

[HIGH COURT OF AUSTRALIA.]

THE FOSTER BREWING CO. LTD. . . . APPELLANT;

AND

THE FEDERAL COMMISSIONER OF TAXA-  
TION . . . . . } RESPONDENT.

H. C. OF A. *Income Tax—Assessment—Company—Income—Deduction—Dividends—Payment*  
1916. *out of profits—Income Tax Assessment Act 1915 (No. 34 of 1915), sec. 16.*

MELBOURNE,  
Oct. 25.

Griffith C.J.,  
Barton, Isaacs,  
Gavan Duffy  
and Rich J.J.

Griffith C.J.

A company, whose assets consisted principally of shares in another company, paid a dividend for each of the half-years ending 31st January 1915 and 31st July 1915. A few days before each dividend was paid the company had no money in hand. It had in its books an account called a reserve fund of the nominal amount of £15,000 which represented undivided profits that had been invested in income-producing property. Immediately before the payment of each of the two dividends the company received by way of income from its assets a sum rather larger than the amount of the dividend. Each sum when received was paid to the credit of the company's banking account, which was then overdrawn, and each dividend was immediately paid by cheques drawn upon that banking account. In its return of income for the year ending 30th June 1915 for the purposes of the *Income Tax Assessment Act 1915* the company claimed to deduct the amount of the two dividends from its total income for that year, but the Commissioner apportioned the dividends between the amount appearing in the profit and loss account for the half-year ending 31st January 1915 as having been brought forward from the previous half-year and the net profit for the year, and allowed a deduction of only the proportionate amount of the dividend so attributed to the net profit for the year.

*Held*, that the fact that in the profit and loss accounts the dividends paid were debited against the gross sums made up of the net profits of the preceding half-years together with the balances brought forward from the previous periods was not conclusive to show that the dividends sought to be deducted were not wholly income distributed to the members of the company within the meaning of sec. 16 of the *Income Tax Assessment Act 1915*.



*Held*, by *Griffith C.J.*, on the evidence, that the dividends sought to be deducted were wholly income distributed to the members within the meaning of sec. 16.

H C. OF A.  
1916.

CASE STATED and hearing of appeal from the Federal Commissioner of Taxation.

FOSTER  
BREWING  
CO. LTD.  
v.  
FEDERAL  
COMMISSIONER OF  
TAXATION.

On the hearing of an appeal by the Foster Brewing Co. Ltd. to the High Court against an assessment of them by the Federal Commissioner of Taxation for income tax for the year ending 30th June 1915, *Griffith C.J.* stated the following case for the determination of the Full Court :—

1. The Foster Brewing Co. is a company duly incorporated under the Companies Acts of Victoria and has its registered office in Melbourne in the State of Victoria. The Company is what is called a "holding company," its assets consisting principally of shares in another company.

2. The Company issued half-yearly balance-sheets and profit and loss accounts as on 31st January 1915, 31st July 1915 and 31st January 1916.

3. The actual net profit of the Company for the two half-years from 1st August 1914 to 31st July 1915 was £6,044 2s. 11d.

4. In respect of that period the sum of £5,760 was distributed by the Company amongst its members by way of dividends and bonuses pursuant to the following resolutions duly passed by the members of the Company :—

"22nd February 1915. That a dividend at the rate of 8 per cent. per annum and a bonus at the rate of 2 per cent. per annum for the half-year ended 31st January 1915 be declared."

"30th August 1915. That a dividend at the rate of 8 per cent. per annum and a bonus at the rate of 2 per cent. per annum for the half-year ended 31st July 1915 be declared payable forthwith."

5. The Company kept a single current banking account, to the credit of which it paid all moneys received. A sum of £15,000, representing undistributed profits, was invested in income-producing property. This sum was called a reserve fund.

6. The said dividends and bonuses, which amounted respectively to £2,880 were paid by the Company out of the moneys standing to the credit of its banking account. Except as appears by the



H. C. OF A.  
1916.

FOSTER  
BREWING  
CO. LTD.  
v.  
FEDERAL  
COMMISSIONER OF  
TAXATION.

profit and loss accounts they were not specially debited to, or paid out of, any particular fund.

7. The amount standing to the credit of the said banking account on 22nd February 1915 prior to the payment of dividend was £3,083 11s. 9d., which sum was in fact made up entirely of dividends and interest received by the Company after 9th February, on which date the account was overdrawn.

8. The amount standing to the credit of the said banking account on 30th August 1915 prior to the payment of dividend was £3,161 7s. 11d., which sum except as to £114 2s. 11d. was in fact made up entirely of dividends and interest received by the Company after 23rd August, on which date the account was overdrawn. The said sum of £114 2s. 11d. was part of the proceeds of the Company's investments, and was not part of the year's income.

9. On 11th November 1915 the Company pursuant to the *Income Tax Assessment Act* 1915 furnished to the Federal Commissioner of Taxation a return setting forth a statement of the income received by it during the year beginning 1st August 1914 and ending 31st July 1915, which return was accepted by the Commissioner in lieu of a return for the year beginning on 1st July 1914 and ending on 30th June 1915. In such return the Company claimed to deduct the said sum of £5,760 from the said sum of £6,044 for the purpose of arriving at the taxable income, which was accordingly stated as £284.

10. Pursuant to the Act the Commissioner caused an assessment to be made for the purpose of ascertaining the taxable income upon which income tax should be levied and gave a notice in writing of such assessment to the Company. The Commissioner apportioned the said dividends and bonuses paid to the shareholders ratably to and between the net profits disclosed by the balance-sheets and profit and loss accounts of the Company for the said period, namely, the £6,044 2s. 11d., and the amount brought forward in the profit and loss account of the Company for the period beginning 1st August 1914, which was £8,115 2s. 6d.

11. The Company duly gave notice of objection to the assessment, and the Commissioner having considered the objection on 29th April 1916 disallowed it. The appellant, being dissatisfied with



the decision of the Commissioner, on 3rd May 1916 asked the Commissioner to treat the objection as an appeal and forward it to the High Court pursuant to the provisions of the Act, and the Commissioner pursuant to the Act duly transmitted the objection to the High Court for determination as a formal appeal.

Upon hearing the appeal certain questions which in the opinion of the Court were questions of law arose, and the case was stated for the opinion of the Full Court thereon.

H. C. OF A.  
1916.

FOSTER  
BREWING  
CO. LTD.

v.  
FEDERAL  
COMMISSIONER OF  
TAXATION.

On the hearing before the Full Court the case was amended so as to state the following question:—"Whether the fact that in the profit and loss accounts the dividends paid were debited against the gross sums made up of the net profits of the preceding half-years together with the balances brought forward from the previous periods is conclusive to show that the dividends sought to be deducted were not wholly income distributed to the members of the Company within the meaning of sec. 16."

The profit and loss account for the six months ended 31st January 1915, was as follows:—

DR.

To Salary, Directors' and Audit Fees,

General Expenses ..		£172	4	9
„ Balance brought forward	£8,115	2	6	
„ Net Profit for Half-year	3,011	2	8	
„ Balance ..		11,126	5	2
		£11,298	9	11

CR.

By Balance from last Half-year	£10,419	2	6	
„ Less Dividend Paid	2,304	0	0	
		£8,115	2	6
„ Dividend C. & U. Breweries Ltd.	3,045	0	0	
„ Interest ..	138	7	5	
		3,183	7	5
		£11,298	9	11

H. C. OF A. The profit and loss account for the six months ended 31st July  
1916. 1915 was as follows :—

FOSTER  
BREWING  
CO. LTD.  
v.  
FEDERAL  
COMMIS-  
SIONER OF  
TAXATION.

DR.		
To Salary, Directors' and Audit Fees,		
General Expenses	..	£140 9 10
„ Balance brought forward	£8,246 5 2	
„ Net Profit for Half-year	3,033 0 3	
„ Balance	..	11,279 5 5
		<u>£11,419 15 3</u>

CR.		
By Balance from last Half-year	£11,126 5 2	
„ Less Dividend and Bonus	2,880 0 0	
		£8,246 5 2
„ Dividend C. & U. Breweries Ltd.	3,045 0 0	
„ Interest and Commission	128 10 1	
		3,173 10 1
		<u>£11,419 15 3</u>

The profit and loss account for the six months ended 31st January  
1916 was as follows :—

DR.		
To Salary, Directors' and Audit Fees,		
General Expenses	..	£132 18 10
„ Balance brought forward	£8,130 6 5	
„ Net Profit for Half-Year	2,298 15 1	
„ Balance	..	10,429 1 6
		<u>£10,562 0 4</u>

CR.		
By Balance from last Half-year	£11,279 5 5	
Less Dividend and Bonus		
Paid	.. £2,880 0 0	
Income Tax Re-		
serve	.. 268 19 0	
		3,148 19 0
		£8,130 6 5
„ Dividend C. & U. Breweries Ltd.	2,301 17 6	
„ Interest and Commission	129 16 5	
		2,431 13 11
		<u>£10,562 0 4</u>



*Mann*, for the appellant.

*Starke* (with him *Morley*), for the respondent.

[Counsel for the respondent stated that he could not argue the question.]

GRIFFITH C.J. We are all agreed that the fact that in the profit and loss accounts the dividends paid were debited against the gross sums made up of the net profits of the preceding half-years together with the balances brought forward from the previous periods is not conclusive on the question whether the dividends have been paid out of income or not. Whether the dividends have been so paid is a question of fact which will be determined by the Justice who will hear the appeal.

*Question answered in the negative. Case remitted.*

*Costs to be costs in the appeal.*

The hearing of the appeal was then proceeded with before *Griffith* C.J.

*Starke*. On the facts the proper conclusion is that the whole amount of the two dividends was not paid out of the profits of the particular year of assessment but was paid out of, and appropriated in the books and accounts to, the general balance of profit and loss. If that is so, there should be an apportionment of the dividends.

GRIFFITH C.J. A few days before each of the dividends in question was paid, the Company had no money in hand. It had in its books an account called a reserve fund of the nominal amount of £15,000, which represented undivided profits that had been invested in income-producing property. Immediately before the payment of each of the two dividends, it received by way of income from its property a sum of money rather larger than the amount of the dividend. Each sum when received was paid to the credit of the Company's banking account, which was then overdrawn, and each dividend was immediately paid by cheques drawn

H. C. OF A.  
1916.

FOSTER  
BREWING  
CO. LTD.  
v.  
FEDERAL  
COMMISSIONER OF  
TAXATION.



H. C. OF A.  
1916.

FOSTER  
BREWING  
CO. LTD.

v.

FEDERAL  
COMMISSIONER OF  
TAXATION.

upon that banking account. Under these circumstances I find as a matter of fact, and, indeed, of common sense, that so much of the income of the Company as was paid as dividends was income distributed to the members of the Company within the meaning of sec. 16.

The point was raised that because in each of the Company's profit and loss accounts a previous balance was brought forward and added to the income for the half-year and the amount of the dividend was subtracted from the total amount, showing a new balance to be carried forward, therefore the dividends should be treated as having been apportioned by the Company between the previous balance and the half-year's income. The Full Court has just held on the case stated that that fact is not conclusive on the point. I think it is hardly even evidence on the point. I am at any rate not bound to decide to the contrary of what I believe to be the truth, which is that each of these dividends was in fact distributed to the members out of the actual income of the half-year.

Any other conclusion would lead to the taxation of profits accumulated before the Act came into operation. The whole of the income of a Company is within the area of taxable income, but the Company is not taxable in respect of its whole income. So much of the income which it receives as is distributed among its members is not, however, withdrawn from the area of taxable income, since the members are taxable in respect of it if their incomes are of taxable amount. If they are not, they go free, so that, in the result, so much of the income of the Company as is paid to them goes free from taxation altogether. But, if the contention of the Commissioner were accepted, it would follow that income earned by a Company before the Act came into force would be made taxable. Suppose, for instance, that (as in this case) the amount carried forward had been earned before the Act came into operation, and was equal to the amount of the income for the year—in this case it was in the proportion of about 4 to 3,—then, if the dividend equal in amount to the net income were apportioned as claimed by the Commissioner, it would follow that the amount distributed to the members, and so falling within the taxable area, would be made up, as to one half, of income earned before the commencement of the



Act and, as to the other half, of income earned after its commencement. The income earned after the commencement of the Act was, as already stated, within the taxable area. The total amount falling within the taxable area would therefore be one and a half times as great as the actual income of the year. I do not think that this was the intention of the Act. If it was, it could be easily escaped by a slight change in the mode of keeping profit and loss accounts.

I am asked to base my decision upon the intention of the Company as shown by the way in which it kept its accounts. In my opinion there is nothing to show that it intended to make an appropriation the only result of which would have been a gratuitous assumption of liability to income tax. I think it intended to do what it actually did, that is, to apply the sums just received by it as income to the immediate payment of dividends.

The appeal must, therefore, be allowed.

*Appeal allowed with costs.*

Solicitors for the appellant, *Pavey, Wilson & Cohen.*

Solicitor for the respondent, *Gordon H. Castle*, Crown Solicitor for the Commonwealth.

B. L.

H. C. OF A.  
1916.

FOSTER  
BREWING  
CO. LTD.

v.  
FEDERAL  
COMMISSIONER OF  
TAXATION.