Summary Jurisdiction Act of 1908. That section enacts that "No conviction, sentence, judgment, order of court, or other proceeding whatsoever shall in any event be quashed unless on the ground of incompetency" and certain other grounds. Of these grounds the one fixed upon as justifying the quashing of this conviction was that of incompetency, the incompetency being that the Clerk of Court had failed to note the two documents I have referred to on the record in terms of section 41 of the Act.

Prior to 1908 that omission would probably have been a fatal objection as the law then stood. But it seems to me that section 75 of the 1908 Act was passed just because it was realised that in a great many cases persons who were quite properly convicted so far as substance was concerned were being released from any penalty upon purely technical grounds, and that it was undesirable that that state of things should continue. Accordingly, while it provides that no conviction shall be quashed in any event except on specified grounds, the section also says, "Provided always that the High Court may amend any conviction, sentence, judgment, order of court, or other proceeding, or may pronounce such other sentence, judgment, or order as they shall judge expedient."

Within reasonable and proper limits I think the section ought to receive effect. And I confess I can hardly conceive of a case which was more suitable for its application than the present. The complaint says that there was in the premises in question a large quantity of exciseable liquors kept for the purpose of being consumed, and I suppose the more active of the consumers were among those fined £1 each. The objection taken is that the Clerk of Court failed to note two documents, which for the purposes of this case I am prepared to accept as falling within the definition of documentary evidence. To that extent a fault of procedure probably took place. But assuming it to be so, I think that is a long way off from incompetency. For my part I am prepared to accept for this case, although it was pronounced in a small-debt action, what Lord Justice-General Dunedin said in the case of *Robson* v. *Menzies*, 1913 S.C. (J.) 90, 7 Adam, 156, 50 S.L.R. 802—"I may say at once that I think it quite impossible to hold that under the head of incompetency you could deal with anything that is wrong in the procedure of the case itself. I think that incompetency means, and can only mean, an inability to deal with the matter in hand; and I think the reason why the phrase is used — incompetency, including defect of jurisdiction—is not really to add anything, but is merely to look at the matter from another point of view. In other words I think incompetency pure and simple would mean any case with which the Court as a Court had not power to deal." Similar views have, I think, been expressed by other judges, but Lord Dunedin's pronouncement is one of the most recent, and it seems to me perfectly apt and appropriate to indicate the meaning of the word "incompetency" in section 75 of the 1908 Act. Accepting it as correct, I read section 75 in view of what was argued to us as saying that we are not to quash a conviction except on the ground of incompetency. No doubt prior to 1908 the omission of a detail of procedure was often regarded as sufficient to invalidate the conviction; but in the view which I take of section 75 I am of opinion that the failure to note these two documents does not amount to incompetency within the meaning of the section, and I move that the suspension should be refused.

Lord Dundas—I have reached the same conclusion and substantially on the same grounds, and I have nothing to add.

Lord Ormidale — I concur with your Lordships. It is not necessary to decide it, but I should like to say that the suspenders might not have been without a remedy had they had the courage to go on with the Stated Case which they craved the Court to adjust. In section 75 I find that it falls to be read along with section 60 and section 72, and under these sections the suspenders, it appears to me as at present advised, might have proceeded with the Stated Case, and they might have got some relief although not the relief now sought.

The Court refused the bill.

Counsel for the Complainers—Aitchison. Agent—Alex. Ross, S.S.C.

Counsel for the Respondent — Keith. Agents—Mackenzie & Black, W.S.

HOUSE OF LORDS.

Tuesday, April 12.

(Before Viscount Haldane, Viscount Cave, Viscount Finlay, Lord Moulton, and Lord Sumner.)

JOHN SMITH & SON *v.* INLAND REVENUE.

(In the Court of Session, December 20, 1919, 57 S.L.R. 147.)

Revenue—Excess Profits Duty—Deductions — Purchase Price of Coal Contracts — Finance (No. 2) Act 1915 (5 *and* 6 *Geo. V, cap.* 89), *secs.* 38 *and* 40, *and Schedule IV, Part I, secs.* 1 *and* 3, *and Part III, sec.* 1 (*a*).

A coal merchant carrying on business under a firm name instructed his testamentary trustees to make over his business with its whole assets to his son at a valuation. One of the items at his death on 7th March 1915, as from which date the business was taken over by his son, consisted of certain coal contracts which were entered in the valuation at £30,000, and none of which extended beyond 31st December 1915. *Held* (Viscount Finlay *dissenting*) (*aff.* judgment of Second Division, *diss.* Lord Salvesen) that for the purpose of ascertaining the profits for the accounting period from 7th March 1915 to 31st December 1915

the £30,000 paid by the son to the trustees was a sum employed as capital in the business and not admissible as a deduction.

The case is reported *ante ut supra*.

John Smith & Son appealed to the House of Lords.

At delivering judgment—

VISCOUNT HALDANE—The question in this appeal is whether the appellants are entitled to deduction of a certain sum of £30,000 in the estimation of the excess profits on which they were liable under section 38 of the Finance Act, No. 2, of 1915, for excess profits duty, in an accounting period between 7th March 1915 and 31st December in the same year. The appellants say that this £30,000 was a disbursement or expense incurred by them for the purposes of their trade or business, and necessitated in order to earn its profits, having in truth been paid for the purchase of coal as part of their stock-in-trade. The respondent, the Surveyor of Taxes in Glasgow, who contests this claim on behalf of the Crown, says that the £30,000 was capital expenditure which cannot, consistently with the statute, be deducted. He contends that it was paid, not as the price of coal for stock-in-trade, but as part of the price given for a business which the appellants acquired, the value of which formed part of the capital of their own business.

The Second Division of the Court of Session, sitting as the Court of Exchequer in Scotland in the exercise of original jurisdiction, and consisting of the Lord Justice-Clerk, Lord Dundas, Lord Salvesen, and Lord Guthrie, decided by a majority in favour of the respondent, Lord Salvesen dissenting. The question was brought before them on a case stated under the Taxes Management Act of 1880. There was another point on which the judgment of the Court of Session was taken as to an allowance for management salary of £20,615, 17s. 9d. to a Mr Fair as a manager of the business. This latter point was, however, abandoned at the bar of the House and has not to be considered.

In the accounting period between the 7th March and the 31st December 1915 the gross profits made by the firm on certain coal contracts amounted to £98,897, and after deducting expenses and making adjustments there remained £90,366, which was taken as the profit in the period through which the appellants were assessed for excess profits duty. It is from this amount that the appellants claim to be entitled to make the deduction in controversy.

It is necessary in the first place to state the circumstances under which the appellants became entitled to the business. The late John Smith junior died on 7th March 1915. At the time of his death he was carrying on alone the business of John Smith & Son, a firm which had pursued the business of coal and shipping agents for many years. By a trust-disposition and settlement he directed his trustees to make over the business after his death, in the events which happened, to his son John Ross Smith. The goodwill and firm name were to belong to the latter without payment for them. But he declared that "the whole assets of the said business shall be taken over at the value which may be ascertained from a balance sheet made up as at the date of my death by a chartered accountant, but nothing shall be charged for goodwill."

Pausing here I will state the interpretation which as I think ought to be placed on the trust-disposition. It appears to me that the testator meant to leave his business as an entirety to his son the appellant, subject only to this qualification, that his son should be willing to pay over to the trustees an amount in respect of what was so given to him which would in part fill the gap in the testator's estate made by his gift. Nothing was to be payable in respect of the goodwill, but the amount to be replaced was to be ascertained by a valuation of all the other assets as they stood in the business at the date of the testator's death. These assets were to pass under the gift along with the business and its goodwill if the son elected to take them, and he was to be charged not as on a sale to him of each asset in the open market but on a valuation, to be made in the manner prescribed of the whole assets of the business, the goodwill being included without charge for it.

The appellant elected to take on the terms of the will. A firm of chartered accountants prepared a balance sheet in which they valued the assets, among which were two especially valuable items—debts outstanding as due to the firm, amounting with agents' balances to over £32,000, and coal contracts which the accountants valued at £30,000. These contracts had been entered into by the testator with several colliery owners, and under them the latter had agreed to deliver over periods certain quantities of coal at prices which turned out in the end to have been very advantageous. The accountants stated, in a note to their balance sheet, that having regard to contingencies existing at the date of the testator's death and to a doubt whether sales to outsiders of the contracts would have been recognised by the colliery owners, they thought the amount of £30,000 in all the circumstances a fair and equitable one.

The appellant took over the business as from the 7th March and carried it on through the accounting period to 31st December 1915. He made the profit by means of these coal contracts of £90,000 to which I have already referred. The contracts were contracts which apparently were for short terms, and it was therefore necessary to realise their fruits. This was done, and a large profit was the result.

Profit may be produced in two ways. It may result from purchases on income account, the cost of which is debited to that account, and the prices realised therefrom are credited, or it may result from realisation at a profit of assets forming part of the concern. In such a case a prudent man of business will no doubt debit to profit and loss the value of capital assets realised, and take credit only for the balance. But what

was the nature of what the appellant here had to deal with? He had bought as part of the capital of the business his father's contracts. These enabled him to purchase coal from the colliery owners at what we were told was a very advantageous price, about fourteen shillings per ton. He was able to buy at this price because the right to do so was part of the assets of the business. Was it circulating capital?

It is not necessary to draw an exact line of demarcation between fixed and circulating capital. Since Adam Smith drew the distinction in the second book of his "Wealth of Nations," which appears in the chapter on the Division of Stock, a distinction which has since become classical, economists have never been able to define much more precisely what the line of demarcation is. Adam Smith described fixed capital as what the owner turns to profit by keeping it in his own possession, circulating capital as what he makes profit of by parting with it and letting it change masters. The latter capital circulates in this sense.

In the case before us the appellant of course made profit with circulating capital by buying coal under the contracts he had acquired from his father's estate at the stipulated price of fourteen shillings and and re-selling it for more, but he was able to do this simply because he had acquired, among other assets of his business including the goodwill, the contracts in question. It was not by selling these contracts, of limited duration though they were, it was not by parting with them to other masters, but by retaining them, that he was able to employ his circulating capital in buying under them. I am accordingly of opinion that although they may have been of short duration they were none the less part of his fixed capital. That he had paid a price for them makes no difference. Indeed the description of their value by the accountants, in the words I have earlier referred to, as of doubtful validity in the hands of outsiders, emphasises this conclusion. The £30,000 paid for the contracts therefore became part of the appellant's fixed capital and could not properly appear in his revenue account. If that be so, then it was a sum employed as capital in his trade, and has to be excluded as a deduction from the profits on which he is assessed. This results from the express provisions of sections 38 and 40 of the Finance Act 1915 (No. 2), which governs his case, and the first part of the Fourth Schedule to that Act, which incorporates certain analogous provisions of Schedule D of the Income Tax Act of 1842, including Rule 3 of the First Case. Capital within the meaning of these provisions seems to me in any view to include such fixed capital as I think we have described to us in this appeal.

For these reasons I have come to the conclusion that the contention for the Crown is right, and that the appeal ought to be dismissed with costs.

VISCOUNT FINLAY—In this case the appellant John Ross Smith, who carries on business under the name of "John Smith & Son," appealed to the Court of Session against an assessment for excess profits duty made under section 38 of the Finance (No 2) Act 1915 in the sum of £52,081 for the accounting period from the 7th March 1915 to 31st December 1915. He claimed that in arriving at these profits a deduction should be made for £30,000 paid to the trustees of his father, the late John Smith junior, for unexpired coal contracts.

The business is that of a coal exporter, and it has been carried on for many years. John Smith junior was the sole partner up to his death on the 7th March 1915. By his trust disposition and settlement dated 7th January 1909 he appointed trustees to whom he made over his whole estate in trust. The third trust was to make over to the appellant, who is himself one of the trustees, the said business of coal exporter, the goodwill to belong to the appellant without any payment being made by him for it, declaring that the whole assets of the said business shall be taken over at the value which may be ascertained from a balance sheet made up as at the date of the testator's death by a chartered accountant. The capital of the estate was left on trusts.

The appellant became the sole partner in the business as from 7th March 1915. A balance sheet was prepared as directed by the settlement. It showed £27,927, 18s. 1d. to the credit of the trustees in respect of the assets of the business. This amount was arrived at by allowing £30,000 as the amount to be paid to the trustees as the value of certain coal contracts. These coal contracts had been entered into by the settlor with certain colliery owners who thereby agreed to deliver certain large quantities of coal at fixed prices. The duration of these contracts varied, but none extended beyond the 31st December 1915. The chartered accountants appended a note to their balance sheet giving their reasons for considering £30,000 as the fair amount to be paid in respect of these contracts. Since the contracts were entered into the value of coal had risen greatly owing to the war and the contracts were beyond all question very valuable. The price in the contracts was 14s. a ton, while the market price at the settlor's death was 44s. per ton.

The appellant continued to carry on the business and in the course of it he used the coal which he got under these contracts for supplying his customers. He claimed to have allowed as against his profits the £30,000 which he had paid to the trustees for the coal so used in the business. This claim is contested by the Crown and forms the subject of the present appeal.

The Second Division of the Court of Session (Lord Justice-Clerk, Lord Dundas, and Lord Guthrie) decided for the Crown, Lord Salvesen dissenting.

The year ending 31st December 1915 was divided into two parts for the purpose of the assessment of the profits of the business. The trustees of the deceased John Smith junior were assessed in respect of the profits arising up to the date of his death (7th March 1915), while the appellant was assessed in respect of the period subsequent to that

date down to the end of the year. It was contended for the appellant that the £30,000 represented a sum which he had to pay for the coal which he used to supply his customers, and that it could not be excluded from the computation of his profits for the accounting period. For the Crown, on the other hand, it was contended that the assessment of excess profits duty is upon the business as a continuing business, and that as the succession of the son to the business was part of a family arrangement he could not make this deduction any more than his father could have made it if he had carried on the business for the whole year, and further that the £30,000 was capital expenditure which cannot be deducted.

The excess profits duty was introduced by Part III of the Finance (No. 2) Act 1915, and the decision in this case must depend on the effect of the provisions of that Act.

Section 38 (1) provides for the levy as excess profits duty of an amount equal to 50 per cent. of the amount by which the profits of any trade or business in any accounting period exceed by more than £200 the pre-war standard of profits. By section 40 (1) the profits for excess profits duty are to be determined on the same principles as profits for the purpose of income tax, subject to the modifications set out in Schedule 4 to the Act, one of which is that the profits are to be the actual profits arising in the accounting period. This same section 40, sub-section 2, provides for the fixing of the "pre-war standard." It is to be ascertained by reference to the average profits of any two of the three last pre-war years to be selected by the taxpayer, provided that if their amount is less than the "percentage standard" the latter shall be the pre-war standard. The percentage standard is the amount of the statutory percentage (6 per cent. for corporations, 7 per cent. in other cases) on the capital of the trade or business as existing at the end of the last pre-war trade year, and provision is made for ascertaining for this purpose the amount of the capital according to Part III of Schedule 4 of the Act.

It was not disputed, and indeed could not be disputed, on the statements contained in the case stated that the £30,000 represents the fair value of these contracts taken over by the appellant. If the amount had been in any way unduly inflated it would have been brought to the notice of the Commissioners when the case was heard.

Of course if payment of the £30,000 had been merely a transference by the appellant from one pocket to the other the case would have assumed a totally different aspect. For instance, if the appellant had been the sole beneficiary under his father's will he in fact would have paid nothing for these coal contracts as he would have been himself the recipient of the price. There was a faint suggestion in the course of the argument for the Crown that the appellant is one of the beneficiaries who would take under the first and second trusts of the will. The terms of these trusts are not stated. We do not know whether the appellant would take any substantial interest under these trusts. The point was not mentioned in the Court of Session. If there were anything in it, it should have been raised before the Commissioners, who would have found upon it. The argument on behalf of the Crown was threefold—1, That the excess profits duty is a tax upon a continuous business, and that the change of ownership must for this purpose be disregarded; 2, that the deduction sought was in respect of capital expenditure; and 3, that the case is governed by the decision in *The City of London Contract Corporation* v. *Styles*. I take these points in the order in which I have mentioned them.

1. The contention most pressed at the bar of your Lordships' House on behalf of the Crown was that the excess profits duty is a tax upon the business itself as distinguished from the persons who may from time to time to carry it on. It was urged that the business is continuous, and that as these beneficial coal contracts had been acquired in the course of the business when it was carried on by the father, the sum which under the father's will the son had to give for them could not be allowed as an item in reduction of profits. It was pointed out that if the father of the appellant had lived until the end of the year the profits assessable to excess profits duty would have been precisely those on which the Crown now seek to charge the appellant, and it was urged that as the duty is on the business the change in the persons carrying it on should make no difference.

It is quite true that the statute imposing the excess profits duty treats the business as continuous for one purpose. As its name denotes, the excess profits duty is charged in respect of the excess of the profits yielded by any business after the outbreak of war as compared with its yield before the war. The business is regarded as remaining the same although the person by whom it is carried on may have changed. This is consistent with the popular conception of a business as a thing which may exist for a century or more while the persons through whose hands the business passes may have changed over and over again from generation to generation by transmission or transfer, and it cannot be disputed that this conception of the business as an entity which continues is correct. But though for this purpose the business is treated as continuous, the essential incidence of the tax is upon the person by whom it is conducted at the time in question. Just as a rate is imposed upon the occupant in respect of the house, so income tax and super-tax are imposed upon individuals in respect of the business. The yield of the business during any particular period depends upon the amount of profit which is got from it by the person carrying it on for the time being, and this must largely depend upon his personal qualities. The profits are not earned by the business; they are earned by the person who carries it on. The profits of this particular business down to the 7th March were the profits earned by the appellant's father. After the 7th March they were the profits earned by the appellant himself. In ascertaining what

was the amount assessable to the tax, deductions have to be made from the gross profits of all the expenses incurred by the owner for the time being for the purpose of earning these profits. This, indeed, is involved in the very idea of profits.

The tax is leviable by section 38 on the amount by which the profits arising from any trade or business in the accounting period exceed by more than £200 the pre-war standard. The same form of expression—"the profits arising from any trade or business"—is adopted in section 40, sub-sections 1 and 2. The business makes no profits. The profits are not fruits yielded by a tree spontaneously. They are the result of the operations carried on by the owner of the business for the time being and of the ability which he brings to bear upon it.

For a long time the main stress of the argument for the Crown was rested upon section 45 (2) of the Excess Profits Duty Act. It was contended that the effect of this enactment is that any owner for the time being of a business may be assessed to the excess profits duty although he had nothing to do with the business during the accounting period in which these excess profits were earned. It was insisted that this showed that the taxation was imposed upon the business and not upon the owner. I cannot so read the clause. The excess profits duty is charged not on the business but on the person who carried it on in the relevant accounting period. I cannot consider section 45 (2) as empowering the Commissioners to assess to the duty a person who had no interest in the business during the accounting period in respect of which the assessment is made. The last words of the subsection providing for a change of ownership are meant to meet the case of a change of ownership in the course of an accounting period, and in such a case to enable the Crown to take the accounting period as ending at the date of the change and assess the duty on the person who carried on the business at that date. I agree with the view which is expressed by Rowlatt, J., as to the meaning and effect of this clause (section 45 (2)) in the case of *Wankie Colliery Company* v. *The Commissioners of Inland Revenue*, 1920, 3 K.B. 287. The clause is not mentioned in any of the judgments in the Court of Session, and appears to me to have been very properly left out from the pages in the appendix on which are printed the sections which are relevant to the case.

It is quite clear that if the appellant's father had lived down to the end of the year 1915 he would have been chargeable on the whole profits for that year. He had made these contracts in the course of the business, and their existence coupled with the fact that coal went up so greatly in value would have enabled him in the course of the year 1915 to make these very large profits. The coal contracts were his own. He had not to pay £30,000 nor any other sum in order to get the coal under them at 14s. a-ton. But the change of the ownership of the business entirely altered the situation. The appellant was compelled under the trust settlement made by his father to pay £30,000 as the price at which he acquired these contracts, and it was with the coal that he got under them that he carried on the business.

Separate computations in respect of the earlier and later parts of the year were necessary. Up to the 7th March the business was the business of the father. From that date to the end of the year it was the business of the son. The profits must be computed in the usual way by comparing the amount got by the sale of the coal with the amount which it cost the owner for the time being to acquire it. Lord Salvesen at the close of his judgment points out with great force to what absurdities the argument for the Crown would lead—"Had there been no further rise in price, but the appellants had simply realised by sale the price paid by them (including the £30,000), the result would have been that in your Lordships' view they must be assessed as for excess profits on this sum, or in other words, would have to pay £18,000 out of capital in name of excess profits duty although they had not earned a penny of profit. I can find no warrant for so construing the statute. Its object was not to confiscate capital used in trading but to levy a tax on profits made by trading. Where no profits are made the Act has no application." If the father had lived he would have made in 1915 a profit of £99,315, 19s. 11d., because he already had these highly beneficial coal contracts. How can it be said that the son is to be held to have made this profit when in fact he had made only £69,315, 19s. 11d. owing to the circumstance that he had to pay £30,000 to his father's trustees for these coal contracts? If one assessment at the end of the year had been possible there would have been separate computations for the two parts of the year, and the result would have been the same as on the separate assessments which have been made.

2. The second contention for the Crown was that the £30,000 was capital expenditure.

It appears to me that this contention fails upon the facts. The contracts purchased all expired by the end of the current year. They covered only the stock required for the year ending 31st December 1915. It does not appear that the appellant or his father stored coal for delivery to the purchaser from them. It was more convenient to have the coal sent straight from the colliery to the purchaser. These contracts put at the command of the coal dealer the coal he required for delivery during the year. If the amount of coal which they represented had been in stock in yards belonging to the coal dealer it could not have been disputed that the price paid for it would have been a proper deduction as against the price realised by the re-sale. It can make no difference for this purpose that the coal dealer followed the more convenient practice of having contracts with the collieries and despatching it from the pit's mouth straight to his customers. There is not here any provision of coal for a long time ahead — there is no purchase of a colliery from which the coal is to be extracted — there is merely provision in the only convenient

way for the stock required up to 31st December 1915 from 7th March 1915. There is nothing in the nature of capital expenditure in the purchase of the stock wanted for re-sale during the current year.

The coal represented by the contracts was circulating capital. It was bought for use in the business, and was so used. At one stage of the argument in this House an attempt was made to distinguish the case of contracts for coal from the case of coal already delivered and stored in a coal-dealer's yards, and the Lord Justice-Clerk in part rests his judgment in favour of the Crown upon the distinction between "goods" and "choses in action," such as contracts for coal. This distinction seems to me to be for this purpose untenable. The contracts gave the means of getting coal, and there is no difference for this purpose between having coal stored in your yard and having a contract which enables you to get it from time to time as you want it. This, indeed, was admitted by the Lord Advocate in argument when he was asked the question specifically by Lord Haldane. If the Crown is entitled to disallow what the appellant had to pay for these contracts it would be equally entitled to disallow as a deduction the price paid for coal actually in stock.

For the present purpose these coal contracts are not distinguishable from the coal which they represent. What the appellant had to pay for the coal was the £30,000 which he gave for the contracts which would enable him to get the coal at a comparatively low price plus the sums which from time to time he paid for particular quantities deliverable at 14s. per ton. The price to him was made up of the 14s. per ton and a proportion of the £30,000 on each delivery. The contracts cannot be regarded either in whole or in part as a fixed asset like a coal mine; they are merely the machinery for getting coal, and the coal which they commanded is the article by the re-sale of which the appellant made his profit. A contract for delivery of certain quantities of coal at a certain price may be made in consideration of a bonus paid when the contract is entered into, in which case the price to be paid on delivery would be somewhat lower, or it may be constituted simply by the price to be paid on each delivery. In each case the whole amount so paid represents circulating capital, the coal which the purchaser means to re-sell. The purchaser does not re-sell the contracts; he uses them from time to time as he requires coal for re-sale. Where there is no bonus paid, it would not, I suppose, be suggested that there was any element of fixed capital in such contracts. How can the payment of a bonus affect the case? The only difference is that the price which the mineowner is content to take and the coal dealer to pay is in the first case made up by a bonus on entering into the contract, and the amounts paid on each delivery, while in the other case it consists simply in the payment of a larger amount as the price payable on each delivery.

It was further urged by the Crown that section 159 of the Act of 1842 forbids any deductions on account of diminution of capital employed. This provision, of course, would cover the case of diminution of value of wasting assets as they are termed. If the owner of a coal business has a coal mine, the coal from which he uses for sale in his business, he would not be entitled to any deduction in respect of the fact that from year to year the mine is being worked out. The whole law on this point was investigated in the *Alianza* case (1904, 2 K.B. 666; 1905, 1 K.B. 184; 1906, A.C. 18). It has never before been contended that such a doctrine had any application to the case of goods purchased for re-sale, and re-sold in the course of business. The whole argument for the taxpayer in the *Alianza* case was an attempt to assimilate the *caliche* beds to the case of goods bought for re-sale.

The £30,000 cannot be treated as being part of the price paid for the business itself. This is clear from the terms of the trust-disposition and settlement. Nothing was to be paid for the goodwill, but the assets were to be taken over at their value to be ascertained. Under these contracts the coal had been bought at 14s. a ton. Coal had risen to 44s. per ton market value, and the £30,000 represented the value of the contracts which gave the right to acquire at 14s. a ton of coal worth 44s.

In the appendix there occurs the following passage in the judgment of the Lord Justice-Clerk — "The appellants founded very strongly on the *Scottish North American Trust* (1912 S.C. (H.L.) 26), and particularly on Lord Atkinson's judgment at the foot of page 29, and on *J. & M. Craig (Kilmarnock), Limited* (1914, S.C. 338). Of course these judgments are binding on us, and I accept and respectfully agree with them. But they do not appear to me to affect the present case. They were both before the passing of the Act of 1915, and were therefore in no way affected by the statutory definition of capital contained in the schedule to that Act."

With the utmost respect for the opinion of the Lord Justice-Clerk I cannot see how the application of these authorities is in any way affected by the statutory definition of capital in the schedule to the Act of 1915. In that schedule special provision is made with regard to the calculation of capital for the purpose of reaching the percentage standard (section 40, Part 3 of the Fourth Schedule), but the law as to the deductions to be made from gross profits is in no way affected by the statutory definition.

In *Craig Limited* v. *The Inland Revenue Commissioners* (51 S.L.R. 321, pp. 326-27, and 1914 S.C. 338, pp. 349, 350) Lord Johnston stated very clearly the difference between fixed assets and floating assets. The fixed capital assets comprised, he says, land, leases, works, and plant. He goes on — "But there were other assets of a different kind, namely, the floating assets, consisting of the stocks of material to be worked up and of the manufactured articles to be sold. With these the appellant company had to commence business, and it was on the turn-

over of these and their replacement by further material and further manufactured articles that the company was to make its profit or loss." The whole of the argument which has been addressed to your Lordships on behalf of the Crown on the score of the £30,000 being in the nature of capital expenditure appears to me to ignore the broad distinction between these two classes of assets, the one class consisting of fixed assets, the other consisting of circulating assets which are bought for the very purpose of being re-sold.

I desire in this connection to refer to what was said by Lord Atkinson in delivering the judgment which was adopted by the other members of the House in *Farmer* v. *The Scottish North American Trust, Limited* (1912 A.C. 118), and to quote what Lord Herschell said in *Russell* v. *The Town and Counties Bank* (1888, 13 A.C. p. 424). He was dealing with the income tax, but his language is just as applicable to the excess profits duty. "The duty is to be charged upon 'a sum not less than the full amount of the balance of the profits or gains of the trade, manufacture, adventure, or concern'; and it appears to me that that language implies that for the purpose of arriving at the balance of profits all that expenditure which is necessary for the purpose of earning the receipts must be deducted, otherwise you do not arrive at the balance of profits; indeed, you do not ascertain, and cannot ascertain, whether there is such a thing as profit or not. The profit of a trade or business is the surplus by which the receipts from the trade or business exceed the expenditure necessary for the purpose of earning those receipts. That seems to me to be the meaning of the word 'profits' in relation to any trade or business. Unless and until you have ascertained that there is such a balance, nothing exists to which the name 'profits' can properly be applied."

What has to be ascertained for the purpose of excess profits duty in the present case is what profit the appellant made out of the business during the period from 7th March to 31st December. In this calculation how is it possible to ignore what he had to pay for the coal by the sale of which his profits were made?

3. The third point made on behalf of the Crown was that the present case is governed by the decision in *The City of London Contract Corporation, Limited* v. *Styles*, 1887, in Divisional Court, 3 T.L.R. 512, and in the Court of Appeal, 2 Tax Cases 239, and 4 T.L.R. 51.

It appears to me that the facts in that case differ from those in the present on all points material for the present purpose, and that the decision affords no guidance in this case.

The company there was formed to purchase the business of Charles Philips & Company, contractors for public works, and their contracts, plant, and materials, and to carry on the business. On assessment to income tax the company claimed a deduction of £80,000. They stated that the £80,000 represented part of the purchase money, £180,000 paid to C. Philips & Company for the purchase of the contracts and business on which their profits were realised. The business consisted entirely of partially executed or wholly unexecuted contracts. It was urged for the company that the money had been expended for the purchase of the business. "My whole contention," said their counsel, "is that it was not money invested as capital. You can use your capital in purchasing contracts from which you derive your annual profits. It is capital to start with, but then you use your capital wholly and exclusively for the purpose of your concern." To this Bowen, L.J., answered (2 Tax Cas. p. 243)—"You do not use it 'for the purpose of' your concern, which means for the purpose of carrying on your concern, but you use it to acquire the concern." This answer was conclusive and really sums up the whole case. Lord Esher amplifies this a little. He points out that the £80,000 was part of the purchase money of the business—part of the capital embarked in the business—and that to carry on the business other money must be found to meet the current expenses.

The business acquired in that case was the business of carrying on contracts for works, and as part of the business the contracts on hand were purchased. These contracts were for the construction of public works, railways, &c., to be carried out by the contractors. In the present case the business acquired was that of a coal dealer and the contracts were for the supply of coal for re-sale in the course of the business. The business was not to carry on these contracts; they were entered into and afterwards acquired merely as the most convenient way of getting coal to be supplied to customers of the business. The coal which they represented was all wanted for the current year and was all used for delivery during the year.

For the reasons which I have already given in dealing with the second contention for the Crown these coal contracts in no way partake of the nature of capital; the £30,000 was not paid as the price of the business but as part of the price of coal with which to carry it on.

For these reasons I think that the decision in the Court of Session was erroneous and should be reversed.

VISCOUNT CAVE—I have arrived at the same conclusion as the noble and learned Lord on the Woolsack, though by a somewhat different road.

The argument for the appellants appears to me to be founded upon the assumption that for the purpose of assessment to excess profits duty under the Finance (No. 2) Act 1915 the profit made by Mr John Ross Smith in acquiring the coal contracts and carrying on the business during the accounting period from the 7th March to the 31st December 1915 is to be compared with the trading profits earned by Mr John Smith junior in the selected pre-war period. In my opinion this is not the comparison which the Act requires. The business of John Smith &

Son, coal exporters, is one business, carried on by John Smith junior for many years before and down to his death on the 7th March 1915, and thenceforth passing to and continued by his son John Ross Smith, and it appears to me that in such a case—the case of a continuing business which has changed hands during the war—the comparison to be made for the purposes of excess profits duty is a comparison between the trading profits earned in carrying on that business during the accounting period and those produced by the same business in the pre-war period without regard to the change of ownership.

This appears from the terms of the Act. Section 38 (1) and section 40 (2) refer to "the profits of the trade or business." Section 40 (3) provides for a "change in the constitution of a partnership." Section 44 (1) authorises the Commissioners to require a return of profits from any person engaged in the trade or business, "or who was so engaged during any accounting period or pre-war trade year." Section 45 (2) gives the Commissioners a discretion where there has been "a change of ownership of the trade or business" either to commence a new accounting period or to allow the accounting period to remain unaltered. All these provisions, as well as Rule 4 of Part II of Schedule IV, appear to me to support the conclusion that a business commenced before the war and continued in war time though in new hands is to be treated as one business for the purposes of the Act, and Rule 5 of Part II of the same schedule, which relates only to the profits earned in the pre-war period, does not afford any valid argument to the contrary. Where the change consists only of the accession of a new partner, I doubt whether anyone would contend that the business is to be treated as a new business and the consideration paid by the new partner for his share brought into the account, and I think that for this purpose a transfer of the business with its goodwill and assets to a new owner stands on the same footing. In either case the business is treated as a going and continuing concern, and the comparison to be made under the Act is a comparison between the trading profits produced by carrying on that concern in the war and pre-war periods respectively. The whole purpose of the Act is to tax the profits of a business so far as enhanced by war conditions, and in this connection a change of partners or of owners is irrelevant so long as the real continuity of the business is maintained. The business is the tree of which the produce in different periods is to be compared.

I have dealt on this point because I think that if the construction of the Act is that which I have indicated there is an end to this appeal. If the profits which are to be considered are the profits derived from the trading operations of the continuing firm of John Smith & Son, however constituted, then the expenses to be deducted are those, and those only, which were incurred in the course of those trading operations, and it is plain that the £30,000 deduction of which is claimed does not fall within that description. It was wholly unnecessary for any trading purpose of the business (regarded as a continuing concern) that £30,000 or any other sum should be paid for the coal contracts, for those contracts belonged to the firm from the time when they were entered into. The £30,000 was not paid by the firm for coal, nor was it paid by the trading firm as such for coal contracts. It was paid by John Ross Smith out of his private pocket as part of an overhead transaction under which the business with its assets and future profits passed into his hands, and it left the trading profits of the firm unaltered. If I buy the crop of an orchard in a particular year for £20 and sell it for £40, my profit is only £20. But the profit of the orchard is £40, and in comparing the produce of the orchard in the year with its produce in another year it is the £40 and not the £20 which must be taken into account.

I may add that the contrary view would lead to strange results. If John Smith junior had lived until the end of 1915 it is clear that he would have earned the profits assessed and would have had to pay the duty claimed. Can it be that because he died in March, and the business and business assets were transferred to his son upon terms involving a payment of £30,000 for one of the assets, the assessable profit was reduced by that amount? If so, then if John Smith junior had lived for another six months and had then died, the contracts being still unperformed, the contracts might then have been valued at £60,000, and the assessable profits would have been reduced by that sum. And upon the same showing, if John Smith junior instead of dying had at some time in 1915 converted the business into a company, the company paying £30,000 or a larger sum for the coal contracts, the company would have been entitled to deduct the whole purchase money paid for those contracts from its assessable profits, and John Smith junior, if he had held all the shares of the company, would have received the whole profit freed to that extent from excess profits duty. I cannot think that this is the true meaning and effect of the Act.

In any case the figures put forward by the appellants could hardly be accepted. If for the purpose of ascertaining the profits during the accounting period the business is to be treated as a new business commenced by John Ross Smith in March 1915, it must also be so treated for the purpose of fixing the pre-war standard of profits, and in that case the profits of the accounting period would have to be compared, not with the pre-war figure of £4137 (for John Ross Smith was not in business before the war), but with a percentage on his capital to be fixed in accordance with Schedule IV, Part II, Rule 4. In my view, however, of the construction of the Act these are not the figures which have to be taken into account.

For the reasons given above it appears to me that the £30,000 cannot be deducted as claimed by the appellant, and accordingly that this appeal fails and should be dismissed.

Lord Sumner—Since the appellants have abandoned the point as to Mr Fair's remuneration there is only one point before your Lordships for decision, namely, whether the appellants are entitled to bring the sum of £30,000, no more, no less, into an assessment in all other respects duly made upon them, as a proper deduction before arriving at profits under the Acts relating to Income Tax and Excess Profits Duty.

The business carried on by John Smith & Son is of a kind fairly familiar. The merchant who carries on such a business makes firm forward contracts for long terms to buy coal from collieries in periodic instalments and at fixed prices, generally f.o.b., and then during the term sells it at a better price if he can, in greater or in less quantities, choosing his own time and employing his foresight, diligence, and business connections. This system makes the colliery business less irregular, and gives the managers a stable programme to work to; it secures to the merchant a fixed basis for a business, which in ordinary times is not very speculative, and during the war turned speculation into a certainty "beyond the dreams of avarice." Such appears to have been the principal business of John Smith & Son in 1914 and 1915. There is or was a converse side, namely, to make forward contracts to supply bunkers to liners or coals to foreign railways and gasworks, and then the merchant must cover himself by current contracts with the pits, or to a less extent by buying parcels in the market. Furthermore, by buying f.o.b. and selling c.f. and i., there is a chance of making something out of chartering and freights. Whether this business, either in the hands of the father or of the son, included the two latter branches we do not know.

One thing, however, is clear, In such a business the colliery dispatches the coal by rail to the point of shipment alongside, and the middleman never sees the coal at all. Legally, no doubt, he acts as a conduit through which the property in the coal flows from the pit to the consumer, but he is hardly conscious of it. He need never have any stock-in-trade. The balance sheet of this firm shows that all the chattels it had were worth only £30, 4s. 6d., and they were office chairs and tables.

Mr Smith, the son, bought the business from those representing the estate of Mr Smith, the father, of whom he was himself one. That he did so in accordance with the provisions of his father's trust-disposition and settlement, made some years before, makes no difference, at least in his favour. The effect of what he did is plain. He bought a business and its assets at a valuation made in manner provided in the settlement. He bought no coals; the business had none, nor any stock-in-trade; nor did he acquire any stock-in-trade in any business sense of the term. He did not pay £30,000; he paid £27,745 as the balance of an account, which showed £30,000 as a fair valuation for the current contracts as between him and the representatives of the estate, agreed to by both and debited on one side of the account. Whether the contracts so valued could have been sold to strangers for that sum we do not know. The valuers evidently had their doubts about it. He did not pay this sum as the consideration for an assignment of the benefit of these contracts to himself; he took no assignment. The contracts were presumably in the firm's name and were part of its assets. He acquired the business carried on by his father in that name and with it these assets, and in that capacity, no question being raised, he enjoyed the benefit of contracts to which he was not a party in name and to which he was a stranger at the time when they were made.

In effect the father died with a number of unfulfilled contracts on his hands which it had been his business to implement at a profit, and this was what, perhaps among other things, he was then engaged in doing. To the business of further working out these contracts his son succeeded by purchase. £30,000 was the value of an important part of the subject-matter of the business, to use a neutral term. It is an accident that the last of the contracts expired during the accounting period. The business carried on was not that of buying and selling contracts but of buying and selling coals, and the contracts which enabled the seller of the coals to acquire the coals was no more the subject of his trading as a stock-in-trade for sale than a lease of a brickfield would be the subject of a sale of bricks.

The *City of London Contract Corporation* v. *Styles* (2 Tax Cases, 239) was decided 33 years ago. It has never been questioned. It was expressly approved by the Court of Appeal in the *Alianza* case, Collins, M.R., greatly relying on it, and Stirling, L.J., actually saying (1905, 1 K.B., at page 196) that effect could not be given to the argument for the company without departing from that decision. As your Lordships' House confirmed the decision of the Court of Appeal, expressing satisfaction with the reasons given in their judgments, the *City of London Contract Corporation* v. *Styles* has virtually been approved here. Even if I doubted it, which I certainly do not, I should follow it. Tax cases ought not to be unsettled.

That decision seems to me indistinguishable from the present case. There the tax-paying company was incorporated to buy as a going concern the business of a firm of contractors who had been entirely engaged in executing some construction contracts still uncompleted. The company bought this business, including the benefit of these incomplete contracts, and proceeded with the execution of them. In the purchase price was included a sum, ascertainable if not ascertained, for their value. The company claimed that before their profits from carrying out these contracts could be ascertained there must be deducted whatever sum represented their value in the price paid for the contractor's business generally. They said, much as has been said in this case, that before profits can be made out of working a contract the contract has to be got and the payment of its price is the root

of the profits. The Court held that this sum was paid with the rest of the aggregate price to acquire the business and thereafter profits were made in the business; the sum was not paid as an outlay in a business already acquired in order to carry it on and to earn a profit out of this expense as an expense of carrying it on. The same is true of the appellants. The whole price paid in cash or in account was a sum employed or intended to be employed as capital in the trade of the company and therefore cannot be deducted in ascertaining profit for Income Tax or Excess Profits Duty.

Much has been said as to the nature of capital and the right description of this sum of £30,000 assuming it to be capital. I neither think it necessary to attempt to define the term nor to select an appropriate adjective for it. Doubtless Mr Smith would wisely provide for some replacement of his outlay before flattering himself that he had made this handsome profit, but we are dealing with a firm which, consisting as it did of one person only, was under no legal obligation to keep its accounts in any particular form, or even to keep accounts at all. If he paid his taxes and paid his way and kept out of debt, it did not matter what he called the money with which he did it. The only question is whether he can claim to deduct this £30,000 without making a deduction, which the law calls, in the language of the Income Tax Acts, a sum "employed as capital" in his trade, and without making a deduction from the profits or gains from his trade "on account of diminution of capital employed." I think the answer is that he cannot, and so his appeal fails.

LORD MOULTON died before their Lordships' judgment was delivered.

Their Lordships ordered that the interlocutor appealed from be affirmed, and the appeal dismissed with costs.

Counsel for the Appellants — Sir John Simon, K.C.—Latter—Fleming. Agents—Wright, Johnston, & Mackenzie, Glasgow—Arch. Menzies & White, W.S., Edinburgh—Ince, Colt, Ince, & Roscoe, London, Solicitors.

Counsel for the Respondent—Attorney-General (Sir Gordon Hewart, K.C.)—Lord Advocate (Morison, K.C.)—R. C. Henderson—Hills. Agents—Stair A. Gillon, Solicitor for Scotland of the Board of Inland Revenue—H. Bertram Cox, Solicitor for England of the Board of Inland Revenue.

COURT OF SESSION.

Thursday, March 3.

FIRST DIVISION.

(SINGLE BILLS.)

[Sheriff Court at Glasgow.

ALBERTI v. BERNARDI.

Process—Removal to Court of Session for Jury Trial—Remit to Sheriff—Action of Slander—Trivial Character of Action—Test of Suitability for Jury Trial—Sheriff Courts (Scotland) Act 1907 (7 *Edw. VII, cap.* 51), *sec.* 30.

An action of damages for slander having been remitted to the Court of Session for jury trial under section 30 of the Sheriff Courts (Scotland) Act 1907, the Court *remitted* the case back to the Sheriff-Substitute as unsuitable for jury trial in respect of the trivial character of the action as revealed by the pleadings.

Observed (*distinguishing Greer* v. *Corporation of Glasgow*, 1915 S.C. 171, 52 S.L.R. 109) that the test of suitability for trial by jury was different in actions of damages for slander from what it was in actions of damages for physical injury.

The Sheriff Courts (Scotland) Act 1907 (7 Edw. VII, cap. 51) enacts—Section 30—"In cases originating in the Sheriff Court . . . where the claim is in amount or value above fifty pounds and an order has been pronounced allowing proof . . . it shall within six days thereafter be competent to either of the parties who may conceive that the cause ought to be tried by jury, to require the cause to be remitted to the Court of Session for that purpose, where it shall be so tried: Provided, however, that the Court of Session shall, if it thinks the case unsuitable for jury trial, have power to remit the case back to the Sheriff. . . ."

Mrs Ida Aimarosti or Alberti, 16 Douglas Street, Glasgow, brought an action in the Sheriff Court at Glasgow against Amedo Bernardi, 405 Argyle Street, Glasgow, concluding for £150 damages for slander.

The pursuer averred, *inter alia*—"(Cond. 2) On the evening of Tuesday, 27th July 1920, between 11 and 12 o'clock, while the pursuer along with two of her children was on her way home from her husband's shop at 415 Argyle Street, the defender met her at the corner of Carrick Street and Argyle Street, and addressing her in Italian made statements of and concerning her to the effect that she was 'budello,' which in English means that she was a 'whore' and worse than a whore. The pursuer denied that she was 'budello,' and asked defender if he could prove it. The defender answered 'Yes,' and repeated the expression 'budello' over and over again in the presence and hearing of a large number of persons, and in particular of Mrs Ward, 69 Cadogan Street, Mr Herron, 67 Cadogan Street, Thomas Knox, 16 Brown Street, and Mrs