[HIGH COURT OF AUSTRALIA.]

JOSHUA BROTHERS PROPRIETARY LIMITED APPELLANT;

AND

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

H. C. OF A. 1923.

MELBOURNE, *Feb.* 19, 20; *Mar.* 12.

Knox C.J., Isaacs, Higgins, Rich and Starke JJ.

Income Tax—Assessment—Income—Company in voluntary liquidation—Realization of assets by liquidator—Sale of manufactured goods—Profits realized on sale—Income Tax Assessment Act 1915-1918 (*No.* 34 *of* 1915—*No.* 18 *of* 1918), *secs.* 3, 16, 45A, 52—*Companies Act* 1915 (*Vict.*) (*No.* 2631), *secs.* 155, 184, 186-200, 221.

A company incorporated in Victoria, which carried on the business of manufacturing and selling certain goods, went into voluntary liquidation and thereupon ceased to manufacture, and, through the liquidator, from time to time sold, in the mode in which it had theretofore done, the stock of manufactured goods which it then had in hand.

Held, that the sum by which the proceeds of the sales of goods, less the amount at which such goods were valued at the beginning of the liquidation, exceeded the cost of realizing those goods and other expenses incurred in connection therewith during the period of the liquidation was income of the company liable to assessment under the *Income Tax Assessment Act* 1915-1918, notwithstanding the fact of liquidation.

CASE STATED.

On the hearing of an appeal by Joshua Brothers Proprietary Ltd. from an assessment for Federal income tax for the year 1920-1921, *Starke* J. stated, for the opinion of the Full Court, a case which was substantially as follows :—

1. Joshua Brothers Proprietary Ltd. is a company incorporated under the law of Victoria.

2. The company carried on the business of the manufacture, storage, maturing and sale of alcoholic liquors.

3. On 12th January 1920 a resolution that the company be voluntarily wound up, which had been duly passed, was duly confirmed as a special resolution, and John Melbourne Joshua was appointed liquidator of the company.

4. From 12th January 1920 the company entirely ceased all manufacturing operations, and thereafter the liquidator on behalf of the company, in lieu of the company itself, began and has since continued to realize the company's stock of liquor to the best advantage with due regard to the capacity of the local market and the opportunities available in overseas markets, principally Great Britain. The liquidator in addition to the acts aforesaid continued and completed the performance of a contract for the supply of spirit which subsisted at the date of such liquidation. The liquidator incurred and discharged the usual expenses and charges incidental to the carrying on of the business, save and except those relating to the manufacture of alcoholic liquor, such manufacture having ceased.

5. A large quantity of the company's liquor was immature and was not saleable for immediate consumption.

6. The liquidator on behalf of the company furnished to the Federal Commissioner of Taxation a return setting forth the income derived by the company from sources in Australia during the year ending 30th June 1920. In the said return the liquidator stated the income of the company up to 12th January 1920, and stated that on the said date the company went into voluntary liquidation.

7. Upon the request of the Commissioner the liquidator subsequently supplied to the Commissioner a copy of the liquidation account of the company from 12th January 1920 to 30th June 1920.

8. On 6th May 1921 the Commissioner caused an assessment to be made of the taxable income of the company at the sum of £56,281, and claimed thereon by way of tax the sum of £7,504 2s. 8d. The liquidator paid the last-mentioned amount, and on 3rd June 1921 caused to be lodged with the Commissioner notice of objection in writing to the said assessment.

9. On 14th September 1921, in pursuance of a request made by the Commissioner, the liquidator forwarded to the Commissioner a

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certain statement of accounts of sales, expenses, &c., of the company from 12th January to 30th June 1920 (which was annexed to the case as an exhibit and marked "C").

10. On 4th November 1921 the Commissioner caused an amended assessment to be made wherein the company's taxable income was stated at the sum of £43,275. The Commissioner repaid £1,734 2s. 8d., being tax overpaid.

11. The said sum of £43,275 includes a sum of £3,778, as income of the company to 12th January 1920. The balance, £39,497, is the excess of receipts over expenditure for the period 12th January 1920 to 30th June 1920, as shown in the statement of accounts referred to in par. 9.

12. By letter dated 8th November 1921 the Commissioner disallowed the objection of the company except as to ground 6 thereof; and the company, being dissatisfied with such decision, gave notice requesting the Commissioner to treat such objection as an appeal and to forward it to the High Court of Australia for hearing.

13. Upon the hearing of this appeal before me the parties thereto agreed upon the facts hereinbefore stated and I state this case for the opinion of the High Court upon the following question arising on the appeal, which in my opinion is a question of law:—

Whether the said sum of £39,497 is taxable income of the company.

Exhibit C set out the gross proceeds of sales of goods between 12th January and 30th June 1920, and deducted therefrom the amount at which such goods were taken into stock on 12th January and the expenses subsequently incurred in connection therewith.

The grounds of objection stated in the notice referred to in par. 8 were as follows:—

(1) As from 12th January 1920 the company was in liquidation, and ceased to carry on any business or to engage in any operations other than the realization of its assets for the purposes of winding up.

(2) The said amount of £52,503 (being the difference between the £56,281 mentioned in par. 8 of the case and the £3,778 mentioned in par. 11) represents no more than the conversion into money of certain assets of the company existing at the date of liquidation.

(3) Such assets were manufactured by the company in former years, and their value was included in ascertaining the profits and taxable income of the company on which tax was assessed and paid in such years respectively.

(4) No part of the said amount of £52,503 should properly be regarded as profits of the company.

(5) No part of the said amount of £52,503 should properly be regarded as income of the company.

(6) Alternatively, and at least, if (which is not admitted but is denied) any part of the said amount of £52,503 should be regarded as profits and as taxable income of the company, such part should be no greater sum than a duly prepared profit and loss account would show to be the excess (if any) of the said amount of £52,503 over the value or cost to the company at 12th January 1920 of the assets which realized the said amount and all proper costs of realization.

Latham K.C. (with him *Gregory*), for the appellant. *Primâ facie* the income of a company is its profits, and there is nothing in the *Income Tax Assessment Act* which alters that definition of its income. Upon liquidation a company ceases to make profits; for the profits of a company are the moneys out of which it can pay dividends, and after liquidation no dividends can be paid. (See *Lawless* v. *Sullivan* (1); *Companies Act* 1915 (Vict.), secs. 182 *et seqq.*) What the liquidator was doing was not carrying on the business of the company, but was realizing the assets of the company for the purpose of winding up that business (see sec. 155 of the *Companies Act* 1915 (Vict.)). Any gain that was made is an accretion to the mass of assets which is to be distributed as the *Companies Act* directs, and is not profit in the nature of income. [Counsel also referred to *J. & R. O'Kane & Co.* v. *Commissioners of Inland Revenue* (2); *Commissioner of Taxation (W.A.)* v. *Newman* (3); *Webb* v. *Federal Commissioner of Taxation* (4); *Pool* v. *Guardian Investment Trust Co.* (5); *Commissioners of Inland Revenue* v. *Blott* (6); *Knowles* v.

(1) (1881) 6 App. Cas., 373.
(2) (1922) 126 L.T., 707.
(3) (1921) 29 C.L.R., 484.
(4) (1922) 30 C.L.R., 450.
(5) (1922) 1 K.B., 347.
(6) (1920) 2 K.B., 657.

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Ballarat Trustees Executors and Agency Co. (1); *In re Armitage*; *Armitage* v. *Garnett* (2); *Bishop* v. *Smyrna and Cassaba Railway Co.* [*No.* 1] (3); *Commissioners of Inland Revenue* v. *Marine Steam Turbine Co.* (4); *Commissioners of Inland Revenue* v. *Korean Syndicate Ltd.* (5).]

[ISAACS J. referred to *Melbourne Trust Ltd.* v. *Commissioner of Taxes* (*Vict.*) (6); *Ex parte Emmanuel*; *In re Batey* (7).]

Ham and *Eager*, for the respondent, were not called upon.

Cur. adv. vult.

Mar. 12.

The following written judgments were delivered :—

KNOX C.J. This is an appeal against the assessment to income tax of the amount of profits realized by the liquidator of the company after 12th January 1920—the date of the confirmation of a resolution to wind up the company voluntarily. Par. 4 of the special case is as follows :—[That paragraph was here set out.] It is not disputed that, if there had been no liquidation, profits made by the company as the result of operations similar to those conducted by the liquidator would have been assessable as income to income tax even though the company had before making such profits ceased to carry on the manufacturing portion of its business; but Mr. *Latham* insists that these profits, having been made after the company had gone into liquidation, are not income liable to taxation. He contends that after the confirmation of a resolution for winding up, a company cannot have income liable to income tax. No authority was cited in support of this proposition, and in my opinion it cannot be maintained. The sole question for decision is whether the profits now in question are profits derived by the company from a trade or business carried on by it. The consequences which ensue on the voluntary winding up of a company are stated in the *Companies Act* 1915, more particularly in secs. 186 to 200. A liquidator is to be appointed, and on his appointment the powers of the directors are to cease except so far as the company in general

(1) (1916) 22 C.L.R., 212, at p. 238.
(2) (1893) 3 Ch., 337, at p. 346.
(3) (1895) 2 Ch., 265.
(4) (1920) 1 K.B., 193.
(5) (1920) 1 K.B., 598.
(6) (1912) 15 C.L.R., 274.
(7) (1881) 17 Ch. D., 35.

meeting or the liquidator sanctions their continuance. The liquidator is charged with the duty of winding up the affairs of the company, and is empowered (*inter alia*) without the sanction of the Court to carry on the business of the company so far as may be necessary for the beneficial winding up thereof. The company remains in existence as a legal person until the winding up has been completed and an order for distribution has been made, and even after such an order the Court may, under sec. 221, within two years declare the dissolution to have been void. It is clear that under the *Companies Act* whatever the liquidator does in realizing assets he does as agent for and in the name of the company, and, as my brother *Isaacs* pointed out during the argument, a liquidator is included in the designation of " trustee " by sec. 3 of the *Income Tax Assessment Act* 1915-1918. He is, therefore, made answerable by sec. 52 for the payment of income tax on income derived by him in his representative capacity. In *J. & R. O'Kane & Co.* v. *Commissioners of Inland Revenue* (1) Lord *Atkinson* points out that there are several ways of winding up a business. One of these ways the learned Lord described as follows (2): " There is another way quite as effectual, and that is by continuing to carry on his business in the ordinary way, but not replenishing his stock which he has accumulated as it is sold." From the statement in par. 4 of the special case it appears that, except for the manufacture of alcoholic liquor, the method adopted by the liquidator to realize the stock-in-trade of the appellant was that which would have been followed by the company in realizing its stocks if there had been no liquidation.

In these circumstances I feel no doubt that the profit derived by the liquidator as shown in the statement marked " C " annexed to the special case was the proceeds of a business carried on by the appellant, and so income of the company within the meaning of the *Income Tax Assessment Act* 1915-1918.

In my opinion the question submitted should be answered in the affirmative.

ISAACS J. In my opinion the respondent succeeds. The taxpayer's case rests on the position that, once a winding up commences,

(1) (1922) 126 L.T., 707. (2) (1922) 126 L.T., at p. 710.

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there is, so to speak, an agglomeration of all the property of the company under the name of "assets," and that so remains, however the property is altered in character or dealt with or added to. It is said that, whether the property is realized in one solitary operation unconnected with any other operation, or in a series of operations so connected as to be ordinary trading, it does not matter—the main body of the property and all accretions fall under the one designation "assets," and cannot be separated into capital and income. The result, it was urged, was that in the course of winding up a company there could be no such thing as "income" to be taxed under the Commonwealth *Income Tax Act*.

Mr. *Latham* relied on some decisions and observations in this Court, in support of this contention; but on the whole I feel free to express the opinion I hold. One thing is plain: the Commonwealth Parliament did not regard the position as presented for the taxpayer. Sec. 52 of the *Income Tax Assessment Act* with respect to every "agent" and every "trustee" enacts that (*a*) "He shall be answerable as taxpayer . . . in respect of the *income derived by him in his representative capacity* . . . and the payment of income tax *thereon*." Other paragraphs in that section make consequential provisions. Sec. 3 declares that the word "trustee" includes "liquidator." The intention of the Act was indubitably to reach income of a company "derived" during the regime of a liquidator. Unless, therefore, the Commonwealth Parliament's intention fails because it radically misunderstood the very nature of the case, and unless under the State law controlling the functions and property of companies there be such an indistinguishable agglomeration of "assets" that no "income" can ever come into existence at all, it is manifest the argument cannot be sustained.

What, then, is the true position? Essentially, I take it to be this:—The *Companies Act* of Victoria, like all corresponding Acts in Australia as well as in England, affords facilities and provides methods for individuals associating themselves as a trading corporation. While so associated the corporation is a separate legal entity, and can in conformity with its constitution trade and makes income. Creditors and shareholders are protected by appropriate provisions. But the Act also makes provision for appropriate

methods by which the individuals composing the corporation may discontinue their association and dissolve the corporation. Safeguards are again provided for this process. Creditors and shareholders are protected by enactments which modify the corporate powers of the company during its moribund condition with a view to its eventual extinction. When liquidation is once commenced, whatever the company earns, whatever it acquires, whatever property it for any reason owns—and "property" is only another name for "assets" (*Webb* v. *Whiffin* (1))—has impressed on it what I may for convenience call a trust, and must be applied so as to ensure security and justice to the parties interested. But calling the property "assets" works no magical transformation: it neither obliterates its natural character, nor its legal diversity. Land is still land, goods are still goods, money is still money. Capital is still capital, and, if it fructifies and produces income, as it may, the income is still income. If a company in process of liquidation has deposits in a bank or outstanding mortgage investments, the interest does not change its legal character by reason of the winding up resolution.

The inherent fallacy in the appellant's argument is twofold. First, it seeks under the general term "assets" to drown the inherent distinction between "capital" and "income." A profit made by the ordinary employment and risk of capital in trading operations is "income." A profit made by an isolated transaction outside trade by which property is simply transformed, say land into cash, is not income. It is then a mere change in form of capital by which the resultant form may be larger or smaller than the original form. No legal formula can determine for all cases whether an enhancement is increased capital or is income. It must be determined by commercial principles. But one thing is very clear, namely, that profits made in the ordinary course of business are income. It was contended on behalf of the appellant that the process of selling the company's stock was properly described as "realization." The same could be truly said of all sales in business. Every merchant "realizes" his stock when he sells goods for money. But I dealt with that contention in the *Melbourne Trust Case* (2), and quoted a passage from a Scottish case to the effect that enhanced values obtained from

(1) (1872) L.R. 5 H.L., 711, at p. 724. (2) (1912) 15 C.L.R., at pp. 302-303.

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realization are assessable where " what is done is *not merely* a realization or change of investment, but an act done in what is truly the carrying on, or carrying out, of a *business*." That passage was declared by the Privy Council, on appeal, to state correctly the principle (*Commissioner of Taxes* v. *Melbourne Trust Ltd.* (1)). Consequently, the mere fact of " realization " does not conclude the matter. Was the enhanced value here obtained in carrying on the business ? Obviously, and indeed confessedly, it was. True the business was carried on only for the purpose of winding up, but it was in fact and in law carried on. The sales took place, it is stated, from 12th January to 30th June 1920, that is, over the whole period of six months. Reference to the figures and dates as stated in the case will forcibly illustrate what I have said. The winding-up resolution was passed on 12th January 1920. At that date the stock is stated to have been valued at £21,291 17s. 2d. If, therefore, assuming that to be an accurate valuation, the stock had been immediately sold, that is the sum which it must be assumed would have been realized. But by risking the capital in business a huge profit was made. The stock as sold from 12th January to 30th June in ordinary trading realized £66,704 6s. 6d., or an accretion of £45,412 9s. 4d.; and, after allowing for all proper expenditure, there remains for the period a net balance of profit of £39,496 19s. 7d. That was the result in money of the operations of the business as a profit-making machine, and the mere fact that no fresh fuel was supplied—though a cause of its ultimate stoppage—did not alter the nature of its production while it functioned. The second fallacy in the appellant's argument is a highly important one. It regards the application of the income, its aggregation at the moment of its birth, so to speak, with the rest of the assets for winding-up purposes, as destroying its identity for taxing purposes. The taxing Acts affect neither the internal rights of shareholders to their due proportion of the assets, nor the rights of creditors to be secured: but they equally ignore those private individual rights, and look to the actual operations of the company as a producer of income. If income is actually made it is taxed, notwithstanding the

(1) (1914) A.C., 1001, at p. 1010; 18 C.L.R., 413, at pp. 420-421.

company is on its way to dissolution. There are many cases illustrating this, among which are *Mersey Docks and Harbour Board* v. *Lucas* (1); *Webb* v. *Australian Deposit and Mortgage Bank Ltd.* (2); *Port of London Authority* v. *Commissioners of Inland Revenue* (3). The question should be answered in the affirmative.

HIGGINS J. On the facts of the case as stated, I see no ground for the view that income tax is not payable on the balance of receipts over expenditure for the period from 12th January to 30th June 1920.

The business has been carried on by the company just as before 12th January, with two exceptions: (1) that it has been carried on by the liquidator; (2) that the liquidator ceased all manufacturing operations. The business that the company could carry on under its memorandum (cl. 3 (b)) comprised not only that of distillers but also that of "wine and spirit merchants . . . dealers in . . . other drinks and any other businesses which can be conveniently carried on by the company in connection with the above or any of them." The statement exhibit C furnished by the liquidator sets out clearly the accounts—"which" (as he says) "in a company carrying on business would constitute the profit and loss account." It shows profits of the business, just as if the company were not in liquidation; and I cannot find that it differs in the slightest from an ordinary profit and loss account of a going concern, except that there is no more manufacture of spirits. For aught that appears in the case stated, the sales of the spirits may go on indefinitely—so long as the spirits last. This is an extract from the account:—"Stock sold from 12th January to 30th June 1920, £66,704 6s. 6d.; Less the amount at which it was taken into stock at 12th January 1920, £21,291 17s. 2d.: £45,412 9s. 4d." As against this sum there are salaries and wages, sundries, plant maintenance, office charges, duty (excise), coopers' wages, insurance, cartage, rates, advertising, &c. I know of no principle binding us to hold that what are profits in ordinary parlance must not be treated as profits if they are made by the liquidator of a company instead of by the directors and manager of the company; and if they are profits of carrying on any of

(1) (1883) 8 App. Cas., 891. (2) (1910) 11 C.L.R., 223, at p. 235.
(3) (1920) 2 K.B., 612.

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the businesses authorized by the memorandum, they are income, and taxable. As Lord *Parmoor* puts the matter, in *J. & R. O'Kane & Co.* v. *Commissioners of Inland Revenue* (1), "the question is this: Were the transactions in question in this appeal transactions which took place in carrying on a trade or business? If so, the profits arising from any such trade or business are undoubtedly subject to excess profits duty." That was a case as to excess profits duty, but the same observations apply to our income tax. The liquidator "*carries on* the business of the company so far as may be necessary for the beneficial winding up thereof" (Victorian *Companies Act* 1915, sec. 155 (1) (*b*), sec. 186).

I have been rather surprised to hear the decision on the Western Australian Act cited as an authority in favour of the appellant (*Commissioner of Taxation* (*W.A.*) v. *Newman* (2)). There a pastoralist simply sold off his station and stock; and it was held that the proceeds could not be treated as profits derived from carrying on the business of pastoralist.

RICH J. We are asked whether the sum of £39,497 is taxable income of the company. This sum is the excess of receipts over expenditure for the period 12th January 1920 to 30th June 1920.

On 12th January 1920, when the resolution for voluntary winding up was passed and the liquidator was appointed, the company ceased to carry on its business except so far as might be required for the beneficial winding up thereof (*Companies Act* 1915 (Vict.), sec. 184), and the powers of the directors ceased. That is to say, the liquidator displaced the directors and became the agent of the company and carried on its business in a due course of winding up. The course of business is described in clause 4 of the case stated, where it appears that "the liquidator incurred and discharged the usual expenses and charges incidental to the carrying on of the business, save and except those relating to the manufacture of alcoholic liquor, such manufacture having ceased."

Counsel for the company put forward two propositions in support of the exemption claimed. The smaller proposition was based on the cessation of the company to manufacture alcoholic liquor, which

(1) (1922) 126 L.T., at p. 711. (2) (1921) 29 C.L.R., 484.

counsel suggested was tantamount to a cessation of business. This contention, so far as it is a matter of fact, is effectually disposed of by clause 4 of the case. The provisions of sec. 184 of the *Companies Act* expressly state that a company in liquidation is carrying on business, and show that there is no legal reason why the actual facts should not be recognized. The larger proposition was that the sum of £39,497 is an accretion to the mass of assets and is not profit in the nature of income. The property or assets of a company for distribution among its creditors and shareholders may consist of a mass comprising capital and income, but before such distribution is made it is a simple process to distinguish income from capital so as to arrive at the subject of taxation; and, reading sec. 52 of the *Income Tax Assessment Act* with sec. 3, not only does it appear that the Act contemplated the taxation of income arising during winding up, but, when reference is made to sec. 45A (inserted by the Act No. 18 of 1918), it is clear that that section, read with the other two sections, was intended to and does cover the case of income made by the liquidator for the company as well as any unpaid tax incurred before the winding up.

I answer the question propounded in the affirmative.

STARKE J. The taxpayer, in this case, is incorporated under the law of the State of Victoria as a proprietary company with a limited liability. It is in course of liquidation pursuant to a resolution passed by its members that it be voluntarily wound up. The liquidator ceased the manufacturing operations of the company, but proceeded to realize its stocks of liquor in the same manner and by the same methods as were practised by the company before the liquidation. Profits were thus made, and the Commissioner has assessed the company to income tax in respect thereof.

It was not disputed that the series of acts or transactions which produced the profits in this case would, in the case of a company not in liquidation, be properly described as a business carried on by the taxpayer, and the proceeds thereof as income within the Income Tax Acts. It was insisted, however, that a company in liquidation does not carry on business, but simply realizes its assets, and, after discharging the expenses of the winding up and the liabilities of

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the company, distributes such assets amongst its members, as surplus assets and not as profits. The main flaw in the argument resides, in my opinion, in the assumption that a company in liquidation cannot continue its business for purposes of the winding up. The *Companies Act* 1915, secs. 155 and 186, however, empowers the liquidator to carry on the business of the company so far as may be necessary for the beneficial winding up thereof. Whether the business of the company is continued or not is a question of fact, and in this case there is no doubt that it was carried on. *J. & R. O'Kane & Co.* v. *Commissioners of Inland Revenue* (1) and *Armitage* v. *Moore* (2), though not directly in point, assist the conclusion stated. The argument, moreover, omits to notice that once taxable income has been earned, the destination of that income, the character in which it reaches the hands of other persons, or the purposes to which it is devoted, are all equally immaterial (*Mersey Docks and Harbour Board* v. *Lucas* (3)).

The question stated ought to be answered in the affirmative.

Question answered in the affirmative.

Solicitors for the appellant, *àBeckett & Chomley.*

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

B. L.

(1) (1922) 126 L.T., 707. (2) (1900) 2 Q.B., 363.
(3) (1883) 8 App. Cas., 891.