NO. 655.—HIGH COURT OF JUSTICE (KING'S BENCH DIVISION).—20TH MAY, 1927.

COURT OF APPEAL.—1ST, 4TH, 5TH, 6TH AND 15TH JULY, 1927.

HOUSE OF LORDS.—13TH AND 14TH FEBRUARY, 1928.

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1. THE REES ROTURBO DEVELOPMENT SYNDICATE, LIMITED *v.* DUCKER (H.M. INSPECTOR OF TAXES).(1)

2. THE REES ROTURBO DEVELOPMENT SYNDICATE, LIMITED *v.* THE COMMISSIONERS OF INLAND REVENUE.(1)

Income Tax, Schedule D—Excess Profits Duty—Sale of patents—Profits of trade or realisation of capital assets.

The Appellant Company was formed in 1906 *for the purpose,* inter alia, *of acquiring patents, inventions and the like, and of using them, granting licences in respect of them, selling them or otherwise turning them to account.*

Throughout the Company's existence their only assets had been one particular group of patents, and the receipts brought into their Profit and Loss Account had been made up of royalties for the use of these patents, interest, etc. It was shown that the Company had never originated an offer to sell foreign patent rights but that foreign manufacturers usually required to be given an option to purchase as a condition of agreeing to take a licence to manufacture. In 1917 *the Appellant Company granted a licence, with option to purchase, to a foreign company who exercised the option. The Special Commissioners decided, on appeal, that the profits on sale of patents arose in the course of the Appellant Company's business and were chargeable to Income Tax and Excess Profits Duty.*

Held, *that there was evidence on which the Commissioners could come to their decision.*

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(1) Reported C.A., [1928] 1 K.B. 506; and H.L., [1928] A.C. 132.

CASES.

1. *The Rees Roturbo Development Syndicate, Limited* v. *Ducker.*

CASE

Stated under the Income Tax Act, 1918, Section 149, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the King's Bench Division of the High Court of Justice.

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 9th December, 1924, for the purpose of hearing appeals, the Rees Roturbo Development Syndicate, Ltd. (hereinafter called the Appellant Company), appealed against assessments to Income Tax in the sums of £7,500 for the year ending 5th April, 1920, £6,161 for the year ending 5th April, 1921, and £5,340 for the year ending 5th April, 1922, made upon the Appellant Company by the Additional Commissioners of Income Tax for the Seisdon Division of the County of Stafford, under the provisions of the Income Tax Acts.

2. The Appellant Company was incorporated under the Companies Acts on the 4th October, 1906, with a share capital of £30,000, and with the following objects (inter alia) :—

(*a*) To purchase or by other means acquire, and protect, prolong, and renew, whether in the United Kingdom or elsewhere, any patents, patent rights, brevets d'invention, licences, protections and concessions which may appear likely to be useful or advantageous to the Company, and to use and turn to account and to manufacture under or grant licences or privileges in respect of the same, and to expend money in experimenting upon and testing and in improving or seeking to improve any patents, inventions or rights which the Company may acquire or propose to acquire, and in particular to acquire from Edmund Scott Gustave Rees, of Dunscar, Oaken, near Wolverhampton, in the County of Stafford, electrical engineer, and Thomas Parker, Ltd., the benefit of certain existing inventions in relation to centrifugal turbine and similar pumps, and with a view thereto, to to enter into and carry into effect the agreement referred to in Article 2 of the Articles of Association of this Company with such modifications (if any) as may seem expedient.

(*f*) To improve, manage, develop, exchange, let on lease or otherwise, mortgage, sell, dispose of, turn to account, grant rights and privileges in respect of, or otherwise deal with all or any part of the property and rights of the Company. A copy of the Memorandum and Articles of Association of the Appellant Company (marked A) is attached hereto and forms part of this Case.(1)

3. Early in 1906 the said Edmund Scott Gustave Rees made and patented an invention consisting of improvements in centrifugal turbine and similar pumps and further developments of the invention were subsequently patented by him. The first patent was dated February, 1906, and was numbered 4810, and the whole series of patents related to one invention, the fundamental basis of which was the Roturbo principle. The word " Roturbo " was also registered as a trade mark and the new type of pumps was named and became known and is still known as the Rees Roturbo Pump.

4. The said Edmund Scott Gustave Rees was also managing engineer and director of Thomas Parker, Ltd., a company carrying on the business of electrical engineers. The business of Thomas Parker, Ltd., was restricted owing to lack of capital and when the said Edmund Scott Gustave Rees invented the pump in 1906 he desired to extend that business by granting to Thomas Parker, Ltd., an exclusive licence to manufacture the pump. As however he was not satisfied with the financial stability of that company, he was unwilling to transfer the ownership of the patents to it and he accordingly caused the Appellant Company to be formed for the purpose of taking over the existing patents and all future development patents based on the Roturbo principle, and of providing additional working capital for Thomas Parker, Ltd.

5. By an agreement dated the 22nd October, 1906 (a copy of which, marked B, is attached hereto and forms part of this Case(1)) being the agreement referred to in Article 3 (*a*) of the Memorandum of Association and Article 2 of the Articles of Association of the Appellant Company, after reciting that by an agreement dated the 28th May, 1906, the said Edmund Scott Gustave Rees had agreed to grant a licence to Thomas Parker, Ltd., to use a certain patent numbered 4810 for improvements in centrifugal turbine and similar pumps for which provisional protection had been granted to the said Edmund Scott Gustave Rees it was agreed that the said recited agreement should be cancelled and that the said Edmund Scott Gustave Rees and Thomas Parker, Ltd., should sell and the Appellant Company should purchase the benefit of the said patent and the benefit of all improvements on the invention to which that patent related, and two equal third parts or shares of and in any foreign

(1) Not included in the present print.

patents in respect of the said invention or improvements thereon, provided that the remaining one equal third part or share in such foreign patents should remain and be the absolute property of the said Edmund Scott Gustave Rees, and that the said Edmund Scott Gustave Rees and the Appellant Company should be tenants in common of such patents and the profits thereof in the shares aforesaid.

6. " Foreign " patents in relation to the said invention were granted to the said Edmund Scott Gustave Rees in respect of the following countries, amongst others, namely :—

France, Switzerland, Belgium, Germany, the United States of America and the Dominion of Canada.

7. The consideration for the sale effected by the last mentioned agreement was the sum of £29,000, viz., £500 for the interest in the patent and patent rights in each of the countries of France, Switzerland, Belgium, Germany and the United States of America, £500 for the interest in the said patent and patent rights in all other foreign or colonial countries, and £26,000 for the interest in the British patent. The said purchase price of £29,000 was to be paid and satisfied by the payment to the said Edmund Scott Gustave Rees of £2,000 in cash and the issue to him or his nominees of 5,500 fully paid up £1 shares in the Appellant Company and by the payment to Thomas Parker, Ltd., of £21,500 in cash or the issue to that company of fully paid up shares in the Appellant Company of the nominal value of the whole or any such part of the said sum of £21,500 as should not be paid in cash.

8. By a further agreement dated the 22nd October, 1906, made between the Appellant Company and Thomas Parker, Limited, and which was entered into in pursuance of a proviso in that behalf contained in the agreement mentioned in paragraph 5 hereof it was provided that Thomas Parker, Ltd., should during the term of the patents have the sole right of manufacturing and should manufacture for the Appellant Company all pumps, turbines or other machines required for use in the United Kingdom, the Channel Islands, the Isle of Man, the Colonies or foreign countries subject to any agreement for sale of the foreign patents thereafter made by the Appellant Company and which could or might be manufactured under the patents. For the purposes aforesaid but no further Thomas Parker, Ltd., might exercise and use the rights vested in the Appellant Company under the patents and might vend such articles in the United Kingdom, the Channel Islands or elsewhere unless the Appellant Company should have sold the patent rights. Thomas Parker, Ltd., was to pay all costs of manufacture, and was to have the sole and exclusive control of the sale and disposition of all pumps turbines machines and goods manufactured under the

provisions of the agreement, and was generally to act as the sole and exclusive agent for the sale of such articles and was to defray all the costs of sale. The Appellant Company was to bear the expenses of protecting, maintaining and renewing the patents or obtaining patents for improvements on or development of the invention. The gross profits were to be divided and paid as to two-thirds to Thomas Parker, Ltd., and as to one third to the Appellant Company where the gross profit was forty per cent. or less on the selling price, and if the gross profit on any pumps or articles should exceed forty per cent. on the selling price, Thomas Parker, Ltd., was to retain one-third of such excess profit and to pay two-thirds to the Appellant Company. So long as Thomas Parker, Ltd., was able to meet the demands with reasonable despatch the Appellant Company was not to grant to any other person a licence to use and exercise the invention or any improvements or alterations thereof in the United Kingdom, the Channel Islands and the Isle of Man. A copy of the said agreement marked " C " is attached hereto and forms part of this Case.(1)

9. In 1908 a new Company, the Rees Roturbo Manufacturing Co., Ltd., was formed, with the said Edmund Scott Gustave Rees as managing director, to take over the business of Thomas Parker, Ltd., including the licence to manufacture pumps, and since that time this Company has carried on the whole manufacture of the pumps in the United Kingdom and the sale of the pumps in the United Kingdom or elsewhere except as regards countries for which exclusive licences have been granted to other concerns or the foreign patents have been sold.

10. The Appellant Company has obtained further patents both in the United Kingdom and abroad, but they have all related to the original invention or improvements and development thereof, and throughout the Appellant Company's existence its assets have consisted entirely of this group of patents and investments, and the receipts brought into its profit and loss accounts have been made up of royalties for the use of the patents, interest, and such incidental receipts as transfer fees. The Appellant Company has in fact never acquired or held or attempted to acquire or hold any patents whatever other than patents relating to Rees Roturbo pumps and certain ancillary or incidental patents relating to Roturbo condensers.

11. The development of the patents by the granting of manufacturing licences has always been the main business of the Appellant Company, although the possibility of the sale of foreign patents or rights has always been contemplated by the Appellant Company in respect of such interest as it possessed in the foreign patents, as

(1) Not included in the present print.

is shown by the following extracts from the Directors' Reports submitted to the shareholders at annual general meetings :—

Report for 1907.—" As a proof of the interest excited by the " Roturbo pump, a number of applications have already been " received from leading engineering firms in England for " manufacturing rights, and also applications for selling " agencies in foreign countries. In the initial stages, the " directors do not propose to grant manufacturing licences. As " the detail patents are developed, it may be advisable to make " arrangements for the granting of licences so as to increase the " business as rapidly as possible . . . .

" The directors have been approached with regard to the " sale of some of the foreign patents, and negotiations are in " progress."

Report for 1908.—" Negotiations are still pending for the " sale of manufacturing rights of Roturbo Patents in foreign " countries and the Colonies, but the directors have hitherto not " considered it policy to hurry these negotiations as each year " in the early stages of development makes them more valuable, " due to the larger amount of practical work done, which is " necessary before a fair estimate of their value can be " determined.

" These negotiations at the present time cover America, " Canada, France, Belgium and other Continental countries " and pumps have been running for some considerable time " very satisfactorily in these countries to demonstrate the " advantages secured under the Patents."

Report for 1909.—" The year just ended shows a very satis- " factory development and increase in the sales machinery " under the patents owned by this Syndicate. A large amount " of experimental work has been done, and the results of this " work are secured under further patents taken out during the " twelve months. A satisfactory feature of the rapid increase " of the output of the Rees Roturbo machines is the opening " out of foreign and Colonial markets."

Report for 1911.—" The development of the Company's " property during the year has been in every way satisfactory. " New and important patents have been added to the group " controlled by the Syndicate, and further patents are " pending.

" The directors are glad to be able to report that after " negotiations extending over a considerable period they have " concluded an important agreement with Messrs. Krupp of " Germany, for manufacturing rights of the Rees Roturbo " patents in that country. It is intended to issue further " licences on the Continent of Europe in the various countries

" covered by these patents, and for the control of these licences, " when a sufficient number of firms are secured, it is intended " to form a supplementary Company in Hamburg, which will " be controlled by this Syndicate. . . . .

" Since the closing of the account, the directors have also " concluded a satisfactory sole licence agreement with a firm " in the United States of America, having works suitable in " every way for the manufacture of Rees Roturbo machinery. " . . . . The American licence carries the option of purchase " outright within a period of three years. Otherwise a " minimum royalty is guaranteed during the life of the " patents."

Report for 1912.—" The development of the Company's " property during the year has been highly satisfactory. . . . . " The supplementary Continental Company referred to in the " last report has now been registered in Hamburg under the " title of the Continentale Rees Roturbo Gesellschaft, and " licences for manufacturing in the various countries of Europe " are being dealt with through the Continental Company."

Report for 1913.—" The output of plant manufactured " under the patents in England show a steady progress year by " year, and the various foreign businesses connected with the " Company are establishing themselves on a firm basis."

Report for 1914.—" The output of plant manufactured " under the patents in England shows a slight decrease com- " pared with last year due to the dislocation of business caused " by the War. Your directors consider it advisable to write off " all the expenditure incurred in connection with the formation " of a Continental Company."

Report for 1915.—" The development of the business of our " licences in the United States of America is progressing " satisfactorily."

Report for 1918.—" The rights for sole manufacture in the " United States of America have been disposed of to the " original licensees and the new licensees for manufacture of " Rees Roturbo machines in Canada are making satisfactory " progress. Since the issue of the last balance sheet satis- " factory arrangements have been made for the manufacture " under royalty in France."

12. The said Edmund Scott Gustave Rees stated in evidence and we accepted his evidence that the Appellant Company had never originated offers to sell the foreign patents or to grant licences thereunder to foreign manufacturers, but applications for licences had been received from abroad and the experience of the Appellant Company was that the foreign manufacturers usually required to be

given an option of purchase as a condition of agreeing to take a licence. In any case where the Appellant Company had granted an option of alternate purchase the option price was purposely fixed at a high figure which it was thought would be prohibitive. Messrs. Krupp had refused to enter into a manufacturing agreement unless a syndicate was formed with its head office in Hamburg to take over the German patents, but it was intended that this syndicate should be controlled by the Appellant Company. The said Edmund Scott Gustave Rees was at all relevant times owner in his own right of the one-third share in the foreign patents.

13. By an agreement dated the 15th March, 1912 (a copy of which marked D, is attached to and forms part of this Case(1)), the Appellant Company and the said Edmund Scott Gustave Rees agreed to grant to the Manistee Iron Works Company of Manistee, Michigan, in the United States of America (hereinafter called the Manistee Company) an exclusive licence to manufacture and sell pumps and other articles under the American and Canadian patents within the United States of America and Canada for all the unexpired residue of the terms of the patents and any prolonged or extended terms thereof in consideration of a payment of £10,000 to the licensors and royalties at the rate of 10 per cent. on the selling price of all articles made, with guaranteed minimum royalties of £2,000 during 1913, £3,000 during 1914, £4,000 during 1915, and £5,000 during 1916 and every subsequent year, the Manistee Company being precluded from exporting either directly or indirectly to the United Kingdom or certain other specified countries. The licensors retained the right by notice in writing to determine the licence in the event of failure to pay the royalties or other breach of the terms of the agreement and thereby the said licence and all rights of the Manistee Company thereunder were forthwith to cease and determine. The Manistee Company was also given the option to purchase the American and Canadian patents for £45,000 at any time before the 30th June, 1912, or for £50,000 at any time between the 30th June, 1912, and the 31st December, 1914. On the same date a licence was granted to the Manistee Company in accordance with the terms of such agreement.

14. Under the agreement mentioned in the preceding paragraph the Manistee Company made the stipulated payment of £10,000 of which £6,000 was received by the Appellant Company in 1912. Of this sum £750 was absorbed by expenses, £1,000 was taken to the credit of the Appellant Company's profit and loss account, and £4,250 was placed to reserve. The Manistee Company did not exercise its option to purchase the American and Canadian patents and it failed to pay the minimum royalties, but the Appellant Company was satisfied with the efforts made by it to develop the business in America, and allowed the licence to continue in force

(1) Not included in the present print.

and the royalties to accumulate. By the end of 1916 the arrears of royalties due from the Manistee Company amounted to £13,500. These royalties were not brought into the Appellant Company's accounts in any form.

15. The Appellant Company and the said Edmund Scott Gustave Rees were desirous of recovering the right to use the patents in Canada and in January, 1917, they entered into a supplemental agreement with the Manistee Company, a copy of which, marked E, is attached hereto, and forms part of this Case(1). This supplemental agreement after reciting that the Manistee Company had failed to carry out and perform certain obligations set forth in the agreement of 15th March, 1912, and was in default thereunder and had requested the licensors to refrain from enforcing their rights, confirmed the said agreement except as amended or altered by the supplemental agreement, and provided that the Manistee Company should pay the licensors a minimum royalty of £416 per month during the balance of the term of the said agreement, and that so long as the Manistee Company should not be in default in paying the royalties and should not fail to perform any of its obligations from and after the 1st January, 1917, the licensors should hold the accrued and unpaid royalties due to them, then amounting to £13,500, in suspense and refrain from enforcing their rights, and the unpaid royalties should be liquidated at the rate of £2,250 per annum over a period of six years. The Manistee Company surrendered all its rights and interest to the use of Canadian territory and to Canadian licences and patents, but in the event of the Manistee Company continuing to fulfil the terms thereof and of the contract thereby amended the Manistee Company should continue to hold an option to purchase the United States patent rights outright at any time before 1st January, 1918, for the sum of £26,500. In the event of such outright purchase all claims for accrued royalties owing up to 1st January, 1917, were to be cancelled and considered and treated by the licensors as paid and liquidated.

16. The Manistee Company paid the royalties accruing due during 1917, and then exercised its option to buy the American Patents for the sum of £26,500. The royalties received by the Appellant Company were brought into its profit and loss account. Of the sum of £26,500 paid for the American patents £2,653 was paid to an agent in America, £7,949 to the said Edmund Scott Gustave Rees, and the balance of £15,898 was received by the Appellant Company. This sum was not included in the Appellant Company's profit and loss account but (after deduction of £333 for special expenses incurred in connection with the sale) was written off the value of patents in the balance sheet. In 1922, by Special Resolution passed on the 14th July and confirmed on the 31st July

(1) Not included in the present print.

(a copy of which is included in the attached copy of the Memorandum and Articles of Association) the Appellant Company reduced its paid up capital under Section 40 of the Companies (Consolidation) Act, 1908, by returning out of accumulated profits a sum equal to 95 per cent. of the capital paid up on its shares.

17. By an agreement dated the 11th January, 1918 (a copy of which marked F is attached hereto and forms part of this Case(1)) the Appellant Company and the said Edmund Scott Gustave Rees granted to the Goldie and McCulloch Co., Ltd., of Galt, Ontario, an exclusive licence to manufacture and sell pumps and other articles comprised in the Canadian patents within the Dominion of Canada in consideration of the sum of $5,000 and a royalty at the rate of 10 per cent. on the selling price of all vacuum pumps condensers and air compressors and at the rate of 6 per cent. on the selling price of all water pumps and other articles manufactured and sold under the patents or licence, subject to the right of the licensors to grant a licence to one other party for the Dominion of Canada in case the royalties paid in any one year should be less than certain minimum amounts. It was further provided that when the total amount of the royalties paid, together with compound interest thereon at 5 per cent. per annum should have reached the total amount of $90,000 together with compound interest thereon at 5 per cent. per annum, then all further royalty payments should cease and the licensors should transfer and assign all their right title and interest to the Canadian patents to the Goldie and McCulloch Company. In the event of failure to pay the royalties or other breach of the terms of the agreement the licensors retained the right by notice in writing to determine the licence and thereupon the licence and all rights of the Goldie & McCulloch Company thereunder should cease and determine.

18. By an agreement dated the 12th June, 1919, a copy of which marked G is attached hereto and forms part of this Case(1), the Appellant Company and the said Edmund Scott Gustave Rees granted to La Société des Moteurs Gnome et Rhone of Paris an exclusive licence to manufacture and sell water pumps and other articles under the French patents within the Republic of France and the colonies thereof in consideration of the sum of 130,000 francs and a royalty at the rate of 5 per cent. on the selling price of all condensers air pumps and compressors and 4 per cent. on centrifugal pumps manufactured under the licence, subject to the right of the licensors to grant licences to other manufacturers in France if the royalties paid should be less than certain minimum amounts. It was further provided that when the total amount of the royalties paid, together with compound interest thereon at 5 per cent. per annum, should have reached the total amount of

(1) Not included in the present print.

625,000 francs (£25,000 sterling) together with compound interest thereon at 5 per cent. per annum, then any further royalties should be at the rate of 2 per cent. on the selling price of all articles manufactured and sold under the French patents or the licence. If the royalties should be unpaid or there should be other breach of the terms of the agreement the licensors should be at liberty by notice in writing to determine the licence.

19. Copies of the accounts, balance sheets and reports of the directors of the Appellant Company for the years 1907 to 1922 inclusive are attached hereto and form part of this Case.(1)

20. The royalties received by the Appellant Company in respect of its patents from the date of its incorporation to the 31st December, 1923, were as follows :—

Period.	*British.* £ s. d.	*Foreign.* £ s. d.	*Total.* £ s. d.
4th October, 1906, to 31st December, 1917	444 16 9		444 16 9
Year ended 31st December, 1908	1,470 17 6		1,470 17 6
1909	2,585 15 0		2,585 15 0
1910	2,820 10 2		2,820 10 2
1911	2,538 17 1		2,538 17 1
1912	3,139 1 4		3,139 1 4
1913	4,378 17 0		4,378 17 0
1914	3,877 15 5		3,877 15 5
1915	3,702 6 0		3,702 6 0
1916	3,750 0 0		3,750 0 0
1917	3,750 0 0	3,083 0 1	6,833 0 1
1918	3,750 0 0	2,207 18 0	5,957 18 0
1919	3,750 0 0	230 12 7	3,980 12 7
1920	8,108 14 0	526 15 9	8,635 9 9
1921	14,539 2 7	602 10 4	15,141 12 11
1922	2,100 15 11	470 2 4	2,570 18 3
1923	476 14 2	812 2 2	1,288 16 4

21. The sole question on which the opinion of the Court is desired is whether the sum received by the Appellant Company from the Manistee Company on its exercising its option to buy the American patents as stated in paragraph 16 of this Case, or any part thereof, was a profit of the Appellant Company's business in respect of which it was assessable to Income Tax. The Appellant Company, while not admitting liability in respect of the sums received from the Goldie & McCulloch Co., Ltd., and La Société

(1) Not included in the present print.

des Moteurs Gnome et Rhone as stated in paragraphs 17 and 18 of this Case, did not press its objection to the inclusion of these sums in the computations on which the assessments were based.

22. It was contended on behalf of the Appellant Company :—

(*a*) That the patents sold to the Manistee Company were capital assets of the Appellant Company.

(*b*) That the Appellant Company in selling these patents was realising a part of its capital assets.

(*c*) That the Appellant Company had not made a business of buying and selling patents but had acquired only a part share as tenants in common of a single group of patents relating to one invention and improvements thereof with the main object of holding such patents and obtaining an income from royalties for the use of them.

(*d*) That the sum received from the Manistee Company was not as a whole or in regard to any part thereof a profit of its trade or business in respect of which it was assessable to Income Tax or Excess Profits Duty.

23. It was contended on behalf of the Crown (inter alia) :—

(*a*) That the sum of £26,500 received from the Manistee Company was a receipt of the Appellant Company's business and as such assessable to Income Tax.

(*b*) That the assessments appealed against were in this respect correct and should be confirmed.

24. We, the Commissioners who heard the appeal, after considering the facts and arguments put before us gave our decision on the 18th March, 1925, that the profits on sale of patents arose in the course of the Appellant Company's business and were chargeable to Income Tax and Excess Profits Duty, and we amended the assessments to amounts which upon this basis, were agreed between the parties to be correct as a matter of figures.

25. The Appellant Company immediately upon the determination of the appeal declared to us its dissatisfaction therewith as being erroneous in point of law and in due course required us to state a Case for the opinion of the High Court pursuant to the Income Tax Act, 1918, Section 149, which Case we have stated and do sign accordingly.

P. WILLIAMSON, } Commissioners for the Special
MARK STURGIS, } Purposes of the Income Tax Acts.

York House,
23, Kingsway,
London, W.C.2.
10th February, 1927.

2. *The Rees Roturbo Development Syndicate, Limited* v. *The Commissioners of Inland Revenue.*

This case related to assessments to Excess Profits Duty made upon the Appellant Company for the accounting periods ending 31st December, 1918, and 31st December, 1920. The assessments were in respect of the same profits as the Income Tax assessments, and the Case was stated in like terms, *mutatis mutandis*.

The cases came before Rowlatt, *J.*, in the King's Bench Division on the 20th May, 1927, when judgment was given in favour of the Crown, with costs.

Mr. A. M. Latter, K.C., and Mr. J. H. Bowe appeared as Counsel for the Company, and the Solicitor-General (Sir Thomas Inskip, K.C.) and Mr. R. P. Hills for the Crown.

JUDGMENT.

Rowlatt, J.—This is one of those cases which raise great difficulty in applying a principle which in itself is perfectly clear. It has been said before in this Court, and in more important Courts, and it is perfectly clear, that where profit accrues from the sale of property a question arises whether that forms the basis of liability to Income Tax. Now Income Tax is not attracted by the mere circumstance that there is a profit; because the profit may be a mere accretion of the value of the article, and the profit may not accrue in the course of any trade at all. On the other hand the circumstance that the profit is due to an accretion in the value of the article does not negative the application of Income Tax, because the accretion of value to the article may have been the very thing that a trade within Case I was established to secure. In that case you have a trade which is going to be in articles with a view to securing the accretion of value to those articles, and the accretion of value does not negative the incidence of Income Tax. Nor does the circumstance that the accretion of value can be described as an accretion of capital in one sense; because you may have an adventure, such a case as the recent linen case(1), and such a case as of companies which are formed to nurse assets, salvage companies of all sorts; you may have a case where the whole capital of the concern is put into property, and the whole object of the concern is to sell that property at a higher price; and if the accretion of value comes about, it affects the assets that represent the whole capital of the company, and it is profit of trading in the

(1) Martin *v.* Lowry, 11 T.C. 297.

(Rowlatt, J.)

clearest possible way. But if it is an accretion of value of what is described as a capital asset, of course the matter is different. In one sense the words " capital asset " are words of art, because you do not have one set of assets representing capital and another sets of assets representing income, of course; but what is meant by the phrase " capital asset " is that this is an asset which represents fixed capital as opposed to circulating capital, that is to say, that this is an article which is possessed by the individual in question, not that he may turn it over and make a profit by the sale of it to his advantage, but that he may keep it and use it and make a profit by its use. Then if an article of that sort is sold at a profit, that profit is not a profit of trade. For instance, if a bank or a mercantile company finds it is more expensively housed than it needs, and sells its counting house and its offices, that is not part of the business of banking; and any profit which comes does not come into its profit and loss account, it is represented in the diminution of assets grouped as Premises, and so on, in its accounts.

Now that is all perfectly clear. The trouble that arose in the case of *Collins* v. *Firth-Brearley Stainless Steel Syndicate, Ltd.*, (9 T.C., page 520) arose because I misunderstood the findings of the Commissioners in that case. They found that the amounts realised were an appreciation of capital. If they had said an appreciation of a capital asset I should have known quite well that they meant an appreciation of fixed capital. When they said it was an appreciation of capital I thought they meant that they were finding that the accretion had occurred in the course of trade, and if you get an accretion of value of property which arises in the course of trade which it is the object of the trade to secure, of course it is a trade profit, although it is appreciation of capital in the sense that it is an appreciation of an asset which is there to answer capital. That is what I thought was the case, but the Court of Appeal pointed out that when the phrase in the finding of the Commissioners is read with the contentions, it appears that what they meant to find was that this was an appreciation of a capital asset, that is to say, an appreciation of an asset which was not intended to be turned over and sold in the sense of trade, but was intended to be kept and used, the trade being limited to something exclusive of selling this particular piece of property; and on those grounds they decided the other way. I did not intend to reverse the findings of the Commissioners in that case, in the least. I misunderstood what their finding was. That is the explanation of that.

(Rowlatt, J.)

Now I have to apply the finding in this case. It is really lamentable that these cases are beginning to turn on nice pleading distinctions really, upon the findings, and I do hope that Commissioners, both Special and General, will express themselves definitely. It is not rude to find the contrary to somebody's contention. If they find against somebody's contention it is much better to say so perfectly plainly and to express it, and not to take refuge in a possibly not very clear intermediate phrase which may leave open to argument whether it negatives or affirms the particular contention.

Now what happened is this. The Appellant Company contended that the patents sold were capital assets. That is perfectly clear. That in selling these patents it was realising a part of its capital assets. It is perfectly clear what that means: that the Appellant Company had not made a business of buying and selling patents but acquired in them a part share. That is an argument. Then (*d*) " That the sum received from the Manistee " Company was not as a whole or in regard to any part thereof " a profit of its trade or business in respect of which it was " assessable to Income Tax or Excess Profits Duty ". I read that in this way: If these patents were capital assets and the sale of them was realising capital assets, then the sum received was not a profit of its trade or business. What I think is that they affirm the affirmative there contended for, and they negative the contrary. That is what I think it is. I think (*d*) is putting the contrary to (*a*) and (*b*). There it was contended on behalf of the Crown that the sum received was a receipt of the Appellant Company's business—it would have been better if they had said " trade or business "—was a profit earned in the trade or business. They ought to have said that; they said " a receipt of the " Appellant Company's business." What was meant ? It cannot mean that it was a receipt of the Company. The only thing to deny or affirm is whether it is a receipt in respect of the business that the Company was carrying on, or whether it was a receipt in respect of a capital asset, as it is called, which it was selling. Those are the only two alternatives that have to be distinguished between, and when this contention is put forward on behalf of the Crown, I can only read it as being a contention that what was negatived in contention (*d*) of the subject is here affirmed on the part of the Crown, namely, that this was a receipt of the trade or business, in respect of which it is assessable to Income Tax. I think the Commissioners, although they again have not adopted quite the same words, found that fact. They say that the profits on the sale of patents arose in the

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course of the Appellants' business. I think that must mean in the course of the Appellants' business, not because they were getting rid of a capital asset and putting an end to it, but because it was in the course of their business to sell the patents. I cannot read what they find in any other way. So if it turns on what the Commissioners have found I think the Crown are entitled to hold this decision.

But then Mr. Latter says that there was not any evidence, that they have misdirected themselves or gone wrong in law in coming to this conclusion, that there was no evidence to support that view of the case, and the facts are all the other way. Paragraphs 10, 11 and 12 are the important ones in the Case. It is clear, so it is said, that they never had any other assets except this group of patents and investments, and that the receipts have always been of royalties, and so on, and that they never acquired any patents whatever other than these patents. That may be true. Of course that is a strong fact in a way, but it is not conclusive, as the linen case(1) showed among other things. Paragraph 11 is: "The development of the patents by the "granting of manufacturing licences has always been the main "business of the Appellant Company, although the possibility "of the sale of foreign patents or rights has always been con-"templated by the Appellant Company in respect of such interest "as it possessed in the foreign patents, as is shown by the "following extracts from the Directors' Reports submitted to the "shareholders at annual general meetings." When they discuss yearly throughout their career as to whether it would be a good thing to sell these things or not, and they always incline to the policy that it was better to hold them, and when they are compelled by business reasons to give an option of purchase they take care to put the price very high because they really do not want to sell them. That is quite true.

Then you come to paragraph 12. Mr. Rees stated in evidence, and his evidence was accepted, that he never originated offers to sell but that the option to buy was really forced upon them by their purchasers.

Frankly, I wish I could say that there was not any evidence to support the findings which I am obliged to find here, because I feel very uncomfortable about the *Firth-Brearley* case(2) being decided one way and this case being decided the other way—the facts are so very nearly the same. But when you have got

(1) Martin *v.* Lowry, 11 T.C. 297. (2) 9 T.C. 520.

(Rowlatt, J.)

liability to Income Tax dependent upon findings of fact and there are different tribunals who find those facts, the result of such things is unavoidable. I notice that although the Court of Appeal were inclined to agree in point of fact with the Commissioners as they read their findings in the *Firth-Brearley* case, still I think that certainly the Master of the Rolls at any rate indicates that they might have found the other way; and they certainly emphasise the circumstance that the finding of the Commissioners is not to be lightly disturbed.

Now I cannot say there is no evidence here. It is clear that those in charge of this Company thought their better policy was to keep these things and not to sell them. That may very well be, but I do not think that throws a very great deal of light upon it, because one may think that the first is the best way of doing business and another may think that the second is the best way of doing business, but both courses are doing business. That does not carry it very much further; undoubtedly all the time they got these patents they were working upon them, improving them, nursing them, advertising them, and so on. They might exhaust their value by having royalties from them all their life, they might, of course, sell them, although they did not think that was the most advantageous way to deal with them. Now the Commissioners have looked at it and they have decided the facts, and, as I say, rather to my regret, I do not think I can disturb their finding.

But Mr. Latter put one other observation, which struck me as rather forcible at first. He said: " How can these people be " treated as including in their business such a thing as the possible " sale of these patents, when they do not even own them all ? " I do not think that carries it any further there because, as the Solicitor-General pointed out, it is true they have not got all the interest in the patents. They share with Mr. Rees what the patents bring in, but they have got to give to these people options to buy these patents, and so they set to work and must arrange with Mr. Rees that that shall be done, and that if the option is exercised Mr. Rees will concur with them in executing the necessary documents, and so on. They work on that basis and they work with their two-thirds interest, and they finally, when they are asked to sell it, can sell it, and can sell it very well, and the money comes in. I do not see that that circumstance brings about the result that only one conclusion of fact is open to the Commissioners. I think it does not bring that result about, and I am afraid it does not help Mr. Latter.

(Rowlatt, J.)

All I can say is, I suppose the case will be taken to the Court of Appeal, and possibly they may see their way to put the two cases on the same footing, but I cannot see that I can do more than dismiss the appeals now, and that must be the order, with costs.

The Company having appealed against the decision in the King's Bench Division, the case came before the Court of Appeal (Lord Hanworth, *M.R.*, and Scrutton and Sargant, *L.JJ.*) on the 1st, 4th, 5th and 6th July, 1927, when judgment was reserved.

Mr. A. M. Latter, K.C., and Mr. J. H. Bowe appeared as Counsel for the Company, and the Solicitor-General (Sir Thomas Inskip, K.C.) and Mr. R. P. Hills for the Crown.

On the 15th July, 1927, judgment was delivered against the Crown, with costs (Scrutton, *L.J.*, dissenting), reversing the decision of the Court below.

JUDGMENT.

Lord Hanworth, M.R.—These two appeals are from judgments of Mr. Justice Rowlatt dated the 20th May whereby he confirmed the decisions of the Commissioners that the above-named Company was liable to pay Income Tax and Excess Profits Duty upon a sum of £15,898. The details of the figures are not in dispute and the full facts are stated in the Cases and in the judgment of Mr. Justice Rowlatt. For the purpose of this judgment it is enough to say that the Company contends that the above sum was not liable to Income Tax or to Excess Profits Duty, because it represents the Company's share of the sale price of the patent rights in the United States of America of the group of patents relating to centrifugal turbine and similar pumps which it was the purpose of the Company to acquire and to turn to account by granting licences or by sale. This is the sole question raised in the Case, although the dealings by the Company in other directions are stated for the purpose of giving full information upon its activities. To avoid any misconception, I say that in my judgment the group of patents which were acquired by the Company may be treated as the one patent which the Company was formed originally to acquire. The other patents which have been added to the original relate to devices subsidiary to the main one, and are dependent for their purpose and use upon the central invention, the fundamental basis of which was what is called the Roturbo principle.

(Lord Hanworth, M.R.)

It is claimed on behalf of the Company that what they have disposed of, in return for which they have received the £15,898, was a capital asset—that the transaction was a realisation of a part of their capital assets, and not a profit of their circulating capital. The Revenue authorities contended that it was a receipt and profit made in the course of carrying on the ordinary business of the Company and so chargeable to the tax and duty. Thus the question—which is the same in both cases—is the difficult one of deciding whether a profit realised belongs to the capital or profit and loss account.

The cases were heard in December, 1924, but the Commissioners delayed their decision until a judgment was delivered by Mr. Justice Rowlatt in the case of *Collins* v. *The Firth-Brearley Stainless Steel Syndicate, Limited*(1), which involved a similar question. That judgment was delivered by Mr. Justice Rowlatt on the 2nd March, 1925; and the Commissioners then gave their decision in the present cases on the 18th March, holding " that " the profits on sale of patents arose in the course of the Appellant " Company's business and were chargeable to Income Tax and " Excess Profits Duty." They followed the question put and answered affirmatively by Mr Justice Rowlatt in his judgment in the *Firth-Brearley* case, namely, whether the Company benefited by this appreciation in the course of its trade, with the same result as decided by Mr. Justice Rowlatt in the *Firth-Brearley* case, that the Syndicate was liable to the tax. That question so answered in the *Firth-Brearley* case was held in this Court, on the 25th June, 1925, not to have concluded the matter. The finding of the Commissioners in the present cases was not that the profit was realised as part of its ordinary trading, although interpreted to bear that meaning by Mr. Justice Rowlatt in his judgment now under appeal.

In the *Firth-Brearley* case in this Court, Lord Justice Atkin pointed out that it was necessary not only to determine that the Syndicate carried on a trade but also what was the scope of the trade(2): " For that purpose I think in order to examine the " facts you must look at what the Company purported to do, and " also at what it did in fact." Finally, upon an examination of the findings of the Commissioners, the Court of Appeal held that they had intended to find that upon the sale of the patent there was a transmutation of a capital asset from the form of a patent to a sum of money, and that upon that finding the Firth-Brearley Syndicate was not liable to Income Tax.

(1) 9 T.C. 520. (2) *Ibid.* at p. 573.

(Lord Hanworth, M.R.)

The present cases therefore come before this Court with a finding by the Commissioners which in itself is not sufficient. The scope of the trade in the course of which the profits on sale of patents arose is not examined or stated. Mr. Justice Rowlatt regretfully felt that he could not disturb the finding of the Commissioners, which he interpreted as meaning that the profits arose out of the Syndicate's trading and in the course of their seeking the objects of their ordinary business. It is unfortunate, as the learned Judge observes, that the question decided in the *Firth-Brearley* case and presented in the one before us involves such a nice examination of the language used, but it is not possible to do justice to the issues raised, and the decisions given, without it.

Two points arise for this Court to determine : (1) Is the question raised by the appeal one of fact, upon which the decision of the Commissioners is final, or one of law ? (2) Have the Commissioners rightly directed themselves in applying the law to the facts ? It is not necessary to go over again all the cases in which this problem of fact or law has been discussed. They are referred to in the decision of this Court in *Currie* v. *Commissioners of Inland Revenue*(1), [1921] 2 K.B. 332, particularly in the judgment of Lord Justice Scrutton who quotes the observation of Lord Parker in *Farmer* v. *Cotton's Trustees*(2), [1915] A.C. page 932, saying : " The views from time to time expressed in " this House have been far from unanimous." It is useful however, to observe that in *Currie's* case the question for the Court was whether a man was carrying on a profession. That was held to be one of fact. On the other side, in *The Commissioners of Inland Revenue* v. *Korean Syndicate*(3), [1921] 3 K.B. page 258 —which was decided in this Court and two members of it were those who had decided *Currie's* case—it was held that the Commissioners had misdirected themselves on a matter of law, namely, the true interpretation of an agreement and the Memorandum and Articles of Association of the company. Thus the Court felt able to reverse the decision of the Commissioners which had been upheld by Mr. Justice Rowlatt. I have come to the conclusion that the later decision applies to the present case. The circumstances under which the decision of the Commissioners was given confirm me in this view, for not only had the Commissioners to consider the Memorandum and Articles of Association of the Syndicate and the agreements made with the Manistee Company, dated the 15th March, 1912, and January,

(1) 12 T.C. 245. (2) 6 T.C. at p. 600. (3) 12 T.C. 181.

(Lord Hanworth, M.R.)

1917, but avowedly they waited for the guidance to be derived from the judgment of Mr. Justice Rowlatt in the *Firth-Brearley*(1) case, a judgment which was afterwards reversed.

Dealing with the case, therefore, as one open to review in this Court, it appears that the asset of the Syndicate, which was incorporated in 1906, was this group of Roturbo patents with the rights which accrued to them in foreign countries under international conventions. The facts as to the Syndicate's business for a succession of years are stated in Paragraph 11 of the Case. When the option to purchase the American rights was exercised by the Manistee Company in 1917, the Syndicate marked the distinction between the royalties paid to them for the user of the patent during 1917 and the sum received for the sale of the American rights, by bringing the former into their profit and loss account, and deducting the latter from the value of the patents in their balance sheet in 1918. In 1922 the Syndicate reduced their paid-up capital under Section 40 of the Companies Act, 1908. The Syndicate were not trading in buying and selling patents generally. They had secured these particular patents and patent rights which formed the totality of their assets. It was proved by evidence which the Commissioners accepted (see paragraph 12) that the Syndicate had never originated offers to sell the foreign patents.

If the Commissioners had had an opportunity of considering the judgment of this Court in the *Firth-Brearley* case(1), in my judgment they would, and ought to, have come to the conclusion that the sale of these U.S.A. patent rights was the transmutation of a capital asset into money. It was an out and out disposal of a right which, up to the date of the sale, enhanced the capital assets, and upon its transfer to the Manistee Company operated as a deduction from them. It was a substitution of one form of fixed capital assets for another, not a profit of circulating capital.

In the *Gloucester Wagon* case(2), [1925] A.C. 469, Lord Dunedin held that the selling of the wagons was an incident of buying and selling in the ordinary course of the business of the Company, for it was an integral part of the Company's business to deal in and sell wagons. The business was of a different nature here.

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(1) 9 T.C. 520. (2) 12 T.C. 720.

(Lord Hanworth, M.R.)

Holding, as I do, that the decisions of the Commissioners are open to review in this Court, I have come to the conclusion, which I gather that Mr. Justice Rowlatt would have desired to reach, that these appeals must be allowed and this sum of £15,898 must be treated as a capital asset.

The appeals will be allowed with costs and the assessments discharged.

Scrutton, L.J.—These two appeals by the Rees Roturbo Syndicate, Limited, one in respect of Income Tax, one in respect of Excess Profits Duty, raised the same point, whether the Syndicate were liable to taxation on the result of certain transactions in respect of their patents. The Special Commissioners held that the results were profits on the sale of patents arising in the course of the Syndicate's business, and as such were liable to taxation. Mr. Justice Rowlatt declined to interfere with what he considered to be a finding of fact by the Commissioners, and the Syndicate appeal.

The case is complicated by the fact that this decision of the Special Commissioners was pronounced after Mr. Justice Rowlatt had reversed a previous decision of theirs in a somewhat similar case(1), but before the decision of the learned Judge in that previous case had been reversed by the Court of Appeal. Mr. Justice Rowlatt's decision in the present case was, however, given with full knowledge of the decision of the Court of Appeal in the previous case.

I deal with the facts of the present case first. The Syndicate had a very large interest in a series of patents relating to centrifugal pumps and condensers both in England and foreign countries. As a company it was formed to acquire these patents, to manufacture them and to " sell, dispose of, turn to account, " grant rights and privileges in respect of . . . . . all or any part of " the property and rights of the Company." The Company desired if possible to exploit these patents by granting manufacturing licences in consideration of royalties, and to retain the ownership of the patents. But it was found that some foreign manufacturers would not agree to take a licence on payment of royalties, even an exclusive licence, unless they were also given an option to purchase the patents. Under those circumstances, besides a number of royalty licences in varying countries, these transactions are mentioned in the Case :—1. An exclusive licence to the Manistee Company for the United States and Canada in

(1) Collins *v.* The Firth-Brearley Stainless Steel Syndicate, Ltd., 9 T.C. 520.

(Scrutton, L.J.)

consideration of a cash payment of £10,000 and royalties of 10 per cent. on the selling price, with a guaranteed minimum, coupled with an option exercisable within fixed dates to purchase the United States and Canadian patents for a lump sum. The Manistee Company paid the £10,000 but not the minimum royalties, and ultimately another agreement was made by which the Manistee Company was excused royalties up to January 1st, 1917; and its option was changed into one to purchase the United States patents only for a sum of £26,500. The Manistee Company paid royalties for 1917, and then exercised its option, and £15,898 net was received by the Syndicate, and written by them off the value of the patents. This appears to be the sum in dispute in this case. I find it difficult to understand how part of this complicated transaction is in the course of business, and part not. 2. In 1918 an agreement was made with a Canadian company, by which an exclusive licence was granted to them to manufacture and sell Roturbo pumps within the Dominion of Canada in consideration of a payment of 5,000 dollars, a royalty on selling price with a guaranteed minimum, and a provision that when the royalties came to $90,000, all royalties should cease and the Canadian patents should be transferred to the Canadian company. 3. By an agreement of 1919, an exclusive licence was granted to a French company to manufacture and sell in France in consideration of 130,000 francs paid down, and royalties to be reduced when the royalties reached a certain amount.

In paragraph 21 of the Case it is stated that the Syndicate, while not admitting liability in respect of cases 2 and 3, did not object to the sums received under them being included in the assessment. The practical difference between an exclusive licence for a district and an assignment of the patent for that district is very small. The licensor cannot, having granted an exclusive licence, make any money out of the patent in the district of the licence except from the licensee under the licence. He does retain to himself the right to sue for infringements, which would pass to the assignee under an assignment of the patent, but in agreements 2 and 3 he binds himself to sue infringers in the licensed districts at his own expense. It does not appear to be disputed that the royalties would be proper subject matter of taxation, and it follows in the Canadian case that when, the royalties having reached $90,000, the patents were assigned to the licensee, the whole amount of the consideration for the assignment would have paid tax. The Syndicate have not objected to the lump sums in cases 2 and 3 being included in the taxation, and no

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question is apparently raised about the royalties or first lump sum in the Manistee case. The Syndicate have done sufficiently well in exploiting the patents to return 95 per cent. of their capital out of accumulated profits, which must all have been taxed as profits.

The line between receipts which are not taxable as being the result of sale of capital assets, and receipts which, though receipts of sale, are taxable as profits of trade is stated by Lord Dunedin in the Privy Council in *Commissioner of Taxes* v. *Melbourne Trust, Limited*, reported in [1914] A.C. 1001, at page 1010 as follows: " Their Lordships think that the principle is correctly " stated in the Scottish case quoted, *California Copper Syndicate* " v. *Harris*(1). ' It is quite a well settled principle in dealing " ' with questions of Income Tax that where the owner of an " ' ordinary investment chooses to realise it, and obtains a greater " ' price for it than he originally acquired it at, the enhanced " ' price is not profit in the sense of Schedule D of the Income " ' Tax Act of 1842 assessable to Income Tax. But it is equally " ' well established that enhanced values obtained from realisa- " ' tion or conversion of securities may be so assessable where " ' what is done is not merely a realisation or change of invest- " ' ment, but an act done in what is truly the carrying on, or " ' carrying out, of a business.' In the present case the whole " object of the company was to hold and nurse the securities " it held, and to sell them at a profit when convenient occasion " presented itself. Their Lordships therefore come to the con- " clusion that there is ample evidence here that the company is " a trading company and that the surplus realised by it by selling " the assets at enhanced prices is a surplus which is taxable as " profit." This case was followed by the Privy Council in *Rex* v. *Anderson Logging Company, Limited*, reported in [1926] A.C. 140. Illustrations of the two classes of cases as regards sale of land may be found in *Stevens* v. *Hudson's Bay*(2) (price of land not taxable), and *Thew* v. *South West African Co., Ltd.*(3) (price taxable as proceeds of trade). Cases of taxation on the profits of realisation by sale of one and the only asset will be found in *Martin* v. *Lowry*(4), reported in [1927] A.C. at page 312, and the *Cape Brandy Syndicate* v. *Inland Revenue Commissioners*(5), reported in [1921] 2 K.B. at page 403. This being the question to be decided, the Commissioners heard arguments from the Syndicate that the sum in dispute was a

(1) 5 T.C. 159. (2) 5 T.C. 424. (3) 9 T.C. 141.
(4) 11 T.C. 297. (5) 12 T.C. 358.

(Scrutton, L.J.)

realisation of capital assets, and from the Crown that it was a receipt of the Company's business, and decided that " the profits " on sale of patents arose in the course of the Syndicate's " business." If this is a finding of fact, it is unappealable if there was evidence on which the finding could be made, even if the Court would not have made such a finding. If it includes a finding of law, it is appealable on the law.

In my view it is impossible to reconcile the various statements of high authorities on the division between fact which is unappealable and law which is appealable. One may compare the view of Lord Parker in *Farmer* v. *Cotton's Trustees*(1), and Lord Wrenbury in *Great Western Railway* v. *Bater*(2)—which I think would make every finding of fact appealable on the ground that it was a question whether the Commissioners had rightly construed the statute or law which used the word in which they described the " fact "—with the views of the House of Lords in *American Thread Co.* v. *Joyce*(3) (reported in 106 L.T. at page 171 and 108 L.T. at page 353) affirming the judgment of Mr. Justice Hamilton, and in *Usher's Wiltshire Brewery, Limited* v. *Bruce*(4) (reported in [1915] A.C. 433, at page 465) negativing the view of Sir Samuel Evans that the question was one of law. I have myself twice expressed my views on the subject at some length, first in *Smith* v. *Incorporated Council of Law Reporting for England and Wales*(5), [1914] 3 K.B. 674, a decision which has several times been cited with approval in this Court and in the House of Lords, and secondly in *Currie* v. *Inland Revenue Commissioners*(6), [1921] 2 K.B. at page 343. In my view, the point at which sales of assets resulting in a profit are of such a number and nature as to constitute a trade or business, or the point when a sale of an asset is so connected with a trade carried on that profits received from it are profits of a trade, is a question of degree and of fact. How many sales of pictures will make a man a picture dealer is a question of degree. I agree with the view of Lord Justice Atkin in *Cooper* v. *Stubbs*(7), reported in [1925] 2 K.B. at page 772, that questions of degree are questions of fact, and that whether a trade is being carried on is a question of degree and fact. Looking at this case alone I think there was evidence on which the Commissioners could find that these profits arose in the course of a trade and business. The Syndicate were making profits out of

(1) 6 T.C. 590. (2) 8 T.C. 231. (3) 6 T.C. 1 and 163.
(4) 6 T.C. 399. (5) 6 T.C. 477. (6) 12 T.C. 245.
(7) 10 T.C. 29.

(Scrutton, L.J.)

the manufacture of their pumps largely by granting licences in exchange for royalties. They found difficulties in getting agreements to pay royalties unless they would grant options to purchase, or agreements to assign when royalties reached a certain amount. I find it impossible to say that there was no evidence on which the Commissioners could find that these transactions were part of, incidental to and arose out of the Appellants' trade or business. Indeed the Appellants did not object to cases 2 and 3 and the royalties under case 1 being included in the assessment.

So far on the case under appeal. There remains the question how far the present case is affected by the proceedings in the previous case of *Collins* v. *Firth-Brearley Stainless Steel Syndicate, Limited*(1). In that case the company had patents for the manufacture of stainless steel, and granted licences for their use. Three transactions were stated in the Case. (1) An agreement by which the United States patent was sold in consideration of 550 shares in the purchasing company. The selling company here exchanged the patent under which they could receive royalties for shares in a company which itself would pay dividends out of the sums made by exercising or licensing the use of the patent. This certainly looks like the exchange of one capital asset for another. (2) An agreement for the sale of a Japanese patent for a price, payable by ten yearly instalments, and for a fixed royalty per year for the life of the patent. (3) An agreement whereby a French patent was assigned in consideration of a royalty per pound of all stainless steel dealt with under the patent. These last two cases are similar to cases 2 and 3 of the present case, on which the present Respondents submitted to be taxed.

The General Commissioners for one of the Divisions of Yorksire heard similar arguments to those in the present case and decided that " the amounts realised were an appreciation " of capital and not taxable profits." Mr. Justice Rowlatt reversed their decision. He has explained in his judgment in the present case that he did so under the impression that they had only found an appreciation of capital in the course of trade; and that if he had understood that they intended to find an appreciation of a capital asset not in the course of trade, he would not have reversed their decision. However that may be, the Court of Appeal reversed Mr. Justice Rowlatt's judgment and restored

(1) 9 T.C. 520.

(Scrutton, L.J.)

the decision of the Commissioners. The ground of their opinion appears to be that it was a finding of fact with evidence justifying the decision, though there was evidence on which an opposite finding might be arrived at. Lord Hanworth at the end of his judgment, Lord Justice Warrington, and Lord Justice Atkin at the beginning of his judgment, all treat the finding as one of fact, with evidence to support it, with which the Judge had no right to interfere, he not being the judge of fact. I approach the present case in the same way; in my view there is here a finding of fact, with evidence to support it, and no misdirection in law. It would have been possible in each case to come to a decision the other way; this is always so when the question is one of degree judged of by different bodies of Commissioners. The Special Commissioners are at least as competent to decide questions of fact and appreciate the law as the Commissioners of this Division of Yorkshire—one might perhaps go further with safety. In my view Mr. Justice Rowlatt's refusal to interfere with the decision of the Commissioners, even after reading the decision of this Court in the *Stainless Steel* case, was justified, and the appeal must be dismissed.

Sargant, L.J.—In the first case, namely, that as to Income Tax, I think that Mr. Latter was right in his contention that the decision of the Special Commissioners must be interpreted in the light of the learned Judge's decision in the analogous case of *Collins* v. *Firth-Brearley Stainless Steel Syndicate, Limited.* The appeal in that case had been decided by the learned Judge on the 2nd March, 1925, while the decision in the present case was given by the Special Commissioners on the 18th March, 1925, having been held over by them since the argument before them on the 9th December, 1924. It is fairly clear therefore from these dates, as is confirmed by the internal evidence of the decision itself in the present case, that the Special Commissioners have taken for their guide the observations of the learned Judge in his judgment in the *Firth-Brearley* case.

Now in that case the Commissioners had decided that the sums received by the Company on the sale of their patents in Japan and the United States of America were an appreciation of capital and not assessable profits. But the learned Judge reversed their decision because (as he says in the present case) he misunderstood their finding, and thought that they did not mean that there had been an appreciation of a capital asset but that they meant that the appreciation had occurred "in the

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" course of trade which it was the object of the trade to secure." Unfortunately, however, for the decision of the present case, the learned Judge in the language of his decision in the *Firth-Brearley* case did not make it clear that his judgment was based upon the supposition that the appreciation was " in the course " of trade which it was the object of the trade to secure " but used language which was much more general, namely, that any appreciation in the course of the Company's trade would have been sufficient to involve liability to Income Tax.

With that judgment before them the Special Commissioners here, while stating correctly the contention on behalf of the Company that the sale of the patents in the U.S.A. was a sale of part of their capital assets, (i.e., of assets representing fixed capital and not circulating capital) state the contention of the Crown in terms which fall short of being the contrary to that contention, but satisfy the less definite language of the judgment of Mr. Justice Rowlatt in the *Firth-Brearley* case, namely that the sum received on the sale was " a receipt of the Appellant " Company's business and so assessable to Income Tax." And in the same way the decision of the Commissioners is worded in language equally wanting in the necessary precision, namely, that " the profits on sale of patents arose in the course of the " Appellants' business and were chargeable to Income Tax and " Excess Profits Duty."

In this state of things, the first question that arises is : What is the right interpretation to be put upon the finding of the Commissioners in the present case ? The learned Judge has held that it amounted to a direct negativing of the contention of the Company and to an assertion that the profit arose " in the course " of the Appellants' business, not because they were getting rid " of a capital asset and putting an end to it, but because it was " in the course of their business to sell the patents." With all respect to him, I cannot take that view. In my opinion the Commissioners carefully abstained from directly negativing the Company's contention, and found in favour of the Crown enough and no more than enough to involve liability to Income Tax on the basis of the incomplete test stated by the learned Judge in his decision in the *Firth-Brearley* case.

I arrive at this conclusion on the language used by the Commissioners in stating the contention of the Crown and their own finding. But the conclusion is immensely strengthened by a consideration of the specific facts found by the Commissioners

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in the previous paragraphs of the Case and particularly in paragraphs 10, 11 and 12. It appears that the Appellant Company, so far from making it their business or part of their business to attempt to sell their foreign patents or any of them, always endeavoured to avoid any such sale; and that the sale now in question is the only sale the Company have ever in fact made. The specific facts found point unmistakeably to the Company's patents having constituted fixed assets or capital as distinguished from assets or capital circulating in the course of the Company's business, and so resulting in a profit or loss attributable to income. And it is in my judgment inadmissible to attribute to the somewhat ambiguous and indefinite words of the general conclusion in paragraph 24 of the Case a meaning which would be directly in the teeth of the facts specifically found in the preceding paragraphs. Indeed, if the conclusion in paragraph 24 has the meaning attributed to it by the learned Judge, there was not, in my judgment, any evidence on which the Commissioners were entitled to come to this conclusion.

Further, I do not consider that the decision of the Commissioners in Clause 24 (for that is what they call it) was, or was intended by them to be, a finding of fact. I think it was a decision as to the law resulting from the facts previously found by them and stated in detail in the preceding paragraphs of the Case. In my judgment that decision as to the law was wrong, and should on the specific facts found by the Commissioners have been the other way; and the facts so specifically found and stated are in my opinion sufficient to entitle this Court to deal with and answer the question raised by the twenty-first paragraph of the Case.

On these facts, which are practically on all fours with those in the *Firth-Brearley* case, or so far as they differ are more strongly in favour of the taxpayer, this question should be answered in the negative, since the assets sold were obviously part of the fixed capital of the Company and not part of its circulating capital. And I think therefore that the decision of the learned Judge to the contrary should be reversed.

I may add that this decision does not in my view prejudice such claim, if any, as the Crown may have, to Income Tax in respect of the years in which the Company earned the royalties to the extent of £13,500 which were ultimately included in the purchase price of £26,500. The reversal of the decision as to Income Tax of course involves a reversal of the corresponding

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decision as to Excess Profits Duty. It has throughout been agreed that the two claims by the Crown rest on the same foundation.

Mr. Bowe.—My Lord, the appeal will be allowed with costs?

Lord Hanworth, M.R.—Yes, with costs here and below and the assessments discharged.

Mr. Bowe.—If your Lordship pleases. I am informed that we have paid the Excess Profits Duty. I ask your Lordship for the customary Order for repayment with interest at 4½ per cent.

Lord Hanworth, M.R.—You do not want an Order, do you?

Mr. Bowe.—I think it is usual.

Scrutton, L.J.—Can we make an Order on the Crown?

Mr. Bell.—I am instructed that an Order is usually made to the effect that my friend asks.

Lord Hanworth, M.R.—You say it is usually made?

Mr. Bell.—Yes.

Lord Hanworth, M.R.—Very well, we will make the Order.

Mr. Bell.—If your Lordship pleases.

The Crown having appealed against the decision in the Court of Appeal, the case came before the House of Lords (Lord Buckmaster, Viscount Sumner, and Lords Wrenbury, Carson and Warrington of Clyffe) on the 13th and 14th February, 1928, when judgment was given unanimously in favour of the Crown, with costs, reversing the decision of the Court below.

The Attorney-General (Sir Douglas Hogg, K.C.), the Solicitor-General (Sir Thomas Inskip, K.C.) and Mr. R. P. Hills appeared as Counsel for the Crown, and Mr. Latter, K.C., Mr. Stamp and Mr. Bowe for the Company.

JUDGMENT.

Lord Buckmaster.—My Lords, this is an appeal from the Court of Appeal by His Majesty's Attorney-General, seeking to reverse a judgment given by that Court, Lord Justice Scrutton dissenting, which overruled a judgment of Mr. Justice Rowlatt, who had affirmed a finding of the Commissioners assessing the present Respondents as liable to Income Tax. The amount of the assessment is not in dispute. The ground of the appeal rests upon this : That the sum to which the Respondents have been assessed is a sum which in fact represents part of the capital assets of the Company and ought not to be brought into account for the purpose of considering profits subject to Income Tax.

The facts are these : The Respondent Company was formed on the 4th October, 1906, for the general purpose of purchasing and acquiring patents, licences and concessions, improving them, using them, and turning them to account, and with the special purpose of acquiring from a Mr. Rees and Thomas Parker & Co., Limited, the rights in regard to a particular invention that had relation to centrifugal turbine pumps. In one of the general clauses of the Memorandum of Association the Company had power to sell, dispose, turn to account and grant rights and privileges in respect of all or any part of the property and rights of the Company. The special purpose was carried out but it was not the whole of the patent rights that the Company so acquired ; one-third of the rights in foreign patents was reserved to the vendors, and it was in conjunction with the vendors that the Company proceeded to carry on its business. The Company appears to have decided from the first that it would never manufacture under these patents, but that it would either grant licences to other people to manufacture or deal with the patents in such manner as it thought fit. In the course of its business the Company acquired further foreign patents—in France, Switzerland, Belgium, Germany, the United States of America and the Dominion of Canada. It dealt with the patent rights with regard to the United States by granting to an American company the right to use the invention, which the patent protected, upon the terms of paying certain royalties, with an ultimate right of acquiring the whole patent by purchase. It is unnecessary to go through the history of the agreements by which this result was reached, but in the end it led to this conclusion, that there was a substantial sum of money owing in respect of royalties from the American company, and this sum was brought into account with another sum, making up together the purchase price of £26,500 for which the patent was sold. It is the Company's share of this

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sum less proper expenses which has been the subject of the present assessment. The Company also dealt with the patents in Canada and the patents in France, not under agreements containing exactly the same provisions, but by agreements which did enable the people with whom it dealt in each case in certain circumstances to acquire the whole of the patent rights. The contention of the Company is that the transaction entered into with the American company was nothing but the solitary disposition of a capital asset, and that the proceeds arising therefrom should not be brought into account.

My Lords, I think it is undesirable in these cases to attempt to repeat in different words a rule or principle which has already been found applicable and has received judicial approval, and I find that in the case of the *Californian Copper Syndicate* v. *Harris*, which is reported in Volume V, Tax Cases, page 159, it is declared that in considering a matter similar to the present the test to be applied is whether the amount in dispute was " a gain made in an opera- " tion of business in carrying out a scheme for profit-making." (1) That principle was approved in a judgment of the Privy Council in the case of *The Commissioner of Taxes* v. *Melbourne Trust, Limited*, reported in [1914] Appeal Cases, page 1001, and it is, I think, the right principle to apply.

My Lords, following from that there are only two things that result. First of all, whether the Commissioners in the exercise of their power properly directed themselves with regard to determining whether these monies were profits in accordance with this test or no; and the second thing is whether in fact they have done so.

Now the real contention here has been chiefly directed to the form of the Commissioners' finding—which it is suggested was based on a mistaken view of the law rather than on a proper consideration of the facts. The reasons which have been urged here by the Respondents in support of their view depend to a large extent upon the fact that in a case known as *Collins* v. *The Firth-Brearley Stainless Steel Syndicate*, which is reported in 9 Tax Cases, page 520, a finding of the Commissioners in a closely similar case had been upset by Mr. Justice Rowlatt on the 2nd March, 1925, and his decision was in turn reversed by the Court of Appeal on the 26th June, 1925. Now the Commissioners' finding in the present case was on the 18th March, 1925, and it is therefore argued that it is based upon the direction of Mr. Justice Rowlatt,

(1) 5 T.C. at p. 166.

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which had been given on the 2nd of the same month, and that as that direction had been held to be unsound it consequently followed that the foundation of their finding had fallen away. My Lords, I think there are one or two comments to be made upon that argument. In the first place, what Mr. Justice Rowlatt did was to reverse a finding of fact, and the enunciation that he made of the law appears to me to be open to very little criticism. In the Court of Appeal each one of the learned Judges who reversed his finding expressly and definitely stated that the circumstances were such as to lead to the conclusion that the finding was essentially a finding of fact by the Commissioners which, when once found, ought not to be interfered with. It seems to me impossible in those circumstances to say that Mr. Justice Rowlatt in inadvertently disturbing a finding of fact of the Commissioners, which the Court of Appeal restored, was laying down directions which were so unsound that the Commissioners, whose finding in this case followed his judgment, must necessarily have been led to their conclusion by erroneous arguments.

Turning to the findings of the Commissioners, I find that they set out in detail the circumstances connected with the working of this Company, and, in particular, the reports, which begin in 1907 and continue down to 1918. These reports show that the directors were contemplating from the earliest the possibility of the sale of some of these patents. It is quite true that they preferred not to sell them if a sale could be avoided, but the statement in paragraph 11 of the Case is quite plain, that " the possibility of the sale of " the foreign patents or rights has always been contemplated by " the Appellant Company in respect of such interest as it possessed " in the foreign patents." It is one of the foreign patents with which this appeal has to do, and the agreements, which are set out, showing the way in which the foreign patents in the case of France and of Canada have also been dealt with, show that that statement was not a statement of a mere accidental dealing with a particular class of property, but that it was part of the Company's business which, though not of necessity the line on which it desired its business most extensively to develop, was one which it was prepared to undertake.

My Lords, I find myself unable to see that in this case the Commissioners have wrongly directed themselves, and, if they have not wrongly directed themselves, there appears to me to be abundant evidence upon which their conclusion of fact could be supported. It is for this reason that I think this appeal should be allowed.

Viscount Sumner.—My Lords, I agree.

Lord Wrenbury.—My Lords, I agree, and I do not feel it necessary to add anything at all.

Lord Carson.—My Lords, I also agree.

Lord Warrington of Clyffe.—My Lords, I agree.

Lord Buckmaster.—I do not know whether there is any question about the costs in this appeal. Are there any arrangements made by the Crown?

The Attorney-General.—My Lord, there are no arrangements in this case. There are two appeals, and I assume your Lordships' Order will be the same in both cases?

Lord Buckmaster.—Yes.

Questions put :—

In *Ducker* v. *Rees Roturbo Development Syndicate, Limited.*

That the judgment appealed from be reversed.

The Contents have it.

That this appeal be allowed with costs.

The Contents have it.

In *Commissioners of Inland Revenue* v. *Rees Roturbo Development Syndicate, Limited.*

That the judgment appealed from be reversed.

The Contents have it.

That this appeal be allowed with costs.

The Contents have it.

[Solicitors :—Messrs. Sharpe, Pritchard & Co., for Messrs. Underhill, Neve & Co., of Wolverhampton; the Solicitor of Inland Revenue.]