[HIGH COURT OF AUSTRALIA.]

LEONARD . . . . . APPELLANT;

AND

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

H. C. OF A. 1919.

MELBOURNE, *June* 2.

Isaacs, Gavan Duffy and Rich JJ.

Income Tax—Assessment—Income—Partner—Interest on money lent to partnership—Income Tax Assessment Act 1915-1916 (*No.* 34 *of* 1915—*No.* 39 *of* 1916), *sec.* 25.

The appellant had lent a sum of money at interest to a partnership of which he was a member. During the year upon the income of which the assessment of the appellant's Federal income tax for the year 1916-1917 was based, the appellant was credited by his bankers, who were also the bankers of the firm, with the amount of interest payable for that year, and during the same year the firm made a loss the appellant's share of which included his share of the interest so credited.

Held, that the whole of the interest so credited to the appellant was properly included in the assessment of the appellant for the year 1916-1917.

CASE STATED.

On an appeal to the High Court by Herbert Napier Leonard from an assessment of him by the Federal Commissioner of Taxation for income tax for the year 1916-1917, *Isaacs* J. stated the following case for the opinion of the Full Court :—

1. Herbert Napier Leonard (hereinafter called "the taxpayer") was at all times material to this case on active service abroad, during the present war, with the military forces of the Commonwealth. At all such times the taxpayer was also a member of the firm of Cameron

H. C. OF A. 1919.

LEONARD v. FEDERAL COMMISSIONER OF TAXATION.

& Leonard, carrying on business in the State of Queensland as graziers, and had a half share and interest therein.

2. Prior to 1st July 1915 the taxpayer advanced to the said firm of Cameron & Leonard the sum of £22,000 on the terms that he was to receive interest from the said firm thereon at the rate of £5 per centum per annum, and the sum of £1,100 (being the amount of such interest for the year ended 30th June 1916) was accordingly debited to the account of the said firm of Cameron & Leonard and credited to the account of the taxpayer in the books of the Australian Mercantile Land & Finance Co. Ltd., which was then acting as banker for the said firm of Cameron & Leonard and also for the taxpayer. The taxpayer operated in the ordinary way on his said account.

3. The said firm of Cameron & Leonard made a loss in the business carried on by it as aforesaid during the year ended 30th June 1916, and the taxpayer's share of that loss was £6,318. The said sum of £6,318 includes the sum of £550, being one-half of the said sum of £1,100 credited to the taxpayer as mentioned in par. 2 hereof.

4. The taxpayer included in his return of income from property for the financial year ending 30th June 1916 the sum of £1,100 credited to him as aforesaid, but claims that as to portion thereof—namely, the sum of £550—the same should be regarded as being a loss or outgoing actually incurred by the taxpayer in Australia in gaining or producing the said sum of £1,100 or portion thereof, or alternatively that the whole sum of £1,100 should not be regarded as income of the taxpayer but that only portion thereof, namely, the sum of £550, should be so regarded.

5. The Commissioner has included in the assessment of the taxpayer in respect of income tax for the financial year 1916-1917 (based on income derived during the year ended 30th June 1916) the whole of the said sum of £1,100, and has refused to treat the said sum of £550, being the portion thereof paid or contributed by the taxpayer, as a loss or outgoing actually incurred by him in Australia in gaining or producing the said £1,100 or portion thereof, or to make any deduction whatever from the said sum of £1,100.

6. On the hearing of the appeal, the following questions arose, which in the opinion of this Court are questions of law—that is to say,

whether the whole of the said sum of £1,100 was rightly or wrongly included in such assessment, and whether, if it were rightly so included, the said sum of £550 should have been allowed as a deduction. This Court doth therefore, so thinking fit, state this case in writing for the opinion of the High Court upon the said questions so arising in the appeal.

Dethridge, for the appellant. One-half of the interest credited to the appellant, namely, £550, is not his income in any sense of the term. It is merely a payment of his own money to himself. The advance of £22,000 must be taken as an advance by the appellant to himself and Cameron, in return for which he receives from himself and Cameron £1,100 as interest.

[ISAACS J. Sec. 28 (3) of the *Partnership Act* 1915 (Vict.) provides that a partner making advances to the partnership beyond the amount of the capital which he has contributed is to be entitled to interest at a certain rate.]

Sec. 25 of the *Income Tax Assessment Act* 1915-1916 means that in assessing the income of a partnership any advances made to the partnership by a partner are to be ignored. That is shown by the use of the words " without regard to the respective interests therein," and is supported by sec. 28 of the *Partnership Act*. The result is that the £1,100 ought not to have been included in the partnership assessment. Whatever mistake, if any, has been made in respect of the assessments of the partnership, it has to be determined in the present assessment what the appellant actually received in the way of income. It cannot be said that the appellant actually received the £550 by way of income. [Counsel referred to *Bohemians Club* v. *Acting Federal Commissioner of Taxation* (1).]

Starke, for the respondent, was not called upon.

The judgment of the COURT, which was delivered by ISAACS J., was as follows :—

The question we have to determine is a question of assessment

(1) 24 C.L.R., 334.

H. C. OF A. 1919.

LEONARD v. FEDERAL COMMISSIONER OF TAXATION.

of income, and that depends upon the construction of the *Income Tax Assessment Act* 1915-1916, which was in force at the material time. We think that the matter is concluded, in the first place, by the rule enacted in sec. 25 of that Act, which provides that "(1) Partners"—and that term is defined in sec. 3 as including "persons who are in receipt of income jointly"—"shall be assessed and liable in respect of the income derived by them as partners as if it had been derived by a single person,"—stopping there for a moment, the section enacts in effect that a partnership shall for the purposes of the Act be deemed to be a single entity; the separate natural personalities of those comprised are merged in one taxable entity, the partnership. The section continues: "without regard to the respective interests therein or to any deductions to which any of them may be entitled under this Act, and without taking into account any income derived by any one of them separately or as partner with any other person." That makes clear and emphasizes what the section has already said as to the single personality of the firm. The section then proceeds: "(2) Each partner shall in addition be separately assessed and liable in respect of (*a*) his individual interest in the income"—that is, the income of the partnership—"together with (*b*) any other income derived by him separately"—that means, not derived by him as a member of the firm but outside the firm—"and (*c*) his individual interests in the income derived by any other partnership"—which again keeps up the provision of the section as to the separate entity of a firm.

If, for instance, the firm of Leonard & Cameron had borrowed the £22,000 from another firm, consisting of (say) Leonard and Smith, it would be perfectly clear that Leonard & Smith as a single entity would have received the £1,100 from Leonard & Cameron, and that Leonard as a member of the firm of Leonard & Smith would then have been taxable for it in respect of the income of Leonard & Smith. But it would be indisputable that that income would have been received by the firm of Leonard & Smith quite independently of Leonard's interest in the firm of Leonard & Cameron. Leonard received the £1,100 as an individual, and he received it in the same way; it does not affect the principle at all.

So that, on the law as enacted in sec. 25, the question must be answered against the appellant.

On the facts of this case it is also clear that, if that section had not been enacted, the general principles of law would have rendered the appellant liable in the same way. We would have arrived at the same conclusion independently of sec. 25 on the facts as they actually occurred. That section, however, makes it clear beyond question.

The questions will be answered by saying that the whole of the sum of £1,100 was rightly included in the assessment, and that the sum of £550 ought not to have been allowed as a deduction.

Questions answered accordingly.

Solicitors for the appellant, *Whiting & Aitken.*

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

B. L.