

[HIGH COURT OF AUSTRALIA.]

CARPENTERS INVESTMENT TRADING COM- }  
PANY LIMITED . . . . . } APPELLANT ;

AND

THE FEDERAL COMMISSIONER OF TAXA- }  
TION . . . . . } RESPONDENT.

*Taxation—War-time (company) tax—Assessment—Assessable income—“Taxable profit”—“Holding” company—Moneys received from “branch” company as dividends—Exclusion from income of holding company—Dividends received by holding company from other companies—Deduction in entirety from taxable profits—“Included”—War-time (Company) Tax Assessment Act 1940-1944 (No. 90 of 1940—No. 29 of 1944), ss. 3, 13, 17, 24.*

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SYDNEY,  
Aug. 8, 9.  
Latham C.J.  
Dixon,  
Williams and  
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Included in the income derived during the relevant year by the appellant, a “holding” company under s. 3 of the *War-time (Company) Tax Assessment Act 1940-1944*, were dividends received from a subsidiary company (£2,250), treated under s. 17 as a branch of the holding company, and also dividends from other companies (£816). The commissioner charged against that sum of £816 a sum of £248 as portion of the indirect general expenses of the appellant’s business, and therefore deducted from the taxable profit ascertained in accordance with s. 3 of the Act, not £816 but £568 only. On appeal,

*Held* that in ascertaining the amount of taxable profit the sum of £816 should have been deducted in lieu of the sum of £568.

Decision in *Douglass v. Federal Commissioner of Taxation* ((1931) 45 C.L.R. 95) applied.

CASE STATED.

On the hearing of an appeal to the High Court by Carpenters Investment Trading Co. Ltd. from an assessment for war-time company tax made by the Federal Commissioner of Taxation under the *War-time (Company) Tax Assessment Act 1940-1944*, upon the company, *McTiernan J.* stated for the opinion of the Full Court a case which was substantially as follows :—



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Carpenters Investment Trading Co. Ltd. (hereinafter called "Carpenter's") is a public company incorporated under the law of the State of New South Wales. It is a company limited by shares, and having an authorized capital of £100,000. Its paid-up capital during the relevant accounting period was £20,000, consisting of 2,000 fully-paid shares of £10 each.

2. Cittco Pty. Ltd. (hereinafter called "Cittco") is a proprietary company incorporated under the law of the said State. It is a company limited by shares, and having an authorized capital of £2,000. Its paid-up capital during the relevant accounting period was £34, consisting of thirty-four fully-paid shares of £1 each, of which one share was held by each of its four directors and thirty shares were held by Carpenter's.

3. Carpenter's is a "holding company" and Cittco (in relation to Carpenter's) is a "subsidiary company" within the respective meanings of those terms as defined in the *War-time (Company) Tax Assessment Act* 1940-1944. Under the provisions of s. 17 of that Act, Carpenter's elected to have Cittco treated for all purposes of that Act as a branch of Carpenter's.

4. During the period of twelve months ended on 30th June 1945, which is the relevant accounting period, Carpenter's earned a net profit of £2,866, and was assessed for income tax on a taxable income of £2,866, in the sum of £91 12s. Subsequently, by an amended assessment, dated 17th June 1947, the income tax on the said taxable income was reduced to £13 2s.

5. For the purposes of the amended income-tax assessment there was included in the taxable income of Carpenter's an amount of £2,818 representing £2,250 dividends from Cittco and £568 dividends from other companies.

6. Cittco was assessed for income tax in respect of that accounting period on a taxable income of £4,945 in the sum of £1,483 10s.

7. Following upon the said election, the Commissioner of Taxation made an assessment of War-time (Company) Tax on Carpenter's in respect of taxable profit derived in the relevant accounting period. Notice of that assessment was issued to Carpenter's on 29th July 1946, the amount of taxable profit being assessed at £3,695 18s. and the tax thereon being assessed at £1,166 2s. The commissioner forwarded an explanatory statement with this notice of assessment.

8. By letter dated 6th August 1946, Carpenter's lodged an objection against the last-mentioned assessment. The notice of objection was in the following terms:



1. The amount taken out of the taxable income under the heading "Dividends Included" is wrongly shown at £2,540, whereas the correct total is £3,066 so that the excess of taxable profit should be £2,169 and not £2,695 as shown.
2. The Company elected to have its subsidiaries treated as branches and the Department has not done so. Had the Department done so the company would have been taxed as follows :—

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To Expenses .. ..	£593	By Company Dividends	£816
Profit for War-time		Cittco Pty. Ltd.	
Companies Tax ..	5,562	Branch .. ..	4,945
		Interest Account ..	275
		Agencies and Trading Account ..	119
	<hr/>		<hr/>
	£6,155		£6,155
	<hr/>		<hr/>

*Adjustment for War-time Companies Tax.*

Profit as above .. ..	£5,562
Deduct—	
Income Tax Payable .. ..	£1,575
Dividends Included .. ..	816
Percentage Standard .. ..	1,000
	<hr/>
	3,391
	<hr/>
Excess of Taxable Profit ..	£2,171
	<hr/>

In view of the amount of tax that is involved and in view of the recent High Court decision which would seem to indicate that our objection should be allowed, we would very much appreciate your giving an early decision.

We did not object to the assessment in respect of our ordinary income tax as the rebate was taken off the calculated amount of tax and no explanation was given as to how the amount was arrived at so we assumed that the Department's workings would be correct as we had no information upon which we could check the calculation of rebate and assumed that the Department's workings would be correct.

From the adjustment sheet received with the War-time (Company) Tax it appears to us that the Department has wrongly deducted certain expenses from the dividends received when calculating this



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rebate and we have already written you asking that you re-open the matter and refund us the amount of tax overpaid in respect of that assessment.

9. By letter dated 4th December 1946, the Commissioner of Taxation informed Carpenter's that he had disallowed the said objection, and by letter dated 16th December 1946, Carpenter's requested the Commissioner of Taxation to treat the objection as an appeal and to forward the same to the High Court for decision.

10. A notice of amended assessment, dated 17th June 1947, made under the *War-time (Company) Tax Act* was issued by the commissioner to Carpenter's, in which the amount of taxable profit was reduced from £3,695 18s. to £3,496 8s. and the tax was reduced from £1,166 2s. to £1,022 17s. 7d. The commissioner again forwarded an explanatory statement with this notice of amended assessment.

11. Carpenter's forwarded to the Commissioner of Taxation a letter, dated 30th June 1947, which was in the following terms: "We are in receipt of your letter of the 17th inst. enclosing an amended assessment giving us a credit of £143 4s. 5d. together with your adjustment sheet. However, we cannot accept this amended assessment as satisfying the objection which we lodged and which we have requested to be forwarded to the High Court for consideration and we, therefore, wish to object to same on the same grounds as we objected to the original assessment.

We would also like to draw your attention to the fact that on February 17th last we requested you by registered letter, and in accordance with the Act, to refer this matter to the High Court.

The Act provides that within sixty days you do this, but so far it has not been referred to the High Court, and we now once again under the provisions of the Act ask you to refer this matter immediately to the High Court, failing which we will have no course open to us other than to apply to the Court for a mandamus."

12. The Commissioner of Taxation having been requested by Carpenter's to treat the objection of Carpenter's as an appeal forwarded it to the Court.

13. The appeal came on for hearing before me on 3rd May 1948, when I reserved my decision.

14. No oral evidence was tendered by either party at the hearing.

15. There were put in evidence at the hearing the following documents:—

- A. (i) Copy of income-tax return—1st July 1944 to 30th June 1945—Carpenter's Investment Trading Co. Ltd. (showing the net profit and taxable income as £2,866).



- (ii) Report of the directors of Carpenter’s dated 4th July 1945.

(iii) Notice of the annual general meeting of Carpenter’s.

(iv) Carpenter’s share trading account for the year ended 30th June 1945.

(v) Document headed “ Carpenter’s Investment Trading Co. Ltd.” and consisting of a list of dividends (aggregating £816 5s. 1d.) received by the company from (eleven) companies other than the subsidiary.

(vi) Carpenter’s trading account, profit and loss account, profit and loss appropriation account for year ended 30th June 1945 (showing as revenue, *inter alia*, company dividends £816 5s. 1d., subsidiary company dividends £2,250).

(vii) Carpenter’s balance sheet as at 30th June 1945.
- B. Notice of assessment dated 30th April 1946, *Federal Income Tax Act*—Cittco Pty. Ltd.

C. Notice of assessment dated 27th May 1946, *Federal Income Tax Act*—Carpenter’s Investment Trading Co. Ltd.

D. Notice of assessment War-time (Company) Tax dated 29th July 1946—Carpenter’s Investment Trading Co. Ltd.—with adjustment sheet.
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ADJUSTMENT SHEET

CARPENTERS INVESTMENT TRADING COMPANY LIMITED.

The capital employed in gaining or producing the taxable profit of the company for the year ended 30th June 1945, as set out on the attached notice of assessment, has been ascertained in the following manner, viz. :—

Name of Coy.	Capital Employed	Taxable Income	Div'ds. Included	Inc. Tax Payable	Taxable Profits	Super Tax
Carpenters Invest-ment Trading Co. Ltd.	} £20,000	£2,866	£2,540	£91 12 0	£234 8 0	—
Cittco Pty. Ltd.		£4,945		£1,483 10 0	£3,461 10 0	—
Totals	£20,000	£7,811	£2,540	£1,575 2 0	£3,695 18 0	—

- E. Notice of objection by Carpenter’s Investment Trading Co. Ltd. dated 6th August 1946, to assessment of 29th July 1946.
- F. Commissioner’s notice of disallowance dated 4th December 1946.
- Letter dated 16th December 1946—Carpenter’s Investment Trading Co. Ltd. to Commissioner of Taxation, acknowledging the notice of disallowance and requesting that the objection be treated as an appeal and forwarded to the High Court.



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G. Notice of amended assessment *Federal Income Tax Act*, dated 17th June 1947.

G1. Adjustment sheet of amended assessment Federal Income Tax—

In arriving at the taxable income shown on the enclosed notice of amended assessment, the following adjustments have been made in the figures of the company's original assessment for the year ended 30th June 1945 :—

Income as previously assessed .. ..			£2,866.				
	Commis- sion	Sale of Shares	Sub. Coy. Divs.	Other Divs.	Sec. 160AB Inter- est	Other Inter- est	Total
Gross Income .. ..	802	63	2250	816	75	200	2406
Less : Direct Expenses	686	60					746
	116	3	2250	816	75	200	3460
Less : Indirect Expenses £594*							
802:63:816:75:200 of 594							
<u>1956 .. ..</u>	243	19	—	248	23	61	594
	Dr. 127	Dr. 16	2250	568	52	139	2866
Deduct : .. ..	127	16			39	104	
	—	—	2250	568	13	35	2866

Sec. 46 (1) rebate : Dividends—2250 plus 568 ... 2818 @ 6/- £845 8 0  
Sec. 160AB rebate : re interest on loans issued subsequent to 1/1/40—  
£13 @ 2/- ... .. £1 6 0

\* as per P. & L. A/c.

H. Notice of amended assessment *War-time (Company) Tax Act* dated 17th June 1947, and adjustment sheet.

CARPENTERS INVESTMENT TRADING CO. LTD.

The capital employed in gaining or producing the taxable profit of the company for the year ended 30th June 1945, as set out on the attached notice of amended assessment, has been ascertained in the following manner, viz. :—

Name of Coy.	Capital Employed	Taxable Income	Divs. Incl.	Inc. Tax Payable	Taxable Profits
Carpenters Invest- ment Trading Co. Limited	20000	2866	2818	13 2 0	34 18 0
Cittco Pty. Ltd.		4945	—	1483 10 0	3461 10 0
Totals ..	20000	7811	2818	1496 12 0	3496 8 0

Super Tax—Nil.

J. Letter dated 17th June 1947, Deputy Commissioner of Taxa-  
tion to Carpenter's Investment Trading Co. Ltd.



Letter dated 30th June 1947, from Carpenter's Investment Trading Co. Ltd. to the Deputy Commissioner of Taxation. H. C. OF A. 1949.

The documents referred to in par. 15 were annexed to and formed part of the case stated. CARPENTERS INVESTMENT TRADING CO. LTD.

The following questions were stated for the opinion of the Full Court of the High Court :—

(1) Whether the Commissioner of Taxation determined the amount of the taxable profit of Carpenter's derived during the year ended 30th June 1945, in accordance with the *War-time (Company) Tax Assessment Act* 1940-1944 ?

(2) If the answer to (1) is in the negative, in what manner ought the Commissioner of Taxation to have determined the amount of the said taxable profit ?

*Hardie* K.C. (with him *Hannan*), for the appellant. The commissioner has failed to treat the subsidiary company as a branch of the holding company as provided in s. 17 of the *War-time (Company) Tax Assessment Act* 1940-1944. This failure has resulted in the issuing of an excessive assessment. In order to construct the profit and loss account of the notional entity consisting of the appellant, the holding company, and Citto Pty. Ltd., the subsidiary company, there should be deleted from the revenue account the item of £2,250, dividends from the subsidiary company, and substituted for it the net profit, £4,945, of the subsidiary company for the year. From the notional entity's taxable income so determined deductions should be made as provided in the definition of "taxable profit" in s. 3. The deduction is a deduction of only the dividends received by the appellant from companies other than the subsidiary company, namely, £816. The phrase "as assessed under the Income Tax Assessment Act" as used in the definition of "taxable profit" in s. 3, means the taxable income as ascertained, or determined, or calculated and not as charged with tax because the holding company and the subsidiary company have not, in fact, been charged with tax as one entity. Even if a contrary intention did not appear, the phrase "as assessed" means, unless taxed in a case when s. 17 directs an amalgamation of the accounts as determined. Support for this is derived from the definition of "assessment" in s. 6 of the *Income Tax Assessment Act*. A subsidiary company cannot be regarded in s. 17 as "any other company." In calculating the taxable profit the appellant is entitled to a deduction of the whole of the said sum of £2,250, and of the sum of £816. The latter sum should not have been diminished by £248.

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The *War-time (Company) Tax Assessment Act* requires the commissioner to determine one taxable profit for the purposes of the Act and to determine one taxable profit of the taxpayer on the footing that its subsidiary is a branch only. The commissioner has determined two taxable profits in this case. The documents in evidence show that the said sum of £2,250 has been included twice and taxed twice. Alternatively, if the commissioner's method of approaching the matter is correct, he should treat the whole of the amount of £3,066 as being dividends included because the whole of that sum was included in the calculation of the taxable income of the appellant. In order to determine the taxable profit, the profits of the parent company and of the branch, that is the subsidiary company, should be aggregated (*Incorporated Interests Pty. Ltd. v. Federal Commissioner of Taxation* (1)). If a calculation be made of each of the holding company and the subsidiary company, and the dividends included in each case and the income tax payable be calculated separately, in fact assessed by the commissioner in each case, then in determining what amount should be deducted as dividends included in the taxable income there should be deducted the whole of the dividend in fact received by the holding company and taken into account in the calculation of the holding company's assessable income. The taxable income of the two companies was £5,562 and not £7,811 as shown by the commissioner. The commissioner erred in the adjustment sheet in not taking the sum of £3,066 as dividends included instead of the sum of £2,818. This case is stronger on this point than *North Australian Pastoral Co. Ltd. v. Federal Commissioner of Taxation* (2). The commissioner was not entitled to charge any portion of the indirect expenses against the dividends. The dividends of £816 were included in the calculation of taxable profit, and, having regard to the scheme of the Act, the whole of those dividends is deductible. That scheme contemplates that capital invested in shares in companies and the whole of the revenue of those shares shall be disregarded, which makes it a stronger case than s. 46 of the *Income Tax Assessment Act* 1936, as amended.

[DIXON J. referred to *Douglass v. Federal Commissioner of Taxation* (3).]

The *War-time (Company) Tax Assessment Act* strongly indicates that it was intended that all dividends taken into account in the revenue account of the company in arriving at the taxable income should be deducted. From the net profit of the appellant there

(1) (1943) 67 C.L.R. 508, at p. 526.  
(2) (1946) 71 C.L.R. 623, at p. 634.

(3) (1931) 45 C.L.R. 95, at pp. 105, 106.



should be deducted the amount of dividends actually received as dividends from other companies. H. C. OF A.  
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*Holmes K.C.* (with him *Downing*), for the respondent. The documents before the Court show that the only figure in dispute was £248 which was deducted from the said sum of £816. The correctness of that deduction at that stage is not in issue here. It could have been, but it was not, brought as an issue on the appeal from the assessment of income tax. This is not such an appeal so the starting point is the assessment of taxable income. The fallacy of the argument presented on behalf of the appellant is the notional company, with a notional taxable income and a notional assessment. That is completely at variance with par. (a) of the definition of "taxable profit" in s. 3 of the *War-time (Company) Tax Assessment Act*. That definition indicates that the first figure so far as that Act is concerned is the taxable income assessed under the *Income Tax Assessment Act*. There is not any provision in the last-mentioned Act for assessing the taxable income of a notional company. Nor does the *War-time (Company) Tax Assessment Act* require or authorize the reconstruction of a new set of accounts for the purpose of making a new assessment. The construction of the said par. (a) cannot be altered by the fact of s. 17 and the amalgamation, as it were, of two companies into one for the purposes of the Act. A subsidiary company is treated as a branch within the meaning of s. 17 when its income is consolidated with the taxable income of the holding company and the income tax payable by it is consolidated with the income tax payable by the holding company. The whole, and not merely a part, of a dividend paid by a subsidiary company to a holding company is in fact deducted. The attribution by the commissioner of the sum of £816 was a reasonable attribution of expenses having regard to the fact that the appellant was not simply a company which held shares in another company, but it was a company which carried on trading in shares which were part of its stock-in-trade. The sum of £816 is part of the assessable income being dividends not *simpliciter* but received by the appellant as part of its trading operations in shares, and it is therefore proper to apply s. 51 of the *Income Tax Assessment Act* to that item, the assessable income, and allocate as against it some part of the revenue of the appellant. *Douglass v. Federal Commissioner of Taxation* (1) is quite distinguishable from this case. Neither of the items of expenditure there under consideration, though proper as

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a deduction from income tax, was in any sense an outgoing attributable to the earning of income from property. It is proper where there is part of the income, the revenue, which is the total assessable income, and there is as against that an item of expenditure properly attributable to the earning of that income, to put that one against the other (*Douglass v. Federal Commissioner of Taxation* (1)). There was a relation between the £816 of dividends and the items of expenditure. It was a proper thing to put deductions against those dividends. Not the whole of the £816 was included in the taxable income, but that sum less the deductions which have been properly placed against it, because they were not simple deductions from a total gross assessable income; they are deductions which are related to the earning and receipt of that item of assessable income. It does not follow from s. 24 (3) that dividends should be deducted altogether from the taxable income for the purposes of the Act. This view is supported by the presence in par. (b) of the definition of "taxable profit" of the words "so much of any dividend received by a company."

[WILLIAMS J. referred to *Associated Newspapers Ltd. v. Federal Commissioner of Taxation* (2).]

The following judgment of the Court was delivered by *Latham C.J.* This is a case stated by *McTiernan J.* in an appeal from an amended assessment of the appellant company to war-time (company) tax under the *War-time (Company) Tax Assessment Act 1940-1944* in respect of the excess above the percentage standard of the taxable profit derived during the year ended 30th June 1945: see the Act, s. 13.

The material facts, shortly stated, are that the appellant is a holding company within the meaning of s. 3 of the Act and that under s. 17 of the Act the company elected to have a subsidiary company, *Cittco Pty. Ltd.*, treated as a branch of the holding company.

Included in the income derived by the appellant during the relevant year for the purposes of ordinary Federal income tax were dividends received from the *Cittco* company amounting to £2,250, and from other companies amounting to £816.

In our opinion, it is clear that when *Cittco* became, for the purposes of the *War-time (Company) Tax Assessment Act*, a branch of the appellant by reason of the election made under s. 17 of the Act, the dividends received from *Cittco* could no longer be included

(1) (1931) 45 C.L.R., at pp. 102, 103, 105, 106. (2) (1944) 69 C.L.R. 257, at p. 262.



in the income of the appellant for the purposes of that Act, because a company cannot be paid a dividend by one of its branches.

The election by the appellant to have Cittco treated as one of its branches meant that the business carried on by Cittco became, for the purposes of the Act, part of the business of the appellant and the net profit of Cittco became part of the net profit of the appellant.

The arithmetical result of the method of assessment adopted by the commissioner for the purposes of the Act was to exclude from the taxable income of the appellant company the dividends received from Cittco and to substitute the net profit for the amount of the dividends. But the commissioner also sought to charge against the sum of £816, that is, against the dividends received from other companies, a sum of £248, being a portion of the "indirect" general expenses of the business of the appellant, and, therefore, to deduct from the taxable profit ascertained in accordance with s. 3 (b) of the Act (definition of "taxable profit") not the whole sum of £816, but this sum less £248, that is to say, a deduction of only £568.

The question whether the appellant is entitled to a deduction of the former amount, that is, of £816, is the real and sole outstanding question between the parties. On this point we are of the opinion that the appellant is right.

Section 24 of the Act provides, so far as is material, that the capital employed in any accounting period shall, for the purposes of the Act, be ascertained by adding certain items and deducting certain items, including "any capital, averaged over the accounting period, invested in shareholdings in any other company."

The scheme of the Act is, therefore, to eliminate as part of the capital of a company employed in any accounting period all capital invested in shareholdings in any other companies. This fact indicates that par. (b) of the definition of "taxable profit" in s. 3 of the Act should be construed in the same manner as a similar provision in s. 16 (d) of the *Income Tax Assessment Act 1922-1927* was construed by this Court in the case of *Douglass v. Federal Commissioner of Taxation* (1) that is to say, to use the words of our brother *Dixon* in that case: "The word 'included' should be treated as referring to the amount by which the taxable income is increased by reason of the presence of the dividends in the assessable income."

For these reasons, we are of opinion that the questions asked should be answered as follows:—

- (1) No. (2) The Commissioner of Taxation, in ascertaining the amount of taxable profit should have deducted the sum of £816 in lieu of the sum of £568.

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The case is remitted, with these answers, to *McTiernan J.* The costs of the case are to be costs in the appeal.

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*Questions answered as follows:—*

- (1) *No.*
- (2) *The Commissioner of Taxation, in ascertaining the amount of taxable profit should have deducted the sum of £816 in lieu of the sum of £568. Case remitted to McTier-*  
*nan J. Costs of case to be costs in the*  
*appeal.*

Solicitors for the appellant, *G. W. L. Charker & Co.*

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

J. B.