seek to deduct this £31,784 as a sum which has been wholly and exclusively laid out and expended for the purposes of trade and so deductible under Rule 3 of Cases I and II of Schedule D(1). The Commissioners came to the conclusion, upon the authority of *Hancock* v. *General Reversionary & Investment Company, Limited*(2), that this contribution was an admissible deduction in computing the profits of the Company for the purpose of the Income Tax Acts; and Mr. Justice Rowlatt, although he seems a little uneasy in his judgment, a little hesitating, as to whether he would or would not have come to that conclusion, feels that the principle of *Hancock* is such that he acquiesces in, if he does not endorse, the decision come to by the Commissioners.

We have to determine whether or not this is a proper deduction. I say at once that it is a difficult case because the line is not easy to draw between what is a deduction allowable in ascertaining the profits and gains of a company and what is to be attributed to capital expenditure. A number of cases have been cited to us as illustrations rather than as guides, and we have to make up our minds on which side of the line this falls. It is to be observed that Rule 3 tells how the amount of the profits and gains is to be computed, but it begins by saying that no sum is to be deducted in respect of any disbursements which are not money wholly and exclusively laid out or expended for the purposes of the trade. Therefore, unless this money, the £31,784, was wholly and exclusively laid out for the purposes of trade it could not be deducted. It is pointed out that it has many of the characteristics which are to be found in the cases where deductions have been held justified. It is done for the purpose of ensuring a good, efficient, and contented staff; it is done in order that the position of the staff may be better in the future. It is said it is done to make a payment to-day in order that benefits might accrue in the future, and then it is said, therefore, that it has been, as many other deductions which have been allowed have been, wholly and exclusively laid out or expended for the purposes of the trade. I am content that it should be so treated. Unless it were so treated the question could not arise, but when it has been so treated as wholly and exclusively laid out we then have to see whether or not it falls within Sub-clause (*f*) of Rule 3 which provides that no deduction shall be allowed "in respect of . . . any sum employed "or intended to be employed as capital in such trade."

Now what is capital and what is attributable to revenue account I suppose is a puzzling question to many accountants,

(1) Income Tax Act, 1918. (2) 7 T.C. 358.

(Pollock, M.R.)

and I do not suppose that it is possible to lay down any satisfactory definition. We had to consider the question in the *Rowntree* case(1), a case in which a large sum of capital had been provided by Messrs. Rowntree, the income of which was to be applied to what was called the invalidity of their workmen; and, having considered the cases very carefully, we came to the conclusion that that deduction could not be allowed. First of all, treating this as being an expenditure prudent and useful for the purposes of the trade and so having some of the characteristics which would prima facie justify its deduction under Rule 3 (*a*)(2), that does not conclude the question. We have to consider whether or not it is an item employed and intended to be employed as capital in such trade. For my part I think it would be very difficult to say that this contribution which is not essential, although satisfactory from the employees' point of view, could be treated simply as a revenue item. I do not think that it would have been provided unless the Company had been in such a condition that it would be possible from their existing assets to provide it. The homely phrase, unless they had had the money to do it they would not have done it, I think applies in this sense, that having the money they were prepared to make use of a certain amount of capital in giving this satisfactory benefit to the employees. If they had not had the money to do it they would not necessarily, or indeed at all, have made this expenditure, still less would they have charged it on ordinary principles to the revenue account. Asking myself the question in that form I say: Would anyone at the present time have treated this as a necessary expenditure in seeking profits and gains, or would they say: "Well, if you have got the money "to do it it will be a satisfactory use of the money provided it is "possible for you to provide it." It seems to me upon the facts as found, that it ought to be treated as being a sum employed as capital in such trade.

It is said that the case of *Hancock*(3) points in a different direction. I have said what I have to say about the *Hancock* case in the *Rowntree* case. All that I will add here is, that I think it is a case which depends upon its facts, and I doubt myself, although the question of the payment in that case being a capital expenditure was argued, whether full attention was given to that question in the judgment. In *Hancock's* case there was an existing liability, a sum which had to be paid from year to year, and it may well have been good business to have paid or provided a lump sum in order to get rid of that accruing

(1) Rowntree & Co., Ltd. *v.* Curtis, 8 T.C. 678.
(2) Income Tax Act, 1918, Schedule D, Cases I and II. (3) 7 T.C. 358.

(Pollock, M.R.)

and continuing yearly liability. The case is not the same here. There was no liability in law. This is a general expenditure like an outlay which might improve the plant or make the plant more easy to work, although it would not actually increase the output.

Then it is said that the question of whether it is a legal liability or not does not determine the case, because the decision of the House of Lords in *Usher's Brewery* case(1) determined that where you have an outlay made for the purposes of the business, it being an item which the directors might legitimately incur in their prudent and perhaps generous estimation of how business ought to be carried on, then you may deduct such outlay as an expense for seeking profits. Of course *Usher's Brewery* case is binding upon us, and I desire to point out that both in *Rowntree's* case and again here I should wish to conform to what Lord Parker and Lord Sumner have said about the area of revenue expenditure and capital expenditure. But I should like also to point out that in *Usher's* case there was a Supplementary Case, and you will find that the supplementary statement on page 436 of [1915] A.C.(2) includes this: "The cost is "incurred not as a matter of charity but of commercial "expediency and is necessary in order to avoid the loss of "tenants and consequent transfers to which the Licensing "Justices object"; and it will be found that the reference to the expenditure being necessary is referred to and repeated in a number of the speeches that are made. Lord Atkinson refers to it on page 451(3),and on page 458(4) Lord Parker says: "The "better view, however, appears to be that, where a deduction "is proper and necessary to be made in order to ascertain the "balance of profits and gains, it ought to be allowed." He refers to it again later on in his speech at page 462(5). It seems to me, therefore, that you have to remember in *Usher's* case that there had been that finding, that the expenditure was necessary in order to secure the gains and profits. Here, as I pointed out, there was no liability and the Commissioners only find that it is admissible in accordance with the ruling or principle, as they understand it, of *Hancock* v. *General Reversionary & Investment Company, Limited*(6), and I do not think that what the Commissioners have found here is sufficient or is parallel to what was found in *Usher's* case. They have only held it to be an admissible deduction; they have not said that it was a necessary deduction. The facts, to my mind, would not justify them in finding that it was a necessary deduction.

It appears to me that when you consider what is the purpose of this payment, the right attribute to apply to it is that it was a

(1) Usher's Wiltshire Brewery, Limited, v. Bruce, 6 T.C. 399. (2) *Ibid.* at p. 403.
(3) *Ibid.* at p. 424. (4) *Ibid.* at p. 429. (5) *Ibid.* at p. 432. (6) 7 T.C. 358.

(Pollock, M.R.)

payment made as a capital outlay and cannot be deducted from the revenue as a payment made in the course of seeking profits and gains.

It appears to me, therefore, for these reasons that the right course is to allow the appeal, and to allow the appeal with costs.

Warrington, L.J.—The question in this case is whether a contribution of £31,784 made by the Company to a Pension Fund established for the benefit of its clerical and technical salaried staff is an admissible deduction in computing its profits for the purpose of assessment to Income Tax for the year in question, the year in question being the year ending 5th April, 1918. Whether or not deductions are to be allowed for the purpose of ascertaining the net income for the purposes of Income Tax is a question of considerable difficulty, and for this reason—that whereas the Income Tax Act enacts this, that in arriving at the amount of profits or gains for the purpose of Income Tax no other deductions shall be made than such as are expressly enumerated in this Act, the Act does not in fact enumerate any deductions at all, except those which are not to be made. The meaning and effect of that curious structure of the Act was considered both by Lord Parker and by Lord Sumner in *Usher's Wiltshire Brewery, Limited* v. *Bruce* in [1915] Appeal Cases, beginning at page 433(1). The passage in Lord Sumner's speech at page 468(2) I will read: "The "effect of this structure, I think, is this, that the direction "to compute the full amount of the balance of the profits must "be read as subject to certain allowances and to certain prohibi- "tions of deductions, but that a deduction, if there be such, "which is neither within the terms of the prohibition nor such "that the expressed allowance must be taken as the exclusive "definition of its area, is one to be made or not to be made "according as it is or is not, on the facts of the case, a proper "debit item to be charged against incomings of the trade when "computing the balance of profits of it." The rules applicable to Schedule D provide that "No sum shall be deducted in "respect of any disbursements or expenses, not being money "wholly and exclusively laid out or expended for the purpose "of the trade, profession, employment or vocation." That is a prohibition. Such a payment as that in question may, in my opinion, upon the authorities be taken to have been wholly and exclusively laid out or expended for the purposes of the Company's trade (and that I think is not disputed by the Attorney-General), and for this reason, that to provide for pensions to its officers and servants is generally, and may be universally, for the benefit of a Company as a trader, as enabling it to be better served by its officers and servants and to get a better class of men

(1) 6 T.C. 399. (2) *Ibid.* at p. 436.

(Warrington, L.J.)

to serve it; but though you may arrive at that, that is to say, that the deduction is not prohibited by Rule 3 (*a*)(1), yet still it is not to be allowed unless, to use again the words of Lord Sumner, it is " on the facts of the case a proper debit item " to be charged against incomings of the trade when computing " the balance of profits of it." To my mind the real question that we have to determine is not whether this is prohibited by Sub-clause (*a*) or whether it is prohibited by Sub-clause (*f*), which prohibits the deduction of capital withdrawn from or any sum employed or intended to be employed as capital of such trade, profession, employment or vocation. The real question I think which we have to determine is whether this is a proper debit item to be charged against the incomings of the trade when computing the balance of profits of it; that is to say, to put it in a shorter form, is it a payment which can rightly be charged against the incomings of the trade for the purpose of computing the balance of profits of it?

The circumstances under which this particular payment was made can be very shortly stated. The Company was desirous of establishing a Pensions Fund and the Pensions Fund was to be made up by contributions from the officers and servants of the staff—it was a superior staff, if I may so call them—and by a contribution by the Company of one half of the contributions from the members of the staff; that is to say, the staff were to contribute 5 per cent. of their salaries, and the Company were to contribute 2½ per cent. of, I suppose, the total amount of the salaries. But the Fund was to be started at a time when there were already in the service of the Company a number of officers and servants of mature years, who had been many years in the Company's service; and inasmuch as the benefit which the servants were to take was this, that in the event of retirement at the age of 65 and in certain other circumstances an officer was to be entitled to a pension depending on the length of service, it is obvious that the contributions of the actual servants at the time and the contributions of the Company would, in the ordinary and natural course of events, not be enough to render the Fund solvent, but the Fund would be exhausted in payment of the first few pensions that arose to be paid, and would cease to be solvent, and, therefore, there would be no pensions payable out of it for the younger members as they might become entitled to them. Accordingly an actuarial calculation was made of the amount which was necessary as a capital sum to be contributed to the Fund in order to render it solvent and thus to meet the peculiar difficulty which had arisen. That calculation resulted in the actuary reporting that a sum of £31,784 was required to make up the deficiency. That is the sum which is now in question, and which was paid

(1) Income Tax Act, 1918, Schedule D, Cases I and II.

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to trustees under a trust deed of the Fund, and, as the Commissioners find, to provide the capital necessary in order that past years of service of the then existing staff should rank for pension. That is the object of the payment as found by the Commissioners. Was that a payment properly deducted from income for the purposes of Income Tax? In my opinion it was not. I am not saying for the moment whether a recurring payment may or may not be redeemed by a capital payment and that capital payment allowed in lieu of the recurring income payments. I assume for the moment that that is so, but in this case the payment made by the Company was not of that nature. They never undertook and they never intended to undertake to pay out of their current income pensions to their servants. What they intended to do was to provide a Pensions Fund by contributions made by them and by contributions made by the servants themselves out of which the pensions should be paid. They did not undertake to make, and they never contemplated making themselves, the periodical payments which had to be made towards their pensions. What they did do was this: Realising that for the first few years, at all events, it would be impossible to pay the full pensions to their older servants without rendering the Fund insolvent, they made the Fund solvent by contributing this money. It seems to me that that stands altogether on a different footing from that of a payment made by a person who is under an obligation legally or morally to make an annual payment and redeems that annual payment by making it once for all. It seems to me that this is a payment which was in every sense a payment made once for all, and not a recurring or in the nature of a recurring payment so as to come within either the definition of Lord Dunedin in the *Vallambrosa* case(1) or any similar definition.

I think it is plain from his judgment that Mr. Justice Rowlatt would have arrived at the conclusion which I have already expressed if he had not considered himself bound by the decision of Mr. Justice Lush in *Hancock* v. *The General Reversionary and Investment Company, Limited*(2), [1919] 1 K.B.25. With all respect to Mr. Justice Rowlatt that case appears to me to have nothing to do with and to be perfectly distinguishable from the present case. In *Hancock's* case the facts were these (they are sometimes lost sight of):—An actuary named Bumstead had been employed for many years by the Company in question. He desired to retire, and on his retirement the Company allowed him a pension of £666 odd; they paid that pension for a good many years, but at length (it is put expressly in the findings) as a matter of internal arrangement it became

(1) Vallambrosa Rubber Co., Ltd. v. Farmer, 5 T.C. 529.
(2) 7 T.C. 358.

(Warrington, L.J.)

in their view convenient, instead of continuing to pay him the annuity, to buy for him an annuity from an insurance office, and that they did by expending a sum of £4,000 odd. It was that deduction, the expense of buying from the insurance company an annuity to the amount of his pension instead of paying the pension every year as it became due, that Mr. Justice Lush regarded as a deduction which could properly be made for the purposes of Income Tax. Whether that was correct or not I do not propose to say. If the question arises in the exact form in which it came before Mr. Justice Lush, we may have to consider it, but what I do say about it is that it is as different from the case with which we have to deal almost as one case can be from another.

For the reasons I have already given I think in this case Mr. Justice Rowlatt ought to have acted according to his own view and have reversed the decision of the Commissioners, who also considered themselves bound by the case of *Hancock* v. *The General Reversionary and Investment Company*(1). I think, therefore, that the appeal ought to be allowed.

Scrutton, L.J.—In this case, as in the last one, Mr. Justice Rowlatt, somewhat against the view that he would have taken if left to himself, has thought himself bound to decide in a certain way by a previous decision of a co-ordinate Judge. Therefore, one has to carefully consider exactly the facts of the case and consider whether any principle laid down by the previous case is really applicable to this.

The Helsby Company claimed to deduct from their profits a sum of £31,000 odd which they have paid to establish a Pension Fund for their employees. The deduction is objected to by the Crown on the ground that this sum is either not money wholly or exclusively laid out for the purposes of the trade or that it is a sum employed as capital in the trade. The Commissioners do not make their finding in the words of those two clauses, and I think perhaps it would be better if, in future, they did say exactly what they find in the words of the clauses; but, having stated the contentions, they say, in view of the decision in the case of *Hancock*(1), the contribution of £31,000 was an admissible deduction. Though they do not say it I suppose that involves that it was money exclusively laid out for the purposes of the trade and not a sum employed or intended to be employed as capital. Obviously a case which may result in a definition by this Court of the line between capital and revenue expenditure must require very careful consideration by this Court, and the first thing that it must do is to bear in mind the warning of Lord Macnaghten in *Dovey* v. *Cory*, [1901]

(1) 7 T.C. 358.

(Scrutton, L.J.)

A.C. 477, at page 488 :—" I do not think it desirable for any " tribunal to do that which Parliament has abstained from " doing—that is, to formulate precise rules for the guidance " or embarrassment of business men in the conduct of business " affairs. There never has been, and I think there never will " be, much difficulty in dealing with any particular case on its " own facts and circumstances; and, speaking for myself, I " rather doubt the wisdom of attempting to do more."

Bearing that warning of Lord Macnaghten's in mind, the first thing I do is to see what the facts in this case are, to see whether they will help me to settle whether this is a capital or revenue expenditure, without attempting to lay down any general rule which will cover a number of cases which I have not in my mind at present. The Helsby Company had no Pension Fund for their employees. A man who served them for many years and retired got nothing on retirement, and they came to the conclusion that it was in the interests of the Company that they should have such a Pension Fund, that having such a Pension Fund would keep experienced servants in their employment instead of allowing those experienced servants to go and get higher prices for their experience elsewhere outside the Company. But they were faced with this difficulty. Starting a Pension Fund on the ordinary lines, that each servant should contribute each year a percentage of his salary and that the Company should add to it a sum in each year having some relation to the amount contributed by the servant, if they started on those lines they started a system which would be actuarially insolvent, because the elderly servants who would be the first to retire would not have contributed, even when the contributions of the Company each year were added to their contributions, anything like the sum that would be due to them, and, unless the contributions of the younger servants were fixed far higher than they would be inclined to pay, the Fund would be heading straight to bankruptcy. So the Company determined to start the Fund at once, as far as they could, in an actuarially solvent condition by finding out what sum ought to have been contributed in the past if the Fund was started in a solvent manner and themselves, without any contribution from the servants, providing the Fund with that sum at the outset. The actuary told them that he calculated it would be £31,748, that if the £31,748 was given to the Fund to start with the annual contributions of servants and Company would keep the Fund solvent. So the Company, not being under any liability at the time, not paying it to any particular servant, but paying it to establish a solvent Pension Fund for the future, paid the £31,784. The question is : Is that employing a sum as capital in the trade or is it money exclusively laid out for the purposes of the trade, not of the nature of capital? The Attorney-General started with a definition which I hope I took

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down rightly, " Any money expended upon a business which is " intended to and does result in an asset is capital." The next time the Attorney-General on one side or the other of a Revenue case formulates that definition I hope he will look at Lord Justice Swinfen Eady's very careful description in the *Ammonia Soda Company* v. *Chamberlain*, [1918] 1 Ch. 266, at page 286, of the difference between fixed capital and circulating capital, because I think there is no doubt that circulating capital as defined by Lord Justice Swinfen Eady would not come within the terms of the Income Tax Act " to be employed as capital," but it would come within the terms of the Attorney-General's definition. Without professing or intending for a moment to lay down a definition myself, having Lord Macnaghten's warning in my mind not to embarrass business men, I think clearly you must add to the words defining " asset " something to show that you were only speaking of assets in the nature of fixed capital. You expend your capital goods to get back a profit, but the fact that you expend the goods or buy the goods does not make the asset which results a capital asset, because it is not fixed capital, but is something that, in the language of Lord Justice Swinfen Eady, is going to be circulated. I think, therefore, to get capital you must have some permanent extension of the business which results in some sort of asset. Again I am not proposing to lay down a definition, but anybody who tries to lay down a definition will find the statement in the first volume of " Lindley on Companies " under the head of " Capital " of very great value. One of the matters mentioned there as being capital expenditure is the extension of the business. What happened from this expenditure? In my view either capital was withdrawn from the business for this Pension Fund, in which case it would not come within Rule 3 (*f*)[1], or the capital employed in the business created an asset or advantage of the business—this Pension Fund which never existed before and which now did exist for the benefit of the Company. On these lines it seems to me that the payment of the sum was either a withdrawal of the capital or an employment of capital in the trade—no previous liability to do it, but something added to the business not in discharge of any existing liability, but creating some new asset.

Now if that is the proper way to view this case it seems to me that *Hancock*[2] has nothing to do with it. In *Hancock* you start with an existing liability to pay year by year and you discharge that liability by the payment of a lump sum. That does not seem to me to add anything to the business. It may well be said to be money wholly laid out for the purpose of the business in discharging the existing liability to one's servant.

[1] Income Tax Act, 1918, Schedule D, Cases I and II.
[2] Hancock *v.* The General Reversionary and Investment Co., Ltd., 7 T.C. 358.

(Scrutton, L.J.)

On the other hand, when you take a case like *Rowntree*[1], where there was no previous fund and no previous liability but to add to the advantages of the business and of the workmen, and therefore the proper carrying on of the business, you present a sum of £50,000 to form a fund against invalidity, as it is called in the Case, you appear to me to be adding an asset or advantage to the business of a permanent character. If then I am asked which case the facts in the present case come nearest, it appears to me that they come much nearer *Rowntree*—to be practically the *Rowntree* case—than the *Hancock* case; and I cannot see anything in the decision in *Hancock* to preclude a Judge from saying that, whatever there was in *Hancock*, in this case there is the addition of a capital asset to the business. This Fund could not be diverted from the business to any other business. It was for the benefit of the employees in that business, dependent on contributions by the employees in the business and by the Company itself.

The conclusion, therefore, that I should come to is that Mr. Justice Rowlatt was not bound by the decision in *Hancock* to say that this was not an employment of capital in the business, that it is not necessary in this case to say whether *Hancock* was rightly decided (though I am inclined to think it was) and that this case is far more on the lines of the decision of this Court in *Rowntree* than it is on the lines of the decision of Mr. Justice Lush in *Hancock*.

For these reasons I think that Mr. Justice Rowlatt should have acted on his own view, that he was not bound by the decision in *Hancock*, and that, therefore, this appeal should be allowed.

Pollock, M.R.—The appeal will be allowed with costs.

The Company having appealed against the decision in the Court of Appeal, the case came on for hearing in the House of Lords before Viscount Cave, *L.C.*, and Lords Atkinson, Buckmaster, Carson and Blanesburgh on the 22nd, 23rd and 26th October, 1925, when judgment was reserved.

Sir John Simon, K.C., M.P., Mr. A. M. Latter, K.C., and Mr. A. Hildesley appeared as Counsel for the Company, and the Attorney-General (Sir Douglas Hogg, K.C., M.P.) and Mr. R. P. Hills for the Crown.

On the 11th December, 1925, judgment was given in favour of the Crown with costs (Lords Carson and Blanesburgh dissenting), confirming the decision of the Court below.

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(1) Rowntree & Co., Ltd. *v.* Curtis, 8 T.C. 678.

JUDGMENT.

Viscount Cave, L.C.—My Lords, the present appeal is concerned with the assessment of the Appellants to Income Tax for the year ending on the 5th April, 1918, and the relevant facts appear in the Case stated by the Commissioners for the Special Purposes of the Income Tax Acts. From that Case it appears that the Appellants (who are manufacturers of insulated cables) had a large clerical and technical staff, and that prior to the year 1916 they had not paid pensions to their employees retiring on account of old age. In or about that year, however, the Appellant Company (to quote the language of the Case) " found that it had " frequently lost experienced members of its salaried staff, who " left to take up appointments elsewhere, and that the absence " of a regular system of pensions was injurious to its business " in other respects. It was therefore decided to establish under " the powers given to the Company by its Memorandum of " Association a Pension Fund for its clerical and technical salaried " staff, in the hope that the benefits to be derived from the Fund " would induce the members of its staff to remain in its service " and otherwise increase the efficiency of the Company's staff." Accordingly, a Pension Fund for the staff was constituted by a trust deed dated the 8th August, 1916. By this deed each member of the existing staff who elected to join the Fund undertook to contribute five per cent. of his salary to the Fund, the older members of the staff not being called upon to pay any higher rate of contribution on account of their age. Persons joining the staff after the commencement of the Fund were to contribute at the same rate if not above the age of 40 at the time of joining the Fund, but if above the age of 40 the rate of contribution was increased. The Company undertook to contribute to the Fund an amount equivalent to one-half of the contributions of the members, and further undertook to pay the sum of £31,784 to form the nucleus of the Fund, and to provide the capital sum necessary in order that past years of service of the then existing staff should rank for pension. The Company also undertook to make up the income from the investment of the Fund to a net income equal to four per cent. per annum free of tax. The benefits were to take the form (*a*) in the event of retirement at the age of 65, and in certain other circumstances, of a pension depending on the length of service, and (*b*) in other cases of a return of the members' contributions, with interest. The trustees of the Fund had power to apply the income and, as far as necessary, the capital of the Fund in payment of the benefits provided. Two of the trustees of the Fund were to be appointed by the directors of the Company, while the three other trustees were to be contributing members of the Fund. In the event of the winding up of the Fund, the whole of the amount was to be divided among the members, and the Company was not to be entitled to recover any part of the contributions which it had paid.

(Viscount Cave, L.C.)

The above mentioned sum of £31,784 (which is the item giving rise to the appeal in this case) was arrived at by an actuarial calculation, and represented the estimated deficiency which might be expected to arise by reason of the admission to the Pension Fund of the older members of the existing staff without any additional contributions on account of their age. The date when this sum was actually paid to the trustees of the Fund is not stated, but probably it was paid at some time in the year 1916, after the execution of the deed.

In these circumstances the question arose whether in computing for the purposes of Income Tax the profits of the Company for the tax year 1917–18 (which had of course to be based upon its profits for the three preceding years) the above-mentioned sum of £31,784 should be deducted from its receipts. The Commissioners held, on the authority of the case of *Hancock* v. *General Reversionary and Investment Company*(1), [1919] 1 K.B. 25, that this sum was an admissible deduction, and on the hearing of the Case stated by them their decision was affirmed by Mr. Justice Rowlatt; but on the appeal to the Court of Appeal the decision was reversed, and it was held that the deduction could not be allowed. Hence the present appeal.

My Lords, the material sections of the Income Tax Acts may be shortly stated. By the rules for ascertaining the duties to be charged in respect of a trade or manufacture under Schedule D of the Income Tax Act, 1842 (which was in force when the assessment in question was made), it was provided (by Case I, Rule 1) that the duty to be charged in respect thereof should be computed on a sum not less than the full amount of the " balance " of the profits or gains " of such trade or manufacture upon an average of three years, and should be assessed, charged, and paid " without other deduction than is hereinafter allowed "; (by Case I, Rule 3) that, in estimating the balance of profits and gains of a trade or manufacture so chargeable, no sum should be deducted from such profits or gains " on account of any " capital withdrawn therefrom, nor for any sum employed or " intended to be employed as capital in such trade or manu- " facture "; and (by Cases I and II, Rule 1) that no sum should be deducted " for any disbursements or expenses whatever not " being money wholly and exclusively laid out or expended for " the purposes of such trade or manufacture." It was also enacted (by Section 159) that in the computation of duty to be made in any of the cases mentioned in the Act it should not be lawful to make any other deductions than such as were expressly enumerated in the Act.

With reference to the provision last mentioned, and to the similar injunction contained in Rule 1 of Case I, it has been

(1) 7 T.C. 358.

(Viscount Cave, L.C.)

pointed out on several occasions, and particularly by Mr. Justice Scrutton in *Smith* v. *Incorporated Council of Law Reporting*(1), [1914] 3 K.B. 674, at page 681, and by Lord Parker and Lord Sumner in *Usher's Wiltshire Brewery* v. *Bruce*(2), [1915] A.C. 433, at pages 458 and 467, that the Act does not contain any express allowance or enumeration of deductions; and that effect can only be given to these provisions by holding that, when a deduction is proper to be made in order to ascertain the balance of profits and gains for any year, it ought to be made notwithstanding the First Rule applicable to Case I and Section 159, provided that it is not prohibited by the terms of the Act and Rules. From this it follows that in determining whether a particular item may or may not be deducted from profits, it is necessary first to enquire whether the deduction is expressly prohibited by the Act, and then, if it is not so prohibited, to consider whether it is of such a nature that it is proper to be charged against incomings in a computation of the balance of profits and gains for the year.

My Lords, I think it clear that the deduction from the profits of the above-mentioned sum of £31,784 is not prohibited by the First Rule applicable to Cases I and II, which prohibits the deduction of a disbursement not being money wholly and exclusively laid out or expended for the purposes of the trade. It was made clear in the above cited cases of *Usher's Wiltshire Brewery* v. *Bruce* and *Smith* v. *Incorporated Council of Law Reporting* that a sum of money expended, not of necessity and with a view to a direct and immediate benefit to the trade, but voluntarily and on the grounds of commercial expediency, and in order indirectly to facilitate the carrying on of the business, may yet be expended wholly and exclusively for the purposes of the trade; and it appears to me that the findings of the Commissioners in the present case bring the payment in question within that description. They found (in words which I have already quoted) that the payment was made for the sound commercial purpose of enabling the Company to retain the services of existing and future members of their staff and of increasing the efficiency of the staff; and after referring to the contention of the Crown that the sum of £31,784 was not money wholly and exclusively laid out for the purposes of the trade under the Rule above referred to, they found that the deduction was admissible—thus in effect, although not in terms, negativing the Crown's contention. I think that there was ample material to support the findings of the Commissioners, and accordingly that this prohibition does not apply.

Nor, in my opinion, is the prohibition contained in the third of the Rules applicable to Case I directly in point. The £31,784

(1) 6 T.C. 477, at p. 482. (2) 6 T.C. 399, at pp. 429 and 436.

(Viscount Cave, L.C.)

was not " capital withdrawn " from the trade, for it was not paid out of capital but out of the incomings of the year; nor was it (strictly speaking) a sum " employed or intended to be " employed as capital in " the trade, for it did not remain in the Company's hands but was irrevocably paid away to the trustees of the Pension Fund. It follows that, in my opinion, the express prohibitions contained in the Statute, although they may throw some light upon the intention of the Legislature, do not in terms apply.

But there remains the question, which I have found more difficult, whether apart from the express prohibitions, the sum in question is (in the words used by Lord Sumner in *Usher's* case(1)) a proper debit item to be charged against incomings of the trade when computing the profits of it; or, in other words, whether it is in substance a revenue or a capital expenditure. This appears to me to be a question of fact which is proper to be decided by the Commissioners upon the evidence brought before them in each case; but where, as in the present case, there is no express finding by the Commissioners upon the point, it must be determined by the Courts upon the materials which are available and with due regard to the principles which have been laid down in the authorities. Now, in *Vallambrosa Rubber Company* v. *Farmer*, 1910 S.C. 519, 5 T.C. 529, Lord Dunedin, as Lord President of the Court of Session, expressed the opinion that " in a rough way " it was " not a bad criterion of what is " capital expenditure as against what is income expenditure to " say that capital expenditure is a thing that is going to be spent " once and for all and income expenditure is a thing which is " going to recur every year "; and no doubt this is often a material consideration. But the criterion suggested is not, and was obviously not intended by Lord Dunedin to be, a decisive one in every case; for it is easy to imagine many cases in which a payment, though made " once and for all," would be properly chargeable against the receipts for the year. Instances of such payments may be found in the gratuity of £1,500 paid to a reporter on his retirement which was the subject of the decision in *Smith* v. *Incorporated Council of Law Reporting*(2), [1914] 3 K.B. 674, and in the expenditure of £4,994 in the purchase of an annuity for the benefit of an actuary who had retired which, in *Hancock* v. *General Reversionary and Investment Company*(3), [1919] 1 K.B. 25, was allowed, and I think rightly allowed, to be deducted from profits. But when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for

(1) 6 T.C. 399. (2) 6 T.C. 477. (3) 7 T.C. 358.

(Viscount Cave, L.C.)

treating such an expenditure as properly attributable not to revenue but to capital. For this view there is already considerable authority. Thus, moneys expended by a brewing firm with a view to the acquisition of new licensed premises (*Southwell* v. *Savill Brothers*(1), [1901] 2 K.B. 349); "flitting expenses" incurred in transferring a manufacturing business to new premises (*Granite Supply Association* v. *Kitton*, (1905) 8 F. 55, 5 T.C. 168); costs incurred in promoting a Bill which was dropped on the desired facilities being obtained by agreement (*A.G. Moore and Company* v. *Hare*, (1914) 6 T.C. 572); and expenditure incurred by a shipbuilding firm in deepening a channel and creating a deep water berth (not on their own property) to enable vessels constructed by them to put out to sea (*Ounsworth* v. *Vickers*(2), [1915] 3 K.B. 267), have been held to be in the nature of capital expenditure and not to be deductible under the Income Tax Acts; and *Rowntree and Company* v. *Curtis*(3), [1925] 1 K.B. 328, is to the same effect. I think that the principle to be deduced from this series of authorities rests on sound foundations and may properly be adopted by this House.

My Lords, in my opinion the present case falls within the same principle. The payment of £31,784, which is the subject of dispute, was made, not merely as a gift or bonus to the older servants of the Appellant Company, but (as the deed shows) to "form a nucleus" of the Pension Fund which it was desired to create; and it is a fair inference from the terms of the deed and from the Commissioners' findings that without this contribution the Fund might not have come into existence at all. The object and effect of the payment of this large sum was to enable the Company to establish the Pension Fund and to offer to all its existing and future employees a sure provision for their old age, and so to obtain for the Company the substantial and lasting advantage of being in a position throughout its business life to secure and retain the services of a contented and efficient staff. I am satisfied on full consideration that the payment was in the nature of capital expenditure, and accordingly that the deduction of the amount from profits, although not expressly prohibited by the Act, was rightly held by the Court of Appeal not to be admissible.

For these reasons I move your Lordships that this appeal be dismissed with costs.

Lord Atkinson.—My Lords, the facts of this case have been already fully stated; I abstain from repeating them save so far as may be necessary to make my judgment intelligible. I am of opinion that the sum of £31,784 paid by the Appellants to the trustees of the trust deed of the 8th of August, 1916, to be

(1) 4 T.C. 430. (2) 6 T.C. 671. (3) 8 T.C. 678.

(Lord Atkinson.)

employed by them in the manner, for the objects, and under the conditions in the deed set forth, was money wholly and exclusively laid out and expended for the purposes of the Appellants' trade, manufacture, adventure or concern, within the meaning of the First Rule applicable to Cases I and II under Schedule D, Section 100, of the Income Tax Act of 1842, and therefore that the deduction of this sum from the balance of the gains and profits of the Appellants' trade, realised in the years in which the payments were made, was not prohibited by this Rule. But a careful examination of the provisions of the trust deed, coupled with the facts found, has convinced me that the payment of this large sum of money to these trustees for the purposes of the trust amounted to an actual employment or intended employment of it as capital in the Appellants' trade, manufacture or adventure or concern within the meaning of the Third Rule of Case I of Schedule D, quite as much as if it had been devoted to the purchase in fee of recreation fields or bath houses to improve the health of their staff or of a library to increase their knowledge or discipline their minds. The use and enjoyment of these last-named things by the staff might, not unnaturally, make them more contented, more attached to their employers' service, and consequently more efficient than they otherwise would have been, and their employers would in this way be rewarded for their outlay; but if a portion of the profits and gains of the employers' trade and business, received in the year in which those things were acquired, was devoted to their acquisition it would, *prima facie*, I think, lead to an employment of their cost as capital, or an intended employment of it as capital, the deduction of which from the above-mentioned profits and gains for Income Tax purposes is prohibited by this Rule 3 of Case I of Schedule D of the Income Tax Act of 1842. The authorities do not supply any clear, precise, and sufficiently comprehensive definition of the operation styled a capital investment for the purposes of the Income Tax Acts. In the case of the *Royal Insurance Company* v. *Watson*(1), [1897] A.C. 1, the Appellant Company were by statute empowered to acquire and, in fact, did acquire from the Queen Insurance Company, their whole undertaking, which was regularly transferred to the purchasing Company on the 19th of August, 1891. The agreement into which the two Companies had entered for this purpose provided, amongst other things, that the purchasing Company should, until the transfer was completed, retain in their service the former manager of the Queen Insurance Company at a salary of £4,000 per annum. Liberty was reserved, however, to the purchasing Company to commute this salary by payment of a bulk sum calculated on the basis of certain tables in the agreement

(1) 3 T.C. 500.

(Lord Atkinson.)

mentioned. The purchasing Company availed themselves of this liberty and, shortly after the manager had been taken into their service, commuted this salary by payment to him of the sum of £55,846 8*s*. 5*d*.

The Royal Insurance Company contended that they were entitled, in fixing the amount of their liability to assessment for Income Tax for the year ending April 5th, 1893, to deduct this large sum from the gains and profits of the business for the year 1891–1892, the year in which the payments had, in fact, been made. The Court of Appeal, [1896] 1 Q.B. 41, held that the Company were not entitled to make this deduction, and on appeal to this House that decision was affirmed on the ground that this large sum of money was, in reality, part of the consideration to be paid by the purchasing Company to the vending Company for the transfer by the latter to the former of the latter's business, and was, therefore, money employed as capital within the meaning of the aforesaid Rule 3. Lord Halsbury, in delivering judgment, said, page 6(1): "It is often a very "difficult question to ascertain, in dealing with a commercial "account, what is capital and what is income, but, if it is "established as a fact that the expenditure is capital, the "language of the statute itself determines that that expenditure "cannot be deducted from the profits, and that the profits are "to be ascertained without reference to the capital expenditure." It was, as I understood, suggested in this case during the argument of this appeal, that the sum of £31,784 paid by the Appellant Company to the trustees of the trust deed of the 8th of August, 1916, was precisely of the same nature and character as the payment of one-half of the aggregate amount of the subscriptions of the members of the Appellants' staff to the Pension Fund, made monthly by the Appellants to the Trustees, and as this monthly payment was obviously a recurring payment and not capital expenditure, so must the payment of the sum of £31,784 be treated as a recurring payment though, in fact, made once for all.

One of the two principal questions raised upon the appeal, however, is whether the payment made once and for all of this large sum to secure the solvency of the Pension Fund amounts to a real or intended employment of capital. I am quite unable to see how the recurring monthly payment by the same Company of a sum—possibly varying in amount from month to month—can infect, as it were, the payment of the larger sum, so as to convert the payment of each into matters of the same nature and character.

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(1) 3 T.C. at p. 503.

(Lord Atkinson.)

Lord Herschell, in the *Royal Insurance Company's* case, concurred with Lord Halsbury. He, at page 8(1), said that this payment of the sum between fifty and sixty thousand pounds was " made in pursuance of the obligation contained in the contract " by which the business of the Queen Insurance Company was " purchased and, therefore, is properly capital expenditure."

Lord Macnaghten held that the payment of this same large sum was a payment on account of capital, and Lord Davey held that it, in fact, formed part of the consideration for the purchase of the Company's business and connection, and that being so, the point was sufficient for the decision of the case. It will be observed that no question was raised as to the source from which the sum paid to the manager was obtained, no suggestion was made that it was obtained from capital withdrawn from the business of the Appellants. The natural conclusion from the reports of the case would appear to be that it was paid out of the gains and profits of the year in which the payment was made. In the argument of the present appeal your Lordships' attention was not drawn to any case in which what was claimed to be a precise, full and accurate definition of the phrase " capital " expenditure " was given. Lord Dunedin, however, in the case of *Vallambrosa Rubber Company* v. *Farmer*, 1910 S.C. 519, and 5 T.C. 529, when dealing with the expenses incurred every year in weeding and tending certain rubber trees on the lands of the Company which trees had not reached the rubber-bearing age, said (2) : " I do not say that this consideration is absolutely final " or determinative; but in a rough way I think it is not a bad " criterion of what is capital expenditure to say that capital " expenditure is a thing that is going to be spent once and for all, " and income expenditure is a thing that is going to recur every " year." This rough test (Lord Dunedin did not pretend it was more than that) has been approved in many cases as though a rough, yet an effective test, and I cannot find any case in which it has been disapproved of. In the case of *Ounsworth* v. *Vickers, Limited*(3), [1915] 3 K.B. 267, Mr. Justice Rowlatt appears to have approved of and adopted it, saying, however, " I take it, " and indeed both sides agree, that no stress is there laid upon " the words ' every year ' ; the real test is between expenditure " which is made to meet a continuous demand, as opposed to an " expenditure which is made once for all."

Much assistance is not to be gained in this case from the judgment of Mr. Justice Scrutton (as he then was) in the case of *Smith* v. *The Incorporated Council of Law Reporting*(4), [1914] 3 K.B. 674. The question for decision there related to a gratuity of £1,500 given by the Respondent Society to a member of their reporting staff on his retirement after long

(1) 3 T.C. at p. 505. (2) 5 T.C. at p. 536. (3) 6 T.C. 671, at p. 675. (4) 6 T.C. 477.

(Lord Atkinson.)

service. The Commissioners had held that this sum of £1,500 was allowable to the Respondents as a business expense in calculating for Income Tax purposes the profits of the year in which it was paid. On a Case stated by the Commissioners, it was held by Mr. Justice Scrutton that the question whether this sum could be deducted from the Respondents' profits as being " money wholly and exclusively laid out for the Respondents' " business " within the meaning of Rule 1 applying to the First and Second Cases under Schedule D, was a question of fact for the Commissioners to decide, and that as there was evidence before them adequate to support their finding of fact their decision was not a matter which could be reversed upon appeal, even although the appellate tribunal might itself have come to a different conclusion upon the evidence given.

In *Usher's Wiltshire Brewery* v. *Bruce*(1), [1915] A.C. 433-4, 456 and 466, the tenants of the Appellant's tied houses were under their agreement bound to repair their houses and to pay certain rates and taxes. They failed to do so. The Appellant Company, though in no way legally or morally bound to do so, paid for these repairs, and paid these rates and taxes. They did so, not as a matter of charity, but of commercial expediency, in order to avoid the loss of their tenants, and consequently the loss of the market for their beer, which they had acquired those houses for the purpose of affording.

It was held that, though the Appellant Company were not legally or morally bound to make those payments, yet they were, in estimating the balance of the profits and gains of their business for the purposes of assessment of Income Tax, entitled to deduct all the sums so paid by them as expenses necessarily incurred for the purposes of their business.

There is no suggestion in the present case that the Appellant Company was bound by a similar necessity to pay the sum of £31,784, or any portion of it to the trustees to carry out the pension scheme.

I now turn to the trust deed of the 8th of August, 1916. First, the payment of the sum of £31,784 was made once for all. It was made to secure that the Pension Fund should be adequate to meet the claims of the older members of the staff on their retirement before the contributions of all the contributors had amounted to a sum adequate to meet those claims—a laudable object, no doubt, and perhaps a prudent one in the interests of the Company's trade.

Second, it was optional with the eligible members of the Appellants' staff to join the scheme, as it is styled, or not, even if their respective salaries amounted to £100 per annum. From the salary of every member who joined, 5 per cent. was to be

(1) 6 T.C. 399.

(Lord Atkinson.)

deducted by the Company monthly and paid over monthly to the trustees of the deed to be added to the Pension Fund. In addition, as I have already pointed out, the Company paid monthly to the trustees for the same purpose one-half of the aggregate amount of these contributions. These are the only recurring payments made to the credit of the Pension Fund. They are, I think, irrelevant to the question for decision touching the payment of the larger bulk sum. Next the Appellant Company are, by the terms of the deed, almost altogether deprived of all direction or control over the management, administration or application of the Pension Fund; so much is that the case, that by the 23rd clause of the deed it is provided that if a resolution should be passed, or an order made for the winding up of the Company and neither the Government nor any other company or body should within six months from the date of the resolution or order undertake the obligations of the Company under the deed, two actuaries are to be appointed, one by the directors' trustees and the other by the staff's trustees, who are to decide in what manner the Fund (i.e., the Pension Fund) should be divided among the members of the Fund or such of them as shall be living or in receipt of retiring pensions, the first charge upon the Fund being the return to the members of all sums contributed by them with interest at 4 per cent. The decision of these actuaries, it is provided, is to be final and binding on all parties concerned. The Fund is not treated as part of the assets of the Company. The debts of the Company due to their creditors are not to be satisfied out of it to any extent. Again, the trustees have absolute power to invest all money in their hands not required for the time being in making payment of pensions in such securities as they may deem fit. They are empowered to pay the pensions allowance as far as may be necessary out of the capital of the Fund. There is to be an actuarial valuation of the position of the Fund every five years from the 1st January, 1916, or at such other period as the trustees may determine. If, as a result of the actuaries' report, there should appear to be a surplus beyond the requirements of the Fund, that surplus or any part of it may be set aside and invested by the trustees as a reserve fund. If, on the other hand, there should appear to be a deficiency, that is to be made good in such manner as the trustees may determine. By the 14th clause it is provided that the business of the trust is to be managed by the trustees or a majority of such of them as may be present at their meetings, and all powers, expressly or by implication given to the trustees, may be exercised by this majority. The trust deed contains many other provisions supporting the conclusion that the Company have once and for all parted with all proprietary rights in, and all powers over, this donation of £31,784.

(Lord Atkinson.)

It is difficult to see on what principle the Company are, for the purposes of the assessment of Income Tax for the year in which the payment was made, entitled to deduct it from their profits and gains for that year, since it cannot, I think, be regarded as forming part of the cost by which those profits and gains have been acquired, nor as an expenditure which, however prudent from the employers' point of view, was essentially necessary for the acquisition in that, or any subsequent year, of any portion of the profits and gains of the Appellants' business. It would certainly appear to me not to be—to adopt Lord Sumner's phrase used by him in his judgment in *Usher's Wiltshire Brewery, Limited* v. *Bruce*(1)—" a proper debit item to " be charged against incomings of the trade when computing the " balance of the profits of it." That is apparently the view of it taken by Lord Justice Warrington. At page 44 of the appendix in the present case(2) he said : " The real question which we have " to determine is whether this is a proper debit item to be charged " against the incomings of the trade when computing the balance " of profits." He held it was not a proper debit item. Lord Justice Scrutton, after pointing out that the Attorney-General's definition of capital expenditure, namely, " money expended " upon a business which is intended to, and does, create an " asset is capital," cannot apply to the circulating capital of a trade or business, holds that the payment of this large sum of £31,784 by the Company, which they were not under any liability to make, was either a withdrawal of capital from the business for the purposes of the Fund, or capital employed in creating an asset or advantage in the business, something added to the business not in discharge of any existing liability but, in the result, creating a new asset. If the word " asset," as used in this connection, be confined to something material—and I do not think it well can be so confined—then I am inclined to agree with Lord Justice Scrutton that, if the existence of this Pension Fund results in making the staff of the Company more contented and less inclined to change their service and therefore, on the whole, more efficient, these results when secured would amount to an " asset " of the Company's business. The Master of the Rolls expresses the same idea at the end of his judgment, in the following words : " It appears to me that when you consider " what is the nature of this payment made, not for the purpose " of meeting any actual liability, but only for the purpose of, in a " very general way, improving the position of the staff, the right " attribute to apply to it is that it was a payment made as and " for the purpose of a capital outlay and cannot be deducted " from the revenue as a payment made in the course of seeking " profits and gains." *Rowntree's* case at 8 T.C. 678 is quite distinguishable from this.

(1) 6 T.C. 399, at p. 436. (2) Page 183 *ante*.

(Lord Atkinson.)

In the case of *Hancock* v. *The General Reversionary and Investment Company*(1), [1919] 1 K.B. 25, Mr. Justice Lush, at page 37 of the report, after commenting upon Lord Dunedin's decision, acted upon by Mr. Justice Rowlatt in *Ounsworth* v. *Vickers*(2), [1915] 3 K.B. 267, said, quoting Mr. Justice Rowlatt : " ' The proper test to apply is this : Was the expenditure—i.e., " ' the money paid to an insurance company to purchase an " ' annuity for an actuary long in their service—incurred in order " ' to meet a continuing business demand, in which case it " ' would be treated as an ordinary business expense, a deduction " ' of which was admissible; or was it an expenditure incurred " ' once for all, in which case it should be treated as a capital " ' outlay? ' " And he says : " I agree with that view,"—and he then proceeds to state the ground upon which he comes to the conclusion that the payment of £4,994 fell within the former class of payments and not the latter, and says : " Apply- " ing that test, I think that it necessarily follows that the " £4,994 should be treated, as the pension was treated, as an " ordinary business expense, and that the deduction should be " allowed. It is the pension in another form; it is actuarially " equivalent in value and it is identical in character. It was " paid to meet a continuing demand which was itself an ordinary " business expense, as the Surveyor had treated it." I cannot find that this reasoning was ever expressly approved of in any authority. The learned Judge apparently treats the payment of this large sum as if it were made by the Company to one of its employees. Little assistance is to be got from *Rowntree's* case(3) and other cases owing to the special findings of the Commissioners on several questions of fact. On the whole I think the judgment appealed from was right and should be affirmed and this appeal be dismissed with costs.

Lord Buckmaster.—My Lords, the facts in this case have already been stated; they do not admit of ambiguity and their repetition is needless. The sole question for decision is whether the contribution of £31,784 made for the purpose and in the circumstances already narrated can be deducted from the profits earned by the Appellants in their business for the year ending 5th April, 1918. The determination of this question depends upon the true meaning of the rules in Schedule D to the Act of 1842. The first and paramount provision is : that the duty to be charged shall be computed on a sum " not less than the full amount of " the balance of the profits and gains " of the trade on a fair and just average for three years. In ascertaining this result there are certain restrictive conditions imposed by the succeeding rules—one prevents any deduction for any disbursements " not being " money wholly and exclusively laid out or expended for the

(1) 7 T.C. 358, at p. 371. (2) 6 T.C. 671. (3) 8 T.C. 678.

(Lord Buckmaster.)

" purposes of the trade "; and another prevents allowance on account of capital withdrawn from the trade, or " for any sum " employed or intended to be employed as capital in such trade." It is, I think, plain upon the findings of fact of the Commissioners that the moneys in question in this case were exclusively laid out for the purposes of the trade—this view is emphatically asserted by Lord Justice Warrington and assented to by the Master of the Rolls. No difficulty arises in this connection. Whether this money should be treated as capital withdrawn from the business or intended to be employed as capital in the business, it is not, in my opinion, necessary to decide, for I agree with Lord Justice Warrington that the real difficulty lies in considering whether the deduction can be made in arriving at the full amount of the balance of profits and gains. In order to examine this question it appears to me that the different contributions to the scheme are not really material—the principle involved would be the same if there were no contributions other than those provided by the employers themselves and they had started and financed this scheme at their own sole cost. So tested I cannot think that this sum, which represents an amount set apart as the nucleus of the Pension Fund, can be properly deducted in determining the balance of the profits and gains. Authorities appear to me to be of little assistance; the *Rowntree* case(1) is different, as the money there was set apart for charitable trusts in which ultimately others than those connected with the business might become the beneficiaries; and the *Hancock* case(2) is nothing but the payment in one sum of an annually recurring liability and is closely analogous to the case of the *Incorporated Law Society*.(3) But neither in their facts nor in their reasoning does it seem to me that these authorities govern the present case.

In my opinion this appeal should be dismissed.

Lord Carson.—My Lords, it was not contended, nor in face of the findings of the Commissioners could it have been successfully argued, that the sum in question was not money " wholly " and exclusively laid out or expended for the purposes of the " trade," and indeed it is under modern views and conditions not only a proper but essential expenditure for carrying on any properly organised business; and that being so the question which has to be determined is whether it is a proper legal deduction to be made in arriving at the " full amount of the balance of profits " and gains." Of course, as Lord Buckmaster points out, if the sum in question cannot be properly deducted in determining the balance of profits and gains, there is no necessity to consider whether this money should be treated as capital withdrawn from the trade or intended to be employed as capital in the trade But as I do not take the same view of this expenditure as my

(1) 8 T.C. 678. (2) 7 T.C. 358. (3) 6 T.C. 477.

(Lord Carson.)

noble friend, I think it necessary to state that I can find no grounds (and here I find myself in agreement with the noble Viscount on the Woolsack) for holding that the sum in question comes within either of the said categories. It is clear from the terms of the trust deed, as already pointed out, that in no sense was the sum an investment, that it would be eventually exhausted in payment of the pensions and that in the event of a winding-up of the Company it could never form any part of the assets of the Company. I cannot, under these circumstances, conceive any system of commercial accountancy under which this sum could ever appear in the capital accounts of the Company. Nor is it capital withdrawn from the business as it was admittedly paid out of the earnings of the year. It is not disputed that an annual sum contributed to the Pension Fund on an actuarial basis for the purposes of making the Fund solvent for paying the pensions of the older members of the staff would be a proper deduction in arriving at the balance of profits and gains; it would be an ordinary business expense. Nor, I think, can it be disputed that if at any time the Fund threatened to become insolvent after it was started a sum paid to prevent such insolvency would be a proper disbursement in arriving at the balance of profits and gains. Why, therefore, should the payment of the sum in question, which by an actuarial calculation represents the sum equal to the annual payments which would be necessary, not be considered as in the same position? To use the words of Mr. Justice Lush in *Hancock's* case(1), [1919] 1 K.B. 25, which was the case of a lump sum paid in purchasing an annuity in lieu of an annual pension, "It is the pension in another form; it is "actuarially equivalent in value and it is identical in character. "It was paid to meet a continuing demand which was in itself "an ordinary business expense." Or as expressed by the Master of the Rolls in *Rowntree's* case(2), [1925] 1 K.B. 328: "Then," he says at page 336, "we come to another class of cases in which "an expenditure is made on business grounds of a sum, "apparently a capital sum, but which really comprises and com- "presses what is an annual charge." My Lords, I agree with their statements of principle, and in my opinion they are entirely applicable to the present case. Indeed a careful comparison of the reasoning on which the judgments are founded in these two cases greatly helps to determine on which side of the line such an expenditure should be placed. I can find no reason for holding that a payment made to make up the contribution to a sufficient sum to enable the older servants of the Company to enjoy the benefits of the Pension Fund brings into existence an asset or an advantage for the enduring benefit of trade and might therefore be attributed not to revenue but to capital. I notice that my noble

(1) Hancock v. General Reversionary and Investment Company, 7 T.C. 358, at p. 371.
(2) Rowntree & Company v. Curtis, 8 T.C. 678, at p. 697.

(Lord Carson.)

friend on the Woolsack agrees with the decision in *Hancock's* case as I also do, but I fail, as Mr. Justice Rowlatt failed, to see how it can in principle be distinguished from the present case. I am of opinion that this appeal should be allowed.

Lord Blanesburgh.—My Lords, it is, I apprehend, now well settled that in the Income Tax Acts, unless the context requires a different meaning to be placed upon them, such words as "profits," "gains," "capital," are to be construed according to their ordinary signification in commerce or accountancy. It will accordingly not be amiss if, remembering the nature of the present controversy, an attempt be made to ascertain from the statements or accepted implications of the Stated Case, but, in the first instance, merely as a business proposition, what was the precise nature and purpose of the payment now in question and, as consequent thereon, its proper place in this Company's accounts.

Up to 1916 the clerical and technical staff of the Company had no superannuation fund existent for their benefit. The lack of one had in practice proved disadvantageous to the Company in several ways. With no continued provision in prospect for their old age, experienced members of its staff had been prone to leave the service for appointments elsewhere more attractive in this regard; and the natural anxiety of those who remained as to their financial position after retirement was not without its effect both upon their contentment and their efficiency. The existence of a pensions fund built up by their own contributions would assist, and, if these contributions were supplemented by additions to be made to them by the Company, would, it was expected, succeed in remedying this state of things. The fund would constitute a strong inducement to the individual contributories to remain during their working lives in the Company's service, and it would tend to their increased efficiency while they so remained.

It was no part of the Attorney-General's case that this was not a reasonable expectation. That the Company's action in this matter was not prompted by anything more altruistic than an enlightened self-interest well calculated to secure for its business as a profit-earning concern and for itself as a good employer the advantages already indicated, the Attorney-General was not concerned to dispute.

Now, expenditure by a trading company of which so much can be affirmed is well within its powers, whether expressly so conferred or not. This is no longer doubtful. Indeed, since the case of *Hutton* v. *West Cork Railway Company*, 23 Ch.D. 654, in which both the *rationale* of the power and its limitations are clearly expounded, this matter has ceased to be debatable. Modern conditions of industry have only tended to make the occasions for its exercise more frequent and more compelling. For myself, I cannot escape the conviction that, if the action of

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the Company in this matter had been seen to be, as in my judgment it clearly is, no more than a striking illustration of the legitimate exercise of its inherent powers as in that judgment described, this case would have been shorn of much of the difficulty which it has presented to those who have regarded it from another angle.

In 1916 the pension which by means of the fund then in contemplation was to be provided for each participant on retirement at 65 was one-sixtieth of his average salary for every year of his service with the Company. And there were to be other benefits. It was believed that if the contributions required of them were not made prohibitive, 300 at least of the Company's then salaried staff would join a fund offering such advantages. It was, of course, of the essence of the scheme that in adequate numbers they should. Practical abstention on their part would have destroyed the whole *raison d'être* of the fund so far as the Company's participation in it was concerned. The necessity of securing their adhesion to it from the Company's point of view explains the specially attractive terms which were offered them. In the case, for instance, of future members of the staff who were to be required to join the Fund as part of their contracts of service, only those under 40 at the date of joining were, under deduction from their salaries of so little as 5 per cent., to be entitled to the benefits of the Fund. Not so the existing members of the staff. They were at that minimum cost to themselves and irrespective of age to be admitted as full participants; and, not only so, but their service with the Company prior to the establishment of the Fund, and when, of course, no payments towards it were being made by them, were to rank as pension years of service. Now, happily as many will think, the time has gone by when terms like these are, in such a connection, to be viewed even by a tax gatherer with jaundiced eyes. Here however it is not even suggested that they were more attractive than the occasion required. They could not, however, without a contribution to the Fund made specially on account of these employees have been fulfilled. A fund composed alone of the proposed future contributions and offering these benefits would from its very inception have been actuarially insolvent. The contribution of £31,784, with which your Lordships are now concerned, was the payment actuarially calculated to be requisite, and it was in the event made by the Company to avoid that result.

On the 8th August, 1916, the Company executed the trust deed constituting the Fund and it thereby covenanted with the trustees to make the following payments:—(*a*) The sum now in question. (*b*) An annual contribution aggregating one-half of every sum in the same year contributed by each participant employee. (*c*) A contribution sufficient to make the annual return upon the invested moneys of the Fund one of 4 per cent.

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This third contribution does not enter into the argument and need not again be referred to. With reference to the other two, however, it is well nigh vital to ascertain what they really represented and what under the trust deed was the duty of the trustees in relation to them when received.

The sum with which your Lordships are immediately concerned, this £31,784, represented the actuarial equivalent of the sum with accretions of interest which would at the date of the establishment of the Fund have been in the hands of its trustees if there had in fact been made by or on account of each of these participant members during each of the previous years of service for which he was to rank for pension the payments which would have been called for had the Fund then existed. It was a payment by the Company on account of each of these employees of a sum which in the language of the Master of the Rolls in *Rowntree's* case(1), [1925] 1 K.B. 328, 336, comprised and compressed a series of prior annual payments on his account. It was a sum, and this is perhaps in the present connection its most important characteristic, actuarially so adjusted in amount that when the last of the existing staff, participant to the Fund, on whose account it had been paid, died or fell out of benefit no part of it or of any accretion to it would remain in the hands of the trustees. It would then have been entirely exhausted in providing the covenanted benefits for the participants on whose account it was paid. It is as if the Company, as it might well have done, had paid this money to the trustees of a pension fund, otherwise identical in its provisions and benefits with that constituted, but in which only then existing members of the staff were to be participant. On the death of the last of these the trustees actuarially would be left with no funds at all. In no sense was this £31,784 the permanent capital of any fund.

As to the annual contributions made, as these were to be, on account of every participant member of the Fund, present and future, what is important to note about them is that it was the duty of the trustees, as with the first sum, to invest and accumulate them when received so far as they were not required to meet current outgoings of the Fund. In other words, there was to be no distinction at all between the way in which the trustees were to deal with payment (*a*) and with payments (*b*) when made and received. All contributions received by them became, on receipt, indistinguishably blended.

My Lords, if what I have so far said be accurate, it follows that in no relevant respect do these payments (*a*) and (*b*) differ from one another. What, then, is the outstanding characteristic of all of them? It is, I think, this, that they are made by the Company for the account, as to the first payment, of some, as to

(1) Rowntree and Company v. Curtis, 8 T.C. 678, at p. 697.

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the later payments, of all of its participant staff employees; made, it is true, in a special form to secure a special end, but, from the Company's side, when regard is had to their purpose, made with the same justification that would attend the payment of an increased remuneration of the individual employees benefited. Regard, in retrospect, after his retirement, the proportion of these payments made by the Company on account of any individual participant. In no material respect, *quoad* the Company, do they differ from any payments of salary made to him direct. In truth, we have here a much plainer case than that of *Hancock*(1). There the payment was made in respect of an officer who had retired. The main justification suggested for it was the protection of the Company against recurrent demands. Here the payments are made on account of officials still in the service, and are made that that service may be more contented, more efficient and more prolonged. Can any higher warrant than this for the payment of any staff salary be suggested?

And it is admitted by the Crown that the Company's periodical contributions (*b*) are all of them properly chargeable to revenue account. But why so? Surely, because they are not only, as I have, I hope, shown, legitimate payments, but because, as such, they are none other than expenses prudently incurred in the course of the Company's business. And such, too, is payment (*a*)—this sum of £31,784. Payments (*b*) are additional remuneration for every one of the participant members of the Fund, proportioned in each case to his own contribution to it. Payment (*a*) is still further remuneration, in no way commercially excessive, for those of them who when the Fund was established were already in the Company's service, and proportioned in each case to the amount of his salary for the time being.

I do not myself see how any of these payments could properly be charged to capital account by any company which keeps its accounts on the double account system. And as the Income Tax Acts contemplate that accounts will be so kept, no other system need here be considered. Under that system, as is well known, the two accounts, capital and revenue, or trading account, as in business language it is usually termed, are separate accounts. The capital account is concerned with the company's fixed capital and its applications. The revenue account is concerned with the company's trading or circulating capital and its application. Dividends may lawfully be paid, although, it may be, the whole of the company's fixed capital has disappeared. No profits available for dividend are, however, existent, unless the company's trading capital would remain intact after they had been distributed as such. If what I have so far said be correct, it follows that for this Company to have charged any of these payments,

(1) Hancock v. General Reversionary and Investment Company, 7 T.C. 358.

(Lord Blanesburgh.)

either (*a*) or (*b*), to capital account would have thrown on that account a revenue charge; would have enabled the Company to ascertain profits and distribute dividends without taking it into account; would have introduced a system facilitating in the case of a company, less prosperous, the concealment more or less successful of the truth, that the dividends declared during a period of depression were in whole or in part being paid out of capital.

My Lords, on the facts of this case there were, as it seems to me, only three funds from which any of these payments (*a*) or (*b*) could, by such a company as this, legitimately have been taken. The first was its undistributed profits—the payments, if thence derived, being no more than a series of bonuses to its employees out of the realised profits of good years. The second was its gross receipts before profits were struck. The third, merely another aspect of the second, and not applicable to this prosperous Company, was working capital to which recourse might properly be had on any occasion when the gross receipts after these payments had been charged against them were less than the outgoings by at least an equivalent amount.

Applied to this Company, on the facts found, there is, as to the first of these, no suggestion of any intention on its part to make these payments out of realised profits. The unqualified covenant into which it entered with regard to them would have effectively disposed of such a suggestion had it been made.

As to the third, the gross receipts, as I have indicated, were more than adequate to meet the payments and still leave a large surplus.

The revenue account, therefore, strictly so called, alone remains as the place in which they can properly appear.

As to the suggestion that the £31,784, representing the notional payments made over a number of years, must be treated as capital because that sum was paid in one year and in one amount, I find myself in entire agreement with Mr. Justice Lush, when in *Hancock's* case[1], he said ([1919] 1 K.B. 25, 37): "It seems to me as impossible to hold that the fact that a lump "sum was paid instead of a recurring series of annual payments "alters the character of the expenditure, as it would be to hold "that, if an employer made a voluntary arrangement with his "servant to pay the servant a year's salary in advance instead "of paying each year's salary as it fell due, he would be making "a capital outlay."

For these reasons I cannot bring myself to doubt that this payment of £31,784, judged of purely as a commercial transaction of this Company and not purporting or intended to be a bonus out of profits, could only properly be brought into charge, as in fact it was, in the revenue account of the Company.

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[1] 7 T.C. 358, at p. 372.

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And if this be the true conclusion, apart from the Income Tax Acts, the propriety of this payment as an admissible deduction in the ascertainment of the balance of the Company's profits and gains under these Acts follows, I think, almost as of course.

My Lords, I will substitute for any re-statement of the relevant provisions of the statutes, already well under your Lordships' notice, two authoritative pronouncements as to their effect. "Profits and gains," said Lord Loreburn, in the case of *Usher*(1), [1915] A.C. at page 444, "must be estimated on ordinary "principles of commercial trading by setting against the income "earned the cost of getting it subject to the limitations prescribed "by the Act."

"The effect . . . I think, is this," said Lord Sumner in the same case, at page 468(2), "that the direction to compute the full "amount of the balance of the profits must be read as subject "to certain allowances and to certain prohibitions of deductions, "but that a deduction, if there be such, which is neither within "the terms of the prohibition nor such that the expressed allow-"ance must be taken as the exclusive definition of its area, is "one to be made or not to be made according as it is or is not, "on the facts of the case, a proper debit item to be charged "against incomings of the trade when computing the balance of "the profits of it."

To these I will add three further statements as to the true result of the Acts in matters relevant to the present discussion. The first, justified by reference both to *Usher's* case and to the judgment of Lord Dunedin, when Lord President, in the *Vallambrosa* case, 5 T.C. 529, is that the fact that the expenditure in question is not referable to the profits of the year in which it is made does not prevent it from being a proper deduction in that year. The second, justified also by *Usher's* case, is that the admissibility of a deduction under the Act is not dependent upon the question whether, at the time the payment was made, the subject was under legal liability to make it. Payments, justifiable on the principle of *Hutton's* case(3), already cited, are well within the limits of admissibility. The third, justified by some observations in the judgment of Lord Justice Scrutton in the present case which command my entire concurrence, is that the reference in Rule 3 of Case I in Section 100 of the Act of 1842 to "capital" withdrawn from or employed in the trade is a reference to fixed capital, as distinct from "circulating" or, in Lord Watson's phrase, "trading" capital, the proper source for payment of wages and other expenses incurred in the conduct of a trader's business. See *Gresham Life Assurance Society* v. *Styles*(4), [1892] A.C. 309, 318.

(1) Usher's Wiltshire Brewery, Ltd., v. Bruce, 6 T.C. 399, at p. 419.
(2) *Ibid.* at p. 436.
(3) Hutton v. West Cork Railway Company, 23 Ch.D. 654. (4) 3 T.C. 185.

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Bearing these authoritative considerations in mind, I proceed now to apply the relevant prohibitions of the Acts to this payment, and I ask myself first whether there is any ground for affirming that this money was not laid out or expended wholly and exclusively for the purposes of this Company's trade, manufacture, adventure or concern? The answer must, I think, be in the negative. The explanation already given of the circumstances in which, and the object for the attainment of which, the payment was made leaves no doubt in my mind on this point, and I believe all your Lordships take the same view. I notice that the Master of the Rolls, for the purpose of his judgment only, and clearly with some reluctance, accepts it. I am myself unable to share his doubts on this point.

I next ask myself whether it is true to say that this payment represented " capital withdrawn from or any sum employed or " intended to be employed as capital " in the Company's trade? Again, I think the answer must be in the negative. Mr. Hills, in his able argument on behalf of the Crown, while disclaiming any desire to attach too much weight to the contention, found in clause 3(*a*) of the trust deed of the Fund, by which the Company covenanted to pay this sum to the trustees " in order to provide " the capital sum necessary in order that past years of service of " the present permanent staff since they received a salary of £100 " per annum or more shall rank for pension," an indication that this was on the part also of the Company a payment on capital account. The suggestion strikes me as novel. I cannot myself see how that which really is a revenue payment on the part of the trader making it—whether it is so or not is of course a question—can become a capital disbursement merely because the recipient invests it or, if you like, agrees to invest it, any more than I can see how that which was a capital payment on the part of the payer becomes a revenue payment merely because the recipient spends it or is left at liberty to spend it. Moreover, the application of this principle to the present case would, in view of the terms of this trust deed, equally extend to the Company's periodic payments all of which the Crown agrees and even asserts are properly chargeable to revenue.

And the difficulty of treating this as a capital disbursement of the Company is appreciated when the divergent grounds on which the Master of the Rolls and Lord Justice Scrutton held it so to be are regarded. In the view of the Master of the Rolls this payment not being " a necessary expenditure in seeking profits " and gains," was only made at all because the Company had a good year; if they had had a bad year they would not have made it, " still less would they have charged it on ordinary " principles to the revenue account . . . therefore . . . it ought " to be treated as being an item of capital to be employed as capital

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" in such trade." My Lords, I demur *in limine* to the statement that a disbursement admissible as a deduction must be a " necessary " expenditure in seeking profits. *Usher's* case(1) I think clearly indicates that it suffices, in this regard, if it be prudent in the proper and reasonable conduct of the trade. One has only to recall in this connection advertising expenditure. But, my Lords, even if the premises be conceded, I cannot myself see that the conclusion follows. The learned Master of the Rolls might, possibly, consistently with his premises have well held that this payment was in truth a bonus out of realised profits and not an expense incurred with a view of maintaining them in the future. That, however, was not open to him on the Case Stated. That they lead to the conclusion that the payment is one either withdrawn from or to be employed as capital—as fixed capital *bien entendu*—seems to me to be quite inadmissible.

Lord Justice Scrutton, to whose views as to the meaning of the word " capital " in the Statute I have already referred, holds that the sum should be disallowed because as a result of the expenditure " either capital was withdrawn from the business " for this Pension Fund or the capital employed in the business " created an asset or advantage of the business "—by which expression, as the Lord Justice explains in another part of his judgment, he means " something in the nature of fixed capital." Now, my Lords, this method of arriving at the same result as the Master of the Rolls is, in my judgment, equally open to destructive criticism. In no sense of the word " capital," circulating, working or fixed, did this expenditure involve any withdrawal. It was made out of gross receipts in a year in which working capital and, *a fortiori*, fixed capital remaining intact, a large surplus still emerged. Nor, in my judgment, did the expenditure in any relevant sense create a new asset of the Company of the nature of a fixed capital asset or any other. The learned Lord Justice does not more closely describe this so-called asset nor, fixed though it was, did he attach it to a name by which it could be recognised. He did not suggest that it resulted in an enhanced goodwill. He could not, in my judgment, have done so with reason, because it has never, I think, even been suggested that a contented personnel is an element in goodwill, whatever else it may be. In that state of things it has occurred to me, my Lords, that the existence or non-existence of this so-called asset might fairly be submitted to the prosaic test of asking what in a liquidation would be forthcoming in respect of it when a liquidator essayed his statutory duty to realise the Company's assets and divide the proceeds amongst his constituents. Certainly no part of the Fund. That in its entirety is completely alienated. And I can myself think of nothing else. Moreover, my Lords,

(1) 6 T.C. 399.

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a reference to the authorities shows, it seems to me, clearly that it is by reference to no such shadowy conceptions that the words of the statute " employed as capital " have to be interpreted. Such things as a purchase of goodwill involving a capital expenditure might come within them—*Smith* v. *Moore*, [1921] 2 A.C. 13, an Excess Profits Duty case; the expense of making a new channel to the sea essential or convenient for approach to a shipyard would be such expenditure, notwithstanding that the channel when constructed would not be the property of the trader and that others jointly with himself would have the right to use it on their lawful occasions—*Ounsworth* v. *Vickers, Ltd.*(1), [1915] 3 K.B. 267, 276; the expenses incurred in the promotion of a private Bill, the capital object of which was ultimately obtained by agreement—*Moore* v. *Hare*, 6 T.C. 572. These advantages are real and definite. I can see nothing comparable here. Moreover, in this connection also the observation already made is true that the principle expounded by the Lord Justice would equally apply to the annual payments to be made by the Company and admittedly properly chargeable to revenue.

The result, therefore, is that, in my judgment, there is so far no prohibition in the Statute which prevents, for the purposes of Income Tax, the application to this disbursement of the principles which for any other purpose are alone, as I think, properly applicable to it. And no other statutory prohibition is suggested.

Lord Justice Warrington's ground of decision against the Appellants is quite different. He would, I think, as I have done, have answered in the negative the two questions already propounded. It is, at any rate, consistent with his judgment that he would have done so. His decision for the Crown is based solely on the ground that in his judgment the payment in question was, in Lord Sumner's words already quoted, " not a proper " debit item to be charged against incomings of the trade when " computing the balance of profits of it." The learned Lord Justice treats these words of Lord Sumner's as extending to a *revenue* disbursement wholly and exclusively laid out or expended for the purposes of the trade, which is, nevertheless, still inadmissible as a deduction because it is not a proper debit item to be charged. I agree with the Lord Justice in thinking that the words do import all that. But what amount of impropriety is to be treated as sufficient to require disallowance as improper of a disbursement which is not the subject of, at all events, express statutory prohibition? It must surely be an expenditure somewhat abnormal or irrational or extravagant. I conceive, for instance, that a payment avowedly made out of realised profits such as is alluded to by Lord Dunedin in another portion of his

(1) 6 T.C. 671.

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judgment in the *Vallambrosa* case(1) would clearly be within the words. I doubt, however, whether the learned Lord Justice would have brought the present disbursement within the same category had there been present to his mind the extraordinarily compelling circumstances which, as a matter of business, had led to it. These properly regarded—I do not again detail them—and the payment treated, on this hypothesis, it must be, as a revenue payment, it seems to me impossible to hold that it was in any sense at all either excessive or improper.

My Lords, I need not expand a judgment already too long by any further discussion of the authorities. I think with the Lord Chancellor that *Hancock*(2) was correctly decided, but I should myself have been prepared to decide this case as I do even if I were of opinion that *Hancock* could not be supported—so much more compelling in a relevant respect are the facts and circumstances here. As to *Rowntree*(3), the disbursement there sought to be justified came, in my judgment, both within the express prohibition of the statute and its implied prohibition as enunciated by Lord Sumner.

On the whole case I am of opinion that the Order of the Court of Appeal should be recalled and that of Mr. Justice Rowlatt restored.

Questions put:

That the judgment appealed from be reversed.

The Not Contents have it.

That the judgment appealed from be affirmed and this Appeal dismissed with costs.

The Contents have it.

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(1) Vallambrosa Rubber Company v. Farmer, 5 T.C. 529.
(2) Hancock v. General Reversionary and Investment Company, 7 T.C. 358.
(3) Rowntree and Company v. Curtis, 8 T.C. 678.