[HIGH COURT OF AUSTRALIA.]

PRODUCERS' AND CITIZENS' CO-OPERATIVE ASSURANCE COMPANY LIMITED . . } APPELLANT;

AND

FEDERAL COMMISSIONER OF TAXATION . RESPONDENT.

H. C. OF A. 1956.

SYDNEY, *May* 8, 9;

BRISBANE. *July* 20.

Webb J.

Income Tax (Cth.)—Assessment—Income or capital—Assessable income—Mutual life assurance company—Investments—Rented premises—Profit-making undertaking or scheme—Intention of taxpayer—Income Tax Assessment Act 1936-1948, *ss.* 6, 26 (*a*), 197—*Life Insurance Act* 1945.

The objects of an assurance company registered and incorporated in New South Wales, and which carried on business in all the Australian States, were, among others: (i) to issue policies of life assurance or endowment or annuities or against death or injury by accident, (ii) to invest the funds of the company as the directors may deem most advisable, (iii) to lease, sell, dispose of or otherwise deal with all or any property of the company, and (iv) to invest the funds of the company in or upon freehold or leasehold securities. In 1934 the company's Brisbane agent indicated its desire to relinquish the agency and it appeared to have been assumed that upon that event the company would have its Brisbane office in other premises. In May 1935, the company obtained a further lease for three years of its office accommodation, and in November 1935, upon a recommendation by one of its officers, purchased for the sum of £70,000 the Strand Building which was fully occupied by tenants but it was not, in its then condition, suitable as an office for the company although the company's requirements were small. At that time it was the policy of the company to invest in freehold property its funds from premiums on policies and other sources. The company never made any use of any part of the building for that purpose but continued to lease its office from its agent and also to let the Strand Building for periods of three or five years with provision for repossession by the company in the event of "rebuilding" the meaning of which was not clear. Apart from the recommendation in 1935 referred to above there was not any reference in the company's records, minutes, annual reports or written communications to shareholders to an intention of the company to use the Strand Building for its office purposes. The company sold that building in 1948 for £125,000. An objection by the

company to the inclusion in its assessable income of the sum of £49,792 11s. 3d., being the profit made by the company on the sale, was disallowed by the commissioner. On appeal,

Held that, in all the circumstances, the transaction of buying and selling the Strand Building was sufficiently related to the appellant's business of life assurance to bring the profit into tax.

Colonial Mutual Life Assurance Society Ltd. v. *Federal Commissioner of Taxation* (1946) 73 C.L.R. 604, and *Forwood Down & Co. Ltd.* v. *Commissioner of Taxation* (*W.A.*) (1935) 53 C.L.R. 403, referred to.

APPEAL.

The facts are sufficiently stated in the head-note and in the judgment hereunder.

B. P. Macfarlan Q.C. (with him *E. C. Lewis*), for the appellant. The only claim of the commissioner now to assess in accordance with the notice of assessment served is on the basis that the profit admittedly made on the sale of the Strand Building is a profit of a revenue nature and should be brought to tax under s. 26 (*a*) or s. 6 of the Act. As a minimum, it was held by the appellant as an asset for more than twelve years and was then sold in the circumstances described: see *Colonial Mutual Life Assurance Society Ltd.* v. *Federal Commissioner of Taxation* (1). Prima facie, a sale of a capital asset, and certainly a capital asset which has been held for a period in excess of twelve years, is a sale which, if profit results, is a profit of capital nature. The passage cited from *Californian Copper Syndicate* v. *Harris* (2) makes it plain that what is the exception to that prima facie rule is taxable. But that which is taxable there is contrasted in the previous lines with what is done merely as a change in investment and a realization is not taxable. This was the realization of a capital asset. The primary purpose for the acquisition of the Strand Building was to install the company's office therein at some future time. The evidence shows there is a purchase primarily for use as a head-office. The profit was not acquired as part of a profit-making undertaking or scheme. Out of the very many properties purchased by the company only five have been sold, and then after they had been held for many years. The members of the Court in *Colonial Mutual Life Assurance Society Ltd.* v. *Federal Commissioner of Taxation* (3) did not lay down a rigid rule of law: see *Californian Copper Syndicate* v. *Harris* (2); *Colonial*

(1) (1946) 73 C.L.R. 604, at p. 614.
(2) (1904) 5 Tax Cas. 159, at p. 166.
(3) (1946) 73 C.L.R. 604.

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Mutual Life Assurance Society's Case (1); and *Peel River Land & Mineral Co. (Ltd.)* v. *Federal Commissioner of Taxation* (2).

L. C. Badham Q.C. (with him *R. J. Ellicott*), for the respondent. The onus is upon the appellant to show that the assessment is wrong. The appellant is, undoubtedly, carrying on the business of an assurance company. Inextricably bound up with, the nature of the assurance company is the obligation and the necessity to invest its money in various types of investments for the purpose of putting itself in a sound actuarial position and to make itself actuarially solvent. The profit was made under circumstances which amount to a carrying-out, if not a carrying-on, of a profit-making undertaking. The express intention is not of itself to be considered except in relation to the surrounding circumstances. It is clear that the Strand Building was sold for the purpose of making a profit in the ordinary course of the business of a life assurance company (*Western Gold Mines N.L.* v. *Commissioner of Taxation (W.A.)* (3); *Colonial Mutual Life Assurance Society Ltd.* v. *Federal Commissioner of Taxation* (4)). The "investment process" there referred to is a reference to the investment process of life assurance companies. The transaction "was sufficiently related to the company's business" (*Forwood Down & Co. Ltd.* v. *Commissioner of Taxation (W.A.)* (5)). It does not really matter why the various properties were sold, but the transactions serve to show that at or about that time the company was interested, not merely in supervising its ordinary investments, but in making a profit by an undertaking for a special purpose (*Colonial Mutual Life Case* (6)).

B. P. Macfarlan Q.C., in reply. The view expressed in the *Colonial Mutual Life Case* (7) that, prima facie, any profit resulting from the sale of a capital asset is a capital profit, is still the law. In every transaction the case is one for inquiry into its particular facts. There has been a constant policy on the part of the directors that they never carried on the business of buying or selling real estate by reason of investment for the purpose of gaining a profit. A similar situation was dealt with in *Scottish Australian Mining Co. Ltd.* v. *Federal Commissioner of Taxation* (8).

Cur. adv. vult.

(1) (1946) 73 C.L.R., at pp. 612-614, 616-618.
(2) (1954) 92 C.L.R. 467, at pp. 480, 481.
(3) (1938) 59 C.L.R. 729, at p. 740.
(4) (1946) 73 C.L.R., at pp. 608, 614, 619.
(5) (1935) 53 C.L.R., at p. 408.
(6) (1946) 73 C.L.R., at p. 621.
(7) (1946) 73 C.L.R. 604.
(8) (1950) 81 C.L.R. 188.

The following judgment was delivered by :—

WEBB J. This is an appeal under s. 197 of the *Income Tax Assessment Act* 1936-1948 against the disallowance by the respondent Commissioner of Taxation of an objection by the appellant company to the inclusion in the assessable income of the appellant of the sum of £49,792 11s. 3d. being the profit made by the appellant on the sale in December 1948 of a freehold property known as the Strand Building, consisting of four floors with a total area of 38,650 square feet and situated in Queen Street, Brisbane. The respondent disallowed the objection on the ground that this profit was assessable income from personal exertion. Section 6 of the Act defines "income from personal exertion" as meaning among other things "the proceeds of any business carried on by the taxpayer . . . and any profit arising from the sale by the taxpayer of any property acquired by him for the purpose of profit-making by sale or from the carrying on or carrying out of any profit-making undertaking or scheme . . ."; and s. 26 (*a*) provides that assessable income shall include "profit arising from the sale by the taxpayer of any property acquired by him for the purpose of profit-making by sale, or from the carrying on or carrying out of any profit-making undertaking or scheme".

The amount of tax involved is said to be about £10,000.

The respondent allowed two other objections and issued an amended assessment, but nothing turns on that.

The appellant is registered and incorporated in New South Wales under the *Companies Act* 1899 of that State. Its memorandum of association provides that the objects for which the appellant is established are, among others, (1) to issue policies of life assurance or endowment or annuities or against death or injury by accident, (2) to invest the funds of the company as the directors may deem most advisable, (3) to lease sell dispose of or otherwise deal with all or any property of the company, and (4) to invest the funds of the company in or upon freehold or leasehold securities.

At all material times the appellant has carried on business in all the Australian States and in the Dominion of New Zealand and has been governed by a board of directors operating in the head office of the appellant in Sydney. It had an office in Brisbane which until 1942 was in premises of the Queensland Primary Producers' Co-operative Agency Ltd. That company, under an agreement made in 1927, acted as the appellant's agent in securing business for the appellant in Queensland. In 1934, the agent indicated its desire to relinquish the agency and it appears to have been assumed that when it did so the appellant would have its Brisbane office in other premises. So in August 1935, an officer of the appellant

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after inquiry recommended the purchase by the appellant of the Strand Building and the purchase was made in November 1935. Meanwhile the appellant had obtained in May 1935 a further lease for three years of the office in the premises of the agent, which, as already stated, continued to act as agent and to provide office accommodation for the appellant until 1942.

When the appellant purchased the Strand Building it was fully occupied by tenants ; but in any case it was not in its then condition suitable as an office for the appellant, as it required alterations for that purpose. Actually the office accommodation required by the appellant at that stage of the development of its business in Queensland was very limited, a room or two at most, and that was the case throughout, the area used ranging from 527 square feet to 1,873 square feet, so that only a small portion of the Strand Building would have been required by the appellant for its office purposes. However, the appellant never made any use of any part of the building for those purposes, but continued to lease its office from its agent and also to let the Strand Building, and decided to do so as early as January 1936, for maximum periods of three years, increased to five years a few months later in the case of three tenants. In a minute of the directors' meeting recording the decision to let for three years it was stated that the new leases should contain provision for the appellant to repossess in the event of " rebuilding ". What they meant by " rebuilding " in not clear. Mr. Higman, the present chairman of directors of the appellant, said in his evidence for the appellant that it referred to proposed internal alterations. That seems unlikely. But whether this provision was inserted in the new leases does not appear. In any case it does not necessarily indicate an intention to rebuild for the office purposes of the appellant which then were and continued to be very limited : it might have been intended to rebuild solely for letting purposes. Moreover, apart from the officer's letter in August 1935, there is no reference in the records of the appellant, either in the minutes, or in its annual reports, or in any written communication to the shareholders to an intention of the appellant to use the building for its office purposes. On the contrary the appellant in its annual report for 1936 referred to the purchase of the Strand Building under the heading of " Investments ", and the appellant continued to have its Brisbane office in its agent's premises, as already stated. However Mr. Higman said that the purchase was made both to secure office accommodation for the appellant and as an investment. At the time the Strand Building was purchased it was the policy of the appellant to invest in freehold properties its funds from premiums on policies and other sources, and no doubt the purchase of the

Strand Building was in pursuance of that policy. But I am not prepared to find that the purchase was also made with the intention of using a part of the building for the appellant's office. When the purchase was made Mr. Higman was a director but not chairman of directors, and his knowledge as director of the intentions of the appellant might not have been so full as it is as chairman of directors. He might have assumed that the appellant purchased for the reasons given by the officer who recommended the purchase; whereas the appellant's annual report for 1936, and its failure to use the building for its office purposes or to record its intention to do so suggest that the purchase was made solely as an investment in freeholds in accordance with the policy of the appellant at that time.

I find then that the purchase of the Strand Building was not made with a view to using any part of the building for the appellant's office purposes. In making this finding I am not influenced by the fact that in 1938 the appellant purchased the Astoria Building in Brisbane, sold it in 1953 at a profit, and in 1955 represented to the respondent that it was purchased for the appellant's office accommodation; whereas Mr. Higman insisted in his evidence that the purchase was made solely as an investment and in fact the Astoria Building had never been occupied by the appellant for its office purposes. The representation appears in the notice of objection to the inclusion of the profit in the assessable income of the appellant for the year ended 31st August 1953, and was made by the public officer of the appellant. This conflict between the views of two important officers of the appellant as to the purposes of the purchase of a large city building—it included a basement, a ground floor and five upper floors—serves to show the need for care before accepting even the statements of a principal officer of the appellant as to the intention of the appellant in purchasing freeholds, when such statements are not supported by the minutes or annual reports of the appellant or in any written communications to the shareholders, or otherwise by the actions of the appellant, but on the contrary are contradicted by the appellant's annual report made just after the purchase and are inconsistent with its action in continuing to occupy the agent's premises as an office until 1942. In saying this I do not suggest that Mr. Higman said what he believed to be untrue: he seemed to believe what he said. What I question is not his veracity but the accuracy of his knowledge, even as a director, of what the appellant intended over twenty years before when it purchased the Strand Building.

But the fact remains that the Strand Building was retained by the the appellant for over thirteen years. Meanwhile however the appellant had indicated that it was prepared to sell it. As early as

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1943, it had named a price to what appeared to be a possible purchaser; and in 1946, it actually sold it for £110,000, subject to the consent of the Treasurer of the Commonwealth under *National Security Regulations* then in force. The consent of the Treasurer was refused. Again in March 1947 Mr. Higman told the then Commissioner of Taxation, the late Mr. Trebilco, that the directors would consider the sale of the Strand Building " for the sole reason that any surplus realized would be added to a fund for the reduction of the assumed rate of interest from four per cent to three and one-half per cent in order to comply sooner with the requirements of the Federal *Life Insurance Act* 1946 ". Eventually the building was sold in 1948 to another life assurance company. For what purpose the other company purchased it we do not know: it might have been for its office purposes, as Mr. *Macfarlan* for the appellant suggested, or it might have been solely as an investment. But, notwithstanding what Mr. Higman told the late Mr. Trebilco, he said in his evidence that the appellant sold it for two reasons (1) because it was becoming less productive as an investment with the increasing land tax and municipal rates and (2) to put the appellant's assurance fund in a healthier position. The sale was for £125,000; the appellant had paid £70,000 for it in 1935. Of the selling price of £125,000, £100,000 was allowed to remain on mortgage at four per cent; the balance was paid in cash and invested at four and one-half per cent. This " switching " of investment gave the appellant a surer if not a greater return, whilst at the same time the appellant's assurance fund was strengthened for the purposes of the *Life Insurance Act* 1945.

It is not necessary to state fully how the proceeds were entered in the accounts of the appellant: it is sufficient to say that they were entered as any item of revenue would be, and that they contributed to a surplus out of which a bonus was credited to policy holders and a dividend declared. Notwithstanding this it was submitted for the appellant that even if the Strand Building was purchased in 1935 solely as an investment still the proceeds of sale in 1948 were not assessable income, as it was not purchased with a view to re-sale at a profit, but with a view to retaining it indefinitely for the sake of the revenue it produced by way of rents, and that it was sold only when that revenue had fallen to a low level. Mr. Higman said that the appellant had thirty freehold properties, including flats, and had sold only six of them between 1939 and 1953, and then only for special reasons, such as the closure of the appellant's premises in one instance and trouble with tenants in others.

I have no hesitation in finding that the Strand Building was not purchased for re-sale at a profit; I find that the appellant intended

to retain it as long as it proved to be a profitable investment. But even so I think the proceeds of the sale in 1948 were assessable income for the reasons that the proceeds of the stock and debentures, sold and matured, in *Colonial Mutual Life Assurance Society Ltd.* v. *Federal Commissioner of Taxation* (1) were held to be assessable income, that is to say, as a profit within the meaning of the second limb of s. 26 (*a*), or alternatively as a profit according to the ordinary usages and concepts of mankind. There, as here, the policy of the taxpayer was to hold its securities as investments and not to traffic in or make profits from realizing them, and the mode of operation as well as the statutory obligations were similiar. It is true that "every word of every judgment must be read *secundum subjectam materiam*" (*The Commonwealth* v. *Bank of New South Wales* (2)), i.e. as referring to stock and debentures in the *Colonial Mutual Life Society's Case* (3) and not to freeholds. Still there are observations in the judgment in that case that are of general application, as I understand them, and that point to the proper solution of the problem here. Their Honours say: "Prima facie the depreciation in or accretion to the capital value of a security between the date of purchase and that of realization is a loss of or accretion to capital and is therefore a capital loss or gain and does not form part of the assessable income: *Lomax* v. *Peter Dixon & Son Ltd.* (4). But in the words of the Lord Justice Clerk in *Californian Copper Syndicate* v. *Harris* (5) which have been so often quoted, 'it is equally well established that enhanced values obtained from realization or conversion of securities may be so assessable, where what is done is not merely a realization or change of investment, but an act done in what is truly the carrying on, or carrying out, of a business'" (6).

For the purposes of this reasoning I see no difference in principle between freeholds and other investments, that is to say, when the freeholds are purchased *as investments* and not for office accommodation or like purposes of the company. Again (7) their Honours refer to *Northern Assurance Co.* v. *Russell* (8), and more particularly to the passage in which the Lord President of the Court of Exchequer of Scotland laid down certain propositions as useful guides for the Tax Commissioners, including the proposition that where the gain is made by the company by realizing an investment at a larger price than was paid for it, the difference is to be reckoned among the

(1) (1946) 73 C.L.R. 604, at p. 621.
(2) (1950) A.C. 235, at p. 308; (1949) 79 C.L.R. 497, at pp. 637, 638.
(3) (1946) 73 C.L.R. 604.
(4) (1943) K.B. 671.
(5) (1904) 5 Tax Cas. 159, at p. 166.
(6) (1946) 73 C.L.R., at p. 614.
(7) (1946) 73 C.L.R., at p. 616.
(8) (1889) 2 Tax Cas. 571.

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profits and gains of the company (1). Here again there is no difference in principle between freeholds and other investments. Then (2) their Honours refer to the speech of Lord *Shaw* in *Liverpool and London and Globe Insurance Co.* v. *Bennett* (3), where his Lordship said that the propositions laid down by the Lord President had never been judicially controverted as a correct guide, and their Honours proceeded to add that Lord *Shaw's* insistence upon the correctness of the propositions " tends to show that the sounder view is that profits and losses on the realization of investments of the funds of an insurance company should usually be taken into account in the determination of the profits and gains of the business " (4). Now I am unable to see why there should be a departure from the usual course in this case, as I find that the Strand Building was not purchased for the office purposes of the appellant but solely as an investment. Again Mr. Higman admitted to Mr. Trebilco that within three years of its purchase the Strand Building had in any event become an ordinary investment because when the Astoria Building was purchased in 1938, the Strand Building was no longer required for office purposes of the appellant, even if, contrary to my finding, it had been acquired by the appellant for those purposes as well as an investment. Moreover, the Strand Building was sold for a reason for which any investment might be sold, i.e., because it was more profitable to " switch " to another investment, and the proceeds of sale were applied to strengthen the position of the appellant in relation to its liabilities under the *Life Insurance Act* 1945, and to swell the surplus against which a bonus was credited to policy holders and a dividend to the shareholders declared. To employ the language of *Evatt* J. in *Forwood Down & Co.* v. *Commissioner of Taxation* (*W.A.*) (5), in all the circumstances the transaction of buying and selling the Strand Building was I think sufficiently related to the appellant's business of life assurance to bring the profits into tax.

The appeal is dismissed and the assessment confirmed.

The appellant will pay to the respondent his costs of the appeal.

Appeal dismissed : assessment confirmed. Appellant to pay respondent his costs of the appeal.

Solicitors for the appellant : *John A. K. Shaw, Lewis & Co.*

Solicitor for the respondent : *H. E. Renfree*, Crown Solicitor for the Commonwealth.

J. B.

(1) (1889) 2 Tax Cas., at pp. 577, 578.
(2) (1946) 73 C.L.R., at p. 617.
(3) (1913) A.C. 610, at p. 617.
(4) (1946) 73 C.L.R., at p. 618.
(5) (1935) 53 C.L.R. 403, at p. 408.