[HIGH COURT OF AUSTRALIA.]

THE PREMIER AUTOMATIC TICKET ISSUERS LIMITED . . . . . } APPELLANT;

AND

THE FEDERAL COMMISSIONER OF TAXATION RESPONDENT.

H. C. OF A. 1933.

SYDNEY, *Aug.* 16, 17; *Nov.* 7.

Rich, Starke, Dixon, Evatt and McTiernan JJ.

Income Tax (Cth.)—Assessment—Income derived from sources in Australia—Patent rights owned by taxpayer—Agreement made in Australia between taxpayer and licensee empowering licensee to sell patent rights—Sale of British patent rights to English company effected by licensee in England—Share of proceeds paid to taxpayer—Income or capital—Source—Profit-making scheme—Income Tax Assessment Act 1922-1929 (*No.* 37 *of* 1922—*No.* 11 *of* 1929), *secs.* 4*, 13*, 16c*—*Income Tax Assessment Act* 1930 (*No.* 50 *of* 1930), *secs.* 2 (*c*), 26 (1).

The taxpayer, a company incorporated in New South Wales, with its registered office and only place of business in Sydney, acquired from the inventors patent rights in respect of a ticket-issuing machine. The objects of the taxpayer included the power to turn to account, sell or dispose of any of

* The *Income Tax Assessment Act* 1922-1929, sec. 4, as amended by sec. 2 (*c*) of the *Income Tax Assessment Act* 1930, provided, in respect of assessments for the financial year beginning on 1st July 1922 and all subsequent years (see sec. 26 (1) of the Act of 1930): "'Income' includes . . . (*ba*) any profit arising from the sale by any person of any property acquired by him for the purpose of profit-making by sale or from the carrying on or carrying out of any profit-making undertaking or scheme." The Act of 1922-1929 also provided:—By sec. 13 (1): "Subject to the provisions of this Act, income tax shall be levied and paid for each financial year upon the taxable income derived directly or indirectly by every taxpayer from sources within Australia during the period of twelve months ending on the thirtieth day of June preceding the financial year for which the tax is payable." By sec. 16c: "Where a taxpayer claims that (*a*) by reason of the manufacture, production, or purchase of goods in one country and their sale in another; (*b*) by reason of successive steps of production or manufacture in different countries; or (*c*) by reason of the making of contracts in one country and their performance in another, or for any other reason whatever, income is derived partly from sources outside Australia, the question whether any, and if so what part, of the income is derived from sources outside Australia shall be determined in accordance with the regulations, or, if there is no regulation applying to the case, shall be determined by the Commissioner."

its patents, licences and concessions. A. Ltd., a company also incorporated in New South Wales and having its registered office and principal place of business in Sydney, was the owner of patent rights in respect of a machine known as a "totalisator." S., an employee of A. Ltd., was the inventor and patentee of another ticket-issuing machine. Both types of machine for issuing tickets were suitable for use with totalisator machines. By an agreement made in Sydney in 1922 between the taxpayer, A. Ltd., and S., A. Ltd. was given the sole right to manufacture, use, sell and operate for use with totalisator machines all ticket-issuing apparatus for which rights by letters patent or otherwise had been or might be acquired by the other parties, and it was provided that, should A. Ltd. dispose of its proprietary rights to the totalisator and/or the ticket-issuing machines in any country, A. Ltd. should make payment to the taxpayer in accordance with a stipulated method of calculation. In 1928 A. Ltd. entered into an agreement in England with an English company for the sale to the latter of the British patent rights covering the totalisator and a ticket-issuing machine, and received payment of the purchase price in England. A. Ltd. thereupon, in accordance with the agreement of 1922, paid to the taxpayer out of the proceeds of the sale the sum of £10,000, which the taxpayer distributed as dividends.

Held that the taxpayer became entitled to the sum of £10,000 by virtue of the agreement of 1922, and that the agreement had been entered into in the course of carrying on the taxpayer's profit-making business: Consequently that sum was not capital and was not derived outside Australia, but was taxable under the *Income Tax Assessment Act* as being income of the taxpayer derived from a source within Australia.

CASE STATED.

On the hearing of an appeal to the High Court by the Premier Automatic Ticket Issuers Ltd. from an assessment of that company by the Federal Commissioner of Taxation for income tax for the year ended 30th June 1930, *Dixon* J. stated a case, which was substantially as follows, for the opinion of the Full Court:—

1. By notice of assessment dated 22nd April 1930 the Deputy Commissioner of Taxation notified the public officer of the Premier Automatic Ticket Issuers Ltd. (in this case called "the taxpayer") that he had assessed the amount of Federal income tax payable by it for the financial year 1929-1930 in respect of its taxable income derived during the year ended 30th June 1929 as under: Amount of taxable income £10,395; Amount of tax £623 14s.

2. By notice of objection dated 14th May 1930 the public officer of the taxpayer objected to the assessment. In the assessable income upon which the assessment was based a sum of £10,000 was included.

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

The grounds of the objection were, in effect :—(*a*) That the sum of £10,000 was received as the sale price of certain patent rights in Great Britain belonging to the company and was not income: (*b*) That the said sum was received for the sale of a fixed capital asset of the company, viz., such patent rights, and was therefore a transmutation of capital and was not income. (*c*) Alternatively, that if the said sum was income it was not derived from a source in Australia but from a source in England where the sale was effected.

3. The Commissioner considered the objection and disallowed it wholly. Thereupon the taxpayer being dissatisfied with the decision of the Commissioner requested the Commissioner to treat its objection as an appeal and forward it to the High Court. The objection was transmitted accordingly and the appeal came on to be heard before me when the facts hereinafter appearing were proved.

4. On 24th July 1911 a company was incorporated in New South Wales called "Totalling Mechanisms Limited." As appears from its memorandum and articles of association, its first object, in effect, was to purchase or otherwise acquire rights in inventions of any totalisator machine or any invention which might seem to the company capable of being profitably dealt with, and, in particular, to acquire from an existing company called "Premier Totalisator Limited," of Perth, the Commonwealth and New Zealand rights in a particular patent which had been granted in Australia and in New Zealand, and with a view thereto to enter into an agreement already prepared and expressed to be made between Premier Totalisator Ltd. and the said company. The company's objects also included power to use, exercise, develop and grant licences in respect of or otherwise turn to account the patents, and power to carry on business as manufacturers of totalisators and contractors in connection with totalisators.

5. On 21st April 1915 another company was incorporated in New South Wales, which was called "Automatic Totalisators Limited." As appears from its memorandum and articles of association, its first object was, in effect, to purchase or otherwise acquire interests in any invention in relation to totalisator machines or any patent which might seem to the company capable of being profitably dealt

with, and, in particular, to acquire from Totalling Mechanisms Ltd. the whole of its assets and with a view thereto to enter into an agreement prepared and expressed to be made between its liquidator and the new company, Automatic Totalisators Ltd. By another object, Automatic Totalisators Ltd. was enabled to use, exercise, develop and grant licences in respect of and otherwise turn to account any such patents, but subject to an agreement dated 24th July 1911 between Premier Totalisator Ltd. and Totalling Mechanisms Ltd. This agreement was not put in evidence, but I inferred that under it Totalling Mechanisms Ltd. acquired the Commonwealth and New Zealand rights in the patent mentioned in par. 4 hereof.

6. On or shortly before 30th October 1917 the taxpayer was incorporated in New South Wales. As appears from its memorandum and articles of association, its objects of association conferred upon it very wide and multifarious powers. The first object enables it, in effect, to acquire trade marks, patents, etc., and in particular to acquire a certain patent for an invention in relation to ticket-issuers and with a view thereto to enter into an agreement mentioned in the articles. The second of the company's articles requires the company to enter into this agreement which is described as an agreement between George Alfred Julius and Frederick Augustus Wilkinson in terms of a draft which had been subscribed for purposes of identification. These persons were the inventors of the invention in relation to ticket-issuers and had applied for a patent for the said invention in the Commonwealth by an application No. 4055. The agreement was entered into accordingly by Julius and Wilkinson, described as vendors, and by the company. For convenience it may be summarized as follows: The vendors sold and the company purchased (*a*) the benefit of the application No. 4055, (*b*) the benefit of foreign patents applied for in the invention, (*c*) the exclusive right to apply for foreign patents in the invention and all future improvements, (*d*) the benefit of any extensions, and (*e*) the benefit of all pending contracts and engagements to which the vendors were entitled in connection with the said patents. The consideration of the agreement was £5 paid to the vendors by the company.

7. In fact, before the incorporation of the taxpayer, namely, on 14th September 1917, the vendors Julius and Wilkinson had entered

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

into an agreement "in connection with the said patents." This agreement was made between them and Automatic Totalisators Ltd. For convenience its effect may be summarized as follows:—The vendors granted to that company an exclusive licence within the Commonwealth and New Zealand to exercise for use in connection with totalisator machines their invention covered by application No. 4055 during the term of the patent and any extension. The company agreed to pay a royalty of £12 a machine and before 31st March 1918, unless prevented by causes beyond its control, to manufacture not less than 320 machines. The agreement contained many usual conditions and was determinable by the licensors on breach of condition. The company was authorized to grant sub-licences but not to assign. The licensors agreed for three years to manufacture and supply, and the company to purchase, certain attachments, required for ticket-issuing machines for the purpose of numbering horses, called electro-types.

8. Application for letters patent No. 4055 was granted. The invention of Julius and Wilkinson covered by the patent was for a device for ticket-issuing machines. The device was suitable for use in connection with totalisators. Totalisators are machines or devices for automatically recording bets made upon the parimutuel system. Automatic Totalisators Ltd. was entitled to patents for inventions and improvements by Julius and others for totalisators.

9. After the incorporation of the taxpayer, Julius and Wilkinson made another invention for an improved ticket-issuing machine described as a "fare admission machine." Protection was obtained for this by a Commonwealth patent and it was assigned to the taxpayer. The invention, however, was never put into actual use. Still later, Julius invented an improvement upon the invention the subject of patent No. 4055. Protection was obtained for this invention by a Commonwealth patent and it was assigned or made over to the taxpayer. Because it related to "win and place betting" it superseded the prior inventions in utility.

10. From its incorporation until 1925 the taxpayer manufactured in Sydney electro-types for supply to Automatic Totalisators Ltd., but it had no other active business. From its incorporation Wilkinson was a member of its board of directors. He was also its paid

secretary and he managed the company. Julius became a director on 18th December 1928. In and before that year he was a director of Automatic Totalisators Ltd. At all material times the substantial shareholders of the taxpayer company, that is shareholders who held more than a nominal share, were four in number. Julius and Wilkinson were two of such shareholders. At all material times Wilkinson was also employed by Automatic Totalisators Ltd. as totalisator manager. His duties were to supervise the installation and operation of its machines.

11. The revenue of the taxpayer consisted of royalties from Automatic Totalisators Ltd. and the proceeds of sale of the electro-types. According to its balance-sheets and profit and loss accounts, royalties amounted to £1,008 for the twelve months ended 30th June 1922 and the gross profit on electro-types to £775 and the patents were set down at a value of £655 as at 30th June 1922. Roughly estimated, the amount received by the taxpayer under the agreement of 14th September 1917 from its incorporation up to 16th November 1922 was about £6,000.

12. Automatic Totalisators Ltd. employed as its works manager one Henry Roy Setright. In or about 1921 or 1922 Setright devised another ticket-issuing machine. He brought his invention to the notice of the directors of Automatic Totalisators and through them to the notice of the directors of the taxpayer. Julius and Wilkinson considered it might prove an improvement upon their invention, and therefore negotiated terms with Setright for the acquisition of the rights in connection with his invention. These terms were embodied in an agreement between Automatic Totalisators Ltd., the taxpayer and Setright, made on 16th November 1922. [The terms of the agreement sufficiently appear from the judgments hereunder.] The issued capital of the company consisted of 1,000 shares of one pound each, but in order to comply with clause 7 of the agreement each shareholder of the taxpayer company made over to Setright thirty per cent of his shareholding. Setright's invention was patented in the Commonwealth and afterwards in Great Britain and it was used upon two racecourses in Australia. In making the agreement of 16th November 1922 Automatic Totalisators Ltd. and the taxpayer company were actuated by apprehension of competition from

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Setright's invention and by the circumstances that ticket-issuer inventions were practically useful only in connection with totalisators.

13. In the taxpayer's balance-sheet for the year ended 30th June 1923 the patents were set down as of the value of £1,155; in the balance-sheet as at 30th June 1924, at £1,405; and in the balance-sheets as at 30th June of the years 1925 to 1928, at £1,815.

14. Before the year 1928, save as appears from previous paragraphs of this case, the taxpayer took no steps towards disposing of its patent rights, except that on 1st May 1919 its board of directors resolved that one J. R. Gorton, a director, should be appointed agent for the sale of the company's patents and patent rights for all territories outside the Commonwealth of Australia and the Dominion of New Zealand and that he be paid or given as his remuneration on any sale made by him or his substitute ten per cent of the consideration paid to the company and that such payment should be made within fourteen days of the receipt of the amount of the purchase money by the company, or, if the consideration consisted in a royalty, within fourteen days of the receipt of each payment.

15. In January 1927 the board of directors of Automatic Totalisators Ltd. caused Wilkinson to go to Europe on behalf of that company. He supervised the installation and erecting of the totalisator in France and this work included looking after ticket-issuer machines. Although he went to Europe at the instance of Automatic Totalisators Ltd. his remuneration as secretary of the taxpayer was continued, but his expenses and other remuneration were borne by Automatic Totalisators Ltd. or a company in which that company and the taxpayer held shares, called Automatic Totalisators (France) Ltd.

16. Wilkinson remained in Europe for three years. In 1927, while he was in France, the English Jockey Club invited him to consult with them concerning the installation of totalisators on English racecourses. This invitation arose from the circumstances that a bill authorizing totalisators was then pending before the British Parliament. He went to England from France and was joined by Julius, who was also in Europe. Separately and together they took part in consultations with select committees of the Legislature and with racing authorities and others with a view of furthering the

passing of the bill and of bringing about a favourable consideration and adoption of their totalisator machine upon English racecourses. They gave demonstrations of a model machine before those bodies and generally endeavoured to promote the use of their totalisator. Julius returned to Australia early in 1928, but after February. Early in 1928 Wilkinson considered it probable that the Jockey Club would not be entrusted by the Legislature with control of totalisators. In January 1928 an inquiry was made on behalf of speculators in England by a cable addressed to a member of the board of Automatic Totalisators Ltd., with a view to the acquisition of the British rights in the inventions for the complete totalisator machine. This inquiry was discussed and considered by that company's board but nothing came of it. In or about March 1928 a syndicate in London made to Wilkinson an offer for the British rights of £100,000 and one-eighth per cent royalty. On 2nd April 1928 Wilkinson communicated this offer by cable to Automatic Totalisators Ltd. in Sydney. About 8th April 1928 he became aware that an inaccuracy had been discovered in the totalisator which the company had installed at Longchamp in France. One Bethell, who had formerly been connected with Automatic Totalisators Ltd., was in England supporting a rival totalisator. Setright was also in England supporting a rival totalisator. Wilkinson believed that Bethell was aware of the defect at Longchamp and of some defects discovered in installations by Automatic Totalisators Ltd. elsewhere. He expected that the third reading of the bill before the British Legislature would take place on 17th April 1928. By a cable proceeding on these grounds he strongly advised the board of Automatic Totalisators Ltd. to accept the offer. After consideration they authorized him to do so but various questions and details were submitted to and considered by the board in Sydney and their views were transmitted by cable to Wilkinson before the transaction was agreed. The syndicate formed a company called Totalisators Ltd. and two agreements were entered into with this company, dated respectively 17th and 18th May 1928. The patents comprised in the schedule to the agreement of 17th May 1928 included the British patents for Setright's invention (No. 201152) and for Julius' invention

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

(No. 15757 of 1927), a ticket-issuing machine for "win and place betting."

17. The bill before the Legislature was passed and is 18 & 19 Geo. V. c. 41. It was assented to on 3rd August 1928.

18. The deposit and balance of purchase money were paid in England to Automatic Totalisators Ltd. But the board of the taxpayer company on 28th November 1928 in Sydney resolved that authority be given to Totalisators Ltd., London, to pay Automatic Totalisators Ltd. cash and royalties payable under the agreement of 17th May 1928 between those companies, and that the directors sign the necessary documents. It further resolved that Julius be authorized to assign to Totalisators Ltd., London, at the request of Automatic Totalisators Ltd. the British patent for his ticket-issuing invention. Further, that the directors sign and seal the assignment from the taxpayer to Totalisators Ltd., London, as "supplemental to the agreement and assignment of rights and interests in ticket-issuers." All these documents were executed in New South Wales. Setright executed the assignment of his British patent in England.

19. In contemplation of the receipt of £10,000 from Automatic Totalisators Ltd., the taxpayer's directors on 18th December 1928 declared a dividend of £8 per share upon their capital of 1,000 shares. This money was in fact paid to the taxpayer by Automatic Totalisators Ltd. in New South Wales.

20. In the profit and loss account of the taxpayer for the twelve months ending 30th June 1929, the revenue items consisted of royalties and dividends from shares in the French company and "sale of English rights, £10,000." In the balance-sheet the value of patents was still set down as £1,815.

21. Throughout, Automatic Totalisators Ltd. had been installing and supervising totalisators in various places and had paid royalties to the taxpayer in respect of the ticket-issuers used in these installations. Except as appears from the previous paragraphs of this case and except that it had formed a separate company for the work in France, which must have involved the parting with some French rights in the invention, it does not appear that Automatic Totalisators Ltd. actually sold or disposed of patent rights. No attempt was made by either company to find in Australia a means of disposing of the

foreign rights in any of the inventions. I rejected evidence tendered to prove that in the period March to June 1928 the board of Automatic Totalisators Ltd. decided upon the price it would be prepared to accept for its patent rights in Chile, gave an authority in relation to, and offer for, patent rights in the United States of America, Mexico and Cuba and gave another authority in respect of rights in countries where the company's totalisators were not in operation and were the subject of negotiations. None of the ticket-issuing devices was of any practical use except in connection with the totalisators. The patents referred to in the schedule of the agreement of 17th May 1928, mentioned in par. 16 of this case, are in respect of inventions covered by Australian patents, and in each case the Australian patent was granted before the application for the British patent was made.

22. The taxpayer and Automatic Totalisators Ltd. each had its registered office in Sydney, although not in the same building. In each case the registered office of the company was its principal place of business and there its books of account were kept, its balance-sheets and reports were prepared and its board of directors met. The taxpayer had no other place of business.

23. The taxpayer did not in fact claim that the income was derived partly from sources outside Australia, but it claimed that it was derived wholly from sources outside Australia. The Commissioner did not, except upon the hearing of the appeal, claim that the income was derived partly from sources in Australia. He claimed that it was derived wholly from sources in Australia. Accordingly he made no determination under sec. 16c of the *Income Tax Assessment Act* 1922-1929, but on the hearing of the appeal before me his counsel contended, as an alternative to the contention that the income was derived wholly from sources in Australia, that the income was at least derived partly from sources in Australia.

The questions reserved for the consideration of the Full Court were :—

(1) Am I at liberty upon the materials included in the special case to find that the sum of £10,000 is not (*a*) income of the taxpayer or (*b*) derived directly or indirectly from sources in Australia ?

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

(2) Is the Commissioner of Taxation entitled as a matter of law upon the materials included in the special case to a finding that the sum of £10,000 formed part of the income of the taxpayer derived directly or indirectly from sources in Australia ?

(3) Is the taxpayer entitled as a matter of law upon the materials included in the special case to a finding that the sum of £10,000 (*a*) did not form part of the income of the taxpayer or (*b*) was not derived directly or indirectly from sources in Australia ?

(4) (*a*) On the materials included in the special case ought I as a matter of law to find that the income is derived partly from sources outside Australia ? (*b*) Does sec. 16c of the *Income Tax Assessment Act* 1922-1929 apply to the assessment in reference to the inclusion of any part of the said sum of £10,000 ? (*c*) If so, is the determination of the question what part of the income is derived from sources outside Australia the exclusive function of the Commissioner of Taxation ?

E. M. Mitchell K.C. (with him *Bowie Wilson*), for the appellant. In order to determine the question whether the £10,000 was income or a realization of capital the proper method of approach is to ascertain whether the appellant is a company part of the business operations of which was the sale of its patents for profits. Upon an examination of the facts, this question must be answered in the negative. The objects of the company are not conclusive on the question of what the company did ; that question can be answered only by the correspondence and documents before the Court (*Ruhamah Property Co.* v. *Federal Commissioner of Taxation* (1)). It was no part of the appellant's business to buy patents, nor in fact did it at any time buy any patents for purpose of sale. From the inception of the company in 1917 to 1928 there was not any sale by it of a patent. The transaction in question is the only instance during the company's existence of a sale of its rights. The appellant's rights are restricted to the Commonwealth and New Zealand, and

(1) (1928) 41 C.L.R. 148, at pp. 151, 152.

do not extend to other places where the patents are also registered. The agreement of November 1922 merely evidences a pooling arrangement between the three parties thereto for the exploitation of their patents in other countries. This is clearly established by the facts, which further show that one party acted as the agent of all the parties. The agreement did not operate as an absolute alienation of all interests then possessed by the appellant: it simply put the company into the position that it had to be an assenting party to a sale. In *Collins* v. *Firth-Brearley Stainless Steel Syndicate* (1) there had been three dispositions of rights within three years as compared with the one disposal of rights here in eleven years; therefore that case is much stronger than the present case for treating the proceeds arising from the various sales as income. The test to determine whether such proceeds are income is: Were the patents acquired for purpose of re-sale at a profit? (*Californian Copper Syndicate* v. *Harris* (2)). Having regard to the terms of the agreement and the circumstances of the case, the appellant's part in the transaction was not an " accidental dealing " but was an exceptional dealing forced upon it (*Ducker* v. *Rees Roturbo Development Syndicate* (3)). The definition of " income," as given in sec. 2 (*c*) of the *Income Tax Assessment Act* 1930, is only a declaration of the then existing law. Its enactment was the result of observations by members of the Court in *Blockey* v. *Federal Commissioner of Taxation* (4). The test still is: Was the transaction a realization of capital, or was it a part of a profit-making enterprise? Here the patents were acquired as " plant " and hence are capital assets. The money received by the appellant is not income derived either wholly or partly from a source within Australia, because it was the profits of the sale of fixed property situate in England, that is, the sale of the English patents.

[DIXON J. referred to *Dickson* v. *Commissioner of Taxation (N.S.W.)* (5).]

Even though there may be only one business, that one business may have various sources of profits, some of which may be within,

(1) (1925) 9 Tax Cas. 520; 133 L.T. 616.
(2) (1904) 5 Tax Cas. 159.
(3) (1928) A.C. 132, at pp. 141, 142.
(4) (1923) 31 C.L.R. 503.
(5) (1925) 36 C.L.R. 489.

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

and some without, Australia (*Commissioner of Taxation (W.A.)* v. *D. & W. Murray Ltd.* (1)).

[EVATT J. referred to *Lovell & Christmas Ltd.* v. *Commissioner of Taxes* (2).]

That case and *Commissioner of Taxation (W.A.)* v. *D. & W. Murray Ltd.* (1) indicate that the source of the income is not determined merely by the place where certain of the preparatory arrangements were made. Here the only thing done in or from Australia was the sending of a sum of money for expenses; everything else was done in England. This case illustrates the principles in *Commissioners of Taxation* v. *Kirk* (3): in that case four stages were taken; in this case one, the implanting of the patent into England.

[STARKE J. The converse of *Lovell & Christmas Ltd.* v. *Commissioner of Taxes* (2) is *Studebaker Corporation of Australasia Ltd.* v. *Commissioner of Taxation (N.S.W.)* (4).]

Here it is the case of a sale entirely negotiated in England, of a property "locally situate" in England, and payment made in England; therefore the source of the income is in England (*English Scottish and Australian Bank Ltd.* v. *Inland Revenue Commissioners* (5); *Potter* v. *Broken Hill Pty. Co.* (6); *Underhill* v. *Hernandez* (7)). It is also important that the sale was made possible only by the passing in 1928 by the Parliament in England of the Act 18 & 19 Geo. V. c. 41, which authorized the use of totalisators in that country. The money was not received by the appellant under and by virtue of the agreement of November 1922. That agreement was a pooling arrangement, and merely fixed the measure of what the appellant might get in the event of a subsequent sale to which it was an assenting party. The appellant had the right to choose the second method as against the first method of payment set out in the agreement, which necessarily means that the appellant was entitled to choose either method. The evidence shows that the appellant did not traffic in or sell patents; that it was not formed for that purpose; that it was formed for the purpose of working patents in conjunction with Automatic Totalisators Ltd.; and that

(1) (1929) 42 C.L.R. 332.
(2) (1908) A.C. 46.
(3) (1900) A.C. 588.
(4) (1921) 29 C.L.R. 225.
(5) (1932) A.C. 238.
(6) (1906) 3 C.L.R. 479.
(7) (1897) 168 U.S. 250.

it had not any power to traffic in patents. Sec. 16c of the *Income Tax Assessment Act* 1922-1931 was enacted subsequently to *Michell* v. *Federal Commissioner of Taxation* (1). Regulations under that section have not yet been issued; until so issued the matter must be determined by the Commissioner as formerly.

Sir *Robert Garran* K.C. and *A. M. Cohen*, for the respondent. The sum of £10,000 in question was derived by the appellant from sources within Australia. The appellant company has only "one locality" (*Federal Commissioner of Taxation* v. *W. Angliss & Co. Pty. Ltd.* (2)); it is incorporated here; it has its only place of business here; and it has received this sum of £10,000, by virtue of a contract made here, from another company also situate here. These facts distinguish this case from *Nathan* v. *Federal Commissioner of Taxation* (3), *Studebaker Corporation of Australasia Ltd.* v. *Commissioner of Taxation (N.S.W.)* (4), and *Commissioner of Taxation (W.A.)* v. *D. & W. Murray Ltd.* (5), but those cases do establish that the only question is the source of the income of the taxpayer himself, and that the source of the income to the payer cannot be considered. The main objects of the appellant company show that from its inception the company contemplated the turning to account of its patents either by licence or by sale. The provisions of the agreement of November 1922 negative the suggestion that it was a "pooling arrangement" by the parties of their respective interests. Under the agreement, Automatic Totalisators Ltd. acquired full rights of disposal of ticket-issuers the letters patent of which were held by the appellant company. No right was reserved to the appellant to veto any sale that might be made by Automatic Totalisators Ltd., nor was the appellant required to join in any such sale. The only right reserved to the appellant was, in certain events, to choose one of the two methods of payment, and even that right was a restricted one, that is, it was a right only to choose the second method as against the first. It is significant that expenses incurred in effecting the sale were not a joint burden but, in accordance with the agreement, were borne entirely by Automatic Totalisators Ltd.,

(1) (1927) 46 C.L.R. 413.
(2) (1931) 46 C.L.R. 417, at pp. 452, 453.
(3) (1918) 25 C.L.R. 183.
(4) (1921) 29 C.L.R. 225.
(5) (1929) 42 C.L.R. 332.

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

and also that the payment of the £10,000 to the appellant was not a sharing by it in the purchase money, but was made under and in accordance with the agreement. Under the agreement the right of Automatic Totalisators Ltd. to assign the patents referred to therein was not any less than its right to grant licences in respect of such patents. The difference between an exclusive licence and an assignment of a patent is very small (*Rees Roturbo Development Syndicate* v. *Inland Revenue Commissioners* (1)). Licences granted pursuant to the agreement are disposals of patents rights in the ticket-issuers (*Collins* v. *Firth-Brearley Stainless Steel Syndicate* (2)). The appellant was not a party to the contract of sale, and did not at any time suggest that it should be joined as such, or that the contract was not a correct form of agreement. Its consent to the sale was not necessary, and, if given, was unnecessarily given. There is not any evidence that the appellant was ever communicated with concerning the sale. If it was so communicated with, it was within the power of the appellant to produce the evidence (*Davies & Fehon Ltd.* v. *Federal Commissioner of Taxation* [(1926), reported in *Ratcliffe and McGrath's Income Tax Decisions* (1891-1927), p. 83]; *Blatch* v. *Archer* (3)). The sale, which was made by Automatic Totalisators Ltd. in pursuance of the agreement of November 1922, has not been challenged by the appellant. The appellant company and Automatic Totalisators Ltd. were, and are, entirely separate entities. There is no such relation between those two companies as would justify the application of the doctrine enunciated in *Nathan* v. *Federal Commissioner of Taxation* (4). Sec. 16c of the *Income Tax Assessment Act* 1922-1931 authorizes the Commissioner to make a determination, subject to regulations, if any; in the absence of regulations the Commissioner is entitled to exercise his discretion (*Federal Commissioner of Taxation* v. *Lewis Berger & Sons (Australia) Ltd.* (5)). That section, however, does not apply, as the whole of the money received by the appellant was derived "directly or indirectly" from a source within Australia (*Lovell & Christmas Ltd.* v. *Commissioner of Taxes* (6); *Grainger & Son* v. *Gough* (7);

(1) (1928) 1 K.B. 506, at p. 515.
(2) (1925) 9 Tax Cas. 520.
(3) (1774) 1 Cowp. 63; 98 E.R. 969.
(4) (1918) 25 C.L.R. 183.
(5) (1927) 39 C.L.R. 468.
(6) (1908) A.C. 46.
(7) (1896) A.C. 325.

Nathan v. *Federal Commissioner of Taxation* (1); see also *Pondicherry Railway Co.* v. *Commissioner of Income Tax* (2)) and was "income" taxable under the *Income Tax Assessment Act*. A distinction should not be drawn as between the "business" and the "ordinary business" of the company; there may be a transaction by a company which is a mere realization (*Ducker* v. *Rees Roturbo Development Syndicate* (3)). Whether there is any distinction between a company and an individual in the matter of carrying on a business is shown in *Inland Revenue Commissioners* v. *Korean Syndicate* (4), *Inland Revenue Commissioners* v. *Westleigh Estates Co.* (5), and *South Behar Railway Co.* v. *Inland Revenue Commissioners* (6). *Collins* v. *Firth-Brearley Stainless Steel Syndicate* (7) is distinguishable, as there the memorandum and articles of association did not give the company a power to sell patents but only to turn them to account; also the cash received was not distributed in dividends as here but treated by the company as capital. This case is stronger than *Rees Roturbo Development Syndicate* v. *Inland Revenue Commissioners* (8): it was not an express object of that company, as here, to sell its patents; also the money received was not distributed as dividends but was treated as capital. An accretion of capital due to conversion or change of investment is taxable (*Westminster Bank* v. *Osler* (9); *Californian Copper Syndicate* v. *Harris* (10)). The patents should not be regarded as capital assets of the appellant but as stock-in-trade the disposal and turning to account of which was a part of the business of the appellant (*Commissioner of Taxes* v. *Melbourne Trust Ltd.* (11)). The mere fact that there were only a few transactions, or even that there was only one transaction, of this nature, is immaterial (*Inland Revenue Commissioners* v. *Westleigh Estates Co.* (5)).

E. M. Mitchell K.C., in reply. The agreement of November 1922 was not a trading agreement; it was merely a re-arrangement of

(1) (1918) 25 C.L.R., at p. 189.
(2) (1931) L.R. 58 Ind. App. 239.
(3) (1928) A.C. 132.
(4) (1921) 3 K.B. 258.
(5) (1924) 1 K.B. 390.
(6) (1925) A.C. 476
(7) (1925) 9 Tax Cas. 520.
(8) (1928) 1 K.B. 506; (1928) A.C. 132.
(9) (1933) A.C. 139.
(10) (1904) 5 Tax Cas. 159.
(11) (1914) A.C. 1001; 18 C.L.R. 413.

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

capital to permit of the admission of Setright. The transaction in question was not an operation in the business or scheme of profit-making, but was an operation calculated to bring that business to an end. Alternatively, the agreement was a "pooling" agreement between the three parties in their joint interests, and the disposition in 1928 was a disposition in the joint interests of all concerned. Under the agreement, the proprietary rights in the ticket-issuers remained with the appellant company; therefore, the profits from the sale in 1928 were not derived under the agreement but from the sale in England of the appellant's property. The agreement did not create any profits, but merely determined how profits should be distributed.

Cur. adv. vult.

NOV. 7.

The following written judgments were delivered:—

RICH J. This is a case stated by *Dixon* J. under sec. 51A of the *Income Tax Assessment Act* 1922-1930 after a hearing upon evidence. The question whether the appellant taxpayer was liable to State income tax in respect of the receipt of the same moneys as are involved in this case came up before us in an appeal by the Commissioner of Taxation for the State of New South Wales from a judgment of the Full Court of New South Wales, which held that such moneys were not chargeable with State income tax. The facts in the special case upon which the Full Court gave this decision were not very fully stated, and as the liability of the moneys to assessment depends upon the same considerations under both Federal and State statutes it seemed better for the appeal against the Federal assessment to be brought to a hearing and for the facts to be stated for the consideration of this Court before we disposed of the State appeal. In that appeal the parties had limited themselves to the question whether the profits under consideration arose from a source in New South Wales, and in the peculiar circumstances of the case, which are fully set out in the case stated by *Dixon* J., a decision of this question against the taxpayer seemed to make it easier for the taxpayer to contend that the profits were of a capital nature. This contention the taxpayer has now raised.

The taxpayer is a company incorporated to take over and use to advantage certain patent rights. The question whether the profits are capital or income depends upon the nature of the business the company carried on, which formed the source of the profits. The locality where the profits arose was determined by the place where the source was situated. The interdependence of the two questions results from the circumstance that if the activities in New South Wales are considered to be the source of the income it must be upon the ground that the profits are all attributable to the agreement made by the company in November 1922. If this is so, the question whether the company was carrying on or carrying out a profit-making scheme consisting of the acquisition and disposal of patent rights must be determined by what it did up to and before that date. The agreement of November 1922 is one of a very peculiar character. The decision of the Full Court depends almost entirely upon the effect ascribed to it. Their Honors took the view, to state it briefly, that it was a pooling arrangement by which the taxpayer contributed its patent rights to a pool into which the other two parties to the agreement contributed their patent rights for the purpose of disposal as a joint enterprise. As the patent rights were ultimately sold in Great Britain, and as this view of the agreement meant that the source of the profit from which the taxpayer derived its share was that sale, it followed that the profit arose from a source out of New South Wales and also of Australia. I have been unable to adopt this view of the agreement. I think its true effect, so far as material, was to confer an exclusive licence upon Automatic Totalisators Ltd. to exercise the taxpayer's inventions and patents and to give Automatic Totalisators power to sell the inventions and patents as their own, the consideration for these rights being a royalty and a payment of ten per cent of the proceeds of the sale. When the taxpayer company made the agreement it had in effect handed over its entire beneficial interest in, and power of disposal of, the patents. If, in common with the patents of Automatic Totalisators, they were advantageously sold, a consideration of ten per cent of the price would become payable to the taxpayer, but the sale would be quite independent of the taxpayer and would not be effected on its behalf as a principal. I recognize that the agreement is in many

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Rich J.

ways difficult to construe and that obscurities and inconsistencies abound in it, but I can find in it no trace of partnership, joint enterprise or agency. I think that in substance it invests Automatic Totalisators with complete control over the patents, exercisable on its own behalf as a principal, reserving only the considerations I have mentioned, which are, of course, contingent in their character. The profits were derived by the taxpayer from its enforceable right, conferred by the agreement in the events which happened, to a sum amounting to ten per cent of the purchase money. The source of this right was the making of the agreement which took place in New South Wales. For these reasons I think that as a matter of law the profits arose from a source in New South Wales.

The question whether the making of the agreement so far as it related to the disposal of the patent was a transaction directed to revenue or to capital has caused me much difficulty. I think that it is a necessary consequence of what I have already said that all the activities of Automatic Totalisators should, for the purpose of this question, be excluded from consideration. Under the definition of income now contained in the *Income Tax Assessment Act* 1922-1930 any profit is included which arises from the sale by any person of any property acquired by him for the purpose of profit-making by sale or from the carrying on or carrying out of any profit-making undertaking or scheme. The company was incorporated in 1917, and, before the agreement of November 1922, it had taken but few steps towards the realization of its patents. The nature of its business must, however, be gathered from its memorandum of association, from the character of the patents which it acquired, as well as from its subsequent acts. I think that the fact was that the company was incorporated to deal with the patents and the rights in relation to the invention and any future similar invention so as to make money out of them in any way which was considered most advantageous. In Australia it may have been thought wiser to exercise the patents; in some foreign countries there can be but little doubt that the company from the first contemplated selling its patent rights; in others it probably looked forward to making more complicated arrangements by which royalties or shares were obtained. But I do not think that the agreement of November 1922 can be considered

as a disposition or arrangement in relation to the company's fixed capital. It was an affair of circulating capital or income.

For these reasons I think the first question should be answered: No, the second: Yes, and the third: No. The fourth question is directed to the difficulties created by sec. 16c of the *Income Tax Assessment Act* 1922-1929, but, in the view I have taken, these do not arise and it is unnecessary to answer the question.

STARKE J. This is a case stated by my brother *Dixon* for the opinion of this Court. The facts are fully set out in the case. It appears that Julius and Wilkinson were the inventors of a ticket-printer machine for the automatic issue of tickets in connection with totalisator machines and various improvements thereon. The rights to these inventions, and letters patent obtained in respect thereof, both in the Commonwealth and in foreign countries, and the benefit of all agreements in respect thereof, were assigned or made over to the taxpayer, The Premier Automatic Ticket Issuers Ltd., which was incorporated under the *Companies Acts* of New South Wales. The objects of the company included the acquisition of these and other inventions and the right to use, exercise, develop, grant licences in respect of, or otherwise turn to account, sell or dispose of, any such patents, licences and concessions or all or any part of the property of the company, real or personal. One of the agreements the benefit of which passed under this assignment to the taxpayer was an agreement, dated 14th September 1917, which conferred upon Automatic Totalisators Ltd., a company incorporated in New South Wales, an exclusive licence to use and exercise in connection with totalisator machines in the Commonwealth and the Dominion of New Zealand, for the consideration and upon the terms stated in the agreement, the inventions of Julius and Wilkinson. Automatic Totalisators Ltd., it should be mentioned, had rights or letters patent in respect of inventions relating to totalisator machines. One Setright invented another ticket-printer machine for the automatic issue of tickets in connection with totalisator machines, and terms were negotiated with him for the acquisition of his invention and the rights in connection therewith. These terms are embodied in an agreement, dated 16th November 1922, between Automatic

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Starke J.

Totalisators Ltd., the taxpayer The Premier Automatic Ticket Issuers Ltd., and Setright. By it the parties agreed that all rights by letters patent or by any other means then held by them respectively as to the use, sale, manufacture or operation in any part of the world of ticket-issuing machines suitable for use in conjunction with totalisators should be governed by the conditions set forth in the agreement. Automatic Totalisators Ltd. were granted the sole and exclusive right to manufacture and sell all such ticket-issuing apparatus for which rights had been or might thereafter be secured by letters patent or any other means by the other parties to the agreement, and Automatic Totalisators were to pay the taxpayer a royalty of ten pounds for every machine manufactured and sold by it pursuant to the agreement. Setright agreed to transfer and assign to the taxpayer all patents then or thereafter to be held by him respecting ticket-issuers and all improvements therein, and the taxpayer to transfer to Setright thirty per cent of the total shares fully paid up of the taxpayer and to pay him thirty per cent of the total proceeds arising from the sale of ticket-issuer rights in any country. Important clauses of the agreement were as follows:— "5. In the event of Automatic Totalisators Limited disposing of the whole or part of their proprietary rights to the totalisator and/or ticket-issuers in any country Automatic Totalisators Limited shall make payment to The Premier Automatic Ticket Issuers Limited by one of the following methods. The said Premier Automatic Ticket Issuers Limited to have the right to choose the second-mentioned method of payment as against the first-mentioned: 1. Payment by Automatic Totalisators Limited to the Premier Automatic Ticket Issuers Limited of the sum of £10 . . . for each and every ticket-issuing machine manufactured or sold by or for the said Automatic Totalisators Limited. 2. Payment by Automatic Totalisators Limited to The Premier Automatic Ticket Issuers Limited of a sum equal to ten per cent of any cash consideration for the sale of totalisator and issuer rights in any country and a sum equal to five per cent of the total royalties received under the terms of such sale for a period of ten years dating from the receipt of such royalties from each individual installation. 6. In the event of Automatic Totalisators Limited disposing of rights as in the

preceding paragraph, Premier Automatic Ticket Issuers Limited and Henry Roy Setright agree to execute all necessary transfers or assignments of patents held by them to effectuate such sales."

Letters patent had been obtained or had been applied for in Great Britain in respect of ticket-printer machines, the inventions of Julius and Wilkinson and of Setright. In May 1928 Automatic Totalisators Ltd. agreed to sell and assign to Totalisators Ltd., a company incorporated under the English *Companies Acts*, the British letters patent for the inventions of Julius and Wilkinson and of Setright in respect of ticket-issuing machines, and the benefit of applications for letters patent in respect of such inventions and any improvements and further inventions in connection with totalisators. The purchase price was £100,000, and further sums equivalent to an amount calculated at the rate of one-eighth of one per cent of the total amount of money passing through any totalisator manufactured, sold or supplied under the letters patent or any improvements thereof or further inventions connected with the subject matter thereof. The purchase money was paid in England to Automatic Totalisators Ltd.

The taxpayer in its profit and loss account for the twelve months ending 30th June 1929 included as part of its receipts the sum of £10,000, "sale of English rights." This sum was paid or credited to it by Automatic Totalisators Ltd. as "a sum equal to ten per cent of any cash consideration for the sale of totalisator and issuer rights in any country" under the agreement of 16th November 1922. The Commissioner assessed the taxpayer to income tax in respect of this sum of £10,000 for the financial year 1929-1930.

The first question stated by my brother *Dixon* is: Am I at liberty upon the materials included in the special case to find that the sum of £10,000 is not (*a*) income of the taxpayer or (*b*) derived directly or indirectly from sources in Australia?

In my opinion, Question 1 (*a*) should be answered in the negative. The test is whether the amount in dispute "was a gain made in an operation of business in carrying out a scheme for profit-making" and "not merely a realization or change of investment" (*Ducker* v. *Rees Roturbo Development Syndicate* (1); *Commissioner of Taxes*

(1) (1928) A.C., at p. 140.

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Starke J.

v. *Melbourne Trust Ltd.* (1); *Commissioner of Taxes* v. *British Australian Wool Realization Association* (2); *Westminster Bank* v. *Osler* (3); *Ruhamah Property Co.* v. *Federal Commissioner of Taxation* (4)). The object of the taxpayer here was to exploit the inventions in its hands. It apparently did not itself work the inventions, though it manufactured electro-types in Sydney for supply to Automatic Totalisators Ltd. It granted a licence to Automatic Totalisators Ltd. to use and vend the inventions in the Commonwealth and New Zealand. It joined in forming or took shares in a company called Automatic Totalisators (France) Ltd., which installed totalisators and ticket machines in France. It appointed an agent and gave him authority to sell its patent rights outside the Commonwealth and New Zealand. The agreement of 16th November 1922 assumes an authority in Automatic Totalisators Ltd. to sell issuer rights for a cash consideration and thereby impliedly authorizes such a sale. The taxpayer received its share of the proceeds of sale, and credited the same to its trading or business operations account, that is, its profit and loss account. In so doing the taxpayer "may well be held bound by its own actions" (*Commissioner of Taxes* v. *Melbourne Trust Ltd.* (5)). Facts such as these preclude any other conclusion than that the sum of £10,000 was a gain made in an operation of business in carrying out a scheme of profit-making.

Question 1 (*b*) should also, I think, be answered in the negative. The agreement of 17th May 1928, under which purchase money amounting to £100,000 was paid to Automatic Totalisators Ltd., was a transaction entered into and carried out in England and in respect of patent rights granted or subsisting in England. It arose from business transacted and wholly carried out in England, and the purchase money paid under it was therefore not income derived directly or indirectly from a source in Australia (*Lovell & Christmas Ltd.* v. *Commissioner of Taxes* (6); *Studebaker Corporation of Australasia Ltd.* v. *Commissioner of Taxation* (*N.S.W.*) (7)). But was the sum of £10,000 paid to the taxpayer derived from this English

(1) (1914) A.C., at p. 1010.
(2) (1931) A.C. 224, at p. 231.
(3) (1933) A.C., at pp. 148, 149.
(4) (1928) 41 C.L.R., at p. 151.
(5) (1914) A.C. 1001.
(6) (1908) A.C. 46.
(7) (1921) 29 C.L.R. 225.

transaction, or was it derived from a transaction entered into in Australia and embodied in the agreement of 16th November 1922 ? That question depends upon the proper interpretation of that agreement. The parties undoubtedly associated themselves together for the exploitation of their various inventions and patent rights. Automatic Totalisators Ltd. had totalisator rights, whilst the taxpayer had ticket-issuer rights, which are of no practical use except in connection with totalisators. An exclusive licence was granted to Automatic Totalisators Ltd. to use and exercise the ticket-issuer rights, paying a royalty of £10 for every machine manufactured or sold by it. Clearly these royalty rights arise from the agreement, and from no other transaction. But clause 5 contemplates the event of a disposition of the whole or part of the proprietary rights to totalisator and/or ticket-issuers. One view is that the clause simply determines the proportion in which proceeds of sale shall be distributed, and provides for their distribution through Automatic Totalisators Ltd. But that interpretation does not fit the first method of payment, namely, payment by Automatic Totalisators Ltd. to the taxpayer of the sum of £10 for each and every ticket-issuing machine manufactured or sold by or for Automatic Totalisators Ltd. This sum is obviously connected with the royalty of £10 mentioned in clause 2, and it is an obligation which arises from the agreement and from no other transaction. The taxpayer has the right to choose the second method of payment, that is, payment by Automatic Totalisators Ltd. to it of a sum equal to ten per cent of any cash consideration for the sale of totalisator and issuer rights in any country, and a sum equal to five per cent of the total royalties received under the terms of sale for a period of ten years. But that choice can only arise, I apprehend, if there be a sale for a cash consideration and royalties. It is noticeable in both cases that the payment stipulated for is payment by Automatic Totalisators Ltd. Again, it is noticeable that the taxpayer is not entitled to ten per cent of the whole consideration for the sale, but only to ten per cent of the cash consideration. The totalisator rights were the property of Automatic Totalisators Ltd., and it had the sole and exclusive rights to manufacture and sell the ticket-issuing apparatus for use with totalisator machines. The clause, as it appears to me, treats

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Starke J.

that company, and not the taxpayer, as the owner and proprietor of the ticket-issuing rights as well as the owner and proprietor of the totalisator rights. It places both those classes of rights unreservedly in its hands for sale and disposition as an owner. But, under the same clause, Automatic Totalisators Ltd. covenants to pay the taxpayer ten per cent of any cash consideration for the sale of totalisator and issuer rights in any country. The right to that payment arises and is derived directly from that covenant, and from it alone. Consequently, in my opinion, the sum of £10,000 paid to the taxpayer does not arise from business transacted and carried out in England, but from an Australian transaction, and is therefore income derived from a source in Australia.

The second question stated in the case is: Is the Commissioner of Taxation entitled as a matter of law upon the materials included in the special case to a finding that the sum of £10,000 formed part of the income of the taxpayer derived directly or indirectly from sources in Australia? An affirmative answer should be given for the reasons already mentioned.

The third question stated in the case is: Is the taxpayer entitled as a matter of law upon the materials included in the special case to a finding that the sum of £10,000 (*a*) did not form part of the income of the taxpayer, or (*b*) was not derived directly or indirectly from sources in Australia? A negative answer should be given for the reasons already set out.

The fourth question stated in the case is: (*a*) On the materials included in the special case, ought I, as a matter of law, to find that the income is derived partly from sources outside Australia? A negative answer should be given. The income, for the reasons already set forth, was derived wholly from sources in Australia. (*b*) Does sec. 16c of the *Income Tax Assessment Act* 1922-1929 apply to the assessment in reference to the inclusion of any part of the said sum of £10,000? (*c*) If so, is the determination of the question what part of the income is derived from sources outside Australia the exclusive function of the Commissioner of Taxation? These questions—4 (*b*) and 4 (*c*)—become immaterial in the view I take of the case. But as the case states that the taxpayer did not in fact claim that the income was derived partly from sources outside

Australia, but wholly from sources outside Australia, the provisions of the section seem inapplicable, and in any case I should think that, as was conceded at the Bar, the determination of the Commissioner would be subject to review and appeal.

DIXON J. The facts, my statement of which is contained in the special case, raise the questions whether the sum obtained by the taxpayer in consequence of the transfer of its patents was capital or income, and whether it was derived from a source in Australia or a source in Great Britain. These questions are not as completely independent of one another as might be supposed. For, in the circumstances of the case, the conclusion that the source of the income is in Australia necessarily confines the activities producing the income within narrower limits not only of area but also of period and description. For this and other reasons, it was thought more satisfactory to decide the taxpayer's appeal against its Federal assessment to this Court before disposing of the appeal of the State Commissioner against the decision of the Supreme Court determining that the moneys in question are not taxable as income derived from sources in New South Wales. The ground of the decision of the Supreme Court is that the sum was not derived from a source in New South Wales. As the money was in fact paid to the taxpayer company in performance of a condition of the agreement of November, 1922, this conclusion necessarily involves a consideration of its provisions. *Street* C.J., who delivered the judgment of the Court, in describing its general character, said that what the parties to it had in contemplation was a pooling of their patent rights and an exploitation of them in combination both in Australia and in other parts of the world, a joint enterprise for the benefit of all parties to the agreement; that the dominant idea was the sale and use of ticket-issuing machines in conjunction with totalisators in the joint interest of all concerned. "The agreement made here by" the taxpayer company "gave it a right, no doubt, to share in the benefit of sales wherever made but as a hard practical matter of fact the income which it received, and which is under consideration, arose from business transacted by Automatic Totalisators

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Dixon J.

in England and wholly carried out there" (1). It cannot be denied that the sum of £100,000 paid for the patents, of which the sum of £10,000 paid to the taxpayer formed ten per cent, arose in the hands of Automatic Totalisators Ltd. from a source in Great Britain. The patents were assets situate in Great Britain (*English Scottish and Australian Bank Ltd.* v. *Inland Revenue Commissioners* (2)); the contract of sale was made there; the assignments were executed there, and the money was paid there. If, therefore, this transaction is to be considered as the source from which the taxpayer derived its ten per cent, the judgment of the Supreme Court would clearly be right. But the transaction was conducted by Automatic Totalisators Ltd., not by the taxpayer. Doubtless, part of the price of £100,000 paid in Great Britain was referable to the patent for the ticket-issuer invention, the beneficial title to which had been acquired by the taxpayer and, perhaps, ten per cent may have represented a proper apportionment. But the sum of £10,000, which the taxpayer received, cannot be considered as derived simply as the proceeds of this piece of British property. For it did not become entitled to the £10,000 simply because of the sale. Its title to ten per cent of the price obtained in Great Britain by Automatic Totalisators Ltd. arose from the agreement of November 1922. The facts are that the taxpayer did nothing outside New South Wales towards bringing about the transaction, which was wholly carried out by Automatic Totalisators Ltd. Thus, except in so far as Automatic Totalisators Ltd. should be considered as acting for or on behalf of the taxpayer, nothing actively done by it abroad constitutes the source of the income now excluded from the assessment as extra-territorial. At bottom, the decision of the Supreme Court treats the agreement of November 1922 as conferring upon the taxpayer a right to share in the distribution of moneys earned by the activities of Automatic Totalisators Ltd. It denies to the agreement the character of a transaction by which the taxpayer earned profit afterwards to be ascertained in amount, and ascribes to it the character of a contractual disposal in favour of the taxpayer of future profit earned by Automatic Totalisators Ltd.

(1) (1932) 33 S.R. (N.S.W.) 107, at p. 116.

(2) (1932) A.C. 238.

The provisions of the agreement of November 1922 fall naturally into four main divisions of subject matter :—

(1) The earlier clauses confer upon Automatic Totalisators Ltd. an exclusive licence in respect of the invention of ticket-issuing apparatus limited to use with totalisator machines. The licence extended to the manufacture, sale, use, and operation of such machines; the consideration for the licence was a royalty of £10 per machine. Provision is then made for the extension of the protection to other countries and also for the inclusion of subsequent improvements.

(2) A special set of clauses deals with the rights in New Zealand in the ticket-issuing invention. These begin with the statement that the provisions of the agreement relating to the payment of royalties by Automatic Totalisators Ltd. shall apply to all countries alike. They then proceed to except New Zealand and to confer upon the taxpayer an election to manufacture, sell, operate and use the apparatus in New Zealand at a royalty of £10 per machine payable to Automatic Totalisators Ltd., subject to an option in Automatic Totalisators Ltd. to purchase the New Zealand rights for a consideration in shares in any company it should form for the purpose of manufacturing totalisators in New Zealand.

(3) A third subject dealt with by the agreement is the acquisition by the taxpayer from the inventor, Setright, of all patents present and future relating to the ticket-issuing invention and all improvements therein.

(4) The fourth description of clauses is that relating to the disposal of the patents themselves. The leading provision is that " in the event of Automatic Totalisators Limited disposing of the whole or part of their proprietary rights to the totalisator and/or ticket-issuers in any country Automatic Totalisators Limited shall make payment to the " taxpayer in one of two methods then set out, the choice of which resided with the taxpayer. The second of these methods was in fact chosen and consisted in payment " of a sum equal to ten per cent of any cash consideration for the sale of totalisator and issuer rights in any country and a sum equal to five per cent of the total royalties received under the terms of such sale for a period of ten years." The next clause requires, " in the event of Automatic

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Dixon J.

Totalisators Ltd. disposing of rights as in the preceding paragraph," that the taxpayer and the inventor shall " execute all necessary transfers or assignments of patents held by them to effectuate such sales." Finally, the agreement provides that, " subject to any contracts or agreements in connection therewith as may have theretofore been lawfully entered into by Automatic Totalisators Limited with any other party or parties," the rights in the ticket-issuing invention should " revert to and become vested in " the taxpayer, if Automatic Totalisators Ltd. should discard the use of the apparatus and use another device, or if that company should be wound up and cease to carry on business, except on a reconstruction or sale. There is much obscurity in many of the provisions of this agreement besides those actually quoted, and both because this is not a litigation between parties to the agreement and because the meaning of some of the expressions and provisions might appear clearer if more of the circumstances were before us to which the instrument was intended to apply, it is undesirable to express any opinion upon the agreement which is not strictly necessary for the determination of this appeal. But it appears reasonably clear that by it the taxpayer conferred upon Automatic Totalisators Ltd. the complete and exclusive enjoyment of the right to exercise all patents for the invention. In my opinion, it confers also a power of disposition of the patents themselves. The clauses are clumsily and illogically expressed, and it is impossible to be confident of their meaning, but I think that when the undertaking to execute transfers of patents is considered with the text of the preceding clause, which fixes the consideration in the event of a disposition, it sufficiently appears that a right to dispose of the patents was intended. Both the right to exercise and the right to dispose of the patents are made liable to determination under the condition subsequent contained in the final provision, but, until the occurrence of this condition, they gave both enjoyment in use of the proprietary right and power of alienation. For the purposes of this case, it may be assumed that by reason of the nature of the terms which govern price the taxpayer might have made any particular sale impossible if it chose. But this does not mean that any action on its part out of the Commonwealth was required to effect the sale, nor that the sale was negotiated

or made by Automatic Totalisators Ltd. for it or on its behalf. In exchange for these rights it stipulated for a defined consideration. Subject to the election given it, the description of the consideration was finally fixed. The pecuniary sum payable depended upon events, but the mode of calculation was defined. The agreement does not make Automatic Totalisators Ltd. the taxpayer's agent. Its liability to the taxpayer is for a consideration in the nature of a price for advantages secured to it by the agreement. There is nothing in the facts contained in the case stated which appears to me to suggest that anything was done by, or, unless under the agreement, on behalf of, the taxpayer in negotiation or carrying out the transaction in Great Britain. In these circumstances, the only source whence the taxpayer derived the sum of £10,000 whether as income, or as a capital profit, must be taken to be the agreement under which it became payable to it, and that was negotiated and made in New South Wales. I am of opinion that the sum was derived from a source within Australia.

The question then arises whether the sum so derived should be considered as income or capital. By Act No. 50 of 1930, par. (*ba*) was inserted in the statutory definition of " income " as from 1st July 1922. This paragraph defines income to include any profit arising from the sale by any person of any property acquired by him for the purpose of profit-making by sale or from the carrying on or carrying out of any profit-making undertaking or scheme.

The adoption of this provision probably has no more effect than to give legislative authority to the tests propounded and applied in decisions of this Court. In *Ruhamah Property Co.* v. *Federal Commissioner of Taxation* (1), in the judgment of *Knox* C.J., *Gavan Duffy*, *Powers* and *Starke* JJ., the rule was restated : " The principle of law is that profits derived directly or indirectly from sources within Australia in carrying on or carrying out any scheme of profit-making are assessable to income tax, whilst proceeds of a mere realization or change of investment or from an enhancement of capital are not income nor assessable to income tax (*Commissioner of Taxes* v. *Melbourne Trust Ltd.* (2) ; *Ducker* v. *Rees Roturbo*

(1) (1928) 41 C.L.R., at pp. 151, 152.
(2) (1914) A.C. 1001 ; 18 C.L.R. 413.

H. C. OF A. 1933. PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION. Dixon J.

Development Syndicate (1); *Commissioner of Taxation (W.A.)* v. *Newman* (2); *Blockey* v. *Federal Commissioner of Taxation* (3)).” Their Honors added: “In our opinion the authorities show that the objects and powers of the company contained in its memorandum and articles of association are not decisive of the question whether the sale was an operation of business in carrying out a scheme of profit-making, but that a consideration of all the matters advanced by the company was relevant to a determination of that question (*Hudson's Bay Co.* v. *Stevens* (4); *Tebrau (Johore) Rubber Syndicate* v. *Farmer* (5); *C. H. Rand* v. *Alberni Land Co.* (6); *Alabama Coal, &c., Co.* v. *Mylam* (7))” (8).

The criterion, which the Legislature has now adopted and established, was formulated by the Courts in the absence of any statutory direction upon the way in which capital profits may be distinguished from income profits. So far as it lacks precision or is uncertain in its application, the cause is to be found in the powerlessness of the Courts to do more than state a wide general proposition and to apply it as each case arose. The statement of the proposition was not a definition, but rather an explanation of principle. No doubt, as the language of the statute it must receive a more literal application. It is not easy to say whether the expression “profit-making by sale” refers to a sole purpose, or a dominant or main purpose, or includes any one of a number of purposes. The alternative “carrying on or carrying out” appears to cover, on the one hand, the habitual pursuit of a course of conduct, and, on the other, the carrying into execution of a plan or venture which does not involve repetition or system (cp. *Federal Commissioner of Taxation* v. *Clarke* (9)).

In the present case, the taxpayer was incorporated for the primary purpose of acquiring and turning to profit a ticket-issuing invention or inventions suitable for use with totalisators. The objects contained in the memorandum of association consisted of the familiar collection of seemingly unrelated powers. But the actual purpose with which the company was incorporated was, doubtless,

(1) (1928) A.C. 132.
(2) (1921) 29 C.L.R. 484.
(3) (1923) 31 C.L.R. 503.
(4) (1909) 5 Tax Cas. 424; 101 L.T. 96 (C.A.).
(5) (1910) 5 Tax Cas. 658.
(6) (1920) 7 Tax Cas. 629.
(7) (1926) 11 Tax Cas. 232.
(8) (1928) 41 C.L.R., at pp. 151, 152.
(9) (1927) 40 C.L.R. 246.

that expressed in the first two objects, namely, to acquire patents, and in particular a patent for ticket-issuers, to that end to adopt an agreement already in draft, and to use, exercise, develop, grant licences in respect of, or otherwise turn to account, sell, or dispose of, any such patents. The taxpayer company, in pursuance of these objects entered into an agreement, which conferred upon it patent rights in the ticket-issuing invention and any improvements. The invention so acquired was saddled with contractual obligations which the vendors had undertaken immediately before the incorporation of the taxpayer. These included an exclusive licence in favour of Automatic Totalisators Ltd. at a royalty for the duration of the patent for the Commonwealth and New Zealand. From its incorporation, in 1917, until the making of the agreement of 16th November 1922, the taxpayer made no attempt to dispose of the patent rights, or any of them, whether by assignment, licence, or otherwise, except that in 1919 it appointed a director agent for the sale of all patent rights outside the Commonwealth and New Zealand. It derived royalties from Automatic Totalisators Ltd., it obtained assignments of the improvements for ticket-issuers for win and place bets invented by the vendors, and it negotiated the agreement with Setright and Automatic Totalisators Ltd. in the circumstances set out in par. 12 of the special case. Except for the manufacture and supply of an attachment used in ticket-issuing machines, these appear to be the only active transactions of the taxpayer until the making of the agreement, which, in my opinion, is the source of the profit in question. In *Collins* v. *Firth-Brearley Stainless Steel Syndicate* (1), *Atkin* L.J., as he then was, upheld the view that profit arising in that case from the disposal of patents was capital and not income because he thought the Commissioners "took the right view in this case, and came to the conclusion that this company was formed for the purpose of acquiring these patent rights as its one capital asset and that it was to make money out of the use of this one capital asset, but that it was not to make money by retailing them or peddling them, but to treat the one asset that it acquired as its capital and to use it accordingly, just

(1) (1925) 9 Tax Cas., at p. 574; 133 L.T., at pp. 622, 623.

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Dixon J.

as if it had acquired a business with goodwill, in which case it was trade, but the business and the goodwill which it had purchased would be its capital out of which it made its profits." This statement expresses, in effect, the final question in the present case. I have come to the conclusion that the question must be answered against the taxpayer. In acquiring the patent rights to the ticket-issuer invention and improvements, the taxpayer appears to me to have embarked upon a venture which had in view any profitable dealing with the property. The primary thing was perfecting the monopoly in such places as seemed desirable and the preservation of the interest by obtaining patent rights in improvements and competitive inventions. But, so far as enjoying or obtaining advantages from those rights, the taxpayer was empowered, and I think prepared, to exercise, licence others to exercise, or dispose of, the patent rights in any country, subject to the existing licence in Australia and New Zealand, as opportunity offered. Because the utility of the invention was so much involved with totalisators, separate or independent opportunities of advantage were less likely to arise. But, nevertheless, the plan or purpose which up to November 1922 the taxpayer was pursuing, however inactive may have been that pursuit, includes the disposal of its interests piecemeal, or in any other fashion. It made the agreement of 16th November 1922 in fulfilment of the plan or end it was independently pursuing. Thereafter, its chief purpose was to await and distribute the profits which might arise under that agreement. But, in making the agreement, the taxpayer was, I think, carrying into execution one of the many alternatives of its scheme of profit-making. The patents were not to be its goodwill out of which it was to make its profits, but the taxpayer was to make money by retailing the patents if it could. The fact that in the end it entered into an anomalous agreement by which it surrendered to another company its right of retailing the patents may obscure, but, in my opinion, cannot alter the result.

For these reasons I think the first question in the special case should be answered: No; the second: Yes; and the third: No. I think these answers deprive the fourth question of relevancy.

EVATT J. The case stated for the opinion of the Full Court raises in a more elaborate form and, between the appellant and the Federal Commissioner of Taxation, the same questions as arose in the appeal of *Commissioner of Taxation (N.S.W.)* v. *Premier Automatic Ticket Issuers Ltd.* (1), judgment in which is also being delivered this day.

The first question, whether the sum of £10,000 should be treated as part of the taxpayer's income, could not arise in such appeal because of the express admission made before the Court of Review that the sum was income of the taxpayer's business.

The additional facts before us in this case may be stated as follows. In October, 1917, the appellant company was incorporated in New South Wales. Its first object, as stated in cl. 3 (*a*) of the memorandum of association, was to acquire patent rights and, in particular, to acquire a certain patent for an invention in relation to ticket-printers or ticket-issuers, and to carry into effect the agreement specified in the articles of association. The second object was

> "to use exercise develop grant licences in respect of or otherwise turn to account sell or dispose of any such patents licences concessions and the like and information aforesaid."

In the year 1921 one Setright invented another ticket-issuing machine. It was considered by those in control of the totalisator company and the appellant company that Setright's invention might prove to be valuable, and the agreement of November 16th, 1922, was then entered into.

Under the agreement referred to in cl. 3 (*a*) of the memorandum of association, the totalisator company used ticket-issuing devices, the patents of all of which belonged to or were made over to the appellant. The appellant also manufactured electro-types for the totalisator company for use in connection with the ticket-issuing machines, and the income of the appellant consisted of royalties from the totalisator company together with the proceeds of the sale to it of the electro-types.

The only step taken by the taxpayer in connection with the exploitation of its patent rights prior to the agreement of 1922 was a decision made in May 1919, appointing a certain person as agent

(1) *Post*, p. 304.

H. C. OF A. 1933.

PREMIER AUTOMATIC TICKET ISSUERS LTD. v. FEDERAL COMMISSIONER OF TAXATION.

Evatt J.

for the sale of its patent rights for all territories outside the Commonwealth of Australia and New Zealand. Later on, in January 1927, the totalisator company caused its representative to visit France where he supervised the installation of a totalisator machine. From France he was invited by the English Jockey Club to visit England with a view to the installation of totalisators on English racecourses. After a long course of negotiation during which a bill authorizing the use of totalisators was successfully promoted before the Parliament at Westminster, the two contracts of sale referred to in my other opinion were entered into on May 17th and 18th, 1928. In these negotiations in England the appellant took no part whatever.

It also appears that, up to the year ending on June 30th, 1922, the totalisator company had installed and supervised totalisators in various places, and had paid royalties to the appellant in respect of the ticket-issuers used in these machines.

In my opinion, these additional facts reinforce the inference that the sum of £10,000 was part of the income of the taxpayer during the year in question. Throughout its existence the taxpayer was engaged in the business of "turning over," "turning to account," or "exploiting," its patent rights, whichever phrase may be preferred: the legal result is to make the £10,000 part of its business income. The agreement of 1922 did not result in the termination of the company's business though it had the effect, elsewhere pointed out, of restricting the company's business activities to the State of New South Wales. No doubt the disposal in one transaction of world rights in a patent tends to resemble what is called "an affair of capital"; but the question whether the receipts flowing from the transaction are capital or income necessarily depends upon the business which the owner of the patent rights is pursuing, and upon all the circumstances of the particular case. In the present case it is clear that, in making the agreement of November 1922, as in the business it conducted both before and after that date, including the year of income, the appellant was pursuing the object described in cl. 3 (*b*) of its memorandum of association, and was turning to account its patents as part of its profit-making business. Therefore the £10,000 receipt is to be regarded as income derived from such business.

The second part of the case raises the question with which I have

dealt with in *Commissioner of Taxation (N.S.W.)* v. *Premier Automatic Ticket Issuers Ltd.* (1). In my opinion the whole of the sum of £10,000 was derived from sources in Australia, those sources consisting of the appellant's business activities in New South Wales, including the due execution by it, in the income year, of the agreement of November 1922.

I answer the questions:—1 (*a*): No. 1 (*b*): No. 2: Yes. 3: No. 4 (*a*): No. The other questions, it is unnecessary to answer.

McTIERNAN J. I agree that the sum of £10,000 which was received by the taxpayer company entirely flowed from the agreement of November 1922, and that this was its only source. This sum was therefore derived from a source within Australia. I also agree that the sum of £10,000 was income. I have nothing to add to the reasons which have been given for these conclusions.

The first, second and third questions should be answered respectively: No; Yes and No. It is unnecessary to answer the fourth question.

Questions answered as follows:—1: *No.* 2: *Yes.* 3: *No.* 4: *Unnecessary to answer. Costs, costs in the appeal.*

Solicitors for the appellant, *Braund & Watt.*

Solicitor for the respondent, *W. H. Sharwood*, Commonwealth Crown Solicitor.

J. B.

(1) *Post*, p. 304.