[HIGH COURT OF AUSTRALIA.]

BENNETT . . . . . APPELLANT;

AND

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

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SYDNEY, *July* 25; *Aug.* 12.

Williams J.

Income Tax—Assessable income—Company—Absolute control vested in managing director—Release of such control—Lump sum paid therefor, by instalments, to managing director—Capital or income—Income Tax Assessment Act 1936-1942 (*No.* 27 *of* 1936—*No.* 50 *of* 1942), *s.* 25.

By an indenture made in August 1935 between B. and T., a broadcasting company, B. was appointed managing director of T. for a term of seven years with wide powers, which in effect gave him complete control, and at a specified salary plus bonus and commission. Under an indenture made in May 1936 B. was appointed for a term of seven years from August 1935 to manage, subject to the control of its directors, the business of S., another broadcasting company, but as T. was entitled to appoint five of those directors B. was in *de facto* control of S. Negotiations for the acquisition by a third company of the shares owned by certain shareholders in T., which would obtain for the acquiring company control of T., resulted in the execution of two indentures in November 1936 in each of which it was recited that for the considerations therein stated B., upon request, had agreed to the cancellation of the indenture of August 1935. One of the indentures provided, *inter alia*, that the indenture of August 1935 should be deemed to be cancelled and that T. covenanted to pay B. the sum of £12,255 in instalments of £3,000 in January 1940; £4,000 in January 1941; and £5,255 in January 1942. The second indenture provided for the re-appointment of B. as managing director of T. until January 1940, at the same annual remuneration but without absolute control and in all respects he was required to conform to and comply with the directions from time to time given to him by T.'s directors. An option to renew the appointment for successive periods until August 1942 was reserved to B. and T. respectively. Provision was made in the first indenture for the refunding by B. to T. of one or more of the above-mentioned instalments in the event of him exercising for a period or periods the option of

renewal. By an indenture made in November 1937 the indenture of May 1936 and the second indenture of November 1936 were cancelled and the provision as to the refunding by B. was deleted from the first indenture of November 1936. The sums of £3,000 and £4,000 respectively received by B. in the years ended June 1940 and June 1941 as part of the said sum of £12,255 were included by the Commissioner in B.'s assessable income for those years.

Held, that the sum of £12,255 was a lump sum payable by instalments as compensation for the cancellation of the indenture of August 1935, under which B. had certain rights, and was of a capital nature and not assessable income.

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APPEAL under *Income Tax Assessment Act*.

Albert Edward Bennett appealed to the High Court against the inclusion in his assessable income by the Commissioner of Taxation of the sums of £3,000 and £4,000 respectively received by him in January 1940 and January 1941 respectively under an indenture from the Theosophical Broadcasting Station Ltd., of which company he had been the managing director.

Objections made by Bennett against the inclusion of these sums in his assessable income had been overruled by the Commissioner.

The material facts appear in the judgment hereunder.

Barwick K.C. and *O'Meally*, for the appellant.

A. R. Taylor K.C. and *Blacket*, for the respondent.

WILLIAMS J. delivered the following written judgment :— Aug. 12.

The sole question for determination on these appeals is whether the sum of £3,000 paid to the appellant during the year of income ended 30th June 1940, and the sum of £4,000 paid to him during the year of income ended 30th June 1941, form part of his assessable income of those years respectively.

These sums were paid to the appellant pursuant to the terms of an indenture made on 12th November 1936 between the Theosophical Broadcasting Station, which I shall call 2GB, of the first part, the appellant of the second part, and Sir H. R. Denison and R. E. Denison of the third part. The circumstances which led to the execution of this indenture, which I shall call for purposes of identification the first indenture, and a second indenture of the same date made between 2GB of the first part, Broadcasting Service Association Ltd. of the second part, and the appellant of the third part, were briefly as follows. The appellant had been acting for many years as the managing director of 2GB. The principal share-

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holders in that company were Theosophical Movements Ltd., which held fifty-two per cent, and the appellant, who held twelve per cent of the shares, at first in his own name and later through the shareholding of his son and daughter in Acme Investments Ltd. as his nominees. By an indenture made on 24th August 1935 between 2GB and the appellant, the appellant was appointed managing director of 2GB for a term of seven years from 24th August 1935 at a fixed salary of £1,040 per annum, a bonus equal to five per cent of the gross revenue of the company, and a commission of ten per cent of the gross return derived by the company from the sale or hire of electrical transcriptions or recordings or scripts sold by or hired by the company with certain exceptions. The indenture conferred on the appellant wide and sweeping powers, the effect of which was to give him complete control of the business of the company. By an indenture made on 26th November 1935 between 2GB, Radio 2UE Sydney Ltd., Sun Newspapers Ltd., and Broadcasting Service Association Ltd., it was agreed that Broadcasting Service Association Ltd. should be appointed the sole agent of 2GB and 2UE for twenty-one years to determine what periods during broadcasting hours should be available for advertising and to enter into such contracts with respect to advertising on their behalf as it should think fit, and for certain other purposes. One of these purposes was to sell or hire the electrical transcriptions previously sold or hired by 2GB, and the indenture provided that upon these sales and hirings the appellant was to receive from the Association the same commission of ten per cent as he had previously received from 2GB.

By an indenture made on 20th May 1936 between Broadcasting Service Association Ltd. of the first part, 2GB of the second part, and the appellant of the third part, the appellant was appointed managing director of the Association for the unexpired portion of the term of seven years from 24th August 1935. He was appointed to manage the business of the Association subject to the control of the directors, but since 2GB was entitled to appoint five of these directors, the appellant was in *de facto* control of the business.

Early in 1936 negotiations took place between the appellant on behalf of Theosophical Movements Ltd., and Acme Investments Ltd. and Denison Estates Ltd., with a view to the last mentioned company, in which Sir Hugh Denison and R. E. Denison were substantially interested, purchasing the shares owned by the two first mentioned companies in 2GB and thereby obtaining control of this company. In case these appeals should go further, and the

appellate court should take a different view, I let in evidence of the contents of the conversations between the appellant and R. E. Denison, who represented Denison Estates Ltd. in these negotiations, subject to objection. However, in my opinion, this evidence is inadmissible. But I am of opinion that evidence is admissible to prove that the negotiations related to Denison Estates Ltd. acquiring a controlling interest in 2GB as shareholders, and to the extent to which control of the business of 2GB should then be left in the hands of the appellant. These negotiations resulted in the execution of the two indentures of 12th November 1936, and the question whether the sums of £3,000 and £4,000 are part of the assessable income of the appellant must depend upon their legal effect construed in the light of the surrounding circumstances (*Inland Revenue Commissioners* v. *Duke of Westminster* (1)). These indentures had a three-fold operation. (i) The indenture of 24th August 1935 was cancelled. (ii) The appellant was re-appointed the managing director of 2GB from 12th November 1936 to 1st January 1940. He was to receive the same annual remuneration fixed and fluctuating as under his previous appointment, but he was shorn of his previous absolute control and was re-appointed to perform such duties and exercise such powers as might from time to time be assigned to or vested in him by the directors of 2GB, and in all respects to conform to and comply with their directions. (iii) Either the appellant or 2GB had the option to renew the appointment of the appellant as managing director for a period or successive periods from 1st January 1940 to 24th August 1942 (that is to say, until the date on which the appointment of the appellant under the indenture of 24th August 1935 would have expired if it had not been cancelled).

Each indenture of 12th November 1936 recited that the appellant had been requested to agree to the cancellation of the indenture of 24th August 1935, and that he had agreed to do so for the considerations thereinafter appearing, but it was the first indenture which operated to cancel the indenture of 24th August 1935, whereas it was the second indenture which operated to re-appoint him as managing director of 2GB. Clause 1 of the first indenture provided that the agreement of 24th August 1935 should be deemed to be cancelled as and from the date thereof. Clause 2 provided that 2GB covenanted with the appellant that it would pay to him the sum of £12,255 as to £3,000 on 1st January 1940, £4,000 on 1st January 1941, and the balance (£5,255) on 1st Jannuary 1942. Clause 3 provided that if the appellant exercised his option to extend

(1) (1936) A.C., at pp. 20, 25.

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the period of his employment as managing director under the second indenture until or after 1st January 1941 he would on that date refund to 2GB the said sum of £3,000, that if he exercised his option to extend his appointment to 1st January 1942 he would on that date refund the said sum of £4,000, and that if he exercised his option to extend his appointment to 24th August 1942 he would on that date refund the said sum of £5,255, provided that in the event of his employment under the second indenture or under any renewal thereof being determined from any cause whatsoever, the provisions of this clause should (except as to any sums then due and payable by the appellant) cease to have any effect. By an indenture made on 17th November 1937 between 2GB of the first part, Broadcasting Service Association Ltd. of the second part, and the appellant of the third part, the indentures of 20th May 1936 and 12th November 1936 were cancelled as from 15th November 1937. By a second indenture made on 17th November 1937 between 2GB of the first part, the appellant of the second part, and Sir H. R. Denison and R. E. Denison of the third part, it was agreed that the first indenture of 12th November 1936 should be varied by deleting clause 3 therefrom, and that otherwise that indenture should remain in full force and effect.

It was contended for the respondent that the sums of £3,000, £4,000 and £5,255 were part of the remuneration of the appellant for his services as managing director under his new appointment commencing on 12th November 1936, and as such part of his assessable income. But the payment of these sums had no relation to any services which he had rendered to 2GB in the past or was bound to render to 2GB in the future. The whole of the £12,255 was payable whether he rendered any services as managing director between 12th November 1936 and 1st January 1940 or not. The payments were not made to him as compensation for the remuneration which he would have received if he had remained managing director for the original term ending on 24th August 1942 instead of his term being shortened to 1st January 1940, because he had the option to extend the term to 24th August 1942. If the company exercised the option to extend the term the payments would not increase his remuneration, because he was entitled to them whether he served the company as managing director during the further term or not. If the appellant exercised the option, they would not increase his remuneration because he had then to refund them wholly or *pro tanto*. The effect of the cancellation of the indenture of 24th August 1935 and the re-appointment of the appellant as managing director of 2GB under the indenture of 12th

November 1936 was that the appellant, instead of having unfettered control of the business of 2GB, was relegated to a position of subordination to the directors. The fluctuating portion of his remuneration as managing director depended upon the success of the company's business. His previous management had been very profitable both to himself and the shareholders, and he was justified in fearing that if he was divested of control his remuneration might diminish. He was therefore entitled to demand a substantial sum as compensation for the cancellation of his existing agreement. On the other hand his fears might prove to be unfounded and his share of revenue might increase. In that event he could exercise his option to extend the term of his re-appointment until 24th August 1942. It would then be reasonable that he should forego the sum of £12,255.

But the substance of the matter is that the sum of £12,255 was a lump sum payable by instalments as compensation for the cancellation of the indenture of 24th August 1935, and such payments are of a capital nature unless the compensation is some form of equivalent for the loss of the income which the taxpayer would have earned under the agreement but for its cancellation, as in the case of the payments in *Commissioner of Taxes (Vict.)* v. *Phillips* (1). The payments in the present case are simply payments made as part of the consideration for the appellant agreeing to cancel one agreement under which he had certain rights and entering into a fresh agreement under which he had different rights. Adapting the words of Lord *Macmillan* in *Van Den Berghs Ltd.* v. *Clark* (2) the congeries of the rights which the appellant enjoyed under the agreement and which for a price he surrendered was a capital asset. The payments are in the same category as those in *Du Cros* v. *Ryall* (3); *Dewhurst* v. *Hunter* (4) and the payment in *Carter* v. *Wadman* (5) so far as attributable to the cancellation of the agreement there in question: cf. *Asher* v. *London Film Productions Ltd.* (6).

For these reasons I allow the appeals with costs.

Order the respondent to amend the assessment for the financial year 1940-1941 *by omitting from the assessable income of the appellant the sum of* £3,000 *paid to him by Theosophical Broadcasting Station Ltd., and to reduce the assessment accordingly.*

(1) (1936) 55 C.L.R. 144.
(2) (1935) A.C., at p. 443.
(3) (1935) 19 Tax Cas. 444.
(4) (1932) 146 L.T. 510.
(5) (1946) 176 L.T. 206.
(6) (1944) 1 K.B. 133, at pp. 139, 140.

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Order the respondent to amend the assessment for the financial year 1941-1942 *by omitting from the assessable income of the appellant the sum of* £4,000 *paid to him by Theosophical Broadcasting Station Ltd., and to reduce the assessment accordingly.*

Respondent to pay the costs of the appellant of both appeals.

Liberty to apply.

Solicitors for the appellant, *C. Don Service & Co.*

Solicitor for the respondent, *H. F. E. Whitlam,* Crown Solicitor for the Commonwealth.

J. B.