[HIGH COURT OF AUSTRALIA.]

EVANS . . . . . APPELLANT;

AND

THE DEPUTY FEDERAL COMMISSIONER OF TAXATION FOR SOUTH AUSTRALIA } RESPONDENT.

ON APPEAL FROM THE SUPREME COURT OF SOUTH AUSTRALIA.

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ADELAIDE, *Sept.* 11, 12, 13.

MELBOURNE, 1936, *Feb.* 13.

Rich, Starke Dixon and Evatt JJ.

*Income Tax (Cth.)—Assessment—Shareholder in company—Profit derived by company from any source—Profit arising from sale of assets not acquired for purpose of resale at profit—Mining company—Acquisition of leases by nominees—Subsidiary companies trustees for parent company—Resale by parent company of property beneficially owned by it—Purpose of acquisition—Enlargement of capital by sale of capital assets or obtaining detachable profits by buying and selling assets—Sale of assets in consideration of shares in other companies—Distribution of those shares—Capital or income—Distribution of surplus assets—Appreciation in value of assets—Income Tax Assessment Act* 1922-1930 (*No.* 37 *of* 1922—*No.* 60 *of* 1930), *sec.* 16 (*b*) (i) (1), (2).

The G. company was registered in 1926 as a mining company. It acquired certain leases in the upper portion of the Bulolo River in New Guinea. Its nominees acquired, in the lower part of the river, leases which were later transferred to subsidiary companies with a small share capital all of which was held by the G. company. It also established an air service which was begun for its own purposes but grew into a separate business. It did considerable work on the upper leases, but its capital was at no time sufficient to enable it to work the lower leases, and reports of its directors spoke of exploitation of these leases by other companies. The upper leases and the airways undertaking had admittedly not been acquired for the purpose of resale. In November 1927 the G. company disposed of the airways undertaking to the A. company in consideration of 10,000 paid up £1 shares in that company. In June 1929 the G. company sold the upper leases to the N. company and

received as part of the consideration for the sale 90,000 paid up £1 shares in that company. In September 1929 the 90,000 shares in the N. company and the 10,000 shares in the A. company were, pursuant to a power contained in the articles of association of the G. company, distributed among the members of that company. One of such members was E. At the time of this distribution the market value of the N. shares was 5s. 6d. per share and of the A. shares £2 per share. In June 1930 the G. company disposed of its interest in the lower leases, and in November 1930 made a cash distribution of 10s. per share among its members out of portion of the consideration received. E. participated in this distribution also. After each of the two distributions the G. company had sufficient assets left to answer its issued share capital. The Deputy Federal Commissioner of Taxation included in E.'s assessable income (at their respective market values) the shares in the N. and A. companies distributed to him and the 10s. per share paid to him in cash.

*Held*:

(1) That the shares in the N. company contained no profit on the sale of the upper leases, that there was no reason to suggest any marked drop in values between the acquisition and the distribution of those shares by the G. company, that they represented surplus assets not required to make good its issued share capital and that the whole amount of 5s. 6d. per share should be included in E.'s assessable income.

(2) By *Rich*, *Dixon* and *Evatt* JJ. (*Starke* J. dissenting) that profit consisting in an accretion in value of the shares in the A. company fell within the charging part of sec. 16 (*b*) (i) (1) of the *Income Tax Assessment Act* 1922-1930 and that the shares should be included in E.'s assessable income except to the extent to which the actual value of the shares in the A. company exceeded their face value at the time of their allotment to the G. company.

(3) By *Rich*, *Dixon* and *Evatt* JJ. (*Starke* J. dissenting), that the object which actuated the G. company in taking up the lower leases was not the making of profit by turning them over at an increased value, but to make money for its shareholders by working or exploiting the leases themselves or transferring them for shares to some other company possessing more capital which could do so, that the leases were assets which were not acquired for the purpose of resale and at a profit and that the 10s. per share cash distribution should be excluded from E.'s assessable income.

*Per Rich*, *Dixon* and *Evatt* JJ.: The "purpose" referred to in the final proviso to sec. 16 (*b*) (i) (2) is the dominant purpose actuating the acquisition of assets, and the proviso is concerned with the difference between the enlargement of capital by sale of capital assets and obtaining detachable capital by buying and selling assets.

Decision of the Supreme Court of South Australia (*Murray* C.J.): *Evans* v. *Deputy Federal Commissioner of Taxation*, (1934) S.A.S.R. 457, varied.

APPEAL from the Supreme Court of South Australia.

The appellant Arthur Ernest Herbert Evans, a resident in Australia, was a shareholder in Guinea Gold No Liability (hereinafter called

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" the company "). In assessing him for income tax for the financial years 1930-1931 and 1931-1932 the Deputy Commissioner included in the assessable income two amounts which represented distributions by the company. The first distribution, on 16th September 1929, was a distribution in specie of 10,000 paid up shares of £1 each in Guinea Airways Ltd. and 90,000 paid up shares of £1 each in New Guinea Goldfields Ltd. The distribution was made in purported pursuance of an article of association which empowered the directors to declare a dividend to be paid to members in proportion to the number and nominal amount of their shares, and to pay dividends, wholly or in part, by the distribution of specific assets, and, in particular, of paid up shares of any other company. The shares were included in the appellant's assessable income at their market value, namely, £2 each for the Guinea Airways shares and 5s. 6d. each for the New Guinea Goldfields shares. The second distribution was of 10s. per share paid in cash on 14th August 1930. The appellant received his proportionate share in each distribution.

The company was incorporated in South Australia on 11th May 1926. Its objects included the acquisition of mines and mining interests in New Guinea and elsewhere, the conduct of mining operations, the formation and flotation of companies to develop its mining interests, the sale and distribution of its property and the division of any of its property in specie among its members. It was formed as a result of communications from a prospector who was operating on the Bulolo River in New Guinea and who had reported that there were, along the river, large areas from which a high return of gold could be obtained. The natural features of the country divided the areas into two parts. Below a gorge the river ran over flats which were considered most suitable for dredging. None of this area had been pegged out. Above the gorge deposits existed which were available for sluicing. Part of this area had been applied for and leases had been granted, one at least of which had been acquired by the prospector. In a memorandum which, before the formation of the company, was circulated among the persons invited to join it, a distinction was drawn between the two fields. The upper section was described as a matter of simple surface working

then being exploited by sluicing, and the lower as one of straightforward dredging. It was explained that the lower section was greater in extent, and that, if it commended itself to experts, the prospector was ready to offer as an adjunct to the lower section the lease he had already acquired in the upper section. A working option for six months from the registration of the company was given over the lease in the upper section. The promoters of the company sent a mining engineer to report upon the field, and on the day of the company's registration, a radio was sent to the prospector requesting him to peg out immediately the best of the lower land " on behalf of the interested ", pending the arrival of the expert. The latter was supplied with powers of attorney to enable him to take up leases in the names of the company's nominees. At the first meeting of the company it was decided to send four more men to assist the expert. The prospector, who had meanwhile acquired another lease on the upper section, was invited to take charge of the party on its arrival in the capacity of field superintendent. He obtained rights in the lower field. Six leases were pegged out, and on 2nd June 1926 applications were lodged in the names of the nominees. The expert reported that it was desirable to obtain further leases lower down and, before his return, informed the company by radio that he had arranged to acquire five such leases which, he advised, could be worked by sluicing. He also advised the company to acquire the upper leases pursuant to its option. As a result the company acquired the leases in the upper section and its nominees obtained eleven leases in the lower section.

The original capital of the company was £2,000 divided into 2,000 shares of £1 each. By September 1926 this was increased to £50,000 divided into 50,000 shares of £1 each. It issued to its vendors 12,513 shares at par, to subscribers who paid £1 in cash 19,700 shares, and to other subscribers who paid a premium of £1 per share, 17,787 shares. Consequently cash subscriptions amounted to £55,274. The company never had sufficient capital to enable it to work the lower sections.

The articles of association included the following :—

" 38. The Directors may at any time and from time to time declare a dividend to be paid to the members in proportion to the number

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and nominal amount of their shares and any such dividend may be paid wholly or in part by the distribution of specific assets and in particular of paid up shares debentures or debenture stock of any other company and for that purpose the Directors may settle any question which may arise in regard to the distribution whether relating to fractional interests or otherwise as they shall think expedient and may fix the value for distribution of any specific assets and may determine that cash payments shall be made to any members upon the footing of the value so fixed.

76. No dividend shall be payable except out of the profits arising from the business of the company."

At a meeting of the company on 25th August 1926 the members were informed that the first thing to be done was to work the upper leases, and in a report of the directors of 10th November 1926 it was announced that it was intended to undertake the flotation of the lower section when complete reports were received. In December 1926 the field superintendent urged a thorough examination of the lower leases and warned the company against too speedy a development. Statements by the directors indicated that they desired to exploit the whole field but contemplated the formation of subsidiary companies to undertake different parts of it. They had been advised that one company could not hold all the leases applied for, and consequently they adopted the course of forming three subsidiary companies—New Guinea Gold North, New Guinea Gold Central and New Guinea Gold South—among which the lower leases were to be distributed. These companies were incorporated on 23rd March 1927, each with a nominal amount of capital which was held entirely by the parent company. It was some time before the leases were transferred by the nominees to these new companies.

In the meantime in a memorandum relating to the issue of further capital, shareholders were told that shares in the company would carry rights to participate in the flotation of further companies to handle the lower areas which were then being sampled and surveyed. In a report of 27th May 1927 the directors said that the three companies had been registered " with a view to acquire and work these areas," and that, when the engineer's reports were made, " flotation will be proceeded with immediately if justified." In

July 1927 the directors stated that shares in the company "carried rights to participate in the share issue of the three new companies, Guinea Gold North, Central and South which hold the lower leases." Much was done by the company, particularly with the upper leases. Grave transport difficulties were largely overcome by the establishment of an air service. This service was begun for the purposes of the company, but it grew into a separate business and became the means of communication with the locality for the service of all.

In April 1927 negotiations with the company were opened by persons who desired to float a company for the active working of part of the lower area. Ultimately, in December 1927, an option was granted to Territory Investment Company Ltd. to incorporate a company for the purpose of acquiring and working some of the lower leases. The option was not exercised, but the work done in the course of the transaction established that the lower leases must be worked by dredging and not by sluicing.

Meanwhile the company had been advised that it might be beyond its powers to conduct the air service, and it accordingly registered Guinea Airways Limited to take over this service. The consideration for the transfer of the air undertaking to Guinea Airways Ltd. was 10,000 fully paid up £1 shares in the capital of the new company. This transfer took place in November 1927, and it was these shares which the company distributed to its members on 16th September 1929.

When the option granted to Territory Investment Company Ltd. fell through, the directors of the company decided to seek for further capital in Great Britain. Before this intention could be carried into effect Placer Development Company Ltd. applied for an option over the lower leases, and on 27th April 1928 a working option was given for their sale for a consideration of £50,000 in cash and 10 per cent. of the shares of the issued capital of the company or companies which should be formed to work the leases. The option extended until 30th June 1930.

About the same time negotiations were opened in New Guinea for an option over the upper leases. As a result an option was granted to New Guinea Goldfields Ltd. over the upper leases in consideration of £2,000 cash and 90,000 paid up shares of £1 in that company.

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The option was exercised on 30th June 1929, and the 90,000 shares were distributed by Guinea Gold No Liability to its members on 16th September 1929, together with the shares in Guinea Airways Ltd.

On 30th June 1930 the Placer Development Company Ltd. exercised its option over the lower leases, and out of the amount paid on account of the consideration the company on 14th August 1931 made its distribution of 10s. a share among its members.

The balance-sheet of the company disclosed as at 28th February 1930 a general reserve of £52,906 12s. 6d. The details of the reserve account were recorded in the books of the company as follows :—

" Reserve Account for the year ended 28th February 1930.

DR.

| | | |
|---|---|---|
| To Distribution to Shareholders as at 16th September, 1929, of Shares in— | | |
| (*a*) New Guinea Goldfields Ltd. in proportion of 9 shares for every 5 shares held in Guinea Gold No-Liability .. .. .. .. | | £90,000 0 0 |
| (*b*) Guinea Airways Ltd. in proportion of 1 share for every 5 shares held in Guinea Gold No-Liability (at market value £2 per share) .. | | 20,000 0 0 |
| ,, Balance Carried Forward .. .. .. .. | | 52,906 12 6 |
| | | £162,906 12 6 |

CR.

| | | |
|---|---|---|
| By Balance 1/3/29 brought forward (Premiums on Share Issues) .. .. .. .. .. .. | | £17,787 0 0 |
| ,, Surplus Received on Sale of Leases, &c., to New Guinea Goldfields Ltd. .. .. .. .. .. | | 41,500 0 2 |
| ,, Surplus Transferred on Revaluation of Shares in other Companies as under :— | | |
| Guinea Airways Ltd. (written up to market value at date of distribution) .. .. .. | £10,100 0 0 | |
| Guinea Gold South N.L. and Guinea Gold Central N.L. (written up to actual net value receivable from Placer Development Ltd.) | 93,519 12 4 | |
| | | 103,619 12 4 |
| | | £162,906 12 6" |

Other material facts appear from the judgments hereunder.

The appellant appealed to the Supreme Court of South Australia against the assessment. The Deputy Commissioner did not deny that the shares distributed to the appellant were the profits of the

sale of assets not acquired for the purpose of resale. He did, however, dispute that the shares when distributed represented nothing but profits from that resale and, accordingly, he allowed only a partial immunity from taxation. In the case of the distribution in cash made in 1930, the Commissioner contended that the company had acquired the lower leases for the purposes of resale at a profit. In the Supreme Court of South Australia *Murray* C.J. upheld both contentions of the Commissioner and dismissed the appeal. From this decision the appellant now appealed to the High Court.

*Ligertwood* K.C. (with him *Phillips*), for the appellant. The distribution of the shares in New Guinea Goldfields Ltd. and in Guinea Airways Ltd. was not by way of dividend, but was in fact a distribution of capital assets of the company and was intended so to be. When the company distributed the shares in the two companies, all that it had left to answer the shareholders, capital was £15, representing the moneys paid for the shares in the subsidiary companies. The company, therefore, in distributing the shares, distributed assets which in part at least represented its shareholders' capital. This was a proceeding which could have been restrained by any shareholder or creditor (*Foster* v. *New Trinidad Lake Asphalt Co. Ltd.* (1)). Assuming that the 90,000 shares in New Guinea Goldfields Ltd. are to be taken at the face value (and the case proceeded on this assumption) the sale of the upper leases represented a capital profit of £41,500, which would have been available for dividend, but it was a profit arising from the sale of assets not acquired for the purpose of resale at a profit and was therefore exempt from taxation. The balance of £48,500 was not taxable because it was not a profit, but was the original investment of shareholders' capital. This is "the substance of the matter," which is what the Court is required to look at. Questions of the liability of the subject to taxation are not to be affected by the actual proceedings which have taken place in drawing up a balance sheet or profit and loss account (See per *Pollock* M.R. in *Sterling Trust Ltd.* v. *Commissioners of Inland Revenue* (2)). The reserve account should not be allowed to affect the substance of the matter, because it did not come into existence until the 28th February

(1) (1901) 1 Ch. 208.

(2) (1925) 12 Tax Cas. 868, at p. 882.

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1930. Assuming that the reserve account must be taken into consideration, it does not disclose " profit " of the company available for dividend except as to the item of £41,500 surplus on the sale of the upper leases. The item of £17,787 premiums on share issues, although available for dividend, was not a profit of the company (*Commissioner of Income Tax (Q.)* v. *Bank of New South Wales* (1) ). The writing up of the Guinea Airways shares was not a profit of the company, because it was not realized. The company did not derive the profit from these shares, because they were handed over in specie. The persons, if any, who derived the profit were the shareholders who received them. The writing up of the Guinea Gold South and Guinea Gold Central shares was not a profit, because it was not realized. It was merely an estimate of what might possibly be received in the future from Placer Development Company Ltd. Assuming that the reserve account does show " profits " in the sense of an excess of capital assets over liabilities, they are capital profits and are more correctly described as surplus assets than as " profits derived by the company," and as surplus assets they are entirely outside the scope of the *Income Tax Assessment Act* which deals with income, not with capital. Where, therefore, the Act uses the word " profit," the word means " revenue profit," not capital profit (*McLachlan* v. *Commissioner of Taxes* (2) ). The scheme of sec. 16 (*b*) is to tax the revenue profits of companies in the hands of the shareholders. It does not contemplate the taxing of capital profits of the company in the hands of the shareholders. The proviso to sec. 16 (*b*) (i) merely contains a definition of what is a revenue profit. That the word " profit " as used in sec. 16 (*b*) (i) means a " revenue " profit as opposed to the appreciation in value of a capital asset, is emphasized by the history of the legislation (*Webb* v. *Federal Commissioner of Taxation* (3); *West Derby Union* v. *Metropolitan Life Assurance Society* (4) ). Assuming, however, that a " capital profit " is intended to be taxed under sec. 16 (*b*), the dividend must be paid out of a profit derived by the company. A profit is not derived merely by the writing up of the

(1) (1913) 16 C.L.R. 504.
(2) (1912) S.A.L.R. 138.
(3) (1922) 30 C.L.R. 450, at pp. 472, 473.
(4) (1897) A.C. 647, at p. 656.

value of assets. Such a writing up only amounts to an estimate of what is likely to be received on a realization of the assets, and no profit is derived until some realization is made (*Rex* v. *Anderson Logging Co.* (1) ). In such a case the profit is made or " arises " not from the writing up, but from the realization. Assuming a revaluation of the assets of the company, the company, by distributing the shares in the two other companies, treated the Airway assets and the upper leases as surplus assets which had cost the company nothing, and treated the whole of the proceeds of those assets as profits arising from the sale of those assets. The whole of such proceeds, being profits and arising from the assets not acquired for the purpose of resale at a profit, was exempt from taxation. This is the proper inference to be drawn from the distribution in specie of the actual consideration received on the sale of the two assets. The only alternative is to say that in making the distributions the company was parting with its share capital, in which case the distributions would be exempt because they were not made out of profit.

The lower leases were not acquired for the purpose of resale at a profit. The purpose for which the leases were acquired was to work them (*Tebrau (Johore) Rubber Syndicate Ltd.* v. *Farmer* (2) ).

*Mayo* K.C. (with him *Brebner*), for the respondent. By sec. 39 the assessment is prima facie correct. All moneys and moneys' worth paid by a company to a shareholder in the capacity of shareholder are " dividends, bonuses or profits " within sec. 16 (*b*) (i) unless the moneys are a return of share capital or represent surplus assets paid to shareholders in the winding up. " Out of profit " in pl. (1) of sec. 16 (*b*) (i) does no more than limit the place whence the profit is derived. If not part of the share capital, every payment to shareholders may be expected to be out of profit in some form. " Out of profit " is co-extensive with the company's power to credit, pay or distribute dividends, bonuses or profits. " Derived " is not to limit the scope of " profit " except as to locality, viz., the " source." Any way in which a usable profit appears will be a method of derivation (*Commissioners of Taxation* v. *Kirk* (3) ; *Federal Commissioner*

(1) (1926) A.C. 140.
(2) (1910) 5 Tax Cas. 658.
(3) (1900) A.C. 588, at p. 592.

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*of Taxation* v. *Clarke* (1); *Dickson* v. *Commissioner of Taxation (N.S.W.)* (2); *Mount Morgan Gold Mining Co. Ltd.* v. *Commissioner of Income Tax (Q.)* (3)). There is express indication that "dividends, bonuses or profits" in sec. 16 (*b*) (i) are intended to include accretions in respect of fixed assets, as otherwise the third proviso would not be necessary. As the "revaluation" appears in sub-sec. (ii) (1), but does not appear in the third proviso to sub-sec. (i), it follows by contrast that a dividend, bonus or profit credited, paid or distributed out of profit disclosed by a revaluation is intended by the Legislature to be taxable although the asset revalued may be a fixed asset (*South Brisbane Gas and Light Co. Ltd.* v. *Hughes* (4); *McNeil* v. *Federal Commissioner of Taxation* (5); *Federal Commissioner of Taxation* v. *Dixon* (6)). Of all "profits," therefore, only those (if any) which are shown by the appellant to be within the third proviso to sec. 16 (*b*) (i) will be non-assessable. The "purpose" of not being acquired for resale at a profit must be established by the appellant (*Isles* v. *Federal Commissioner of Taxation* (7)). If the evidence shows that the purpose was either to resell or work as subsequent inquiries or tests might favour, the purpose of reselling is present and is not negatived. To be within the proviso that purpose must be rejected at the time of acquisition. 90,000 shares in New Guinea Goldfields Ltd. and 10,000 shares in Guinea Airways Ltd. were distributed at the direction of the directors of the company under article 38. As a consequence these must be deemed to be "profits arising from the business of the company" mentioned in article 76, unless the appellant has proved the contrary. The reserve account shows what those profits are. The total profit could be distributed in cash or in specie. In either case the result is the same. That the profits are in part distributed by shares associated with the earning of part of the profit is an accident. The shares represent money's worth instead of money. As to the Guinea Airways shares, the profit shown in the reserve account is not on the sale to Guinea Airways but the increase

(1) (1927) 40 C.L.R. 246, at pp. 260, 261.
(2) (1925) 36 C.L.R. 489, at p. 501.
(3) (1923) 33 C.L.R. 76.
(4) (1917) 23 C.L.R. 396.
(5) (1922) R. & McG. 35.
(6) (1929) R. & McG. (1928-1930) 81.
(7) (1926) R. & McG. 76.

in value of the shares after being held nearly two years before distribution. The increase of £10,100 is undoubted, and it was distributed to the shareholders. The profit cannot therefore be within the proviso to sec. 16 (*b*) (i). The interest of the company in the lower leases was a share interest. These shares had value. That value should be and was brought into the company's accounts. The increase in value was not "profit on sale" at all; therefore it could not be "profit on sale of an asset not acquired for resale at a profit." The increase is a profit unprotected by the proviso to sec. 16 (*b*) (i) (*Federal Commissioner of Taxation* v. *Standard Trust Ltd.* (1) ). Alternatively the company was the beneficial owner of the leases. In that case the leases (not the shares) should have been shown as assets, and the reserve account must be corrected accordingly, the leases being substituted for shares and written up to £93,519. If the distribution be wholly or in part in respect of that profit, it will not be within the proviso to sec. 16 (*b*) (i) so far as it comprises such profit. As a second alternative the profit of £93,519 may be treated as a profit on a sale then pending, but which the company treated as sufficiently certain to warrant a distribution. If the distribution was in part in respect of a sale present or future, the shareholders will be taxed for the year they receive the dividend. Even if the distribution was not warranted, the justification by relation to a sale which actually took place later will bind the company and shareholders. In that case the question whether the profit of £93,519 is taxable will depend on whether the lower leases are shown by the appellant not to have been acquired for resale at a profit. Original advice was that the flats were a dredging proposition. At no time did the company have funds sufficient to dredge. The appellant has not proved that the company did not acquire the leases for the purpose of resale at a profit.

*Ligertwood* K.C., in reply.

*Cur. adv. vult.*

(1) (1933) 49 C.L.R. 609.

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The following written judgments were delivered :—

RICH, DIXON AND EVATT JJ. In assessing the appellant for income tax for the financial years ending 30th June 1931 and 1932 upon his income derived during the respective preceding years, the Commissioner included in the assessable income amounts representing distributions by a company called " Guinea Gold No Liability " in which the appellant was a shareholder.

On 16th September 1929 the directors of that company made a distribution in specie of shares which it had acquired in two other companies. In doing so the directors assumed to act under an article of association adopted for the purpose which empowered them to declare a dividend to be paid to members in proportion to the number and nominal amount of their shares, and to pay dividends, wholly or in part, by the distribution of specific assets, and, in particular, of paid up shares of any other company. The distribution thus made among the shareholders consisted of 10,000 paid up shares of £1 in Guinea Airways Limited which the company had acquired in November 1927, and of 90,000 paid up shares of £1 in New Guinea Goldfields Ltd. which the company had acquired on or after 30th June 1929. For every five shares in Guinea Gold No Liability the shareholders received one share in Guinea Airways Ltd and five shares in New Guinea Goldfields Ltd. The shares were not included in the appellant's assessable income at their face value, but at their market value, which, in the case of Guinea Airways Ltd. was £2 each, and in that of New Guinea Goldfields Ltd. was 5s. 6d. each.

The second of the two distributions with which this appeal is concerned was made by Guinea Gold No Liability on 14th August 1930. It consisted of an amount of 10s. a share paid in cash.

The appellant resides in Australia, and, in including these distributions in his assessable income, the Commissioner relied upon sec. 16 (*b*) (i) (1) of the *Income Tax Assessment Act* 1922-1932. The material portions of the provision require that the assessable income of a shareholder of a company shall include dividends, bonuses or profits paid or distributed by the company to a shareholder, who is a resident, out of profit derived by the company from any source. But a proviso enacts that, where the company distributes any of

the profits arising from the sale of assets which were not acquired for the purpose of resale at a profit, the profits so distributed shall not be assessable income to the shareholder. The appellant claims the protection of the proviso, which, he says, protects both distributions entirely. The shares of which the first distribution consisted were allotted to the Guinea Gold No Liability as part of the consideration for the sale by it of assets which, with a negligible exception, admittedly had not been acquired by it for resale at a profit. The shares in Guinea Airways Limited formed part of the consideration for the sale to that company of an air service established by Guinea Gold No Liability. The shares in New Guinea Goldfields Limited formed part of the consideration for the sale to that company of gold mining leases acquired by Guinea Gold No Liability to work by sluicing.

While the Commissioner does not deny that the shares are the proceeds of the sale of assets not acquired for the purpose of resale, he does deny that the shares when distributed represent nothing but profits from that resale, and, accordingly, he has allowed only a partial immunity as the result of the application of the proviso. To this the appellant answers that, in so far as the shares do not represent profit upon the resale of the assets, they do not represent profit at all, or, at any rate, they do not represent profit " derived " by the company. In other words, he says that the distribution ought not to be included in the assessable income of a shareholder under sec. 16 (*b*) (i), because no profit derived by the company entered into the composition of the amount distributed in the form of shares, except profit arising from the sale of assets which were not acquired for resale at a profit.

In the case of the distribution made in cash in the following year, the ground upon which the Commissioner denies the applicability of the proviso is different. The money distributed arose from the sale of some other leases held by the company. But these leases, the Commissioner says, the company did acquire for the purpose of resale at a profit.

The appellant appealed against the assessments to the Supreme Court of South Australia. His appeals were heard by *Murray* C.J. who found in favour of the Commissioner. From his judgment

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dismissing the appeals the present appeal is brought to this Court.

Guinea Gold No Liability was incorporated in South Australia as a mining company on 11th May 1926. It was formed as a result of communications received from a prospector who was carrying on his operations on the Bulolo River in the Mandated Territory of New Guinea. He had sent reports to his attorney under power that there existed, along the river, large areas from which a high return of gold could be obtained by sluicing or dredging. The natural features of the country divided the areas into two parts. Below a gorge the river ran through flats which were considered most suitable for dredging. None of this area had been pegged out. Above the gorge deposits existed which in fact were not suitable for dredging, but were valuable for sluicing. Part of this area had been applied for and leases had been granted, one at least of which the prospector had acquired. In a memorandum which, before the formation of the company, was circulated among those who were invited to join it, the distinction between the two fields was drawn. The upper section was described as a matter of simple surface working then being exploited by sluicing, and the lower as one of straightforward dredging. The greater extent of the latter was explained, and the announcement was made that, if it commended itself to the experts, the prospector was ready to offer, as an adjunct to the lower section, the lease he had already acquired in the upper section. A working option for six months from the registration of the company was given by the attorney under power over the lease in the upper section. The promoters of the company decided to send a mining engineer to New Guinea to report upon the field, and, in the meantime on the day of registration a radio was sent to the prospector urging him to peg out immediately the best of the lower alluvial land " on behalf of the interested " pending the arrival of the expert. The latter left a week later armed with numerous powers of attorney to enable him to take up leases in the names of the company's nominees.

At the first meeting of the company, it was decided to send after him four men to assist him. The prospector was invited to take charge of the party when it arrived on the field in the capacity of " field superintendent " at a high salary. He, in the meantime,

acquired another lease on the upper section. It was in the neighbourhood of his earlier lease, but situated on a tributary of the Bulolo River. He set about obtaining rights in the lower field. Six leases were pegged out, and on 23rd June 1926 applications were lodged in the name of the nominees. The expert reported that it was thought desirable to obtain further leases lower down, and, before his return, he informed the company by radio that he had made arrangements to acquire five such leases six miles below those already applied for. He reported also that these lower leases could be worked by sluicing. He advised the company to acquire the upper leases pursuant to its option. In the result the company did acquire the leases in the upper section of the field, and its nominees applied for and obtained eleven leases in the lower section. The six leases first applied for were granted to the applicants on 23rd November 1926. Three more, which had been applied for on 8th September, were granted on 4th December 1926 and the remaining two, which were applied for on 13th December 1926, were granted on 21st February 1927. It is these eleven leases which have been held to fall outside the proviso to sec. 16 (*b*) (i) on the ground that in their acquisition the purpose of resale at a profit was not absent. It is the leases in the upper section of the field which admittedly were not acquired for the purpose of resale at a profit.

It appears that, at a meeting of the company on 25th August 1926, the members were informed that the first thing to be done was to work the upper leases, and that, in a report of the directors of 10th November 1926, it was announced that it was intended to undertake the flotation of the lower section when complete reports were received.

In the following month a long report upon the field was received from the original prospector, now the company's field superintendent. He urged a thorough examination of the lower leases and warned the company against too speedy a development. The directors decided to raise some more capital. Their statements appear to show that they desired to exploit the whole field, but contemplated the formation of subsidiary companies to undertake different parts of it. They had been advised by their solicitor in New Guinea that one company could not hold all the leases applied for, and that of

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the various courses open, that to be preferred was to form three more companies among which the lower leases would be distributed. This course they eventually adopted. On 23rd March 1927 they incorporated no liability companies, called respectively New Guinea Gold North, Central and South. But it was some time before the leases were transferred by the nominees to these companies. Each of them issued a nominal amount of capital only, viz., five shares, and these the parent company held. In the meantime, in a memorandum relating to the issue of further capital, the shareholders were told that shares in the company would carry rights to participate in the flotation of further companies to handle the lower areas, which were then being sampled and surveyed. In their report of 27th May 1927 the directors said that the three new companies had been registered "with a view to acquire and work these areas," and that when the engineer's reports were made "flotation will be proceeded with immediately if justified." In July 1927, when more capital was to be issued, the directors stated that shares in the company "carried rights to participate in the share issue of the three new companies, Guinea Gold North, Central and South, which hold the lower leases."

Much was done by the company particularly with the upper leases, and the very great difficulty of transport was largely overcome by the company's establishing an air service. The air service, although begun for the purposes of the company, grew into a separate business of the company. It naturally became the means of communication with the locality for the service of all.

In April 1927 negotiations with the company were opened up by a group of strangers who desired to float a company for the active working of part of the lower area. The proposal was that the company should transfer some of its lower leases for a consideration in cash and shares. The negotiations went on for some time, and, in December 1927, a three months option was granted. But, before the three months were up, the holders of the option decided not to exercise it. The work done, however, in the course of the transaction established that the lower leases must be worked by dredging and not, like the upper, by sluicing.

In the meantime, on 7th November 1927, the company had registered the company called "Guinea Airways Ltd.," to take over the air service. It did so because it was advised that it might be considered beyond the powers of a no liability mining company to conduct an air service. The consideration for the transfer of the air undertaking to Guinea Airways Limited was 10,000 fully paid up £1 shares of its capital. It was these shares which Guinea Gold No Liability distributed to its members on 16th September 1929.

When the option granted over part of the lower area was declined, the directors of Guinea Gold No Liability decided to seek further capital in Great Britain. But, before this resolve could be carried into effect, a Canadian company applied for an option over all the lower leases. After some negotiations, on 27th April 1928 a working option was given for their sale for a consideration of £50,000 in cash, and, in shares, ten per cent of the issued capital of the company or companies which should be formed to work the leases. The currency of the option was long. It extended until 30th June 1930.

Almost concurrently with the negotiations in Australia for this option, negotiations were opened in New Guinea for an option over the upper leases. The proposal came from an independent undertaking. It resulted in the grant of an option to New Guinea Goldfields Ltd. over all the upper leases in consideration of £2,000 cash and 90,000 paid up shares of £1 in that company. The option was exercised on 30th June 1929. The 90,000 shares were distributed by Guinea Gold No Liability to its members on 16th September 1929 together with the shares in Guinea Airways Ltd. The option over the lower leases was exercised by the Canadian company on 30th June 1930, and, out of the amount paid on account of the consideration, the distribution on 14th August 1931 of 10s. a share among its members was made by Guinea Gold No Liability.

It is convenient to deal first with the question whether this distribution is liable to inclusion in the shareholder's assessable income. It depends upon the question whether the money distributed arose from the resale of assets which were not acquired for the purpose of resale at a profit.

The first objection made by the Commissioner to the application of the proviso is that the lower leases were never acquired by the

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company at all; that they were not its assets, but at best the assets of the three subsidiary companies and that it could not resell them. This point is not dealt with in the judgment under appeal, and no evidence appears to have been directed to it at the hearing. It may be inferred that the leases were ultimately transferred by the nominees to the North, South, and Central companies. But no evidence was given of the date or circumstances, and the fact itself was not the subject of distinct proof. It does appear, however, that none of the three companies gave any consideration for the transfer. On the evidence, the position appears to be that the original grantees of the leases were trustees for Guinea Gold No Liability, that by its direction they transferred them to its subsidiary companies which gave no consideration for them either in the form of share capital or otherwise, and that then Guinea Gold No Liability sold the leases, and obtained and distributed the consideration which in no way passed through the subsidiary companies, although, presumably, the latter executed formal transfers of the leases. It is true that the burden of proof is upon the taxpayer. But, on these bare facts, the inference is that the equitable property in the leases of Guinea Gold No Liability was not extinguished by the transfer of the legal interest to the three subsidiary companies.

No question is raised as to the legality of the trust in favour of the parent company upon which the nominees held the leases. The result is that, in so far as the proviso may be considered to require that the moneys shall arise from the resale by a company of property beneficially owned by it, that requirement is satisfied.

The next question is whether the leases were originally acquired not for the purposes of resale at a profit. The learned Chief Justice was of opinion that it had not been established that they were acquired not for such a purpose. His view was much influenced by the fact that the company's capital was quite insufficient for it to hope to work the lower leases, that it never increased its capital to an amount suggesting that it expected to work them, and that the reports of the directors spoke of exploitation by other companies. There can be no doubt that from the beginning the possibility, perhaps probability, of the company promoting another company to take over the leases and work them was kept in view by the

directors. For a time they looked to the three subsidiary companies as the probable instruments for the purpose of raising capital and working them. But at the time when the leases were applied for and up to the time when they were granted to the nominees, the directors did not propose that the profit which the company was seeking should be gained upon a transaction by way of sale. No doubt to transfer the assets to another company for shares is a sale. To that extent the purpose of sale was not absent. But the proviso defines the purpose which it excludes, not as one of resale simply, but as resale at a profit. It is concerned with the well known difference between enlargement of capital by sale of capital assets and obtaining detachable profit by buying and selling assets. The purpose of which it speaks is the dominant purpose actuating the acquisition of the assets—the use to which they are to be put. The object which actuated Guinea Gold No Liability in taking up the leases was not the making of a profit by turning them over at an increased value, whether expressed in money, or in shares, or in securities. Its object was to make money for its shareholders by the working or exploitation of the mining leases. The exploitation might require the formation of a larger company, including many additional shareholders who would, perhaps, subscribe more capital than Guinea Gold No Liability or its shareholders could. But the transaction contemplated as possible at the beginning was no more than a transformation of the leases into shares which, either in its hands or those of its shareholders, would obtain their value through the actual or anticipated recovery of gold from the leases and consequent payment of dividends. From this view it follows that, prima facie, the distribution of 10s. a share on 14th August 1930 obtained the protection of the proviso and did not form part of the assessable income of the shareholder.

The only outstanding question possibly affecting its prima facie immunity is whether it should be treated as composed in part of some other element than the profit made upon the resale of the lower leases. That profit was quite sufficient to cover the amount distributed, and the suggestion that the 10s. a share should be treated as including some extraneous element arises from a mistaken attempt to proportion the profit shown upon an erroneous account

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made up by the company. The account is sufficiently discussed in the succeeding part of this judgment in dealing with the shares in New Guinea Goldfields Ltd. and in Guinea Airways Ltd. distributed on 16th September 1929, and the matter is not worth pursuing in relation to the dividend of 10s.

The question whether the shares in New Guinea Goldfields Ltd. and in Guinea Airways Ltd. should be included in the shareholder's assessable income depends upon the extent to which those shares represent profits arising from the sale, in the one case, of the upper leases, and, in the other case, of the air service. In an account made up by the company after the event, the shares were shown as of their face value. Upon this basis the profit from the resale of the leases was shown as £41,500 0s. 2d., the difference between £90,000 and £48,499 19s. 10d., the amount expended in connexion with the leases. As the whole £90,000 was shown in the account as distributed in shares, it was made to appear that a distribution had been made, not only of the apparent profit of the transaction, but also of something which must, unless the distribution was made in violation of the company's articles, represent profit from some other source. The account showed a profit much more than enough for the purpose, but a great part of it was attributable to the inclusion in the account of a large surplus arising from the writing up of the value of the lower leases, the sale of which, although not concluded, was confidently expected. Problems thus arose, the account being adopted as the basis of assessment, as to the manner of ascertaining how much of the amount contained in the shares distributed represented profit attributable to the sale of the leases. The same problem affected the Guinea Airways Ltd. shares which were put down in the account at a revaluation of £2 a share. The Commissioner's solution was to proportion the total profit disclosed by the account and allow only 25.22 per cent of the value as exempt.

It is unnecessary to enter into the details of these questions, because they do not really arise. The company's account is clearly wrong in putting down the shares in New Guinea Goldfields Ltd. at their face value, and they ought not to be treated as of that value for the purpose of applying the proviso to sec. 16 (*b*) (i). There

is an evident incongruity in treating the same asset as equivalent to 5s. 6d. in the hands of the shareholder to whom it is distributed and £1 in the hands of the company which distributes it. The distribution closely followed the receipt by the company of the shares, and there is no reason to suppose that there was any marked drop in values. It may safely be inferred that the money's worth of the 90,000 shares did not equal £48,499 19s. 10d., the amount expended by the company in connexion with the leases. That amount represents nearly double the value (5s. 6d.) assigned to the shares at the time of distribution. It follows that there was no net profit on the resale of the leases. It was contended for the taxpayer that the proviso was satisfied if profits arose, that is, were realized by the company, out of the sale of an asset not acquired for resale, although the profits were earned otherwise than by the acquisition and resale of the asset itself. This is not the true meaning of the proviso, which is concerned with capital net profits of a particular description. Accordingly, the distribution of the shares in New Guinea Goldfields Ltd. is not exempt under the proviso.

The contention of the appellant that, upon such a footing as this, the distribution would not come within the charging portion of sec. 16 (*b*) (i) (1) is erroneous. In the first place, the fact that the shares contain no profit on the sale of the leases does not mean that they represent capital and not profit of the company. Actually they represented surplus assets, that is, assets not required to make good issued share capital. This appears from the last preceding balance-sheet. In the second place, sec. 16 (*b*) (i) (1) brings into charge all dividends and distributions out of profit, whatever be the nature of the profit. The word " derived " does not connote that the profit must be a realized profit. It is enough at least if it is an ascertained profit, ascertained by a proper account. Under the articles, the 5s. 6d. contained in the share could not lawfully be distributed, except as a dividend satisfied by specific assets, and the dividend must be out of profits. The meaning of profits in sec. 16 (*b*) (i) (1) is no narrower, and the state of the company's affairs, as disclosed by its balance-sheet, permitted such a dividend. It follows that the whole amount of the 5s. 6d. per share should be included in the appellant's assessable income.

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The question whether any profit arose from the sale of the air service for 10,000 paid up shares of £1 each is more difficult. The face value of the shares represented the capital expenditure of the company in relation to the service and, unless the value contained in the shares exceeded their face value, the transaction produced no profit. When, nearly two years later, the shares were distributed, they admittedly possessed a face value of £2 each. Probably much of this value existed in the shares at the time of acquisition. But it does not appear upon the evidence whether any part arose from appreciation in the interval. Profit, consisting in such an appreciation, would, for the reasons already given, fall within the charging part of sec. 16 (*b*) (i) (1) and would not be protected by the proviso. The parties, however, do not seem to have directed any evidence to the matter, no doubt because the Commissioner had adopted the account made up by the company as the basis of the assessment, and it thus became the focus of the controversy between the parties. But apparently it is conceded that, in a proper account of the net profit gained upon the disposal of the air service, the expenditure would be about equal to the face value of the shares forming the consideration. It follows that to whatever extent the actual value contained in the shares at that time exceeded their face value, the shares represented profit upon the sale of the air undertaking.

It appears from the previous balance-sheet of Guinea Gold No Liability that it was in a position, apart from the revaluation of the lower leases, to make the distribution of 16th September 1929 out of surplus assets, leaving more than enough to answer its issued capital. Thus it was open to the company to distribute the net profit upon the transaction, consisting of the establishment and the subsequent sale of the air undertaking. This profit was actually contained in the shares distributed. By handing over in specie the assets containing the profit, the source of the distribution is identified. Thus, to whatever extent the actual value of the shares in Guinea Airways Ltd. exceeded their face value at the time of their allotment or so soon thereafter as their face value was established, to that extent their value should not be included in the shareholder's assessable income. But, because on the evidence it is impossible to ascertain the amount of the excess value, there

is no course open except to set aside the assessment so that it may be made afresh.

The appeals should be allowed with costs.

The amended assessment for the financial year ending 30th June 1931 should be set aside.

The amended assessment for the financial year ending 30th June 1932 should be reduced by excluding from the assessable income the sum of £222, being the dividend of £300, less £78 thereof already allowed by the amendment of the assessment. The assessment should be remitted to the Commissioner to give effect to the reduction.

In the result the taxpayer's appeal from the assessment has succeeded in part and failed in part. But the success of his appeal has been so great that he should have his costs of the proceedings. It does not appear that any substantial costs are exclusively referable to issues upon which the taxpayer failed.

The Commissioner should pay the costs of the appeals to the Supreme Court.

STARKE J. The *Income Tax Assessment Act* 1922-1930 exempts from income tax dividends, bonuses or profits or the face value of bonus shares distributed by a company among its members or shareholders except as provided under sec. 16 of the Act (sec. 14 (1) (*m*) ). Sec. 16 provides that the assessable income of any person shall include, in the case of a member, shareholder, depositor or debenture-holder of a company . . . dividends, bonuses or profits . . . credited paid or distributed by the company to a member or shareholder who is a resident—out of profit derived by the company from any source . . . Provided . . . that where the company distributes any of the profits arising from the sale . . . of assets which were not acquired for the purpose of resale at a profit, the profits so distributed shall not be assessable income to the member or shareholder.

Guinea Gold No Liability was incorporated in South Australia. Its objects included the acquisition of mines and mining interests in New Guinea and elsewhere ; the conduct of mining operations ; the formation and floating of companies to develop its mining interests ; the sale and disposition of its property ; and the division

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of any of its property in specie amongst its members. The original capital of the company was £2,000, divided into 2,000 shares of £1 each, but this, by September 1926, was increased to £50,000, divided into 50,000 shares of £1 each. It issued to its vendors 12,513 shares at par; to subscribers who paid £1 per share in cash, 19,700 shares; and to other subscribers who paid a premium of £1 per share, 17,787 shares. The cash subscriptions therefore amounted to £55,274. The company acquired certain properties on the Bulolo Creek in New Guinea, above a rocky gorge, which have been referred to as the upper leases. Mining operations were carried on by the company upon these properties, which had been acquired for that purpose. They were worked as sluicing claims, and about £48,000 was spent upon them. About June 1929 the company disposed of these properties to a company called New Guinea Goldfields Ltd. for £2,000 in cash and 90,000 shares in that company. The shares were worth about 5s. 6d. each. Guinea Gold No Liability also established an air service in connection with its mining operations; it expended about £10,100 upon aeroplanes, plant, and accessories. The aeroplanes and plant were acquired for the use of the company, and not for the purpose of resale at a profit. A company called Guinea Airways Ltd. was formed, which about the year 1927 took over the service and plant, giving as a consideration therefor 10,100 shares paid up to £1. Mining properties were taken up for or on behalf of Guinea Gold No Liability on the Bulolo Creek below the rocky gorge, and they were known as the lower leases. It was thought at one time that the leases might be worked as a sluicing proposition, but they turned out to be a dredging proposition. The company had not the capital to work them, and at an early stage gave an option to the Territory Investment Company Ltd. for three months of incorporating a company to acquire and work the leases. But the Territory Company was unable to float such a company, and the option fell through. About June of 1930 these leases were disposed of to the Placer Development Company Ltd. for £50,000 in cash and a share consideration. The sum of £30,000 was paid in cash, and the balance was deferred, by consent.

The learned Chief Justice of the Supreme Court of South Australia found that these lower leases were acquired for the purpose of resale

at a profit: "So far (from) the evidence showing that these properties were acquired for the purpose of being worked by Guinea Gold No Liability, and not for the purpose of resale at a profit, it seems to me clear that the company never had any hope of being able to work them, and that its intention was to dispose of them to other companies for a cash or share consideration as soon as its title to them was assured." This finding has been challenged, and the burden of displacing it is upon the appellant. The substantial and dominant purpose, if not the sole purpose, of the acquisition must be "resale at a profit." The chairman of directors of Guinea Gold No Liability deposed that when the company acquired the leases it did not acquire them for the purpose of reselling at a profit—that was never considered; the leases were acquired for the purpose of getting gold out of the ground. But the company's capital was quite inadequate for the purpose, and from the beginning the necessity for the formation of some incorporated body for the purpose of acquiring and working the leases was recognised, and the general terms of its flotation, and of the consideration in cash and shares that should go to Guinea Gold No Liability was discussed and settled. Ultimately the company did dispose of the leases to the Placer Development Company for the consideration already mentioned. The subsequent acts of the company are relevant evidence of its intention or purpose in acquiring the leases. In my opinion, the finding of the Chief Justice was open upon the evidence, and I am by no means satisfied that he came to an erroneous conclusion. It is not the function of an appeal Court to substitute its conclusions of fact for those of a trial Judge whose duty it is to determine the facts, unless satisfied that he is wrong (*Powell* v. *Streatham Manor Nursing Home* (1); *Grant* v. *Australian Knitting Mills Ltd.*, in Privy Council (2)).

On 16th September 1929 Guinea Gold No Liability distributed amongst its shareholders the 90,000 shares received from the New Guinea Goldfields Ltd., and 10,000 of the shares received from Guinea Airways Ltd. in the proportion of nine of the former and one of the latter for every five shares held in Guinea Gold No Liability. In August of 1930 Guinea Gold No Liability distributed amongst

(1) (1935) A.C. 243.

(2) (1936) A.C. 85; (1935) 54 C.L.R. 49.

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its shareholders 10s. per share in cash, portion of the money received from the Placer Development Company. The balance-sheet of Guinea Gold No Liability disclosed as at 28th February 1930 a general reserve of £52,906 12s. 6d., and the details of the reserve account are recorded in the books of the company—how it was formed and how dealt with. The following is a copy :—

Reserve Account for the year ended 28th February 1930.

DEBIT.

| | | | |
|---|---|---|---|
| To Distribution to Shareholders as at 16th September, 1929, of Shares in— | | | |
| (*a*) New Guinea Goldfields Ltd. in proportion of 9 shares for every 5 shares held in Guinea Gold No-Liability .. .. .. .. | £90,000 | 0 | 0 |
| (*b*) Guinea Airways Ltd. in proportion of 1 share for every 5 shares held in Guinea Gold No-Liability (at market value £2 per share) .. | 20,000 | 0 | 0 |
| „ Balance Carried Forward .. .. .. .. | 52,906 | 12 | 6 |
| | £162,906 | 12 | 6 |

CREDIT.

| | | | |
|---|---|---|---|
| By Balance 1/3/29 brought forward (Premiums on Share Issues) .. .. .. .. .. .. | £17,787 | 0 | 0 |
| „ Surplus Received on Sale of Leases, &c., to New Guinea Goldfields Ltd. .. .. .. .. .. | 41,500 | 0 | 2 |
| „ Surplus Transferred on Revaluation of Shares in other Companies as under :— | | | |
| Guinea Airways Ltd. (written up to market value at date of distribution) .. .. .. | 10,100 | 0 | 0 |
| Guinea Gold South N.L. and Guinea Gold Central N.L. (written up to actual net value receivable from Placer Development Ltd.) .. .. | 93,519 | 12 | 4 |
| | £162,906 | 12 | 6 |

The figures may be convenient for the purposes of accountancy, but the value of the shares in New Guinea Goldfields Ltd. was not £90,000, but 5s. 6d. each, or £24,750. And the sum of £41,500 among the credit entries represents the difference between £90,000 and the sum of £48,500 expended by the company on the leases. The expenditure exceeded the value of the shares received by £23,750, and there was no profit on the sale of the leases. But there was nothing to prevent the company distributing surplus profit, and this, it is plain on the figures of the balance-sheet and the reserve account, is what the company purported to distribute. Again, the transaction with the Guinea Airways Ltd. showed, on its face, no

profit, for Guinea Gold No Liability had expended £10,100 upon the service and received in return 10,100 shares paid up to £1. But it seems that in February 1930 the market value of the shares was £2 each. The credit item £93,519 is a valuation of the interests of the Guinea Gold Co. in the leases transferred to the Placer Development Co. Ltd. The appellant, as a shareholder in Guinea Gold No Liability benefited in these distributions to the extent of 1,080 shares in New Guinea Goldfields Ltd., 120 shares in Guinea Airways Ltd., and £300 in cash from the payment made by the Placer Development Co. Ltd.

The Commissioner included in the appellant's assessment to income tax for the financial year 1930-1931 the following items :—

" Received from Guinea Gold No Liability 120 shares Guinea Airways Ltd. at £2 each .. .. .. £240

1,080 New Guinea Goldfields No Liability shares at 5s. 6d. .. .. .. .. .. .. £289."

But he allowed a rebate of 25.22 per cent or £135 on these items, based on the proportion that the profit he treated as exempt under sec. 16 bore to the aggregate surplus shown in the reserve account. The Commissioner also included in the appellant's assessment to income tax for the financial year 1931-1932 the sum of £300 already mentioned, " dividend from the Guinea Gold No Liability," less a similar rebate amounting to £78. The assessments were upheld by the Chief Justice, but he did not agree with the calculation of the rebate but said that it was unimportant, for the error was in favour of the taxpayer, who now appeals to this Court.

In my opinion, the inclusion of the value of the 1,080 shares in New Guinea Goldfields Ltd. at 5s. 6d. per share in the assessment was right. These shares were part of the consideration given by the New Guinea Goldfields Ltd. for the upper leases. These leases were not acquired by Guinea Gold No Liability for the purpose of resale at a profit, but for the purpose of working them. Prima facie, any profit derived from the sale of these leases was not assessable. As already stated, there was no such profit, and none was therefore distributed. Yet the shares received from the Guinea Goldfields Ltd. were distributed, and it is insisted that the distribution was of capital assets and not of profits. But the balance-sheet and the

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reserve account of February 1930 establish that the distribution was based on an estimated surplus of assets over liabilities, though it was made in September of 1929, and therefore on profit derived by the company (*Midland Land and Investment Corporation Ltd.*, cited by *Palmer, Precedents*, 14th ed., Part I., pp. 814-815; *Pool* v. *Guardian Investment Trust Co. Ltd.* (1) ). Admittedly the estimated value of the Guinea Goldfields Ltd. shares was not £90,000, but the other figures of the balance-sheet and reserve account disclose an ample surplus available for distribution. It did not arise from the sale of the upper leases to the Guinea Goldfields Ltd., and must therefore have arisen from the general surplus. The company distributed part of this surplus or profit amongst its shareholders, and the Guinea Goldfields Ltd. shares represented or formed part of this surplus or profit. It was a distribution of profit, not in money but in money's worth. The distribution, however, was not of any profit arising from the sale of the upper leases. It is contended that the distribution was made from a conglomerate fund built up of items that are not assessable to income tax. The argument has force in relation to the item £17,787, premiums on shares, but the exemption in sec. 16 is confined to profits arising from the sale of assets not acquired for the purpose of resale.

In my opinion, the inclusion of the £300 from the moneys received from the Placer Development Co. Ltd. was also right. Accepting as I do the finding of the Chief Justice that the lower leases transferred to the Placer Development Co. Ltd. were acquired by Guinea Gold No Liability for resale at a profit, then the moneys received from the Placer Development Co. Ltd. and distributed among the shareholders of Guinea Gold No Liability are not within the exemption allowed in the proviso to sec. 16. And it was not, I think, a distribution of capital assets or moneys representing capital assets. The accounts establish, in the case of the Guinea Goldfields Ltd. shares, that it was a distribution of estimated profits to shareholders under the main provision of the section. The Guinea Airways shares stand in the same position as the Guinea Goldfields shares, but for one circumstance: the evidence does not state explicitly the market value of the shares on the date of distribution, namely,

(1) (1922) 1 K.B. 347.

16th September 1929, though the reserve account of February 1930 records that they were " written up to market value at date of distribution." But I do not recollect any suggestion that the value appreciated between September 1929 and February 1930. It is unlikely that it did, and in any case the duty was upon the appellant to displace the assessment, which prima facie is correct (Act, sec. 39).

The appeal should therefore be dismissed.

*Appeal allowed with costs. Order of the Supreme Court discharged. In lieu thereof order that the appeals from the amended assessments be allowed with costs, that the amended assessment for the financial year ending* 30*th June* 1931 *be set aside, and that the Commissioner be at liberty to make a fresh assessment, and that the amended assessment for the financial year ending* 30*th June* 1932 *be reduced by excluding from the assessable income the sum of* £222 *being the dividend of* £300 *less* £78 *thereof already allowed in the amended assessment, and that the amended assessment be remitted to the Commissioner to give effect to the reduction.*

Solicitors for the appellant, *Joyner, Phillips & Joyner.*

Solicitors for the respondent, *W. H. Sharwood,* Crown Solicitor for the Commonwealth, by *Fisher, Powers, Jeffries & Brebner.*

C. C. B.