[HIGH COURT OF AUSTRALIA.]

MELROSE . . . . . APPELLANT;

AND

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

ON APPEAL FROM THE SUPREME COURT OF SOUTH AUSTRALIA.

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ADELAIDE, *Sept.* 29, 30; *Oct.* 3.

Barton, Isaacs and Rich JJ.

Income Tax—Assessment—Taxpayer a partner in several partnerships—Total losses on one partnership exceeding total profits on others—Deduction of share of balance of losses from taxpayer's income from property—Income Tax Assessment Act 1915-1916 (*No.* 34 *of* 1915—*No.* 39 *of* 1916), *secs.* 3, 18, 21, 25—*Income Tax Assessment Act* 1918 (*No.* 18 *of* 1918), *secs.* 17, 20.

A taxpayer was a partner in three partnerships, and for the year ending 30th June 1916 his share of the loss from one of them was greater than his share of the profits of the other two, and his income from personal exertion was less than the amount of his net loss in respect of the three partnerships. He also had income from property.

Held, that for the purpose of assessment for Federal income tax for the year 1916-1917 the taxpayer was entitled, under the proviso to sec. 18 (2) of the *Income Tax Assessment Act* 1915-1916, to deduct from his income from property the amount by which his net loss in respect of the three partnerships exceeded his income from personal exertion.

Decision of the Supreme Court of South Australia (*Buchanan* J.) reversed.

APPEAL from the Supreme Court of South Australia.

For the purpose of assessment for Federal income tax for the year 1916-1917 Alexander Melrose sent in a return of his income for the year ending 30th June 1916, from which it appeared that he was a partner in three separate firms, from the first of which a profit was

made of which his share was £150, from the second a profit of which his share was £131, and from the third a loss of which his share was £524. Apart from those businesses he had an income from personal exertion of £10, and an income from property of over £3,000. Melrose included the sum of his share of the profits from the two partnerships, namely £281, in his income from property and claimed the right to deduct from his income from personal exertion £281 of the loss from the third partnership, and the balance, namely £243, from his income from property. The Commissioner allowed the partnership loss to be deducted from the partnership profit, but he refused to allow the balance of £243 to be deducted from the income from property; and he assessed Melrose accordingly. Melrose thereupon objected to the assessment, and appealed to the Supreme Court of South Australia. The appeal was heard by *Buchanan* J., who confirmed the assessment made by the Commissioner.

From that decision Melrose now appealed to the High Court.

Mayo, for the appellant. The general scheme of the *Income Tax Assessment Act* 1915-1916 is to charge *in globo* the whole Australian income directly or indirectly of a taxpayer except that certain deductions are to be charged against income from property, and all other deductions against income from personal exertion. Where a taxpayer has income from property and is also the sole proprietor of one business in respect of which he makes a net loss, that loss may unquestionably be deducted from his income from property. That follows from the definition of "income from personal exertion" in sec. 3 and the provisions of sec. 18. If a taxpayer can deduct a loss made in one business of which he is the sole proprietor from his income from property, he can also, under the same sections, deduct from that income the total loss made from several businesses of which he is the sole proprietor. That being so, sec. 21 merely declares what follows from sec. 18 so far as several businesses in the sole proprietorship of one taxpayer are concerned. Notwithstanding sec. 25, the words "the proceeds of any business carried on by the taxpayer either alone or as a partner with any other person" in the definition of income from personal exertion in sec. 3 must be given a meaning from the taxpayer's point of view. In fact, those

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words bring a partner's interest in the gross proceeds of the partnership within the ambit of that part of his assessable income, and therefore his share of the loss incurred by the partnership comes within sec. 18 (1) (*a*). Therefore a taxpayer's interest in one or more partnership businesses comes within sec. 18 (1) (*a*), and in like manner his interest in one or more individual businesses carried on by him. Sec. 21 merely declares what is contained in the definition of income from personal exertion in sec. 3 and in sec. 18. A resultant loss in sec. 21 is in fact and in law a loss in the production of the taxpayer's assessable income. The object of sec. 25 is not to affect the taxpayer's right to deductions authorized elsewhere in the Act, but to create a taxable entity. It does not impliedly alter the definition of income from personal exertion in sec. 3. In *Leonard* v. *Federal Commissioner of Taxation* (1) this contention was not raised, though it might have been. [Counsel also referred to *Commissioners of Taxation* v. *Teece* (2).]

Ward, for the respondent. There is no provision in the Act for deducting partnership losses from income from property. Partnership losses are losses only of the partnership, which is assessed as a separate entity. There is no power to treat partnership losses as losses of the individual partners except as provided by sec. 21. That section allows partnership losses to be deducted from other business profits which are income from personal exertion. It does not extend to income from property. If there is a partnership loss, there can be no partnership income to form part of the individual taxpayer's assessable income, and therefore the partnership loss, not being incurred in the production of the gross income, cannot be deducted under sec. 18 (1) (*a*). The amendment made by sec. 17 of the *Income Tax Assessment Act* 1918 would be unnecessary if the contention for the appellant were correct. Sec. 21 is a concession to a taxpayer who makes a loss under sec. 25, or in respect of businesses carried on by him on his own account.

Mayo, in reply.

Cur. adv. vult.

(1) 26 C.L.R., 175.

(2) (1899) A.C., 254.

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

This appeal concerns income derived during the year ending 30th June 1916. The appellant is a partner in three different firms, in two of which profits were made in the year referred to, his share of those profits, as accepted by both sides, being respectively £150 and £131, or a total of £281. The third partnership made a loss, and his share of that loss, as accepted by both sides, was £524. On his separate assessment made under sec. 25 (2) of the Act 1915-1916, it appears that he had income from property far exceeding £524. The Commissioner permitted portion of the partnership loss of £524, namely to the extent of £281, to be set against the partnership profits of £281, but the difference, namely £243, he refused to set against the income from property. The Commissioner's view was that a partnership loss can, under sec. 21, be deducted from a partnership profit, but cannot be deducted from income from property. *Buchanan* J. upheld that contention, and we have to consider whether that decision is correct. The case was well and tersely argued on both sides.

The Act imposing the tax (No. 37 of 1916) imposed income tax (1) in respect of income wholly derived from personal exertion, (2) in respect of income wholly derived from property, and (3) in respect of income derived partly from personal exertion and partly from property. That Act incorporated the Assessment Act. By sec. 3 of the Assessment Act certain definitions were enacted. "Income from personal exertion" included "the proceeds of any business carried on by the taxpayer either alone or as a partner with any other person." "Assessable income" meant "the gross income which is not exempt from taxation." "Taxable income" meant "the amount of income remaining after all deductions allowed by this Act have been made." "Taxpayer" meant "any person chargeable with income tax." Sec. 10 provided that income tax should be levied and paid upon "taxable income." Sec. 18 enacted that "In calculating the taxable income of a taxpayer the total assessable income derived by the taxpayer from all sources in Australia shall be taken as a basis, and from it there shall be deducted"; then follow enumerated deductions.

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Before going further, it should be observed that, having regard to the definitions and provisions quoted, sec. 18 in its opening words provides that, in calculating the amount of income on which the tax is to be levied and paid, the first step is to set down the taxpayer's non-exempted gross income from all sources in Australia, and from that income to make the deductions enumerated so far as the facts justify them, the balance being the taxable income.

Sub-sec. 2 of sec. 18 provided that where the third class of income taxed by the imposition Act existed (that is, income derived from personal exertion and from property), which is the present case, certain deductions should be made from property, and all others in the section from personal exertion. Then followed a proviso: "that if the income from either source" (that is, from personal exertion or from property) "does not amount to the sum to be deducted from that source, the balance of the sum to be deducted shall be deducted from the income from the other source." As a good deal depends on this proviso, it is necessary to consider its terms at this point. It preserves the division of income into two classes only—personal exertion and property; it recognizes no subdivision of those sources: it assumes the deductions to represent in their totality one sum as to each source, and to be deducted from that source without regard to the items making up that source, and any balance of the deductible amount unapplied to that source goes over to be deducted from the other source equally without distinction of items composing that source.

The dominating idea is that the taxpayer is regarded as a receiver of income which, in its totality, represents his ability to contribute to the revenue of the country. That ability is affected by the general nature of the source—personal exertion or property—whence the income is received, but is not affected by the particular channel emanating from the given source by which the income passes to him. His ability to contribute for the year, however, is affected by the losses he has sustained in the course of his industry or other income-producing operations, and it is immaterial to his ability in which channel those losses have been sustained provided they are of the nature recognized as deductible. His resultant ability as a taxpayer

is the aim of sec. 18, and so, after appropriating the deductions to their primary class, the balance is allowed to stand against the other class of income. If, therefore, section 18 stood alone, there would be no reason to refuse the taxpayer's right to deduct the sum of £243 from the property income, or, to be quite exact, so much of the £243 as remained after applying it to a sum of about £10 of personal exertion income. But it is contended that, however that might be if sec. 18 stood alone, the provisions of secs. 21 and 25 are opposed to it.

Sec. 25 is divided into two parts. The first part, as held in *Leonard* v. *Federal Commissioner of Taxation* (1), enacts that a partnership is to be assessed as a separate entity. The reason of that is obvious. Partners carrying on a business are a business unit, and are naturally to be held jointly responsible for the tax on the business operations. But in order to avoid the manifest injustice of making—especially in a graduated tax—one partner responsible on a scale dependent on the private and separate income of the other, separate interests and incomes must be disregarded. This is what sub-sec. 1 of sec. 25 did, and the partnership income is assessed without regard to separate interests or separate rights to deductions, or separate incomes outside the particular partnership. This secured each partner from taxation on the basis of another man's income. He became jointly liable for the tax on the partnership income. Nevertheless, his totality, so to speak, as a taxpayer is even there recognized by sec. 21, which allows him to deduct total business losses from total business profits, and whether the losses and profits are made by him alone or in partnership with others. Then sub-sec. 2 of sec. 25 provided that he shall be separately assessed and liable in respect of (*a*) his individual interest in the partnership income, (*b*) any other income derived by him separately, and (*c*) his individual interests in the income derived by any other partnership. Again his totality as a taxpayer is recognized, and on his own personal basis. It is this separate assessment which has taken place in the present case.

Why is not sec. 18 applicable? Why does sec. 21 shut out its

(1) 26 C.L.R., 175.

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application? Even if sec. 21 covers some of the ground, it covers other ground too, and not only is it necessary for the just working of the first sub-section of sec. 25, but, even if it be regarded as tautologous, that is not uncommon, especially in a taxing Act, *ex majori cautelâ* (see per Lord *Macnaghten* in *Commissioners for Special Purposes of Income Tax* v. *Pemsel* (1), and per Lord *Finlay* L.C. in *Cornelius* v. *Phillips* (2)).

Reliance was placed on sec. 17 of Act No. 18 of 1918, which added a sub-section to sec. 21. But again, that, certainly to some extent in recognition of the totality of the taxpayer's ability, declared his right to deduct business losses from property income, the important words being "alone or otherwise." It is not at all clear that that sub-section carries his right further than does sec. 18. It must be remembered that the proviso to sec. 18, which, it is said, is complemented by sec. 21, was passed after sec. 21, namely by Act No. 47 of 1915, whereas sec. 21 had been passed by Act No. 34 of that year. Sec. 21 consequently cannot be taken as a limitation of the proviso to sec. 18.

The cardinal position of the respondent is that the sum of £524—except for the permitted deduction of £281 under sec. 21—is unalterable. But how can that be? Suppose no property income: could the taxpayer's right to deduct his own war contribution, or his insurance premiums be denied? They are expressly ignored in the joint partnership assessment, and it is inconceivable that the Legislature intended to deny them altogether. Nor is it understandable why in the separate assessment a surplus of property deductions should not be set against even partnership income. Besides, the later legislation—if that is to control interpretation—is fatal to the contention. The new sec. 25 (substituted by sec. 20 of Act No. 18 of 1918) speaks of the individual assessment of each partner in respect of (*a*) his individual interest in the partnership income "remaining after allowing all the deductions under this Act" except the deduction under sec. 19. If the later enactment indicates the Legislative interpretation of the earlier Act, it is clear that Parliament understood the earlier one to refer to the partnership gross income. The new section places matters like the present on a new footing; but, on the

(1) (1891) A.C., 531, at p. 589. (2) (1918) A.C., 199, at p. 204.

basis of the law as it stood with reference to this case, the taxpayer's contention appears to us correct and the appeal should be allowed.

Appeal allowed. Order appealed from discharged with costs. Objection of the taxpayer sustained. Respondent to pay costs here and below.

Solicitors for the appellant, *Homburg, Melrose & Homburg.*

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

B. L.

[HIGH COURT OF AUSTRALIA.]

MUNICIPAL TRAMWAYS TRUST AND OTHERS . . . . . Defendants, } Appellants;

AND

SCOTT . . . . . Plaintiff, Respondent.

ON APPEAL FROM THE SUPREME COURT OF SOUTH AUSTRALIA.

Assault—Defence—Justification—Tramway owner and passenger—Obstruction of tramway official in performance of his duty—Breach of by-law—Refusal by passenger to give his name and address—Municipal Tramways Trust Act 1906 (*S.A.*) (6 *Edw. VII., No.* 913), *secs.* 95, 96.

Sec. 95 of the *Municipal Tramways Trust Act* 1906 (S.A.) provides that no person shall "obstruct any person employed on" a tram-car "in the performance of his duty," and imposes a penalty upon a breach of the provision.