[HIGH COURT OF AUSTRALIA.]

BOWLES . . . . . APPELLANT;

AND

THE FEDERAL COMMISSIONER OF TAXATION . . . . . RESPONDENT.

H. C. OF A. 1919.

SYDNEY, *April* 25; *May* 3.

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

Income Tax—Assessment—Special deductions—Deduction of £156*—Apportionment—Method of computation—Income from personal exertion and from property—Income Tax Assessment Act* 1915-1916 (*No.* 34 *of* 1915—*No.* 39 *of* 1916), *secs.* 18, 19.

Where income is derived from both personal exertion and property the proper method of working out the deduction under sec. 19 of the *Income Tax Assessment Act* 1915-1916 is, after making the deductions permitted by sec. 18, first to apportion the sum of £156 *pro ratâ* between the income from personal exertion and that from property; then from the income from personal exertion to deduct the proportional sum attributable to the income from personal exertion less £1 for every £4 by which the income from personal exertion exceeds that proportional sum, and from the income from property to deduct the proportional sum attributable to the income from property less £5 for every £11 by which the income from property exceeds that proportional sum.

So *held* by *Barton, Isaacs, Gavan Duffy* and *Rich* JJ.

Per Griffith C.J.:—The proper method is to apportion between the income from personal exertion and the income from property so much of the sum of £156 as remains after making the prescribed diminutions from it. There is no diminution in respect of either source of income unless that income exceeds £156.

CASE STATED.

On an appeal by Ivor Willans Bowles to the Supreme Court of New South Wales from an assessment of him for Federal income tax for the year commencing 1st July 1916, *Pring* J. stated a case for the opinion of the High Court which was substantially as follows:—

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1. This is an appeal from assessment of income tax for the financial year commencing on 1st July 1916.

2. The appellant duly made a return of his income as required by the *Income Tax Acts* 1915-1916, and by such return it appears that between 1st July 1915 and 30th June 1916 the appellant's gross income for the period mentioned amounted to £416, such sum being made up of £13 income derived from property and £403 income from personal exertion, and that the appellant was entitled to deduct, by virtue of sec. 18 of the *Income Tax Assessment Act* 1915-1916, the sum of £36 and no more from the said sum of £403, and that he was not entitled to any deduction by virtue of the said sec. 18 from the said income from property.

3. The respondent duly assessed the appellant in respect of the said income and claimed income tax thereon made up as follows:— Income from personal exertion, £403; Deduction under sec. 18, £36: Net income from personal exertion, £367. Income from property, £13. Net income from personal exertion, £367; Exemption allowed under sec. 19 (sec. 11 of the *Income Tax Assessment Act* (*No.* 2) 1916), £113: Amount liable for tax, £254—Amount of tax payable thereon, £4 4s. 5d. Net income from property, £13; Exemption allowed under the said sec. 19, £4: Amount liable for tax, £9—Amount of tax payable thereon, 3s. 4d. Total tax payable, £4 7s. 9d.

4. The appellant duly paid the said sum of £4 7s. 9d., and by notice of objection duly objected to the said assessment and claimed that the amount of his taxable income from all sources was the sum of £130 and no more, which sum is arrived at as follows:— Gross income from personal exertion, £403; Deduction under sec. 18, £36: Net income from personal exertion, £367. Gross income from property, £13. Total taxable income, £380; Deductions under said sec. 19, £250: Amount liable for tax, £130.

The appellant claims that in calculating the deductions under the said sec. 19 he is entitled to deduct the sum of £156 in respect of the said income derived from property in addition to the deduction to which he is entitled by virtue of such section in respect of the said income from personal exertion.

5. The respondent has disallowed the claims mentioned in par. 4

hereof, and by arrangement between the parties it has been agreed that the said notice of objection shall be treated as a notice of appeal pursuant to sec. 37 of the said *Income Tax Assessment Act* 1915-1916.

7. On the hearing of the appeal before me the following questions, which in my opinion are questions of law, have arisen, and at the request of the parties I state this case for the opinion of the High Court.

The questions for the determination of the High Court are :—

(1) Is the appellant entitled to deduct from his total income the sum of £156 in respect of his income derived from property ?

(2) If he is not entitled to deduct as aforesaid the said sum of £156, then what sum in respect of his said income derived from property is he entitled to deduct from his total income ?

(3) Upon what sum is the appellant liable to pay income tax—(*a*) in respect of his income derived from personal exertion ; and (*b*) in respect of his income derived from property ?

Knox K.C. (with him *Harper*), for the appellant.

Jordan, for the respondent.

Cur. adv. vult.

May 3.

The following judgments were read :—

GRIFFITH C.J. Under the *Income Tax Act* income is regarded as arising from two sources, and is taxable at different rates according to the source. But it is a single income, although the income from the two sources is calculated separately. In each case certain deductions, specified in sec. 18, are allowed to be made from the gross income.

This having been provided for, comes sec. 19, upon which the present question arises. The section begins :—"(1) . . . there shall be deducted, in addition to the sums set forth in the last preceding section, the following sums : (*a*) in respect of the income derived from personal exertion, the sum of one hundred

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and fifty-six pounds less one pound for every four pounds by which the income" (*scilicet*, that income) "exceeds one hundred and fifty-six pounds; (*b*) in respect of income derived from property, the sum of one hundred and fifty-six pounds less five pounds for every eleven pounds by which the" (*scilicet*, that) "income exceeds one hundred and fifty-six pounds." It is to be observed that the section does not expressly specify the sum from which the deduction is to be made, but only that a sum shall be deducted "in respect of" two separate specified sources. The section proceeds:—"(2) When the total taxable income consists partly of income from personal exertion and partly of income from property the deduction under this section shall be apportioned *pro ratâ* between the income from each source." Here "total taxable income" obviously includes income from both sources after the deductions permitted under sec. 18 have been made. It is to be observed also that this provision uses the words "the deduction under this section," and does not refer to two possible deductions.

Applying an open mind to the construction of this language, without any preconceived idea, the suggested difficulties appear to vanish.

In the first place, the word "deduction," which describes the subject dealt with, of itself connotes that the sum from which the deduction is to be made is large enough to include the sum to be deducted.

In the second place, wherever sub-sec. 2 applies its provisions are imperative and exhaustive. A "deduction" is to be made, and it is to be apportioned between the income from the two sources. If, therefore, the income from either source is less than £156, the provisions as to diminution of "the deduction" have no application so far as that part of the income is concerned. But the sub-section in terms covers every case in which income is derived from both sources.

It is to be observed next that "the deduction under this section" is to be made from the total taxable income. Its apportionment is separately dealt with. When, therefore, the rule of sub-sec. 2 applies, sub-secs. (*a*) and (*b*) can only be read as directions as to

the amount of the diminutions to be made from £156 in applying it. In my opinion, the section authorizes one deduction of £156, subject to diminution, and only one.

By way of illustration I will give a case of income derived from the two sources, £468 and £321 respectively. The sum of £468 exceeds £156 by £312, which amount contains 78 sums of £4; a diminution is therefore to be made of £78. The sum of £321 exceeds £156 by £165, which amount contains 15 sums of £11, in respect of each of which a deduction of £5 is to be made, or £75 in all. Applying the rule of sub-sec. 2 then, "the deduction" of £156 is to be diminished by the two sums of £78 and £75, leaving the permitted deduction at £3, which is to be apportioned as prescribed. This is a literal application of the language of the section.

In the present case the net income from the two sources respectively is £367 and £13. £367 exceeds £156 by £211, which amount contains 52 complete sums of £4. The sum of £156 is therefore to be diminished by the sum of £52, leaving £104. No diminution is required by the Act to be made in respect of the income from property, which is less than £156. The total deduction prescribed is therefore £156 less £52, that is, £104, which is to be deducted from the total income, and to be apportioned between the sources of the total taxable income in the proportion of 367 to 13.

The questions should therefore be answered as follows:—(1) No. (2) Nothing. (3) (*a*) and (*b*) These calculations can be made by the parties.

As both parties are in the wrong, there should be no costs.

[*Note.*—Some confusion has arisen in this case from not distinguishing the "deduction" prescribed by the Act from the "diminutions" (also prescribed by it) to be made from that deduction. In a sense every diminution of one sum of money by another is a "deduction," but the word is not used in that sense in the Act.

The following brief statement of the question set by sec. 19 may elucidate matters.

Let income from personal exertion be represented by E, and let income from property be represented by P. Then the taxable income equals $E + P$, from which is to be deducted so much of

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the sum of £156 as remains after obeying the directions of sec. 19 (1) (*a*) and (*b*). Let the total amount of the two sums by which it may be diminished be represented by *D*, and the amounts of diminution by *De* and *Dp*, in respect of the respective sources of income.

The assessable income is therefore represented by the formula $E + P - D$, or $E + P - (£156 - De) - (£156 - Dp)$.

The expressions *De* and *Dp* expanded mean respectively $\frac{1}{4}(E - £156)$ and $\frac{5}{11}(P - £156)$. Unless, therefore, *E* and *P* respectively exceed £156 by £4 and £11 respectively, these items respectively vanish.

It does not matter whether the items *De* and *Dp* are subtracted successively or together (in which case the total diminution *D* would be expressed as $£156 - (De + Dp)$).

Putting the relative amounts in their places in the formula, we get $E + P - [£156 - (52 + 0)]$, making $D = £104$, which amount is to be proportionally divided between £367 and £13.

The Act nowhere authorizes a diminution of the amount of either source of the income except as already mentioned. "Apportionment" is neither "deduction" nor "diminution."

All this is not a matter of argument but of arithmetical calculation made in the manner directed by the Act.—*S.W.G.*]

BARTON J. Sec. 19 of the *Income Tax Assessment Act* 1915-1916 is substituted by sec. 11 of the *Income Tax Assessment Act* (*No.* 2) 1916 for previous provisions. It deals with special deductions from income in addition to those deductions authorized by sec. 18 in the course of calculating the taxable income of a taxpayer. It provides for three cases: (1*a*) where the income is derived from personal exertion; (1*b*) where the income is derived from property; and, by sub-sec. 2, where the total taxable income consists partly of income from personal exertion and partly of income from property.

Comparing the three cases I am unable to escape the conclusion that (*a*) relates to income solely derived from personal exertion; (*b*) to income solely derived from property. The third case, under sub-sec. 2, is the case where the income is not confined to either source. Further, I cannot see that more than one deduction, the maximum to be £156, can be made under sub-sec. 2, any more than it can

under either (*a*) or (*b*). This is the literal construction, and I think it is the plain meaning of the words.

Now in (*a*) and (*b*) this special deduction is made subject to certain diminutions. Where the income is derived solely from personal exertion, the sum of £156 is to be lessened by £1 for every £4 by which the income exceeds £156. Where the income is solely derived from property, the sum of £156 is to be lessened by £5 for every £11 by which the income exceeds £156. But what is to take place where sub-sec. 2 applies, that is, where the income arises partly from the one source and partly from the other? The Statute says that "the deduction under this section shall be apportioned *pro ratâ* between the income from each source." What is "the deduction under this section"? When the whole income exceeds £156 it is that sum, apportioned and diminished as the section, taken together, directs. But are the diminutions to be made before or after apportionment of the deduction of £156? I think they must be made after it, so that it may be possible to apply the particular diminution to the right proportion of the deduction according to source of income. It is only by reference to pars. (1*a*) and (1*b*) that the diminutions can be made at all. But it cannot be known to which branch of the income one is to apply a diminution unless the proportion of the whole deduction applicable to that branch is first ascertained.

Applying these considerations to the figures constituting the sums in question in this case, we find first that the income from personal exertion has £36 deducted from it under sec. 18 before sec. 19 is applied to it. That is to say it stands as £367 derived from that source. The income from property is £13, so that the total income to which sec. 19 is to be applied is £380. It is necessary now to find the proportion in which the whole £156 stands to the respective sources of income. In respect of the income from personal exertion, the proportion to be allotted is a shade over £150; and in respect of income from property it is a shade under £6. Now, having got these two proportions of £150 and £6, we are enabled to see how the diminutions under (*a*) and (*b*) are to be made. If the £150 be subtracted from the £367 derived from personal exertion, there is left a sum of £217. Applying the diminution under (1*a*), that is found to necessitate the lessening of the £150 by £54, and we have,

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on doing so, £96 deductible from that source of income. The balance is £271. But in respect of property the balance is £7, for the whole £6 must be deducted from the £13 derived from that source, inasmuch as the income therefrom is far below £156. Indeed, there is no way here of diminishing the apportioned deduction of £6. Before a start can be made in that direction the income must exceed £156—see the concluding words of (*a*) and (*b*). Thus the total is £276, of which £271 should be taxed on the scale appropriate to its source of income, namely, personal exertion, and £7 on the scale appropriate to the other source of income, namely, property.

I answer the questions as follows: (1) No; (2) Nothing; (3) (*a*) £271, and (*b*) £7.

The assessment in question was for the financial year beginning 1st July 1916, and therefore the Act No. 18 of 1918, sec. 47, protects the assessment in respect of its computation of the deductions on the basis of the income being the income remaining after allowing all deductions under other sections of the previous Acts. But the section does not avail to protect assessments made on wrong principles under the Act No. 39 of 1916.

Under all the circumstances, as we take a view which does not coincide with that of either of the parties, I think that there should not be any costs.

ISAACS, GAVAN DUFFY AND RICH JJ. This case has been well argued on both sides, and we have arrived at a clear conclusion.

In 1916 the appellant—a person, other than a company, an absentee, or a person without a dependant—had a total taxable income, consisting of £406 from personal exertion and £13 from property. The question is whether under sec. 19 of the Assessment Act as it then stood (for the law is now altered) he was entitled to a double deduction of £156, that is, one of £156 less a prescribed diminution in respect of each source of income, notwithstanding his property income was only £13 in all.

The Commissioner assessed him at £254 for personal exertion, with a tax on that of £4 4s. 5d., and at £9 for property with a tax of 3s. 4d.; total tax liability being £4 7s. 9d. In effect, the Commissioner finally calculated a deduction of £156, less the personal

exertion ratio, as if there were no property income, and then calculated a total deduction of £13 for property, and finally apportioned the sum of the two intermediate deductions.

The appellant claims that he was entitled to have the first deduction stand, and to have a similar deduction of another £156 in respect of the £13, and then to carry over the surplus of the second deduction and add it to the first, and set both against his total income. In our opinion he was not so entitled.

To ascertain the meaning of sec. 19 we must first read sec. 18, to which it expressly refers and without which sec. 19 cannot be understood or applied. Sec. 18 begins by providing that in calculating the "taxable income" of a taxpayer (that is, by sec. 3, the amount of income remaining after all allowable deductions are made) the total "assessable income" (that is, by sec. 3, the gross income not exempt) shall be taken as a basis and from it certain deductions are to be made. If the assessable income taken as the primary basis of calculation be single—that is, either from personal exertion alone or from property alone—sub-sec. 1 can be applied, so far as the several deductions are applicable to the particular case, without further direction. But if it partakes of both characters, sub-sec. 2 comes into operation. That necessitates a separation of the income according to its two sources. The various deductions are appropriated to each specific source. If there is a surplus of deduction over the income from either source, the surplus is, by the proviso, deducted from the income from the other source. But the division into distinct sources is maintained. This is necessary in view of the schedules of the Taxing Act itself (No. 37 of 1916). Now, when we come to sec. 19, a further deduction is provided for. Sub-sec. 1 is divided in (*a*) personal exertion and (*b*) property.

It is said on behalf of the appellant that "in respect of" is distinct from "from" in sec. 18, and, therefore, you do not deduct it "from" the personal exertion income, or the property income, but from the total assessable income taken as the basis. Now, so far as sub-sec. 1 is concerned, the key of the problem is this: there is never any simultaneous operation of (*a*) and (*b*) where the income is of one character only. Reliance is placed on the word "sums." But

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as there can be but one sum, where the income is of one character only, no argument can be sound which rests on the assumption that sub-sec. 2 merely apportions two "sums" or "deductions" that are already in operation apart from the case predicated by sub-sec. 2. Apart from diverse income, there is always one "sum" only, that is, one "deduction" only, and that deduction is always £156, less either one-quarter of the excess of income over £156 in respect of personal exertion income, or less five-elevenths of that excess in respect of property income. When we reach sub-sec. 2 it is with the knowledge that, so far, there is only one deduction under sec. 19, and that sub-section, referring to the "total taxable income," proceeds to apportion "the deduction under this section" *pro ratâ* between the income from each source. That must mean that the £156 is to be apportioned *pro ratâ* so as to apply appropriately to each part so apportioned what concerns specially each branch of income, namely, the personal exertion rate of diminution of the deduction and the property rate of diminution of the reduction respectively. The apportionment is for the very purpose of keeping the two ratios of diminution apart and applying each to its respective class of income.

There are reasons arising, both from the language of the Act and from its evident policy, which operate against both the appellant's contention and the Commissioner's contention. As to its language, sub-sec. 2 is providing for a specific case not already provided for. It provides for apportionment. That assumes that sub-sec. 1 is not itself an apportionment *pro ratâ*. If, however, the appellant's argument is sound that the "deduction" in sub-sec. 2 means the ultimate "sums" in both (*a*) and (*b*) of sub-sec. 1, then the mere operation of sub-sec. 1 in applying (*a*) to one class of income exclusively and (*b*) to the other class of income exclusively, in itself works an apportionment of those sums *pro ratâ* between the income from each source, and nothing further is needed, unless two apportionments are intended, the second to a large extent nullifying the first by mingling the ratios. In other words, sub-sec. 2 is at best superfluous and unmeaning, and generally contradictory of sub-sec. 1. The argument, moreover, disregards the fact that in sub-sec. 2 the word "deduction" is in the singular and not in the plural.

The method adopted in the official assessment presents some formidable objections. In the present instance it has not been unjust to the taxpayer; indeed, it has been too favourable. But as a formula it does not bear the test of the Act. To begin with, the total deduction of a man's property income is not warranted by sub-sec. 1. If income is itself below £156, no deduction is needed; if it is equal to or above £156, then that sum less a given ratio of any excess is deducted. But it is impossible to deduct £156 from a less sum. Next, if, as argued, the principle is to deduct from income below £156 as much of the £156 as covers the income, it is necessary to see where that leads. If it is right, it must apply to all cases; and in many cases it must lead to a deduction exceeding £156. For instance, suppose a total taxable income of £462. Suppose, first, it consists of £196 from personal exertion and £266 from property. The process under sub-sec. 1 gives deductions respectively of £146 and £106, or a total of £252, to be apportioned under sub-sec. 2. If the total income consists of £312 from personal exertion and £150 from property, then the deductions under sub-sec. 1 are respectively £117 and £150, or a total of £267. Having in each case exhausted the statutory operations, you cannot cut down the result. That result, however, is impossible. Besides increasing the total deduction far beyond £156, the process intermingles the ratios by partly applying to whichever is the smaller source of income the ratio specially appropriated to the other source.

As to the policy of the Act, the £156, as is universally known, is an arbitrary sum, taken for a minimum subsistence allowance for a taxpayer (other than a company, absentee, or a person without a dependant—as to which see sec. 3). Unless the income of a person not an absentee, but who is married or has dependants, exceeds this sum, he need not, during the period relevant to this case, even make a return of his income (sec. 28). This sum of £156 during the same period, in the case of a person not married, without dependants and not an absentee, was, for the purpose of returns and for the purpose of assessment, reduced to £100 by sub-sec. 3 of sec. 19. But it would be quite opposed to the clear policy of the Act, as evident from its language (namely, exclusion of company and absentee, and its reference to "dependant") and the modification of sub-sec. 3,

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to allow a double amount for sustenance merely on the ground that the sources of income are diverse. That would permit a person having an income (say) of £500 partly from property and partly from exertion to escape more lightly than if it were wholly from exertion. That result is unquestionably against the policy of the main Taxing Act and its Schedules. It would also allow a man with an income of £312 a year of which half was from one source and half from the other to go free from taxation, while another with £157 a year and upwards from one source alone would pay income tax. Such inequality goes far to make the result improbable, unless the language forces one to the conclusion.

In *Coltness Iron Co.* v. *Black* (1) Lord *Blackburn*, in a passage quoted with approval by Lord *Herschell* in *Colquhoun* v. *Brooks* (2), said: "The object of those framing a Taxing Act is to grant to Her Majesty a revenue; no doubt they would prefer, if it were possible, to raise that revenue equally from all, and, as that cannot be done, to raise it from those on whom the tax falls with as little trouble and annoyance and as equally as can be contrived; *and when any enactments for the purpose can bear two interpretations, it is reasonable to put that construction upon them which will produce these effects.*"

The true deduction works out thus:—The total assessable income being assumed for this purpose to be £380, of which £367 is from personal exertion and £13 from property, the apportionment of £156 *pro ratâ* is, disregarding fractions of a pound, £150 for personal exertion and £6 for property. Then the formula runs thus:—(*a*) In respect of personal exertion income, deduct £150 less £1 for every £4 by which the income exceeds £150, and (*b*) in respect of property income, deduct £6 less £5 for every £11 by which the income exceeds £6. Working out (*a*), we find that £367 exceeds £150 by £217, which contains £4 54 times, and, therefore, requires the £150 to be diminished by £54. The balance £96 is the apportioned deduction in respect of the £367, which then stands at £271 net. Working out (*b*), inasmuch as £13 exceeds £6 by £7 only, it follows that £11 is not reached by the excess, and, therefore,

(1) 6 App. Cas., 315, at p. 330. (2) 14 App. Cas., 493, at p. 505.

the whole £6 must be deducted, leaving a balance of property income £7.

The total taxable income is consequently £278, consisting of £271 from personal exertion and £7 from property.

Questions answered: (1) *No*; (2) *Nothing*; (3) (*a*) £271 *and* (*b*) £7.

Solicitors for the appellant, *Minter, Simpson & Co.*

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

B. L.

[HIGH COURT OF AUSTRALIA.]

THRELFALL (COLLECTOR OF CUSTOMS FOR SOUTH AUSTRALIA) . . . . . DEFENDANT, } APPELLANT;

AND

MATTHEW GOODE AND COMPANY LIMITED . . . . . PLAINTIFF, } RESPONDENT.

ON APPEAL FROM THE SUPREME COURT OF SOUTH AUSTRALIA.

Customs Duties—Duty according to value—Goods purchased abroad—Time at which value to be taken—Time of export or time of purchase—Customs Act 1901-1910 (*No.* 6 *of* 1901—*No.* 36 *of* 1910), *secs.* 154, 155.

Sec. 154 of the *Customs Act* 1901-1910 provides that "When any duty is imposed according to value—(*a*) The value shall be taken to be the fair market value of the goods in the principal markets of the country whence the same were exported in the usual and ordinary commercial acceptation of the term and free on board at the port of export in such country and a further addition of ten per cent. on such market value"; &c.