No. 960—HIGH COURT OF JUSTICE (KING'S BENCH DIVISION)—9TH, 12TH AND 13TH MARCH, 1934

COURT OF APPEAL—26TH, 27TH AND 28TH JUNE, 1934

HOUSE OF LORDS—4TH, 5TH, 7TH AND 8TH MARCH AND 8TH APRIL, 1935

VAN DEN BERGHS, LIMITED *v.* CLARK (H.M. INSPECTOR OF TAXES)[1]

Income Tax, Schedule D—Capital or income—Agreements between competing trading companies for profit-sharing, etc.—Payment received by one company from the other as damages for cancellation of its future rights under the agreements.

In 1908 *the Appell nt Company, which carried on the business* (inter alia) *of manufacturing and dealing in margarine and similar products, entered into an agreement with a competing Dutch company by which the two Companies bound themselves for the future to work in friendly alliance and agreed* (inter alia) (a) *to share the profits of their respective margarine businesses in specified proportions,* (b) *to bring within the operation of the agreement, if required, any interest in other margarine concerns acquired by companies under their control,* (c) *not to enter any pooling or price arrangements with third parties inimical to the interests of the two Companies,* (d) *to set up a joint committee to make arrangements with outside firms as to prices and limitation of areas of supply of margarine and* (e) *to promote generally the interests of the two Companies in the margarine business. Supplemental agreements made in* 1913 *and* 1920 *provided that, with certain modifications, the provisions of the* 1908 *agreement were to continue in force until* 1940.

In the period from 1908 *to* 1913 *payments were made under the agreements by and to the Appellant Company and were treated for Income Tax purposes as trading expenses and receipts, respectively, of the years in which they were made. From* 1914 *to* 1919 *the two Companies were unable to compute their profits owing to the difficulties caused by the war. In* 1922 *the Appellant Company arrived at the sum of* £449,042 *as being the amount due to it by the Dutch Company under the agreements. This liability was not admitted by the Dutch Company, which claimed that under the agreements there was, on balance, a sum due to it by the Appellant Company. The matter was referred to arbitration which, however, proved so lengthy and costly that, in* 1927, *the Companies, in contemplation of a merger of interests,*

(1) Reported (C.A.) 151 L.T. 435; (H.L.) 153 L.T. 171.

entered into negotiations with a view to a settlement of the dispute. The Dutch Company desired to cancel the agreements, but the Appellant Company, which considered that such a course would be to its disadvantage, refused to consent to cancellation unless the Dutch Company paid to it, at least, £449,042.

A settlement was finally reached in 1927, *whereby,* inter alia, (a) *all claims and counter-claims under the agreements for the period* 1914 *to* 1927 *were withdrawn; and* (b), *in consideration of the payment by the Dutch Company of* £450,000 *to the Appellant Company " as damages ", the agreements were determined as at* 31*st December,* 1927, *and each party released the other party from all claims thereunder. That sum was paid in* 1927 *and credited in the Appellant Company's accounts for that year.*

The Company was assessed to Income Tax under Schedule D, for the year 1928–29, *in an amount which included the sum of* £450,000. *On appeal, the General Commissioners decided that the* £450,000 *was paid " in respect of the pooling agreements " and must be brought in for the purpose of arriving at the balance of profits and gains of the Appellants for the year to* 31*st December,* 1927.

Held, *that the payment of* £450,000 *was a payment for the cancellation of the Appellant Company's future rights under the agreements, which constituted a capital asset of the Company, and that it was, accordingly, a capital receipt.*

CASE

Stated by the Commissioners for the General Purposes of the Income Tax for the City of London pursuant to Section 149 of the Income Tax Act, 1918, for the opinion of the High Court of Justice.

1. At a meeting of the said Commissioners held at Gresham College, Basinghall Street, in the said City on the 14th day of December, 1931, Van den Berghs, Limited, an incorporated Company having its registered office at Unilever House, Blackfriars, E.C.4 (hereinafter called " the Appellants ") appealed against an assessment to Income Tax made upon them under the rules applicable to Schedule D of the Income Tax Act, 1918, and subsequent amending Acts for the year ending 5th day of April, 1929, in the sum of £650,000.

2. The question for the determination of the Commissioners was whether or no a sum of £450,000, forming part of the said assessment, was an income or trade receipt of the Appellants for the year ended 31st December, 1927, that being the preceding year by reference to which the Company's profits were computed for the year 1928–1929. No question was raised before us as to the exact amount of the assessment, it being agreed that the above-mentioned assessment should be adjusted in any event.

3. The Appellants were incorporated on the 9th day of March, 1895, as a Company with a capital of £950,000 divided into 90,000 £5 Preference Shares and 100,000 Ordinary Shares of £5 each.

The objects of the Company as contained in its Memorandum of Association comprised (*inter alia*) the following :—

. . . . . .

(B) To carry on business as manufacturers of margarine, oleo margarine and other substitutes for butter, butter merchants, merchants, dealers, brokers or factors in all kinds of provisions, either wholesale or retail; importers and dealers of oil and other oleaginous or fatty matters, seed crushers and merchants, farmers, dairy produce dealers, and dealers in condensed milk, cow-keepers, grasiers, cattle breeders, ship-owners, charterers or brokers, carriers, forwarding agents, warehousemen, wharfingers, lightermen and any other business which the said Messrs. Van den Berghs may have been engaged in or connected with ancillary to their principal business of margarine manufacturers and merchants, or which may be in the opinion of the Company conveniently carried on in conjunction with any of the businesses aforesaid, or calculated directly or indirectly to enhance the value of or render profitable any of the Company's property or rights.

. . . . . .

(D) To enter into partnership or into any arrangement for sharing profits, union of interest, co-operation, joint adventure, reciprocal concession, or otherwise, with any person or company carrying on, or engaged in, or about to carry on, or engage in any business or transaction which this Company is authorised to carry on, or to engage in any business or transaction capable of being conducted so as directly or indirectly to benefit this Company, and to take and otherwise acquire and hold, sell, re-issue, or otherwise deal with shares or stocks in or securities or obligations of and to subsidise or otherwise assist any such company and to guarantee the principal and/or interest of any such securities or obligations and/or the capital and/or dividends of any such shares or stock.

A copy of the Memorandum and Articles of Association of the Company is attached hereto marked "A" and may be referred to as part of this Case(1).

4. At the date of the assessment now under appeal the capital of the Company was £3,575,000 divided into 90,000 Cumulative 6 per cent. Preference Shares of £5 each, 1,000,000 Cumulative 6 per cent. B Preference Shares of £1 each, 1,000,000 Cumulative 7 per cent. C Preference Shares of £1 each, 3,750,000 15 per cent. Preferred Ordinary Shares of 5*s*. each and 750,000 Ordinary Shares

(1) Not included in the present print.

of 5*s*. each. The capital was later further increased. The general voting power of the Company was confined to the holders of Ordinary Shares. Of the said Ordinary Shares members of the Van den Bergh family held 260,000 and through a subsidiary company held a further 152,000 so that the control of the voting power of the Company was vested in the Van den Bergh family. The bulk of the remaining capital, viz. :—the Preferred Ordinary and Preference Share capital, was held by the public.

5. The Appellants had for many years been in keen business competition with another firm of margarine manufacturers, Anton Jurgens Vereenigde Fabrieken of Holland (hereinafter referred to as the " Dutch Company ") and in the year 1908 these two Companies thought it would be to the advantage of their respective trades and of the companies controlled by them to enter into an agreement for profit sharing and other purposes and accordingly made the agreement next hereinafter mentioned. Within the various groups of companies controlled by the Appellants and between the said controlled companies there were other pooling agreements. These agreements however were not of the same type as the agreement next referred to : they related to the regulation of prices.

6. By an agreement dated 13th February, 1908, (which with the agreements referred to in paragraphs 7 and 9 hereof are hereafter referred to as the " pooling agreements ") and made between the Dutch Company of the first part the Appellants of the second part and certain Directors and Managers of the third and fourth parts after reciting (*inter alia*) that the Companies (the Appellants and the Dutch Company) carry on margarine business (which expression includes the business of manufacturing, buying, selling, exporting, importing and dealing in margarine and other butter substitutes) and in addition thereto carry on certain other businesses (therein referred to as the " outside businesses ") and that the Companies are desirous of working in friendly alliance on the terms therein set forth, it was agreed (*inter alia*) as follows :—

(1) " The five year period " means the period comprised in the years one thousand nine hundred and two, one thousand nine hundred and three, one thousand nine hundred and four, one thousand nine hundred and five, one thousand nine hundred and six.

(2) As between the two Companies this agreement is to be treated as having come into operation on the First day of January, 1908, and is to continue in force until it is determined as hereinafter provided that is to say until the expiration of one and a half years after one of the two Companies shall have given to the other notice in writing determining this agreement, but so that such notice shall not be capable of being given before the First day of July, 1926, or until it is determined under Clause 28.

(3) The two Companies shall during the continuance of this agreement work in friendly alliance and shall as regards each year commencing with the year one thousand nine hundred and eight share the profits and losses made or sustained in their respective margarine businesses in proportion to the yearly average amount of the profits (as ascertained in accordance with the regulations contained in Clause 4) of their respective margarine businesses during the five year period . . . . (Then follow certain provisions dealing with the case of one Company making a loss).

(4) The profits of the margarine business of each of the two Companies made during the five year period, shall be ascertained as follows that is to say :—

(1) The profits of one thousand nine hundred and two and one thousand nine hundred and three shall be taken to be as follows :—

Of the Dutch Company for one thousand nine hundred and two, sixty seven thousand five hundred and thirty three pounds.

Of the Dutch Company for one thousand nine hundred and three, eighty four thousand one hundred and twenty pounds.

Of the English Company for one thousand nine hundred and two, eighty one thousand two hundred and forty nine pounds.

Of the English Company for one thousand nine hundred and three, one hundred and forty three thousand six hundred and fifty six pounds.

(2) The amount of the profits of each of the two Companies, and of the scheduled companies under their control of their respective margarine businesses for one thousand nine hundred and four, one thousand nine hundred and five and one thousand nine hundred and six respectively, shall be ascertained and certified in writing by two firms of accountants, one to be appointed by each of the two Companies upon the execution hereof and the joint certificate in writing of such accountants is to be made and signed within two calendar months from the date hereof or within such enlarged period as the two Companies shall in writing agree on and such certificate may be absolute or may be conditional that is to say :—If any differences shall have arisen between the two accountant firms which shall not have been settled the certificate may be made subject to the determination of such differences and in such case the differences shall be specified in the certificate and shall be treated as differences between the two Companies, and shall be referred to an arbitrator to be appointed by the two accountant firms or if they do not make the appointment forthwith, then to an

arbitrator to be appointed by the two Companies, and if the certificate aforesaid is not made within the period or enlarged period aforesaid then the amount of the profits aforesaid shall be considered a matter of difference between the two Companies and such difference shall be referred to arbitration as hereinafter provided.

. . . . . .

(5) At the conclusion of the year one thousand nine hundred and eight, and at the conclusion of each subsequent year during the continuance of this agreement the profits of the margarine business of each of the two Companies and the scheduled companies under their control shall be ascertained and certified by two firms of accountants one to be appointed by each of the two Companies and Paragraph 2 of Clause 4 hereof shall apply as if the same were here repeated *mutatis mutandis*.

. . . . . .

(*g*) The income dividends or profits from the investments specified in the 4th Schedule hereto are to be treated as profits divisible under this agreement apportioned for the period.

. . . . . .

(*i*) On all increased capital introduced employed or appropriated after the 31st December one thousand nine hundred and six in respect of the margarine businesses, or to provide funds for the purchasing of any investments the profits or income from which is, or shall be treated as profits divisible under this agreement whether introduced employed or appropriated as share capital appropriation of profits to reserve funds or profits unappropriated into or by either or both of the two Companies or any or all of the scheduled companies there shall be allowed as a debit in the respective profit and loss accounts interest at the rate of five per cent. per annum.

Except that this Clause shall not apply to any capital for which either of the two Companies or any or all of the scheduled companies are under contract to pay a fixed rate of interest. In such cases the actual rate of interest paid shall be deducted from the profit or added to the loss as the case may be.

(*j*) On all diminutions of capital after the thirty first of December one thousand nine hundred and six by either one or both of the two Companies or any or all of the scheduled companies there shall be added to the profits or deducted from the losses as the case may be in the respective profit and loss accounts, interest at the rate of five per cent. per annum.

(6) When and so soon as the profit or loss of both of the two Companies of any year shall have been ascertained and certified as aforesaid the two accountant firms or arbitrator shall then ascertain what sum on either side has to be paid for adjusting the rights of the two Companies under Clause 3 hereof and shall certify accordingly and a copy of such certificate shall be sent to each of the two Companies and the Company which under such certificate has to pay any sum to the other Company shall within thirty days of the date of the two accountancy firms' Certificate or of the arbitrator's award make payment thereof accordingly either in Dutch currency or in sterling.

. . . . . .

(11) During the continuance of this agreement neither of the two Companies shall enter into or permit or suffer any of the scheduled companies in which it is interested or any other company for the time being under its control to enter into any working or pooling arrangement or any arrangement relating to contract or selling prices or any other arrangement with any other company or companies firm or firms person or persons which may by either of the two Companies be deemed inimical to the interest of the two Companies under this agreement and each of the two Companies shall be true and loyal to the other of them and shall do all in the power of such Company to promote the commercial technical pecuniary buying and selling and other interests of the parties hereto in relation to the margarine business and if any difference shall arise under or in relation to the provisions of this Clause such difference shall be referred to arbitration and if it shall be determined by any means that either party has acted in contravention of this agreement such party shall pay to the other party as and by way of liquidated damages and without references to the actual damage (if any) sustained the sum of two shillings in respect of every kilogram of margarine bought sold manufactured or dealt in in contravention of such provision.

. . . . . .

A copy of the said agreement is annexed hereto marked " B " and may be referred to as part of this Case(1).

7. By an agreement in writing dated the 17th July, 1913, and made between the Dutch Company of the one part, and the Appellants of the other part supplemental to the said agreement of the 13th February, 1908, after reciting that the Dutch Company had discovered a process of hardening oils and that the parties were desirous of formulating a scheme for the merger of assets or unification of financial and commercial interests of the respective parties hereto and their subsidiary companies and for the regulation and allocation of the turnover but no such scheme can at the present time be fully elaborated to the satisfaction of both parties hereto

(1) Not included in the present print.

and it is desirable to regulate their mutual relations in the meantime and to modify and extend the principal agreement in the manner hereinafter appearing it was agreed (*inter alia*) as follows :—

(1) This agreement is to be for a period of one year from the first day of January one thousand nine hundred and thirteen until the thirty first day of December one thousand nine hundred and thirteen except where otherwise provided.

. . . . . .

(6) The provisions of the principal agreement relating to the ascertainment and sharing of profits and losses shall continue in force until the thirty first day of December one thousand nine hundred and forty subject to the following modifications :—

(*a*) There shall be included in the profits and losses to be shared all profits and losses made or sustained by the respective parties hereto from all sources whatsoever subject to Sub-clause (*e*) of this clause including (among other things) all profits or losses made or sustained by them respectively from the acquisition or exploitation of any process or patent for hardening oil or from or in connection with the hardening of oils for any purpose but excluding any profits or losses made or sustained by the English Company in connection with any condensed milk or bacon business carried on by them or in which they may be interested and (in the event of the sale before the thirtieth day of September one thousand nine hundred and thirteen contemplated in the proviso to Clause 4 (*b*) hereof) excluding any profits or losses made or sustained by the English Company in connection with the manufacture and sale of soap prior to the date of such contemplated sale.

(*b*) All profits and losses shall be shared by the parties hereto equally instead of in the proportions mentioned in Clause 3 of the principal agreement.

. . . . . .

(7) A Committee shall be formed consisting of two persons to represent the Dutch Company and two persons to represent the English Company for the purpose of endeavouring to devise and if thought advisable by and subject to the consent of both parties hereto agreeing upon a scheme for the merger of the assets or unification of the financial and commercial interests of the parties hereto and their subsidiary companies and for the regulation and allocation of their turnover.

(8) Should the parties hereto fail to agree before the fifteenth day of December one thousand nine hundred and thirteen upon the scheme contemplated in the last preceding clause they will cause to be prepared and executed a contract whereby the provisions hereof then in operation (particularly Clause 6 hereof) and the provisions of the document set forth in the Second Schedule hereto (particularly with regard to diversion of profits

from the pool) shall be confirmed and extended for the period from the first day of January one thousand nine hundred and fourteen to the thirty first day of December one thousand nine hundred and forty.

A copy of the said agreement marked " C " is annexed hereto and may be referred to as part of this Case(1).

8. Each Company carried on its business independently, but in general the parties observed the terms of the said agreements for each of the years 1908 to 1913, and the profits of the two Companies were accounted for for those years. Payments were in fact made by and to the Appellants under the said agreements in these years. Such payments when made to the Dutch Company were deducted as an expense and when made by the Dutch Company were brought in as a receipt in making up the Appellants' profit and loss accounts for the years in which the payments were made or received. In computing the Appellants' Income Tax liability for the said years, the amount of such payments or receipts was deducted or brought in to the taxable profit respectively and the Income Tax paid accordingly. It was also agreed by the Appellants, when liability for Income Tax and Excess Profits Duty was under consideration for years subsequent to 1913, that the results of working the said agreements should be charged to Income Tax and Excess Profits Duty as trading receipts and payments.

From the commencement of the War in 1914 down to 1919 the two Companies did not communicate and were unable to compute their profits owing to the various difficulties caused by the War so that it was found desirable that a fresh agreement should be entered into in an endeavour to make the above mentioned agreements (which were then running and would not terminate until 1940) workable. In the result the agreement next hereinafter referred to was entered into.

9. By an agreement in writing dated the 15th October, 1920, and made between the Dutch Company of the one part and the Appellants of the other part supplemental to the said agreement of the 13th February, 1908, and the said agreement of 17th July, 1913, reciting that some of the provisions of the principal agreement and the 1913 agreement had proved to be obsolete or impracticable it was agreed (*inter alia*) as follows :—

1. The principal agreement should remain in full force and effect except as amended or added to by this agreement until the 31st December, 1940.

. . . . . .

3. The provisions of the principal agreement relating to the ascertainment and sharing of profits and losses shall continue in force until the 31st day of December, 1940, subject to the following modifications.

(1) Not included in the present print.

(A) There shall be included in the profits and losses to be shared all profits and losses made or sustained by the respective parties hereto from all sources whatsoever (subject to Sub-clause (*e*) of this Clause) including in particular the profits and/or income less losses if any and losses less profits and/or income if any of the two Companies and/or the scheduled companies and the profits and/or income and/or loss derived sustained or accruing by or to either or any of them from any further companies or businesses or investments of any kind in which either or both of the two Companies or any of the scheduled companies is now or at any time may have been or hereafter may be interested (unless excluded under Sub-clause (*e*) of this Clause) and including the income and/or profits and/or losses derived from the investments specified in the Fourth Schedule to the principal agreement but excluding any profits or losses made sustained or accruing by or to the English Company in connection with any condensed milk or bacon business carried on by it or in which it may now be or at any time have been or hereafter may be interested or by any scheduled companies or any businesses or investment so far as it relates to condensed milk or bacon in which the English Company may now be or may at any time have been or hereafter may be interested. The accountants shall for the purposes of Clause 5 of the principal agreement as amended by Sub-clause (*f*) of this Clause have regard to the amount of capital and/or borrowed money employed in relation to any such condensed milk or bacon business or investment as aforesaid. The accountants shall also ascertain what amount shall be credited to the English Company on account of increased capital (including therein " goodwill ") introduced owing to the bringing into the pool of the results of the Naamlooze Vennootschap Vereenigde Zeep-Fabrieken of Zwijndrecht.

(B) All profits and/or income and/or losses shall as from the 1st January, 1914, be shared by the parties hereto equally instead of in the proportion mentioned in Clause 3 of the principal agreement.

. . . . . .

(L) The accountants of both parties hereto shall ascertain the results relating to the year 1914 and all subsequent years during the currency of this agreement in accordance with the provisions of the principal agreement the 1913 agreement and this agreement but in so doing they shall not be bound to follow any principles rules or precedents previously laid down made followed or acted upon by accountants in ascertaining or certifying the results of previous years and if and whenever the regulations and provisions of the said three agreements do not provide for any circumstance which may arise or have

arisen or in case the accountants do not agree as to the meaning or intention of any of the said regulations and provisions the accountants shall decide in such manner as shall in their opinion be fair and equitable having regard to the general intention of the agreements (subject to specific provisions) that the results of each year shall be divided equally between the parties hereto. Nothing in this agreement shall prevent the accountants when ascertaining the profits and/or income and/or losses to be brought into account from controlled companies controlled businesses or controlled investments from bringing into account where equitable profits capitalised and/or not received and/or losses not directly sustained or provided for.

. . . . . .

9. In the event of any dispute of whatsoever nature arising out of or in connection with this agreement the same shall be decided by arbitration in accordance with the provisions of the Arbitration Act, 1889.

A copy of the said agreement marked " D " is attached hereto and may be referred to as part of this Case(1).

10. In the year 1919 the Appellants had endeavoured to estimate what they considered was due to them under the pooling agreements and they decided with the assistance of their auditors on the sum of £715,000 and took credit in their profit and loss account for the four and a half years ended 30th June, 1919, for that amount, a corresponding amount being included in the balance sheet under the heading " Sundry Debtors ". In 1920 it was considered necessary that a fresh estimate should be made and as a result of the said estimate the amount of £715,000 was debited in the Profit and Loss Account and in lieu of that figure a sum of £380,665 was credited in the Profit and Loss Account for the year ended 31st December, 1920, and a corresponding amount was included in the balance sheet under the heading of Debtors. In the Profit and Loss Account for the year ended 31st December, 1921, as a result of further estimate, a further amount of £55,060 was credited, and at that date the total (£435,725) was included in Debtors in the Balance Sheet (£380,665 plus £55,060) and finally in 1922 calculating interest on the said £435,725 the Appellants raised the figure estimated as due under the agreements to £449,042 at which figure it continued in the Balance Sheets included under the heading " Sundry Debtors " until 1927. These amounts were not admitted to be due by or on behalf of the Dutch Company and were excluded by the Appellants in computing their profits for Income Tax purposes for the relevant years. The Dutch Company in fact claimed that on balance the Appellant Company was indebted to it.

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(1) Not included in the present print.

11. The said Companies being unable to agree as to the construction of the said agreements and their respective rights thereunder, in particular as to the computation of profits 1914 to 1924 for the purpose of sharing under the agreements, it was agreed in the year 1925 that the matter should be referred to arbitration. The arbitration proved an extremely complicated matter, the differences involved being very considerable. On the one side the Dutch Company claimed £1,073,000 from the Appellants and on the other side the Appellants claimed £1,408,000 from the Dutch Company. Three arbitrators in all were appointed; the points in dispute in the arbitration covered the period from 1914 to 1924. In the year 1927, the arbitration being still far from finished, and the delay and expense already being prodigious and no accounts for the years 1925 to 1927 having as yet been taken, the parties in contemplation of a merger of interests negotiated with a view to settling the dispute. The Dutch Company had refused to admit that any payment was due to the Appellants under the pooling agreements while the Appellants on the other hand insisted that at any rate the sum of £449,042 which had been included in their own accounts for profit and loss and balance sheet purposes must be paid to them under these agreements. The Appellants also alleged that the capital of the Dutch Company between the years 1919 and 1927 had been increased by £13,847,000 as against an increase of £4,848,000 in the Appellants' capital, and they produced a table of such increases which is annexed hereto and marked " E " and may be referred to as part of this Case(1). They contended that as the profits on the capital in the business in excess of 5 per cent. (and, in fact, these profits largely exceeded 5 per cent.) belonged equally to the Dutch Company and the Appellants, the surrender of the thirteen years which the pooling agreements still had to run would be to their disadvantage. The Appellants intimated that £449,042 was the minimum sum for which they would agree to cancel the old agreements, because if they did not receive at least that amount their Balance Sheets would be incorrect and unjustified. They tried to get more, but could not upon the figures available to them substantiate their claim to more. Finally a sum of £450,000 was paid. This sum was credited as to £449,042 to the Dutch Company's account in the Appellants' books and the balance of £958 was credited in the Appellants' Profit and Loss Account for the year ending 31st December, 1927.

12. The settlement arrived at as above stated was carried out by the three agreements next hereinafter mentioned all dated 24th September, 1927.

(*a*) By the first agreement the members of the Jurgens family and the members of the Van den Bergh family agreed to consolidate their respective interests in a Dutch holding company and an English holding company on the terms therein mentioned.

(1) Not included in the present print.

(*b*) By the second agreement after reciting that the said arbitration was not yet concluded but the expense thereof was continuing and that the parties had been advised by their legal advisers that there was every probability that the said arbitration might be indefinitely prolonged it was agreed as follows :—

(1) Each party withdraws all claims against the other party under the pooling agreements for the years 1914 to 1927, inclusive, and both parties mutually discharge each other from any liability arising under these contracts before the 31st December, 1927.

(2) Each party undertakes to do all things necessary to put an end to the said arbitration.

(*c*) By the third agreement after reciting pooling agreements whereunder parties had agreed to divide between them the results of their respective businesses as therein provided until the 31st December, 1940, and that the Dutch Company had expressed to the English Company a desire to determine the said agreements contrary to the provisions therein contained and that the English Company had consented thereto in consideration of the payment by the Dutch Company to the English Company of the sum of £450,000 as damages, it was agreed :—

(1) The said agreements as between the parties hereto are hereby determined as from 31st December, 1927, and each party hereto releases the other party from all claims thereunder.

(2) The Dutch Company shall forthwith pay to the English Company the sum of £100,000 in cash and shall forthwith hand over to the English Company promissory notes (carrying interest at the rate of 5 per cent. per annum from the 1st January, 1928) for a further amount of £350,000, such promissory notes falling due as follows :— As to £150,000 on the 1st September, 1928, and as to £200,000 on the 1st September, 1929.

Copies of the said agreements are annexed hereto marked " F ", " G " and " H " respectively and may be referred to as part of this Case(1). In fact the full amount of £450,000 was paid in cash in the year ended 31st December, 1927, and this sum was taken into account in arriving at the estimated assessment to Income Tax now under appeal.

13. The Directors' reports for the years 1919 to 1926 referred to the outstanding questions which had arisen due to the War and which were unsettled, including (*inter alia*) the dispute with the Dutch Company but the existence of the pooling agreements was at no time disclosed to the shareholders owing to the clause in the

(1) Not included in the present print.

pooling agreements requiring secrecy. In the report on the year to 31st December, 1927, the Directors stated that the last of the outstanding items had been satisfactorily settled. This last report referred to the dispute with the Dutch Company set out above. The Auditors' reports for the said years referred to the estimates of sums due to the Company as having been reasonably made, but stated it had not been possible to verify such estimates. This referred (*inter alia*) to the dispute with the Dutch Company, but the nature of the claims was not specified.

The reports of the Directors and accounts of the Appellants for the years 1919–1927 inclusive including profit and loss accounts for the periods 30th June, 1919, 31st December, 1920, 31st December, 1921, 31st December, 1922, and 31st December, 1927, are annexed hereto marked " J " and may be referred to as part of this Case[1].

14. For the Appellants it was contended :—

1. That the said sum of £450,000 was paid to the Appellants as compensation for surrendering their future prospects under the pooling agreements, which had thirteen years to run.

2. That a sum paid as compensation for loss of anticipated future profits is not an income receipt at all but is capital.

3. That the £449,042 was merely the measure applied by the Appellants to arrive at the amount of compensation to be paid thereon.

4. That the pooling agreements were not contracts which it was usual for the Company to make in the course of its trade as sellers of margarine but were in the nature of partnership agreements with the Dutch Company.

5. Alternatively that if the sum of £450,000 was to be regarded as payment of amounts due on income account viz. :— sums due to the Appellants as their share of profits under the pooling agreements for the years 1914–1922, such profits or share of profits formed no part of their profits and gains for the year ended 31st December, 1927, and ought not to be included in the computation of their profits for assessment for the year 1928–29.

6. That the £450,000 should be excluded from computation of the Appellants' profits chargeable to tax for the year under appeal.

15. For the Inspector of Taxes it was contended :—

(1) That any amounts received by the Appellants under the pooling agreements were receipts of their trade to be brought into account in computing the balance of profits and gains for Income Tax purposes.

(2) That the sum of £450,000 was a sum paid in settlement of all the Appellants' claims and rights under the pooling agreements and was a receipt of the Appellants' trade for the year ended 31st December, 1927.

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[1] Not included in the present print.

(3) That even if the said sum was wholly or partly paid to cancel the pooling agreements for the future it was a receipt of the trade and not capital.

(4) That the pooling agreements do not create a partnership or any relationship in the nature of partnership between the Dutch Company and the Appellants.

(5) That the said sum of £450,000 was rightly brought into the computation of profits for the year ended 31st December, 1927, and consequently the assessment for 1928–29 was correct in principle and should be confirmed in figures to be agreed.

16. The following cases were referred to :—

Chibbett v. *Joseph Robinson & Sons*, 9 T.C. 48.

Commissioners of Inland Revenue v. *Northfleet Coal and Ballast Co., Ltd.*, 12 T.C. 1102.

Burmah Steamship Co., Ltd. v. *Commissioners of Inland Revenue*, 16 T.C. 67.

Dailuaine-Talisker Distilleries, Ltd. v. *Commissioners of Inland Revenue*, 15 T.C. 613.

Mills v. *Jones*, 14 T.C. 769.

Constantinesco v. *Rex*, 11 T.C. 730.

Short Brothers, Ltd. v. *Commissioners of Inland Revenue*, 12 T.C. 955.

Newcastle Breweries, Ltd. v. *Commissioners of Inland Revenue*, 12 T.C. 927.

Sterling Trust, Ltd. v. *Commissioners of Inland Revenue*, 12 T.C. 868.

Glenboig Union Fireclay Co., Ltd. v. *Commissioners of Inland Revenue*, 12 T.C. 427.

Hart v. *Hart*, 18 Ch.D. 670.

Isaac Holden & Sons, Ltd. v. *Commissioners of Inland Revenue*, 12 T.C. 768.

The Commissioners held that the £450,000 was paid in respect of the pooling agreements and must be brought in for the purpose of arriving at the balance of profits and gains of the Appellants for the year ending 31st December, 1927.

The Appellants thereupon expressed dissatisfaction at the decision of the Commissioners as being erroneous in point of law and required them to state a Case for the opinion of the High Court of Justice which we have stated and do sign accordingly.

H. S. KING,
A. S. SUTHERLAND-HARRIS,
W. HARDY KING,
J. P. BLAKE,
ALAN HOTHAM,
A. C. DAVIS.

COPLEY D. HEWITT,
Clerk to the said Commissioners.
26th October, 1933.

The case came before Finlay, *J.*, in the King's Bench Division on the 9th, 12th and 13th March, 1934. On the last named date judgment was given against the Crown, with costs.

Mr. A. M. Latter, K.C., and Mr. Cyril L. King appeared as Counsel for the Company and the Attorney-General (Sir Thomas Inskip, K.C.) and Mr. Reginald P. Hills for the Crown.

JUDGMENT

Finlay, J.—This is undoubtedly a difficult case, and it is with hesitation that I have arrived at a conclusion, and the more so as the conclusion at which I have arrived differs from that of the General Commissioners.

The case has reference to an appeal by a very well-known company, Van den Berghs, Limited. They appealed against an assessment to Income Tax made upon them for the year ending 5th April, 1929. The question for determination by the Commissioners is defined by them in paragraph 2 of the Case as being " whether or no a sum of £450,000, forming part of the said " assessment, was an income or trade receipt of the Appellants " for the year ended 31st December, 1927, that being the pre- " ceding year by reference to which the Company's profits were " computed for the year 1928–29 ". The Commissioners explained that questions as to figures were not gone into and may have to be dealt with later. It is not altogether easy to ascertain from the Case exactly what it is that the Commissioners decided. I am, of course, going to look at the Case and to look at the facts. It may possibly be convenient to look, first, at the actual finding of the Commissioners: " The Commissioners held that the £450,000 was " paid in respect of the pooling agreements and must be brought in " for the purpose of arriving at the balance of profits and gains of " the Appellants for the year ending 31st December, 1927." I shall return to that finding when I have stated, by reference to the Case, the facts, but it will, I think, then appear that it is by no means easy to discover exactly what it was that the Commissioners intended to find. It is indeed clear that they found in favour of the Crown, that they were of opinion that the £450,000 was assessable income of the year in question, but precisely on which of two grounds they found that is a good deal less clear. I think that there is an ambiguity in the expression " was paid in respect of the " pooling agreements ". In a sense, it is perfectly obvious that the sum was paid in respect of the pooling agreements, and it is the argument on both sides that it was. I am perhaps rather anticipating in saying that, because it is necessary, in order to make the matter as clear as may be, to deal—though quite briefly—with the facts as they are found.

The Company is a company incorporated on the 9th March, 1895, and it is in very extensive business indeed as a dealer in margarine and other such products. Its capital at the time in

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question was over £3,000,000. The general voting power was confined to the holders of ordinary shares and of those ordinary shares the Van den Bergh family—this becomes a little important later—held a preponderating interest; they had the voting control of the Company, although the bulk of the capital, the preferred ordinary and preference share capital, was held by the public. For many years, apparently, there had been keen competition between the Appellants and a Dutch firm of margarine manufacturers called Anton Jurgens & Company. In the year 1908 these two Companies thought that it would be to the advantage of their respective trades to enter into an agreement for profit sharing and for kindred purposes. Pursuant to that policy, three pooling agreements were entered into at different dates. The first was dated the 13th February, 1908. There were elaborate provisions—I do not think it is necessary to go through them; they are set out in detail in the Case—for computing the profits of the two Companies, which was to be done with reference to a period called " the five year period ", and then for a division of the profits of the two Companies; so that the result was that the Appellants acquired an interest in the profits of Jurgens, and Jurgens correspondingly acquired an interest in the profits of the Appellants. There is a material provision—I need not read it—with reference to what was to be done in the obviously likely case of the introduction of further capital. In 1913 there was a supplemental agreement. Some modifications were introduced into the principal agreement and it was agreed, subject to those modifications, that the provisions of the principal agreement relating to the ascertainment and sharing of profits and losses should continue in force until the 31st December, 1940.

Those agreements were duly worked and paragraph 8 of the Case defines what was done: " Each Company carried on its " business independently, but in general the parties observed the " terms of the said agreements for each of the years 1908 to 1913, " and the profits of the two Companies were accounted for for those " years. Payments were in fact made by and to the Appellants " under the said agreements in these years. Such payments when " made to the Dutch Company were deducted as an expense and " when made by the Dutch Company were brought in as a receipt " in making up the Appellants' profit and loss accounts for the " years in which the payments were made or received. In computing the Appellants' Income Tax liability for the said years, " the amount of such payments or receipts was deducted or brought " in to the taxable profit respectively and the Income Tax paid " accordingly. It was also agreed by the Appellants, when liability " for Income Tax and Excess Profits Duty was under consideration " for years subsequent to 1913, that the results of working the said " agreements should be charged to Income Tax and Excess Profits " Duty as trading receipts and payments." That paragraph

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explains quite clearly the course of business. The Attorney-General appeared to attach significance to the circumstance which is found, that the payments made to the Dutch Company were deducted as an expense and those made by the Dutch Company were brought in as a receipt for the years in which the payments were made or received. I do not understand that that is drawing any contrast between the year of earning and the year of receipt. Certainly nothing in the nature of an estoppel could emerge from that. It seems to me to be very natural, and I should think right, to bring in these things in the year in which they were received, but, while I think that the practice followed was quite correct and not open to criticism, I do not quite appreciate the significance which appeared to be attached to that.

In 1914 the war occurred, and the result of the war upon the two Companies, with whose fortunes at the moment we are concerned, was that they ceased to communicate altogether; there were no facilities for the exchange of information with regard to profits, and so forth; and no such exchange of information took place. After the war was over there was another agreement, a third. That was an agreement of the 15th October, 1920, and that was expressed to be supplemental to the two former pooling agreements. There there is an express provision that the principal agreement was to remain in full force and effect, except as amended or added to by this agreement, until 1940. There are then some rather complicated provisions—it does not seem to me to be necessary that I should go through them—adding to or amending the principal agreement. Of course, questions of immense difficulty emerged as the result of the war with reference to the sums which might be due from one Company to the other. The war, of course, introduced wholly unforeseen elements and it became almost impossible, or very difficult anyhow, to calculate what was or might be due. That is reflected by the facts set out in paragraph 10. Apparently the Appellants had made efforts to estimate what they considered was due to them and they first of all estimated £715,000 and put that in their profit and loss account; they then modified that—it is unnecessary to go through the details—but finally they arrived at a figure of £449,042; that was the figure which they were putting forward as being due to them and that appears in their accounts. Those amounts were not admitted by the Dutch Company to be due; on the contrary, the Dutch Company claimed that, on the balance, the English Company was indebted to it. There was, therefore, a complete *impasse*. In these circumstances, the Companies, not agreeing as to the construction of the agreements and not agreeing as to their respective rights or as to the respective sums due to them, went to arbitration. The arbitration, apparently, proved to be more or less unmanageable; there were

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three successive arbitrators and the period covered in the arbitration was the period from 1914 to 1924. In 1927 the arbitration was not finished and, apparently, showed no signs of coming to an end and, as is expressed in the Case, the delay and expense were already prodigious. In these circumstances, further negotiations took place and those negotiations are expressed as having taken place in contemplation of a merger of interests. The position is defined in paragraph 11 in these words: " The Dutch Company had " refused to admit that any payment was due to the Appellants " under the pooling agreements while the Appellants on the other " hand insisted that at any rate the sum of £449,042 which had " been included in their own accounts for profit and loss and balance " sheet purposes must be paid to them under these agreements. " The Appellants also alleged that the capital of the Dutch Com- " pany between the years 1919 and 1927 had been increased by " £13,000,000 odd " as against an increase of " £4,000,000 odd " in " the Appellants' capital, and they produced a table of such " increases, which is annexed hereto and marked ' E ', and may be " referred to as part of this Case. They contended that as the " profits on the capital in the business in excess of 5 per cent. " (and, in fact, these profits largely exceeded 5 per cent.) be- " longed equally to the Dutch Company and the Appellants, the " surrender of the thirteen years which the pooling agreements still " had to run would be to their disadvantage. The Appellants " intimated that £449,042 was the minimum sum for which they " would agree to cancel the old agreements, because if they did " not receive at least that amount their Balance Sheets would " be incorrect and unjustified. They tried to get more, but " could not upon the figures available to them substantiate their " claim to more. Finally a sum of £450,000 was paid. This sum " was credited as to £449,042 to the Dutch Company's account " in the Appellants' books and the balance of £958 was credited in " the Appellants' profit and loss account for the year ending " 31st December, 1927."

That was a settlement, no doubt, of the matters in dispute and a dealing with the future, and the next paragraph, paragraph 12, shows that that settlement was carried out by three agreements—they are marked " F ", " G " and " H ". " F " may be quite briefly referred to, though, no doubt, of great importance from the Companies' point of view. It was an agreement whereby the members of the Jurgens family and the members of the Van den Bergh family agreed to consolidate their respective interests in a Dutch holding company and an English holding company. The second agreement recited that the arbitration was not concluded and the expense was continuing and that the parties had been advised that it might be indefinitely prolonged; and then the following agreement is made: " Each party withdraws all

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" claims against the other party under the said pooling agreements " for the years 1914 to 1927, inclusive, and both parties mutually " discharge each other from any liability arising under these con- " tracts before the 31st December, 1927." Then " (2) Each party " undertakes to do all things necessary to put an end to the said " arbitration."

The third agreement is of critical importance in this case. That says this : " Whereas by three agreements dated respectively " 13th February, 1908, 17th July, 1913, and 15th October, 1920, " the parties hereto agreed to divide between them the results of " their respective businesses, as therein provided, until the " 31st December, 1940, and whereas the Dutch Company have " expressed to the English Company a desire to determine the said " agreements contrary to the provisions therein contained, and " whereas the English Company have consented thereto in con- " sideration of the payment by the Dutch Company to the English " Company of the sum of £450,000 as damages." Then it is agreed as follows : " (1) The said agreements as between the parties hereto " are hereby determined as from 31st December, 1927, and each " party hereto releases the other party from all claims thereunder. " (2) The Dutch Company shall forthwith pay to the English " Company "—then there is a provision for payment, partly in cash and partly by promissory notes, which does not matter.

The position there seems to be reasonably clear, and one has to look at the agreements to see what was done. The general scheme, of course, was this. The future was provided for by this agreement between the members of the Jurgens family and the members of the Van den Bergh family. The English Company had a claim, which they had finally fixed at a sum of £449,000 odd, which they said was payable to them by the Dutch Company. The Dutch Company were saying : " No, that is a mistake ; nothing is payable : we have " got a balance due to us." Then, further, the Dutch Company were saying : " We now want to determine this pooling agreement ; " we do not want it any more after the arrangements with regard to " the family interests which have taken place ; we want it put an " end to." The English Company said : " Well, we do not mind " that, but this will enure to our benefit and, in particular, in this " respect, that we are entitled to a share of your profits, and the " great increase of your capital puts us in an advantageous position " and makes it probable that our share will be a good share ; there- " fore, it is a disadvantage to us to determine this." Thereupon, an arrangement was arrived at and I do not, for one moment, doubt that the fact (which is a fact) that £449,000 odd had appeared in the profit and loss account and balance sheet of the Appellants was an important element and an element which made them stand out for that sum being obtained. But it is necessary to look at

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the agreements to see how it was obtained, and when one does that it seems to me that it is apparent, upon the face of the agreements—I do not see how I can give them the go-by—that the £450,000 was paid as damages in consideration of the determination of the agreement; that is to say, the English Company were saying: " Well, we will determine this agreement, but it is an " agreement advantageous to us; you must pay us for it "; and then the sum of £449,000 odd was fixed by the English Company as payment for that. The matter may be one of some difficulty because it is impossible not to see that this was really one arrangement and that the £450,000 was fixed with reference to that amount which was the claim of the English Company in respect of the past. But, in spite of that, I think that one is bound, unless the agreement can be challenged, to give effect to it and to look at the way in which the people agreed, the agreements which they made. If the agreement which they made is looked at, it seems to me to be clear that this was a payment by way of damages in respect of the cancellation of an agreement which the English Company were saying would, if it had gone on, have been greatly to their advantage, particularly by reference to the matter with regard to capital to which I referred a few minutes ago.

That almost exhausts the facts in the Case. The contentions of the Appellants are set out in paragraph 14, and the contentions of the Inspector of Taxes in paragraph 15. The first two contentions of the Appellants were these: " (1) That the said sum of " £450,000 was paid to the Appellants as compensation for sur- " rendering their future prospects under the pooling agreements, " which had thirteen years to run. (2) That a sum paid as compen- " sation for loss of anticipated future profits is not an income receipt " at all, but is capital." Then the first two contentions of the Inspector of Taxes are these: " (1) That any amounts received by " the Appellants under the pooling agreements were receipts of " their trade to be brought into account in computing the balance " of profits and gains for Income Tax purposes. (2) That the sum " of £450,000 was a sum paid in settlement of all the Appellants' " claims and rights under the pooling agreements and was a receipt " of the Appellants' trade for the year ended 31st December, 1927."

I agree with Mr. Latter that there are three questions here. The first is: What was this payment for? The second is: If a payment for future rights, is it assessable? The third question is: Ought it to go into the year 1927? I referred earlier to an ambiguity which I think resides in the finding of the Commissioners. The words they use are: " that the £450,000 was paid in " respect of the pooling agreements." I think that that may mean one of two things; it may mean that the payment of the £450,000 was a payment in respect of sums due in the past to the Appellants,

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or it may mean that it was paid in respect of the pooling agreements in the sense that it was paid as a price for the cancellation of the pooling agreements. It is proper to mention that the Attorney-General argued that, on either view, he would be right: he said that he was right even if it was paid as a price, or as damages, as it is expressed to be, for the cancellation of the agreements. Which view the Commissioners took it is not quite easy to discover, but I have to make up my mind as to what on these facts—which are very fully and, considering their complication, very clearly stated—is the correct view.

The first point which it is convenient to deal with is the question as to what on the true view this is a payment for. On that, having regard to what I have already said, I can express my view quite concisely. I think that, looking at the agreement, I am bound, by the agreement, to hold that it was a payment by way of damages for the cancellation of the agreements. Therefore, it was a payment in respect of the future rights.

If that is the true view, is it or is it not assessable? On that there was a considerable amount of authority cited, a line of cases cited by Counsel for the Appellants and a line of cases cited by Counsel for the Crown. It is convenient perhaps to refer, though extremely briefly, to the cases. The first cited for the Appellants was the case of *Chibbett* v. *Joseph Robinson & Sons*, 9 T.C. 48. That was a case where the question was as to the loss of employment and the compensation for the loss of employment of a firm of ship managers. There the matter is discussed by Mr. Justice Rowlatt at page 61, and what he says is this: "If it was a payment in respect of the termination of "their employment I do not think that is taxable. I do not think "that is taxable as a profit. It seems to me that a payment to "make up for the cessation for the future of annual taxable profits "is not itself an annual profit at all." That is laying down the general principle. Then there is a case—not, I think, bearing any very close resemblance to the present, but an important case—*Glenboig Union Fireclay Co., Ltd.* v. *Commissioners of Inland Revenue*, 12 T.C. 427. That was a case which went to the House of Lords, and the point there was this. The company were debarred from working part of their clay fields, and they received a sum of money in respect of that, the sum of money being, no doubt, calculated by reference to what they would have got if they had been able to work that part of their field which was, so to speak, sterilised. That case, as I say, appears to me not to have any very direct bearing on the present, although it is an important case and has been often referred to. Nearer the present is the case of *Hunter* v. *Dewhurst*, 16 T.C. 605. It is unnecessary that I should refer in detail to the facts in the case. The matter

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had reference to a rather special agreement. It may be useful, however, without surveying the whole of the facts, that I should refer to a passage in Lord Atkin's speech which does appear to me to be in point. In citing it, I may say that I am fully conscious of the danger and, indeed, perhaps one might almost say the unfairness, of citing a passage divorced from its context: one must always remember that the words were spoken with reference to the particular case. None the less, what Lord Atkin says at page 645 does seem to me to be in point. "The £10,000", he says, "was not paid "for past remuneration, for the condition of its becoming payable, "for instance, loss of office, never was performed. It was not paid "for future remuneration, for that was expressed to be £250 per "annum, which was to be the sole remuneration. It seems to me "that a sum of money paid to obtain a release from a contingent "liability under a contract of employment cannot be said to be "received 'under' the contract of employment, is not remunera-"tion for services rendered or to be rendered under the contract "of employment, and is not received 'from' the contract of "employment." The facts there, of course, were very different; they related to a contract of employment of a director of a company; but the observations of Lord Atkin and, indeed I may add, the decision of the House of Lords do appear to me to afford support to the argument of Mr. Latter here.

On the other side was cited a line of cases: *Short Brothers, Ltd.* v. *Commissioners of Inland Revenue*, 12 T.C. 955; *Commissioners of Inland Revenue* v. *Northfleet Coal and Ballast Co., Ltd.*, 12 T.C. 1102; *Green* v. *Gliksten*, 14 T.C. 364; and *Burmah Steam Ship Co., Ltd.* v. *Commissioners of Inland Revenue*, 16 T.C. 67. I do not think that it would be useful for me to attempt any detailed review of these cases. The principle appears to be clear enough. One may take the *Short Brothers* case as being an illustration. There the company had a valuable contract to build ships. The persons who had given them the contract were desirous of cancelling it. Thereupon the company agreed to cancellation, but very naturally, the contract being a valuable one out of which they would get money, insisted upon a payment being made in respect of their letting off their contract the persons who had contracted. There, of course, the argument was urged that this sum was not profits of the trade at all, that it was a sum paid by reason of the fact that the trade was, as far as those ships were concerned, not to be carried on, and it was sought to liken the case to the *Glenboig* case[1]. It was held in that case and in several other cases following it that that would not do; it was held that where you get a contract made in the course of carrying on the trade—a contract for the building of a ship, if it is a shipbuilding company, and so forth—the sums paid in respect of that contract, even if they be sums paid to cancel the contract, are just trade

[1] 12 T.C. 427.

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receipts. I do not want to multiply reference to cases but a forcible illustration is in the *Gliksten* case(1), where the company which had large stores of timber had a very serious fire, and the question was whether the money received in respect of that from the insurance company had to be brought in. Of course the contention obviously was: "It is no part of the business to have fires; it "cannot be said that that is what it is carried on for." It is not. But it was held that, it being an incidental part of a business of this sort to insure, if you got your circulating capital, timber, destroyed and if you got a sum of money from the insurance company, you must bring that in, just as much as if you had in the ordinary course of events sold timber and got a sum of money from the purchaser.

These cases sufficiently indicate the sort of contention which was made before me and I have upon them to arrive at a conclusion as to whether this sum—paid, as I find it was, in respect of the future—was or was not liable to assessment. Not without hesitation, I have come to the conclusion that it is not liable to assessment. I think that the agreement, being an agreement whereby this Company had a share in the profits of another company, was a capital asset. I think that the case is to be distinguished from the case where there is a cancellation of a contract made in the ordinary course of the company's business. If the Company had had a contract for the supply of materials for making margarine and that had been cancelled and a sum received in respect of it, it is quite obvious, I think, that that would have been a proper trade receipt. But it seems to me that where one gets, as one does here, not a contract made in the course of the Company's business—for it is not the business of this Company to make pooling agreements or to make agreements whereby they acquire shares in the business of another company—it seems to me that where one gets a payment made in respect of the cancellation of that agreement, that, truly, is a sum received by way of capital and not an income receipt at all. The ground is not very easy to express, but the ground upon which I desire to put this part of the case is this, that the true view here is that the agreement which was cancelled was just a capital asset of the Company and, if that is right, it seems to me to follow that, distinguishing such cases as *Short Brothers*(2), one ought to hold that the sum received was not an income receipt at all. That, as well as I can express it, is the view which I have formed.

But the case is one of undoubted difficulty and it is, I think, proper that I should say something, though quite shortly, upon the other view, which is that this was a sum paid in respect of the past, that is to say, that it was a sum paid in order to make an end of, by way of payment for, the claim which the Appellant Company said they had in respect of the past. If it was that, it was

(1) 14 T.C. 364. (2) 12 T.C. 955.

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clearly a revenue receipt in some way or other and at some time liable to pay tax. The question then is as to the year in which it is to be brought in. On that I had several cases cited to me : *Isaac Holden & Sons'* case, 12 T.C. 768—that is the woolcombers case—the *Newcastle Breweries* case, 12 T.C. 927—that is the case which went to the House of Lords, about the rum—and *Lambert's* case, 12 T.C. 1053—that is the peculiar case with regard to the coal pool at Gibraltar. The result of these cases, as I think, is to show that this revenue receipt—and such it is, on the view which I am now taking—is not a receipt which can be brought in for the year in which it was received ; it must, I think, be spread over the years in which it was earned. It seems to me that rather obvious considerations show that. If it is said : " What were the " profits of the Company for the year 1927?", it seems to me to be obvious at once to say : " Well, whatever they were, this £450,000 " did not form any part of them." That was a sum, on the assumption which I am now making, earned, no doubt, by the Company but earned in the years 1914 to 1924, and it seems to me that it is not possible on any view to say that the £450,000 was part of the profits of the year 1927. I do not develop that further because I think that the reasons will be found fully set out in the three cases to which I have referred. If, therefore, I had been of opinion that this was a sum paid, so to speak, in respect of the past—which expresses sufficiently what I mean—I should have thought that the case would have to go back to the Commissioners with a direction to enquire as to the years in which it was to be brought in. Some sort of spreading of the sum over the years, no doubt, would have to be made. It might have been necessary to consider with some care—and I might have wanted the help of Counsel about it—as to what the reference to the Commissioners should be, but it is, of course, unnecessary to go into that.

I have thought it right, having regard to the importance and the difficulty of the case, to express my views upon all the points which arise; and my view is, as I indicated, that this, being a payment in respect of the future, is not assessable to Income Tax at all. If I am wrong upon that and it is a payment in respect of the past, then my view is that it is assessable to Income Tax, but not in the year 1927. I think it unnecessary to say more.

The result is, on both grounds—but I put the first ground as being the main ground of my decision—that this appeal must be allowed.

Mr. Latter.—The appeal will be allowed with costs, my Lord?

Finlay, J.—Yes.

Mr. Latter.—I am instructed that the money was paid. Would your Lordship make the usual Order for repayment, with interest——

Finlay, J.—This case will probably go further, will it not?

Mr. Latter.—I do not know. Would your Lordship make the Order?

Finlay, J.—I make the Order, yes. It is the usual Order, is it not?

Mr. Latter.—Repayment of the money, with interest at four per cent.? That is the rate which is being given now.

Finlay, J.—Very well; I will make the Order. I think probably it will not become operative.

Mr. Latter.—I do not know, my Lord.

Mr. Hills.—I do not know whether your Lordship will consider that the national rate of interest is daily getting worse——

Finlay, J.—No. I think in this particular case, especially as I suspect it is not very important, I shall adhere to what we have lately enforced as to that.

Mr. Hills.—If your Lordship pleases.

The Crown having appealed against the decision in the King's Bench Division, the case came before the Court of Appeal (Lord Hanworth, *M.R.*, and Slesser and Romer, *L.JJ.*) on the 26th, 27th and 28th June, 1934. On the last named date judgment was given unanimously in favour of the Crown, with costs, reversing the decision of the Court below.

The Attorney-General (Sir Thomas Inskip, K.C.) and Mr. Reginald P. Hills appeared as Counsel for the Crown and Mr. A. M. Latter, K.C., and Mr. Cyril L. King for the Company.

JUDGMENT

Lord Hanworth, M.R.—This case raises once more the troublesome question—and it is really always a troublesome question—as to whether a payment or a receipt, according to the particular circumstances, is to be treated as paid or received on account of capital. A number of cases have been cited and quite rightly enquired into. They to my mind afford little help except as providing illustrations where a decision has been given that particular facts fall on one side of the line or on the other. I am inclined to agree with the attitude of the Court in the *British Dyestuffs Corporation* case, 12 T.C. 586, at page 601, where Lord Justice Bankes excused himself from referring to any authorities because they seemed to him to turn upon their own particular facts and were not of any real assistance in that case; and Lord Justice Warrington expressed himself as taking the same view. I have endeavoured, in more than one case—in *Mallett's* case(1), in the *Anglo-Persian Oil Company* case(2), and in a still more recent case the name of which I forget(3)—to go through and try to find some principle on which the

(1) Mallett *v.* Staveley Coal and Iron Co., Ltd., 13 T.C. 772. (2) 16 T.C. 253.
(3) Golden Horse Shoe (New), Ltd. *v.* Thurgood, 18 T.C. 280.

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Court might be advised to determine its case on one side of the line or the other, and I confess that at the present moment I still hold the view that the best test, although I doubt whether it will afford an answer in all cases, is whether or not the sum has been paid, or has been received, in respect of fixed or circulating capital.

Having made those general observations, I turn, as one must turn in all these cases, to the particular facts before us. We are told by the Case Stated that this Company, Van den Berghs, Limited, is a large organisation engaged in carrying on a big business with large capital, dealing with "margarine, oleo margarine and other "substitutes for butter"; and it appears that there was also another big and well-known firm carrying on in competition with it, namely, Anton Jurgens. These businesses were large, and there was a competition between the Companies, and while each Company retained its own business and, after the agreements to which I will refer, still carried on its respective business independently, they came to an agreement, as I understand, for the purpose of eliminating competition. The statement in paragraph 5 of the Case is this: "The Appellants had for many years been in keen business com- "petition with another firm of margarine manufacturers, Anton "Jurgens . . . . of Holland . . . . and in the year 1908 "these two Companies thought it would be to the advantage of their "respective trades and of the Companies controlled by them to "enter into an agreement for profit sharing and other purposes and "accordingly made the agreement next hereinafter mentioned." I pause for a moment to deal with the point which at that stage seems relevant and which may be helpful as contributing to our conclusion. Supposing, when making that agreement, it had been decided that either the one Company or the other should make a payment to the other for the purpose of offering consideration to the other for making the agreement. Let me suppose that Van den Berghs had made a payment to Anton Jurgens in order to secure the adhesion to that agreement of Anton Jurgens. Would such a payment have been made to secure a capital asset? Would such a payment have been made out of fixed or circulating capital? It appears to me, bearing in mind the illustrations which are afforded by the decided cases, that it would be a payment which would have been made by Van den Berghs out of their circulating capital for securing a particular mode in which the business of their own was to be carried on independently, and still independently of Jurgens, but whereby they would eliminate to a large extent the "keen "business competition" which is spoken of in paragraph 5. It seems to me that such a payment would not have secured a capital asset. It would not have secured the purchase of any shares in Anton Jurgens. It would have merely induced the latter to come into an arrangement whereby both of them could carry on their business more satisfactorily to their respective Companies.

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That view seems confirmed when one examines the actual agreement a little more closely. "The Companies", it is expressed, were "desirous of working in friendly alliance on the terms hereinafter "set forth." There is a period set out, and, under clause 3, it is stated that "The two Companies shall during the continuance of "this agreement work in friendly alliance and shall as regards each "year commencing with the year One thousand nine hundred and "eight share the profits and losses made or sustained in their respec-"tive margarine businesses in proportion to the yearly average "amount of the profits (as ascertained in accordance with the "regulations contained in clause 4)." That is all it is. Then there is a provision, which is found on page 4 of the Case, under item (*i*) of clause 5, whereby it is contemplated that there should be increased capital introduced in respect of the margarine businesses, and when that increased capital has been introduced into the Companies—separated, and continued to be separated, but introduced into those separate Companies—then there is a provision in respect of the profit which is expected to be earned on that capital and which is quantified at the rate of five per cent. per annum; and, in clause 11, on page 5 of the Case, we have the statement that "During the con-"tinuance of this agreement neither of the two Companies shall "enter into or permit or suffer any of the scheduled companies in "which it is interested or any other company for the time being "under its control to enter into any working or pooling arrangement "or any arrangement relating to contract or selling prices or any "other arrangement with any other company or companies . . . . "and each of the two Companies shall be true and loyal to the "other of them and shall do all in the power of such Company to "promote the commercial technical pecuniary buying and selling "and other interests of the parties hereto in relation to the marga-"rine business." After that time, could it be said by any shareholders in either of the Companies that they had lost anything, that their capital had been appropriated in a particular way to the other Company? It seems to me the answer must clearly be a negative one, and that all that had been done was that each should continue, while being loyal to the other, to sell its margarine in its particular spheres according to its best energies, but when it had done that there was to be a pooling of profits and a division of them in accordance with the arrangements laid down, not in accordance with any capital provided by or to the one or the other, but for the purpose of eliminating the cutting competition which so far had militated against the advantageous carrying on of the independent business of each Company.

Just to continue the facts, provision was made for the ascertainment of how the figures stood between the two Companies and ultimately an agreement was entered into in July, 1913, whereby the provisions of the principal agreement were extended to the year

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1940, with certain modifications. The Companies worked away on that basis, and, if it was to be said that the one or the other had secured a capital asset in the sense of this working, it is plain that it had secured what must be treated as a wasting capital asset at its best. Difficulties arose in the ascertainment of the sum which was owed by the one to the other, or on which side the benefit lay, and so an arbitration was entered into. In 1925 it was agreed that the matter should be referred to arbitration and three arbitrators were appointed. The figures were large, and the expense involved was " prodigious "—I take that word from the last line on page 9 of the Case. Apparently, in spite of that outlay, not much advance had been made with the arbitration, because we read that in 1927 the arbitration was still far from being finished. At that time—whether rightly or wrongly I do not stop to enquire—the present Company, Van den Berghs, Limited, claimed that there was a considerable sum which ought to be estimated by the arbitrators in their favour, due from Anton Jurgens to it, and there were still thirteen years to run of the original agreement; and, if it were so that a considerable sum had become due at that date, in 1927, in respect of the working, from Anton Jurgens to Van den Berghs, it might be contended with some foundation that, if the agreement had continued and run out its course till 1940, Van den Berghs would have been entitled to receive a large sum for the profits which would enure in their favour on the balance of the thirteen years' period. A demand was made which was ultimately determined at the sum of £450,000, and Van den Berghs agreed to put an end to the agreement, to the arbitration, and to the principal agreement, if they were paid that sum.

The result was that a complete settlement was arrived at and certain agreements were entered into and concluded on the 24th September, 1927. The first agreement had reference to the holdings and details *inter se* of the Jurgens family and the members of the Van den Bergh family, in respect of which I suppose there was some kinship. The second agreement put an end to the arbitration. The third agreement, which is marked " H " as an exhibit, said this. It recited: " Whereas the Dutch Company have expressed to the " English Company a desire to determine the said agreements " contrary to the provisions therein contained and whereas the " English Company have consented thereto in consideration of the " payment by the Dutch Company to the English Company of the " sum of £450,000 as damages. Now therefore it is agreed " that all the agreements should be determined as from the 31st December, 1927, and the £450,000 was to be paid, as to £100,000, in cash, and, as to £350,000, by promissory notes falling due on the 1st September, 1928, and the 1st September, 1929.

Once more reviewing the facts as they stand, it appears to me that there is nothing which will indicate that there is anything but

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circulating capital involved in these agreements and there is nothing like a purchase on the one side or the release on the other of any capital asset. Ultimately, instead of deferring the payment in the manner contemplated, the full amount of £450,000 was paid in cash in the year ended the 31st December, 1927, and this sum was taken into account in arriving at the estimated assessment to Income Tax which is now the subject of this appeal.

It was contended by the Appellant Company, that is, Van den Berghs, before the Commissioners that this £450,000 was paid as compensation for surrendering their future prospects under the pooling agreements and that the sum was paid for loss of anticipated profits and was a capital sum. The contention of the Crown was that the sum of £450,000 was paid in settlement of these probable and prospective receipts under the pooling agreements and to put an end to all the difficulties then existing between the parties. I attach some importance, although it is by no means conclusive, to the finding of the Commissioners. The Commissioners held "that the £450,000 was paid in respect of the pooling agreements "and must be brought in for the purpose of arriving at the balance "of profits and gains of the Appellants for the year ending 31st "December, 1927". It is perhaps noticeable that that Case is signed by six Commissioners, and we have the advantage of the opinion of the late Sir Henry Seymour King, whose signature stands first and who was, from the point of view of a banker and a business man, well qualified to form an opinion upon such facts. The question, however, is still open to us. The appeal was taken before Mr. Justice Finlay. He came to the conclusion, with very considerable doubt, that the view of the Company was right, and he allowed the appeal. His judgment, in which he expresses that doubt more than once, is based upon this[1]: "The English Company "said: 'Well, we do not mind that, but this will enure to our "'benefit and, in particular, in this respect, that we are entitled to "'a share of your profits, and the great increase of your capital puts "'us in an advantageous position and makes it probable that our "'share will be a good share; therefore, it is a disadvantage to "'us to determine this.' . . . . I do not see how I can give "them" (*i.e.*, the agreements) "the go-by—that the £449,000 was "paid as damages in consideration of the determination of the "agreement." He holds that it was a payment in respect of future rights, and finds some foundation for his decision in the *Glenboig* case[2], in which a company agreed to abandon, once and for all, its right to dig the clay in return for a payment, or, as Lord Buckmaster puts it, it sterilised a portion of its capital in return for a payment; it was dealing there with a capital asset.

From my reading of the facts which I have already stated and from my summary which I have given, it appears to me impossible to treat these agreements as having been entered into for the purchase

(1) See pages 409/10 *ante*. (2) 12 T.C. 427.

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of a capital asset or for the discharge of a capital asset. I am going to refer to the case of *Anglo-Persian Oil Co., Ltd.* v. *Dale*, 16 T.C. 253. In that case I made an effort to run a thread through the cases to see if there was any principle on which it could be said the decisions could be founded and I came to the conclusion, which I have expressed before, that the question which will explain most of the cases is whether or not the money has been paid out of or received into the fixed or the circulating capital of the company which pays or receives it, and I found myself in difficulty in applying the test which Lord Cave suggested of an enduring asset. Applying that principle which I have previously suggested, it appears to me that there was no capital asset purchased; there was no capital sum by which the capital of Anton Jurgens was depleted when the agreements were entered into, and there was no capital sum repaid to Van den Berghs when they received the £450,000, and they did not acquire an interest in somebody else's trade, as they would have done if they had purchased shares. They did not secure any control of the trade. All that they did was to secure what might be called a gentlemen's agreement that they should work loyally to each other and eliminate competition.

In the *Anglo-Persian* case it was said, with some force, that a very large payment had been made to secure what was an outlying piece of capital, which was then in the hands of Strick Scott & Company, Limited, but we came to the conclusion that[1] "The "payment is to put an end to an expensive method of carrying on "the business which remains the same whether the distributive "side is in the hands of the Respondents themselves, or of their "agents." So, here, this payment is received in respect of a beneficial arrangement, or so it was supposed, gained by Van den Berghs under an agreement under which the business of each company remained the same and is now restored to the independent initiative and competition of each of them, but it has not secured the return or the release of any capital asset.

Another case which is, to my mind, illustrative of a similar point is the case of *Noble* v. *Mitchell*[2], where a payment was made to get rid of a director who impeded the business. In one sense, if his absence could be treated as permanent and as an advantage, it might be said that that was a payment out of capital, but we held, on principles which are clearly indicated by Lord Justice Sargant[3], that it was a payment in respect of the carrying on of the business of the company.

Under these circumstances, I have come to the conclusion that the appeal ought to be allowed, that the claim of the Crown is right, and that the Order of Mr. Justice Finlay must be discharged and the decision of the Commissioners restored. The appeal, therefore, will be allowed with costs here and below.

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(1) 16 T.C., at p. 268. (2) 11 T.C. 372. (3) *Ibid.*, at pp. 421 *et seq.*

Slesser, L. J.—I have arrived at the same conclusion. In dealing with these questions of assignment to capital or to revenue expense one has, in the first place, I think, to distinguish between that class of case where the Crown is seeking to tax moneys received by the subject and that class of case where the subject is seeking to say that he has been put to an expense in the nature of an income expense and is entitled to a deduction. Some of the authorities have dealt with the one set of facts and some with the other.

In the present case it is the fact that here Van den Berghs, the Respondents, have received a sum of money. This is not a case where they have been put to an expense and, therefore, they are concerned here to show—doubtless it would have been otherwise had they been claiming a deduction—that this money which they have received is in the nature of a capital asset and therefore not liable to tax at all. The sum which they have received, the sum of £450,000, is a sum by way of commutation or compensation for certain rights which, it was accepted, I think, by the learned Judge, by the Commissioners, and certainly by both parties to the agreements, they possessed under three agreements which they had entered into with another and competitive firm of Anton Jurgens. I agree with the learned Judge that, when these complicated negotiations and arbitrations are dissected, it appears ultimately from the agreement of the 24th September, 1927, exhibit "H", as there recited, that "Whereas the Dutch Company have expressed to the "English Company a desire to determine the said agreements "contrary to the provisions therein contained and whereas the "English Company have consented thereto in consideration of the "payment by the Dutch Company to the English Company of the "sum of £450,000 as damages. Now therefore it is agreed as follows: "The said agreements as between the parties hereto are hereby "determined as from 31st December, 1927, and each party hereto "releases the other party from all claims thereunder." If this settlement had been in consideration of the cancellation of a trade agreement, there can be no doubt at all—and if there had been any doubt it is made quite plain by the cases of *Short Brothers* and the *Sunderland Shipbuilding Company*[1]—that this would be a payment in commutation of the trading contract and would itself be in the nature of a revenue payment. The learned Judge himself accepts that view, but he goes on to distinguish between a payment which would be made in commutation of a trading contract which had been abandoned and as to which, therefore, the payee would otherwise have lost something by its termination, and a case like this, which he says is not a contract made in the ordinary course of the company's business. He says[2]: "I think that the agreement, "being an agreement whereby this Company had a share in the "profits of another company, was a capital asset. I think that the

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[1] 12 T.C. 955.

[2] See page 413 *ante*.

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" case is to be distinguished from the case where there is a cancella-
" tion of a contract made in the ordinary course of the company's
" business." As I say, there is no question here that this money was paid to enable Van den Berghs to be free of the contract in the sense that that freedom would be worth something to them. As I read it, it is really a case where Van den Berghs were paid something because they were losing a valuable asset which they would otherwise have got.

Therefore the question really comes down to this, whether that asset, for the loss of which they are compensated, was in the nature of fixed capital or circulating capital. In my view it is not possible here to say that this asset, notwithstanding the interesting and important argument of Mr. Cyril King, is fixed capital. It is not, I think, like a case where this could be sold as a part of the capital rights of Van den Berghs to a third party. As Mr. King argued it, he said this, as I understood him : " This right to deal with Jurgens, " this right to be absolved from certain competition which would " otherwise arise, is a valuable and permanent right which could " have been sold as one of the assets of the Van den Bergh Company, " and the commutation of that right, like the right itself, is therefore " a satisfaction in the nature of capital." But it is not so. This Company, the objects of which are exhibited, has put in its memorandum, not merely as an enabling object, but, as I read it, as one of the principal methods of carrying on its business as manufacturers of various things : to work in arrangement " for sharing profits, " union of interest, co-operation, joint adventure, reciprocal con-
" cession, or otherwise, with any person or company carrying on, or
" engaged in . . . . any business or transaction which this
" Company is authorised to carry on, or to engage in any business or
" transaction capable of being conducted so as directly or indirectly
" to benefit this Company." It appears that there is a direct power taken in the memorandum, and I see, with interest, a power added by order of Mr. Justice Swinfen Eady, in 1912, to the original objects, for the purpose of dealing with the business in just such a manner as has here been adopted.

Then when we look at the actual agreement entered into between the parties, it is, in my opinion, a great deal more than a mere profit sharing arrangement. It is provided that the Companies " are
" desirous of working in friendly alliance on the terms hereinafter
" set forth ", and the terms of friendly alliance include an obligation on the part of each Company to make no arrangements with other persons outside inconsistent with the arrangements made with one another, an obligation which, by clause 8, is extended to each of the scheduled directors ; the setting up of a joint committee of both bodies for the purpose of dealing with the subject matter of the agreement with committees and the like, and power of delegation, and the restriction of their holding inconsistent interests, and, as it

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seems to me, many matters of agreement carrying out the intention to work in friendly alliance set out in the preamble to the agreement itself. It is in relation to the termination of that agreement, which is itself essentially, as it seems to me, a business agreement, that this money was paid in relation to the business as such. The contrast is shown very clearly between such a transaction and the sort of transaction which is referred to or was the subject matter of consideration in *Mallett* v. *Staveley Coal and Iron Co., Ltd.*, 13 T.C. 772. There, at page 787, Lord Justice Lawrence points out that that case, resembling *John Smith and Son* v. *Moore*, 12 T.C. 266, was a case where "'The business carried on'"—he is speaking there of *John Smith and Son* v. *Moore*, but the same sort of considerations applied in *Mallett*—"'was not that of "buying and selling contracts,'"—in *Mallett*, it was a case of dealing with leases—"'but of buying and selling coals, and the contracts, "'which enabled the seller of the coals to acquire the coals, were no "'more the subject of his trading as the stock-in-trade for sale than a "'lease of a brickfield would be the subject of a sale of bricks.'"

In the present case I think that these arrangements were essentially a part of the subject of the trade; they were not some extraneous matter, as has been the case in those cases where it was held to be a capital asset. I use the word "extraneous" in the sense of meaning something not merely ancillary, to quote the language which my Lord used in the *Anglo-Persian Oil* case; my Lord said(1): "It seems rather that the cases of *Hancock*(2), and of *Noble* v. "*Mitchell*(3), and of *Mallett* v. *Staveley Coal Company*(4) give illus- "trations that the test of fixed or circulating capital is the true one; "and where, as in this case, the expenditure is to bring back into "the hands of the Company a necessary ingredient of their existing "business—important, but still ancillary and necessary to the "business which they carry on—the expenditure ought to be debited "to the circulating capital rather than to the fixed capital, which "is employed in and sunk in the permanent—even if wasting— "assets of the business." Here, as I say, as it seems to me, all the arrangements which were made were ancillary and necessary to the business which was carried on, and were part of the trading business and were in the nature, therefore, of circulating capital.

Therefore, I think that the learned Judge was mistaken in coming to the conclusion that he could distinguish this case from the principle laid down in *Short Brothers'* case(5). In the view which I take, in which I agree with the learned Judge, that this compensation was paid in respect of the termination of the agreement and therefore was paid as on the date of the agreement, exhibit "H", namely, the 24th September, 1927, the other question about whether there should be any allocation of the dates when the payments fall due does not arise.

(1) 16 T.C., at p. 268.
(2) Hancock *v.* General Reversionary and Investment Company, Ltd., 7 T.C. 358.
(3) 11 T.C. 372. (4) 13 T.C. 772. (5) 12 T.C. 955.

Romer, L.J.—I, too, have arrived at that conclusion. I agree with Mr. Justice Finlay in his decision that the payment of the £450,000 was not a payment in settlement of the claims that had been made in respect of the period before 1927, but was a payment in respect of the rights to accrue to Messrs. Van den Berghs in the future. I am unable to agree with the learned Judge in the conclusion at which he arrived that that payment was in the nature of a capital payment. For the purposes of considering whether it is to be treated as a capital payment or a revenue payment, it is a legitimate test to apply to consider whether, supposing Messrs. Van den Berghs had paid a lump sum down to secure the advantages of the contract which they entered into with Messrs. Jurgens, the sum so paid could have been treated by them as a payment on capital account. Had the contract been a contract merely for the acquisition of a share in the profits of Messrs. Jurgens, I should not doubt that a payment so made would have been a capital expenditure. The Company would have had in its possession a capital asset which it could value and which it could dispose of, if it thought fit, to somebody else. The contract that they entered into with Jurgens is of a very different nature. I do not propose to analyse the terms of it; that has already been done by the other members of the Court. It is sufficient, I think, to say that, so analysing it, the contract appears to be no more than a trading convention entered into between the two parties for the purpose of so regulating the conduct of their trade that they each might continue to trade to a greater advantage than before. It was, I think, a trading operation entered into in the course of, and for the purposes of, Messrs. Van den Berghs' business. That being so, applying the test that has been laid down in the cases to which the Master of the Rolls has called attention, I think the conclusion one would have to come to would be that a sum laid out for the purposes of acquiring the benefit of a contract would not have been a sum paid as a capital expenditure but a sum paid in the nature of circulating capital.

For these reasons I agree that this appeal must be allowed.

An appeal having been entered against the decision in the Court of Appeal, the case came before the House of Lords (Lords Atkin, Tomlin, Russell of Killowen, Macmillan and Wright) on the 4th, 5th, 7th and 8th March, 1935, when judgment was reserved. On the 8th April, 1935, judgment was given unanimously against the Crown, with costs, reversing the decision of the Court below.

Sir William Jowitt, K.C., Mr. A. M. Latter, K.C., and Mr. Cyril L. King appeared as Counsel for the Company and the Attorney-General (Sir Thomas Inskip, K.C.), the Solicitor-General (Sir Donald Somervell, K.C.) and Mr. Reginald P. Hills for the Crown.

JUDGMENT

Lord Atkin.—My Lords, I have had an opportunity of reading the opinion which is about to be delivered by my noble and learned friend Lord Macmillan. I agree with it, and have nothing to add.

Lord Tomlin.—My Lords, I also have had an opportunity of reading the opinion which is about to be delivered by my noble and learned friend Lord Macmillan, and I concur in it in all respects and have nothing to add.

Lord Macmillan.—My Lords, in the year 1927 the Appellants received payment of a sum of £450,000 from Anton Jurgens Vereenigde Fabrieken of Holland (whom I shall call " the Dutch " Company ") pursuant to the terms of an agreement between the Appellants and the Dutch Company dated 24th September, 1927. The question is whether this sum ought to be taken into account in computing the balance of the profits or gains of the Appellants' trade for the year 1927 on which they are chargeable to tax for the year 1928–29 under Schedule D of the Income Tax Act, 1918.

The Appellants say that the £450,000 was a capital receipt and ought not to be reckoned as forming any part of the profits arising from the carrying on of their trade. The Crown says that the £450,000 was a trade receipt which ought to be included in the computation of the Appellants' profits or gains for Income Tax purposes.

The circumstances in which the Appellants received the payment which has now to be examined are set out in the Stated Case, from which I select the salient facts. The Appellants were incorporated as a limited company in this country in 1895 and have since carried on the business of manufacturing and dealing in margarine and similar products on a very extensive scale both here and abroad. They had as their keenest competitors the Dutch Company, which was engaged in the same business in Holland. On the 13th February, 1908, the two Companies entered into an agreement whereby they bound themselves for the future to " work " in friendly alliance " and to share their profits and losses in conformity with an elaborate scheme detailed in the agreement. Each of the two Companies had a controlling interest in a number of other companies and they undertook that, if either of them or any of the companies which they controlled should acquire an interest in any other margarine concern, the fact should be communicated to the other party, who should have an option to require such interest to be brought within the operation of the agreement. Both Companies further undertook on behalf of themselves and of their controlled companies not to enter into any pooling or price arrangements with third parties which might be deemed inimical to the interests of the two Companies under the agreement. The directors and managers of the respective Companies were parties to the agreement and bound themselves for twenty years not to engage

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in any margarine business other than that of the two Companies. Provision was also made for the setting up of a representative joint committee which was empowered to make arrangements with outside companies and firms as to the selling and buying prices of margarine and the limitation of areas of supply. It was further comprehensively agreed that " each of the two Companies shall be " true and loyal to the other of them and shall do all in the power " of such Company to promote the commercial technical pecuniary " buying and selling and other interests of the parties hereto in " relation to the margarine business." It is not necessary to set out the detailed provisions of the agreement, but its elaborate character is sufficiently indicated by the fact that it consists of thirty-five articles (with numerous sub-heads) and five schedules, and extends to twenty-two pages of print in the Case before your Lordships.

A supplemental agreement was entered into between the parties on the 17th July, 1913, which recited that the Dutch Company had acquired rights in a process for hardening oils and that the parties were desirous of formulating a scheme for the merger of their assets or the unification of their financial and commercial interests and for the regulation and allocation of their turnover, but that such a scheme could not at present be fully elaborated to their satisfaction, and it was desirable in the meantime to regulate their mutual relations and modify and extend the principal agreement in the manner provided in the supplemental agreement. By this second agreement the parties modified the original basis of ascertaining and sharing profits and, subject thereto, agreed to continue in force the relative provisions of the principal agreement until 31st December, 1940. Provision was made for the formation of a Committee to endeavour to devise the scheme of merger or unification mentioned in the recital, and, failing agreement upon such a scheme by the 15th December, 1913, the parties bound themselves to execute a contract confirming and extending to the 31st December, 1940, the provisions of the supplemental agreement and of a scheduled document setting out agreed alterations in their existing pool contract.

According to the Stated Case, " Each Company carried on its " business independently, but in general the parties observed the " terms of the said agreements for each of the years 1908 to 1913, " and the profits of the two Companies were accounted for for " those years. Payments were in fact made by and to the Appel- " lants under the said agreements in these years. Such payments " when made to the Dutch Company were deducted as an expense " and when made by the Dutch Company were brought in as a " receipt in making up the Appellants' profit and loss accounts for " the years in which the payments were made or received. In " computing the Appellants' Income Tax liability for the said years,

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" the amount of such payments or receipts was deducted or " brought in to the taxable profit respectively and the Income Tax " paid accordingly. It was also agreed by the Appellants when " liability for Income Tax and Excess Profits Duty was under con- " sideration for years subsequent to 1913, that the results of " working the said agreements should be charged to Income Tax " and Excess Profits Duty as trading receipts and payments."

During the war the two Companies did not operate the agreements, and after peace was restored they found it desirable to enter into a fresh agreement in an endeavour to render workable the two previous agreements which were then running and would not terminate till 1940. This third agreement, which was dated 15th October, 1920, recited that some of the provisions of the previous agreements had become obsolete or impracticable. It then proceeded to provide that, subject to the amendments and additions thereby effected, the principal agreement should remain in force till the 31st December, 1940. Further provision was made for the mutual communication of information relating to manufacturing processes, the basis of the ascertainment and division of profits was modified, the branches of business embraced were extended and various other matters were regulated. As in the case of the two previous agreements, all disputes were referred to arbitration.

Meantime the Appellants had been endeavouring to estimate the sum which they believed had accrued due to them by the Dutch Company over the war period. After various tentative calculations they brought out in 1922 a sum of £449,042, which they alleged was owing to them. The Dutch Company disputed this figure and claimed that on the contrary the Appellants were on balance indebted to them. The matter went to arbitration in 1925. The proceedings dragged on inconclusively at " prodigious " expense until in 1927 the parties came to an arrangement which was embodied in three agreements all dated 24th September, 1927.

By the first of these agreements the members of the Jurgens family and the members of the Van den Bergh family agreed to consolidate their respective interests in a Dutch holding company and an English holding company on the terms therein mentioned.

By the second of these agreements each party withdrew all claims against the other party under the agreements of 1908, 1913 and 1920 for the years 1914 to 1927 inclusive, and both parties mutually discharged each other from any liability arising thereunder before 31st December, 1927. Each party further undertook to do everything necessary to put an end to the arbitration.

The third of these agreements recited that the Dutch Company had expressed to the Appellants a desire to determine the agreements of 1908, 1913 and 1920 contrary to the provisions therein contained, and that the Appellants had consented thereto in consideration of the payment to them by the Dutch Company of

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£450,000 " as damages ". The agreement consists of two articles only. By the first article the parties agreed that the three agreements of 1908, 1913 and 1920 should be thereby determined as from 31st December, 1927, and each party released the other party from all claims thereunder. By the second article the Dutch Company undertook forthwith to pay to the Appellants a sum of £100,000 and to hand to them promissory notes for a further sum of £350,000 payable as therein stated. In point of fact the total sum of £450,000 was paid in cash by the Dutch Company to the Appellants before the expiry of the year 1927. This is the sum in dispute in the present appeal.

The General Commissioners held that " the £450,000 was paid " in respect of the pooling agreements and must be brought in for " the purpose of arriving at the balance of profits and gains of the " Appellants for the year ending 31st December, 1927 ". That is their sole finding; it is not informative, for everyone agrees that the sum in question was paid " in respect of the pooling agree- " ments ", but there can be no doubt, if regard be had to the contentions submitted to them, that the Commissioners' view was that the sum in question was an income receipt.

Mr. Justice Finlay reversed the determination of the General Commissioners and held that the agreements which were cancelled were " a capital asset " of the Appellants and that the £450,000 was " not an income receipt at all ". The Court of Appeal unanimously reversed this judgment and restored the determination of the General Commissioners, holding that the sum was not received by the Appellants in consideration of the surrender of a fixed capital asset but arose from a transaction attributable to circulating capital, and was consequently an income receipt.

My Lords, the problem of discriminating between an income receipt and a capital receipt and between an income disbursement and a capital disbursement is one which in recent years has frequently engaged your Lordships' attention. In general the distinction is well recognised and easily applied, but from time to time cases arise where the item lies on the borderline and the task of assigning it to income or to capital becomes one of much refinement, as the decisions show. The Income Tax Acts nowhere define " income " any more than they define " capital "; they describe sources of income and prescribe methods of computing income, but what constitutes income they discreetly refrain from saying. Nor do they define " profits or gains "; while as for " trade ", the " interpretation " Section of the 1918 Act (Section 237) only informs us, with a fine disregard of logic, that it " includes every trade, manufacture, adventure or concern in the " nature of trade ". Consequently it is to the decided cases that one must go in search of light. While each case is found to turn upon its own facts, and no infallible criterion emerges, nevertheless

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the decisions are useful as illustrations and as affording indications of the kind of considerations which may relevantly be borne in mind in approaching the problem.

The reported cases fall into two categories, those in which the subject is found claiming that an item of receipt ought not to be included in computing his profits and those in which the subject is found claiming that an item of disbursement ought to be included among the admissible deductions in computing his profits. In the former case the Crown is found maintaining that the item is an item of income; in the latter, that it is a capital item. Consequently the argumentative position alternates according as it is an item of receipt or an item of disbursement that is in question, and the taxpayer and the Crown are found alternately arguing for the restriction or the expansion of the conception of income.

I propose to refer first to the case of *British Insulated and Helsby Cables, Ltd.* v. *Atherton*, [1926] A.C. 205(1). This case has been generally recognised as the leading modern authority on the subject, though I fear that Lord Justice Romer was unduly optimistic when he said that it " placed beyond the realms of " controversy " the law applicable to the matter (*Anglo-Persian Oil Co., Ltd.* v. *Dale*, [1932] 1 K.B. 124, at page 145(2)). The facts were that the Appellant Company claimed to deduct in the computation of its trade profits a sum which it had provided to form the nucleus of a pension fund for its employees. The Crown argued that the sum ought to be debited to capital on the ground that it " was not in its nature recurrent, but was made once for " all " and that it was a case of the " provision of a capital sum " which will for ever after relieve the company from making any " further payment whatsoever "(3). This argument prevailed. The Lord Chancellor, Viscount Cave, found in the decisions " considerable authority " for the view which he recommended to the House to adopt, namely, that " when an expenditure is made, " not only once and for all, but with a view to bringing into exist- " ence an asset or an advantage for the enduring benefit of a trade, " . . . . there is very good reason (in the absence of special " circumstances leading to an opposite conclusion) for treating such " an expenditure as properly attributable not to revenue but to " capital " (pages 213–4)(4). Lord Atkinson (at page 222)(5) indicated that the word " asset " ought not to be confined to " something material " and, in further elucidation of the principle, Lord Justice Romer has added that the advantage paid for need not be " of a positive character " and " may consist in the getting " rid of an item of fixed capital that is of an onerous character " (*Anglo-Persian Oil Co., Ltd.* v. *Dale*, [1932] 1 K.B. 124, at page 146(6)).

(1) 10 T.C. 155. (2) 16 T.C. 253, at p. 273. (3) [1926] A.C., at p. 209.
(4) 10 T.C., at pp. 192/3. (5) *Ibid.*, at p. 199. (6) 16 T.C., at p. 274.

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My Lords, if the numerous decisions are examined and classified, they will be found to exhibit a satisfactory measure of consistency with Lord Cave's principle of discrimination. Certain of them relate to Excess Profits Duty and not to Income Tax, but for the present purpose this distinction is immaterial. A sum provided to establish a pension fund for employees, as has already been seen, is a capital disbursement (*British Insulated and Helsby Cables, Ltd.* v. *Atherton*); so is a sum paid by a coal merchant for the acquisition of the right to a number of current contracts to supply coal, (*John Smith & Son* v. *Moore*, [1921] 2 A.C. 13([1])); so is a payment by a colliery company as the price of being allowed to surrender unprofitable seams included in its leasehold (*Mallett* v. *Staveley Coal & Iron Co., Ltd.*, [1928] 2 K.B. 405([2])). Similarly, a sum received by a fireclay company as compensation for leaving unworked the fireclay under a railway was held to be a capital receipt (*Glenboig Union Fireclay Co., Ltd.* v. *Commissioners of Inland Revenue*, [1922] S.C. (H.L.) 112([3])).

On the other hand, a sum awarded by the War Compensation Court to a company carrying on the business of brewers and wine and spirit merchants in respect of the compulsory taking over of its stock of rum by the Admiralty was held to be a trade or income receipt (*Commissioners of Inland Revenue* v. *Newcastle Breweries, Ltd.*, 12 T.C. 927); so was a sum paid to a shipbuilding company for the cancellation of a contract to build a ship (*Short Bros., Ltd.* v. *Commissioners of Inland Revenue*, 12 T.C. 955); so was a lump sum payment received by a quarry company in lieu of four annual payments in consideration of which the company had relieved a customer of his contract to purchase a quantity of chalk yearly for ten years and build a wharf at which it could be loaded (*Commissioners of Inland Revenue* v. *Northfleet Coal and Ballast Company, Ltd.*, 12 T.C. 1102); so was a sum recovered from insurers by a timber company in respect of the destruction by fire of their stock of timber (*J. Gliksten & Son, Ltd.* v. *Green*, [1929] A.C. 381([4])). Conversely, where a company paid a sum as the price of getting rid of a life director, whose presence on the board was regarded as detrimental to the profitable conduct of the company's business, the payment was held to be an income disbursement (*Mitchell* v. *B. W. Noble, Ltd.*, [1927] 1 K.B. 719([5])); so was the payment made in the case of the *Anglo-Persian Oil Co., Ltd.*, v. *Dale*([6]), in order to disembarrass the company of an onerous agency agreement. There are further instances in the reports, but I have quoted enough for the purposes of illustration.

With the guidance thus afforded I now address myself to the question whether the £450,000 received by the Appellants in the circumstances already narrated can properly be described as an

([1]) 12 T.C. 266. ([2]) 13 T.C. 772. ([3]) 12 T.C. 427.
([4]) 14 T.C. 364. ([5]) 11 T.C. 372. ([6]) 16 T.C. 253.

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item of profit arising or accruing to them from the carrying on of their trade, which ought to be credited as an income receipt. It is important to bear in mind at the outset that the trade of the Appellants is to manufacture and deal in margarine, for the nature of a receipt may vary according to the nature of the trade in connection with which it arises. The price of the sale of a factory is ordinarily a capital receipt, but it may be an income receipt in the case of a person whose business it is to buy and sell factories.

My Lords, the learned Attorney-General stated that he was content to take the agreements of 1927 as meaning what they say. The sum of £450,000 is accordingly to be taken as having been paid by the Dutch Company to the Appellants in consideration of the Appellants' consenting to the agreements of 1908, 1913 and 1920 being terminated as at 31st December, 1927, instead of running their course to 31st December, 1940. If the payment had been in respect of a balance of profits due to the Appellants by the Dutch Company for the years 1914 to 1927, different considerations might have applied, but it is agreed that it is not to be so regarded.

Now what were the Appellants giving up? They gave up their whole rights under the agreements for thirteen years ahead. These agreements are called in the Stated Case " pooling agreements ", but that is a very inadequate description of them, for they did much more than merely embody a system of pooling and sharing profits. If the Appellants were merely receiving in one sum down the aggregate of profits which they would otherwise have received over a series of years, the lump sum might be regarded as of the same nature as the ingredients of which it was composed. But even if a payment is measured by annual receipts, it is not necessarily in itself an item of income. As Lord Buckmaster pointed out in the case of the *Glenboig Union Fireclay Co., Ltd.* v. *Commissioners of Inland Revenue*(1) : " There is no relation between the " measure that is used for the purpose of calculating a particular " result and the quality of the figure that is arrived at by means of " the application of that test."

The three agreements which the Appellants consented to cancel were not ordinary commercial contracts made in the course of carrying on their trade; they were not contracts for the disposal of their products or for the engagement of agents or other employees necessary for the conduct of their business; nor were they merely agreements as to how their trading profits when earned should be distributed as between the contracting parties. On the contrary, the cancelled agreements related to the whole structure of the Appellants' profit-making apparatus. They regulated the Appellants' activities, defined what they might and what they might not do, and affected the whole conduct of their business. I have difficulty

(1) 12 T.C. 427, at p. 464.

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in seeing how money laid out to secure, or money received for the cancellation of, so fundamental an organisation of a trader's activities can be regarded as an income disbursement or an income receipt. Mr. Hills very properly warned your Lordships against being misled as to the legal character of the payment by its magnitude, for magnitude is a relative term and we are dealing with companies which think in millions. But the magnitude of a transaction is not an entirely irrelevant consideration. The legal distinction between a repair and a renewal may be influenced by the expense involved. In the present case, however, it is not the largeness of the sum that is important but the nature of the asset that was surrendered. In my opinion that asset, the congeries of rights which the Appellants enjoyed under the agreements and which for a price they surrendered, was a capital asset.

I have not overlooked the criterion afforded by the economists' differentiation between fixed and circulating capital which Lord Haldane invoked in *John Smith & Son* v. *Moore*, 12 T.C. 266, and on which the Court of Appeal relied in the present case, but I confess that I have not found it very helpful. Circulating capital is capital which is turned over and in the process of being turned over yields profit or loss. Fixed capital is not involved directly in that process, and remains unaffected by it. If this is to be the test, I fail to see how the Appellants could be said to have been engaged in turning over the asset which the agreements in question constituted. The agreements formed the fixed framework within which their circulating capital operated; they were not incidental to the working of their profit-making machine but were essential parts of the mechanism itself. They provided the means of making profits, but they themselves did not yield profits. The profits of the Appellants arose from manufacturing and dealing in margarine.

For these reasons I am of opinion that the judgment of the Court of Appeal should be reversed with costs and the judgment of Mr. Justice Finlay restored.

Lord Wright.—My Lords, I am in full agreement with the opinion which has just been delivered by my noble and learned friend Lord Macmillan, and I have nothing to add.

Lord Atkin.—My Lords, I am asked by my noble and learned friend **Lord Russell of Killowen** to say that he has read the opinion which has just been delivered and that he agrees with it.

Mr. Cyril King.—My Lords, may I make an application with regard to the tax which has been paid by the Appellants in your Lordships' House, and the interest, both being repayable under the Statute, the question for your Lordships being the rate of the interest on the tax paid?

Lord Atkin.—Is there any difference between you as to the rate?

Mr. Cyril King.—No, my Lord. The position was that after Mr. Justice Finlay's judgment the tax which had been paid was returned to my clients by the Revenue with interest at 4 per cent. After the judgment of the Court of Appeal that money was returned; so the position would be that, though I need not trouble your Lordships with the question of the amount of the tax, the question of interest should be settled, I think, by your Lordships.

Lord Macmillan.—The rate is well recognised, is it not?

Mr. Cyril King.—It was 4 per cent. in this case down to the date of repayment under the Order of the Court of Appeal, but my friend and I have agreed that so recently as last Friday Mr. Justice Finlay directed that the rate should be 3½ per cent. A lot of this interest has changed hands on the basis of 4 per cent. down to a certain date.

Lord Atkin.—What was the date of the Order of the Court of Appeal?

Mr. Cyril King.—The date of the Order of the Court of Appeal was 20th July, 1934: at any rate that was the date of the return. I think the Order was rather earlier.

Lord Atkin.—I think it ought to be 4 per cent. on this occasion.

Lord Wright.—It has been 4 per cent. so far?

Mr. Cyril King.—Yes, my Lord. The date of the Order was the 28th June, and I am told that the payment was made on the 20th July.

Lord Atkin.—Do you want an Order if we intimate our opinion about it?

Mr. Cyril King.—If your Lordships would state the rate, that is all I need.

Lord Atkin.—We think that on this occasion it should be 4 per cent. That is not laying down any general rule, but it is simply because in this particular case on other occasions it has been 4 per cent.

Mr. Cyril King.—I am instructed that in this particular case it was 4 per cent.

Lord Atkin.—Then that will be put in the Order.

Questions put:

That the Order appealed from be reversed.

The Contents have it.

That the Order of Mr. Justice Finlay be restored and that the Respondent do pay to the Appellants their costs here and in the Court of Appeal.

The Contents have it.

[Solicitors:—Goulden, Mesquita & Co.; Solicitor of Inland Revenue.]