

COURT OF APPEAL.—20TH AND 21ST MARCH, 1928.

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HOUSE OF LORDS.—22ND FEBRUARY, 1929.

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- (1) GREEN (H.M. INSPECTOR OF TAXES) *v.* J. GLIKSTEN & SON,  
LIMITED<sup>(1)</sup>.
- (2) THE COMMISSIONERS OF INLAND REVENUE *v.* J. GLIKSTEN &  
SON, LIMITED<sup>(1)</sup>.
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*Income Tax, Schedule D—Corporation Profits Tax—Profits of trade—Payment received from insurance company for stock destroyed by fire.*

*A fire occurred on the Company's premises in August, 1921, and destroyed timber the written down value of which in the Company's books was £160,824; the Company's valuation of its stock, based on cost or market value whichever was the lower, had been accepted for purposes of taxation. The timber had been insured for many years and the Company had been allowed to deduct the insurance premiums in computing its assessable profits. In due course the Company received from the insurers the sum of £477,838, representing the*

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<sup>(1)</sup> Reported (K.B.D.) [1928] 1 K.B. 475; (C.A.) [1928] 2 K.B. 193; and (H.L.) [1929] A.C. 381.

replacement value of the destroyed timber, but only a small part of this timber was in fact replaced because the current demand was for timber of a different character. The Company accordingly credited in its profit and loss account as a trading receipt only £160,824 of the insurance payment; the balance did not appear in the profit and loss account but was entered as a reserve in the balance sheet.

The Special Commissioners held that no part of the sum of £477,838 recovered from the insurers was a trading receipt.

Held, that the whole sum recovered was a trading receipt to be taken into account in computing the profits assessable to Income Tax under Case I of Schedule D and to Corporation Profits Tax.

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CASES

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- (1) *Green (H.M. Inspector of Taxes) v. J. Gliksten & Son, Limited.*

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 meetings of the Commissioners for the Special Purposes of the Income Tax Acts held on 25th June, 1924, and 6th April, 1925, for the purpose of hearing appeals, J. Gliksten & Son, Ltd. (hereinafter called the Company) appealed against an assessment to Income Tax in the estimated sum of £100,000 for the year ending 5th April, 1924, made upon them under the provisions of the Income Tax Acts.

2. The Company was incorporated under the Companies Acts, 1862 to 1900, on 14th December, 1905, and carries on business as timber merchants at Carpenters Road, Stratford.

3. On 8th August, 1921, a large quantity of timber which was stored in the Company's timber yard was destroyed by fire.

In respect of the timber so destroyed the Company received in February, 1922, £477,838 from various insurance companies.

4. The timber so destroyed consisted mainly of the best class of hardwood which was purchased by the Company seasoned, unseasoned, or partly seasoned.

A large quantity of seasoned wood which had been taken into stock before the War was destroyed by the said fire.

5. The Company's accounts were made up to the 30th day of June in each year, stocks being valued (following the usual practice) at cost or market value, whichever was the lower, and for the

purposes of this valuation large sums were in the last two years of account prior to the said fire written off the original cost prices of the stock, in respect of depreciation, in order to arrive at the closing stock values; and the reduced sums so arrived at were adopted each year in order to ascertain the Company's profits for Income Tax purposes. In respect of the stock on hand at the 30th day of June, 1921, which was the subject matter of this appeal, the sums so from time to time written off the stock values amounted in the aggregate to £107,000, or thereabouts, and the total stock on hand at that date was thus valued in the Company's accounts at £266,831, after writing off the said sum of £107,000.

6. For many years past the Company had kept its stock-in-trade insured against loss or damage by fire, and had in computing its profits for Income Tax purposes been allowed to deduct the premiums paid by it in respect of the policies of insurance as an expense of its business. For the purpose of fire insurance the stock-in-trade of the Company was valued at replacement value. At the date of the fire the value of timber of the kind which constituted the greater part of the Company's stock was very high, and the Company accordingly claimed from the insurance companies concerned, and was paid by them, in respect of the replacement value of the stock so destroyed, the sum of £477,838 2s. 4d. Out of the said sum of £477,838 2s. 4d. so received by the Company the sum of £160,824 (being part of the said sum of £266,831, the value of stock in hand at the 30th June, 1921) estimated by the Company to be the written down value of the timber so destroyed has been brought into the Company's accounts for the year ending the 30th June, 1922, as a trading receipt.

7. After deducting the sum of £2,845 for law charges, the sum of £1,000 for expenses of clearing the yard, and the said sum of £160,824, the balance of the monies received from the Insurance Companies in respect of the destroyed timber, amounting to £313,168, was carried into the balance sheet for the year ending 30th June, 1922, as a reserve, but was not brought into the profit and loss account.

Copies of the Company's balance sheets and profit and loss accounts for the years ending 30th June, 1920, 1921 and 1922, are attached hereto, marked A, B and C, and form part of this Case<sup>(1)</sup>.

An account entitled " fire account " is attached to the accounts for the year ending 30th June, 1922.

8. Mr. F. W. Gower, Chartered Accountant and Advisory Accountant to the Commissioners of Inland Revenue, who was examined on behalf of the Appellant stated in evidence that in his

<sup>(1)</sup> Copies of the balance sheet and profit and loss account for the year ending 30th June, 1922, only are included in the present print.

experience as a chartered accountant extending over twenty years the normal commercial method of dealing with monies recovered by a trader under a policy of insurance in respect of stock destroyed by fire was to include the actual amount received in the accounts as an ordinary trading receipt in the same way as the proceeds of an ordinary sale of stock.

9. During the war the greater part of the Company's trade consisted in supplying seasoned and specially selected timber of various kinds to Government Departments and various aircraft contractors. The timber required for these purposes being of a special character had to be and was picked out from the Company's stocks. The whole of the Company's stocks of the required types of timber, such as silver spruce, mahogany, walnut and English ash, had (before the fire) been gone over in this way and the Company was at the date of the fire left in possession only of such portions of those stocks as had not been found suitable for the above-mentioned purposes.

Since the Armistice the Company had done an increasing business with the motor body building and like industries and this class of business had led to demand for, and the Company had stocked, timber of types and qualities different from those stocked by the company during and before the war.

For this reason only a small portion of the timber destroyed by the fire had been replaced, viz., to an amount of £18,400, or thereabouts. The word "replaced" in this paragraph includes the purchase of timber suitable for purposes similar to those for which the destroyed timber was used as well as timber of a precisely similar nature. The replacements by timber of a precisely similar nature to that destroyed were almost negligible.

At the date of the fire there was a boom which was being prolonged by the adoption on the part of the larger timber merchants of a policy of holding up stocks. The high prices obtaining at that time, and on the basis of which the insurance companies paid the Company's claim, were due to this boom.

The timber destroyed was of such a character that it would have been practically impossible to have put it on the market without causing a glut and destroying the market for the time being.

10. It was contended by the Appellant on behalf of the Crown (*inter alia*) that:—

- (a) the whole sum received from the insurance companies in respect of the destroyed timber, namely £447,838, constituted a trading receipt and should have been brought into the Company's profit and loss Account for the year in question;
- (b) that the amount of the assessment should be the sum of £85,456, less £373 for wear and tear.

(c) In consequence of our decision with regard to monies arising under a Loss of Profits Policy which was also the subject matter of the appeal before us, but is not the subject matter of this Case, the Appellants subsequently contended that the amount of the assessment should be the adjusted sum of £84,227, less £373 for wear and tear.

11. It was contended on behalf of the Company that :—

(a) No part of the sum received by the Company from the insurance companies in respect of the destroyed timber constituted a trading receipt.

(b) No part of the difference between the said £160,824 and the said £477,838 constituted a trading profit.

12. Having considered the arguments and evidence adduced before us we gave the following interim decisions :—

1. We are satisfied that the sum of £477,838, the sum recovered from the insurance companies, does not represent a trade receipt, and no part of the said sum is assessable as trade profits under Case I of Schedule D.

2. We are of opinion that the burned timber which has been replaced should be brought into stock at the original cost price of the timber.

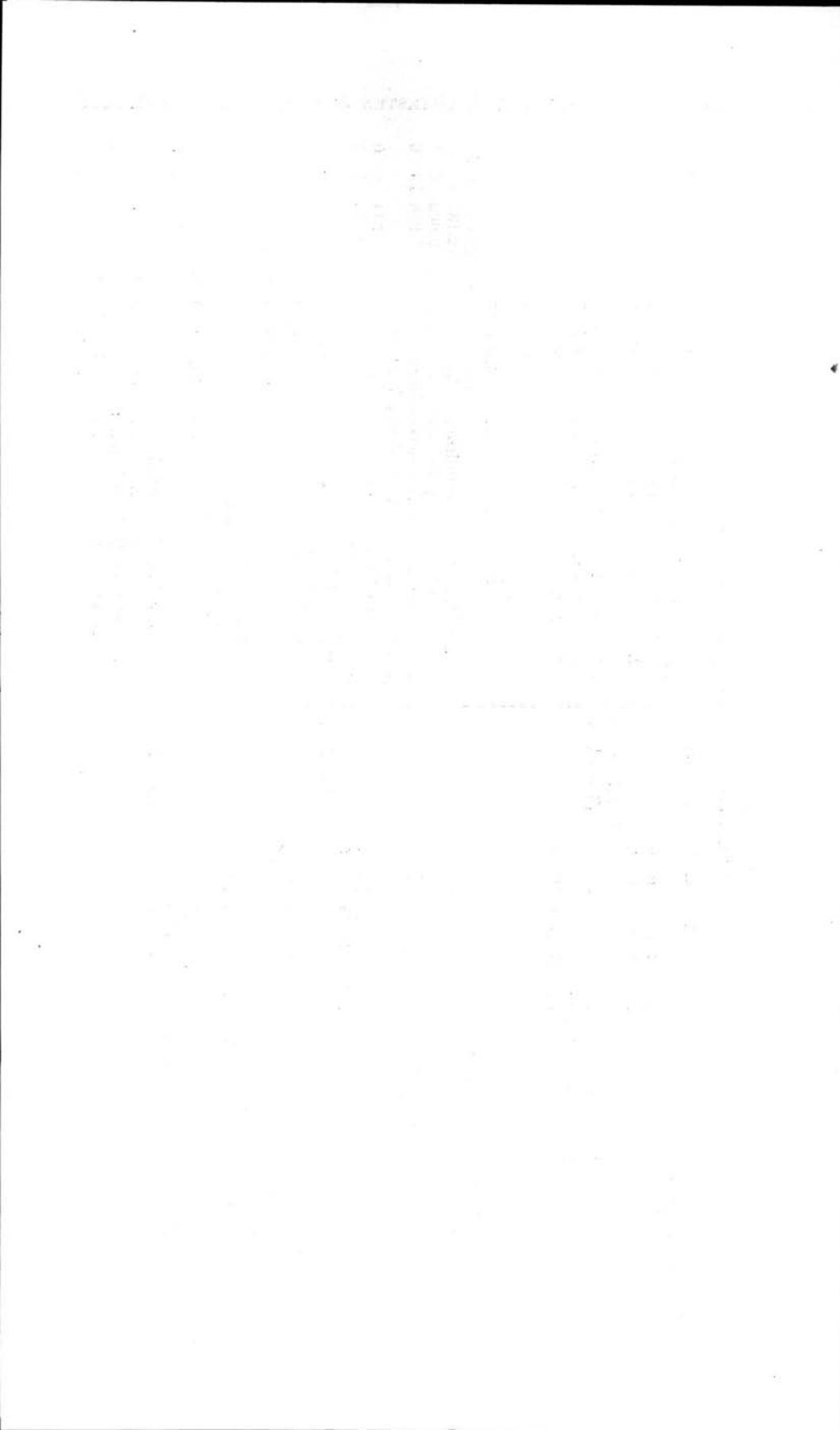
In this case upon a further hearing which was granted to the parties in order to clear up alleged ambiguities in our previous decision as to the meaning to be attributed to the word " replaced " in paragraph 2 of our decision, we held that in order to be a replacement the timber purchased need not be precisely similar to that burned ; it is a replacement if it is timber suitable for similar purposes and we fix the amount of replacements at £18,400.

13. The amount of the assessment having been agreed in accordance with these decisions we reduced the assessment under appeal to Nil.

14. The Appellant immediately upon the determination of the Appeal declared to us his 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.

N. ANDERSON, }  
J. JACOB, } Commissioners for the Special Purposes  
of the Income Tax Acts.

York House,  
23, Kingsway,  
London, W.C.2.  
28th March, 1927.



## BALANCE SHEET, 30th JUNE, 1922.

	£	s.	d.	£	s.	d.
To Capital:—						
Preference Shares	31,085	0	0			
Ordinary Shares	23,693	0	0			
				54,778	0	0
Sundry Creditors	...	...	...	128,355	14	4
Profit and Loss Account as at 1921	...	...	...	134,718	10	1
Less Dividends:—						
On Ordinary Shares, less Tax	...	...	...			
On Preference Shares, less Tax	1,087	19	6			
	3,575	14	6			
Add Profit for year	...	...	...	135,064	2	1
	131,142	15	7			
	3,921	6	6			
Reserve Account:—						
As last year	...	...	...	13,238	11	8
Credit re Fire Expenses recouped under Profit Insurance Policy	...	...	...	313,168	1	10
	10,447	10	0			
	336,854	3	6			
Less proportion to L. Gliksten	12,000	0	0			
	324,854	3	6			
By Lease Wansbeck Road:—						
As last year	...	...	...	3,800	0	0
Less Depreciation	...	...	...	300	0	0
				3,500	0	0
Land and Buildings Carpenters Road:—						
As last year	...	...	...	18,997	0	0
Less Fire Destruction	...	...	...	7,665	13	5
	11,331	6	7			
Further Expenditure on Sheds, Cranes, etc.	...	...	...	16,187	13	3
	27,518	19	10			
Saw Mills, new expenditure	...	...	...	12,135	17	5
Drying Kiln, as last year	...	...	...	9,966	5	1
Motor Trailers, etc., new expenditure	...	...	...	636	13	6
Office Furniture as at June, 1921, and additions	...	...	...	544	2	0
Stock on hand	...	...	...	159,130	4	5
Debtors:—						
On Open Accounts	...	...	...	48,331	13	7
On Acceptances	...	...	...	3,787	18	1
	52,119	11	8			
Less Reserve for Discounts	£3,000	0	0			
Bad Debts	13,939	0	0			
	16,939	0	0			
	35,180	11	8			
Timber Holdings Limited Shares	...	...	...	50,000	0	0
Fullers Electrical Works Ltd.:—						
£500 Shares at cost	...	...	...	518	15	0
	50,518	15	0			

By Cash:			
At Bank	...	4,534	5 5
" on Deposit	...	332,701	13 2
" in France	...		
" Deposit	...	2,207	9 0
" in France	...		
" Deposit	...	4,477	3 5
			<u>343,920 11 0</u>

£643,051 19 11

£643,051 19 11



## PROFIT AND LOSS ACCOUNT FOR YEAR ENDING 30th JUNE, 1922.

	£	s.	d.	£	s.	d.
To Wages ... ..	...	...	...	13,843	4	9
" Yard and Stable Expenses ... ..	...	...	...	671	3	9
" Rent ... ..	...	...	...	386	8	0
" Rates and Water ... ..	...	...	...	1,508	11	2
" Income Tax Schedule " D " ... ..	...	...	...	20,000	0	0
" " " " " A " ... ..	...	...	...	545	0	0
(not deducted from Rent).						
Salaries :—						
Managing Director ... ..	500	0	0			
Office and Travellers ... ..	6,702	5	0			
Commission ... ..	...	...	...	7,202	5	0
Travelling Expenses ... ..	...	...	...	1,754	9	4
General Business Expenses :				5,940	4	11
Bill Stamps, Measuring Light, Heat, etc.				4,259	10	2
Advertising ... ..	...	...	...	571	8	6
Stationery ... ..	...	...	...	105	12	11
Postage ... ..	...	...	...	153	0	0
Accountants' Charges ... ..	...	...	...	210	10	0
Petty Cash ... ..	...	...	...	110	5	0
Discounts and Allowances ... ..	...	...	...	269	9	5
Bank Interest and Charges ... ..	...	...	...	4,074	17	9
Repairs ... ..	...	...	...	436	15	2
Bad Debts ... ..	...	...	...	849	11	3
Director's Fee ... ..	...	...	...	100	0	0
Saw Mill Expenses ... ..	...	...	...	59	1	10
Depreciation, Wansbeck Road ... ..	...	...	...	300	0	0
Balance being Net Profit for year ... ..				63,351	8	11
				3,921	6	6
				£67,272	15	5

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£67,272 15 5

## TRADING ACCOUNT FOR THE YEAR ENDING 30th JUNE, 1922.

	£	s.	d.	£	s.	d.
To Stock-in-Trade	...	...	...	...	...	...
" Purchases	240,905	13	8	161,783	6	5
" Freight	154,584	11	8	159,130	4	5
" Carriage and Cartage	9,969	4	9			
" Lighterage	3,618	13	0	320,913	10	10
" Dock Dues	2,050	0	0	160,824	15	8
" Insurance	547	1	9			
" Difference on Dollars bought to provide for payment of American Purchases which were in error paid otherwise, and so are charged as Purchases at lower prices	3,103	10	4			
	6,439	5	9			
	421,218	0	11			
" Balance being Gross Profit on Sales (of which £25,925 is caused by the error in the Stocktaking at June, 1921)...	60,520	5	7			
	£481,738	6	6	£481,738	6	6

By Sales less Returns ... ..  
 ,, Stock-in-Trade ... ..  
 ,, Timber destroyed at estimated cost prices

## FIRE ACCOUNT.

Received from Insurances for Stock ... ..	£477,838	0	0
Stock at Fire approximately same as at June, 1921, as Accounts ... ..	£240,905	13	8
Add Error discovered by Somerset House Official ... ..	25,925	0	0
	266,830	13	8
Less Stock not burnt at cost prices ...	106,005	18	0
Stock destroyed at cost prices ... ..	160,824	15	8
Law Charges ... ..	2,845	2	6
Expenditure on clearing Yard ... ..	1,000	0	0
Balance transferred ... ..	313,168	1	10
	£477,838	0	0

(2) *The Commissioners of Inland Revenue v. J. Gliksten & Son, Limited.*

This case related to an assessment to Corporation Profits Tax for the accounting period 1st July, 1921, to 30th June, 1922, the material point being the same as in the Income Tax case. The case was stated in similar terms, *mutatis mutandis*.

The cases came before Rowlatt, J., in the King's Bench Division on the 6th and 7th December, 1927, and on the latter date judgment was given in favour of the Crown, with costs.

The Attorney-General (Sir D. Hogg, K.C.) and Mr. R. P. Hills appeared as Counsel for the Crown and Sir J. Simon, K.C., Mr. A. M. Latter, K.C., and Mr. C. King for the Respondents.

## JUDGMENT.

**Rowlatt, J.**—In these cases the question to be decided is what amount of the money received from the insurance company by the Respondents, who lost a large part of their stock by fire—the loss being covered by insurance—they are to bring into their trading account for the purpose of Income Tax and Corporation Profits Tax.

(Rowlatt, J.)

I have the trading account<sup>(1)</sup> before me and it is in the normal form. It starts with the stock-in-trade in hand at the beginning of the year on the left hand side, then the amount of purchases, and then the amount of expenses, and then there is the total. On the other side there is, of course, the amount of sales and the stock-in-trade that is left at the end of the year: that is totalled and the difference between the two would normally show the gross profit or the gross loss on the year's trading. But in the year in question, owing to the fire, some of the stock which they had at the beginning of the year and which they bought during the year is not accounted for either by the sales or by the stock-in-trade which is left, because it has been burnt.

How do the Respondents bring that in? They bring that in as an item "timber destroyed". At what price do they bring that in? The timber is gone and the Respondents have received money from the insurance companies in respect of the timber destroyed, but they do not bring in the money that they have so received instead of the timber. What they bring in is a figure being the estimated cost price of the timber.

That is simply saying this: that the insurance is treated not as having provided money to take the place of the goods burnt, but as having prevented the fire; that is the long and short of it. It seems to me that the Respondents must account for this timber that has been destroyed by fire; they have received the money from the insurance company in place of it. I can see no reason why that money should not be brought into the account instead of the timber. It seems to me not difficult. But it is said by Sir John Simon that it is not the business of the Respondents to have fires and to collect the money from the insurance company. That may be a very attractive way of stating the Respondents' contention, but the fact is that the Respondents' business is to buy, hold and sell timber, and it is part of their business to insure timber while they have it, in order that if the timber is destroyed they may have the insurance money instead of the timber and, in my judgment, they must treat that money in the same way as they would have treated the timber, namely, as an item in their trading account.

In my judgment quite clearly the appeal of the Crown ought to be allowed.

**Mr. Reginald Hills.**—The appeal will be allowed with costs?

**Rowlatt, J.**—Yes.

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<sup>(1)</sup> See page 373 *ante*.

The Company having appealed against this decision, the cases came before the Court of Appeal (Lord Hanworth, *M.R.*, and Sargant and Lawrence, *L.JJ.*) on the 20th and 21st March, 1928, and on the latter date judgment was given unanimously in favour of the Crown, with costs, confirming the decision of the Court below.

Mr. F. H. Maugham, *K.C.*, Mr. A. M. Latter, *K.C.*, and Mr. C. King appeared as Counsel for the Company, and the Attorney-General (Sir D. Hogg, *K.C.*) and Mr. R. P. Hills for the Crown.

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#### JUDGMENT.

**Lord Hanworth, *M.R.***—This case is an interesting one, and has raised an interesting argument by Mr. Maugham and Mr. Latter. But we have come to the conclusion that the decision of Mr. Justice Rowlatt is right.

The case is one in which we have to deal with what I may call the proceeds of a fire. The Company are engaged in large business in the timber trade, and in their accounts, which were made up to the 30th June in each year, the stocks were valued at the cost or market value, whichever was the lower, and for the purposes of valuation large sums were, in the last two years of account before the fire, written off the original cost prices of the stock in respect of depreciation. It appears that a fire took place on the 8th August, 1921, and that a large amount of the timber was burnt. The actual amount of timber which was destroyed stood, at that valuation of cost or market value, at a sum of £160,824. The Company were insured in several insurance companies, and the ultimate amount which was received from the insurance companies in respect of that timber was the sum of £477,838. The discrepancy between the book value of the timber destroyed and the actual sum received from the insurance companies is stated in the Case, which says: "At the date of the fire there was a boom, which was being prolonged by the adoption on the part of the large timber merchants of a policy of holding up stocks. The high prices obtaining at that time and on the basis of which the insurance companies paid the Company's claim were due to this boom". In other words the Company were fortunate, because the contract of fire insurance being one of indemnity, the timber company were able to say to the fire insurance companies: "You must give us the sum which will indemnify us against the loss which we have suffered, because if we were to go into the market to replace in specie this timber which we have lost by fire we should have to expend £477,838, although it is

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“ quite true that in our books we were carrying that same amount “ of timber at a value of £160,824 and no more ”. Now the question arises : How should this large sum which has been received from the insurance companies be dealt with in the trading account of the timber company for the purposes of Income Tax, and, in the second case, for Corporation Profits Tax ?

Now it is said on behalf of the timber company : “ Our business “ is one in which we trade in timber—we buy and we sell—but we “ do not carry on a trade in fires. The misfortune which has over- “ taken us is one which is no part of our business. We do not “ contemplate a fire in the ordinary course of business, and therefore “ this large figure which we have received from the insurance com- “ panies must be taken as an indemnity for the lower sum, the book “ value of the timber, £160,824 and no more, and with regard to the “ margin which we have received from the insurance companies “ beyond that figure, that is a windfall—a nugget of gold dug up “ on our premises—which is no part of our trade and which does not “ fall into our trading account for subjection to Income Tax ”.

Now I think one must look a little more closely into the nature of the business of the timber company. We have got before us, set out or attached to the Case—it is set out conveniently on page 477 of the report of the case in [1928] 1 K.B.<sup>(1)</sup>—an account, and on one side of the account you have the stock-in-trade, purchases, and then also the charges for freight, for carriage and cartage, for lighterage, for insurance. All those items fall rightly within the trade account. The expenses, that is to say, whether of freight for bringing fresh stock-in-trade to the premises of the Company, the insurance for insuring the transit of the timber from overseas, are all items which you would find in the trading account as part of the ordinary business of the trader. On the other side of the account you find the sales, less returns, at a certain figure. Then you take the stock-in-trade, and then you have this sum for the timber which was destroyed at an estimated cost price. I have looked at that trading account because I think it shows conclusively what one would expect it to show, namely, that insurance, whether against marine risks or fire risks, is a part of the ordinary duty of the trader in carrying on his business. It is quite true to say that the timber company does not trade in fires. But governed by ordinary business prudence, and mindful of the fact that untoward events take place both by land and by sea, the Company take steps to insure an indemnity being paid to them whether they lose their stocks in transit to them by perils of the sea, or whether they lose it *in situ* on land by the perils and misfortune of fire. It is pointed out also, and much stress is laid upon it, that certain deductions are to be made in calculating the items to be set against the trading profit.

(1) See page 373 *ante*.

**(Lord Hanworth, M.R.)**

It is agreed that the premiums which are paid for insurance, whether for marine or for fire, are proper subjects for deduction in the ordinary trade account, and then attention is focussed upon the deductions which are allowed in computing the amount of the gains or profits to be charged, which are catalogued in Rule 3 of the Rules applicable to Cases I and II under the Income Tax Act, 1918. It is true that in form that Rule is negative; but, as has been pointed out by Lord Sumner in the House of Lords, while it restricts deductions and says that no sums should be deducted in respect of so and so, it must be read as allowing that in certain other cases there is a deduction to be allowed and to be made. The particular item to which our attention is called is Rule 3 (*k*). Rule 3 (*k*) runs in this way: "In computing the amount of the profits or gains to be charged, no sum shall be deducted in respect of . . . any sum recoverable "under an insurance or contract of indemnity". As Mr. Maugham has pointed out, some explanation of those words is necessary. It seems to contemplate that there has been a loss in respect of which there is an indemnity recoverable. Therefore one must read it in this form, that there is not to be a deduction, where there has been a loss, in respect of the sum which is recoverable in relation to that loss under a contract of indemnity. Putting it in other words, it forbids you to treat as a loss a sum which in fact is recoverable under a contract of indemnity. Thus it appears to me to mean this, that if you have got a loss of, say £100,000, and, let us say £75,000, is replaceable or recoverable under a contract of indemnity, then to the extent of that £75,000 you are not to make any deduction as if it were a loss, because instead of its being a loss the sum is replaceable or recoverable under a contract of indemnity. But Rule 3 (*k*) appears to contemplate that if, and so far as, there is a loss and it is not recoverable under a contract of indemnity, that loss would be a sum which could be deducted. I am, myself, however, unable to find in Rule 3 (*k*) any definite ground for the determination of this case. I think Mr. Justice Rowlatt has treated the question from the right point of view.

Messrs. Gliksten & Son, Ltd., were traders in timber; it was their business to buy and sell timber, and it was a part of their business—ancillary, perhaps—to take steps to insure their trade from the mischances which can be insured against, such as perils of the sea and perils of the land. They had a certain amount of fixed capital in their business, and they had a certain amount of circulating capital employed in the purchase of stock, which is enhanced again when the stock is sold. A part of that circulating capital was invested in timber. That timber might have been sold in the ordinary course of market—as a matter of fact, instead of being actually sold it was burnt. Under a contract of indemnity,

**(Lord Hanworth, M.R.)**

properly entered into for the purpose of safeguarding the possibilities of business in relation to it, a sum has been received in respect of the timber. That is once more a restoration to the actual circulating capital of a sum which had previously been invested in specie in timber. We have got to take the actual sum received, which has been received in the ordinary course of business, plus the ordinary safeguards of business in the events which have happened. As Mr. Justice Rowlatt says<sup>(1)</sup>: "It seems to me that the Respondents must account for this timber that has been destroyed by fire; they have received the money from the insurance company in place of it . . . the fact is that the Respondents' business is to buy, hold and sell timber, and it is part of their business to insure timber while they have it, in order that if the timber is destroyed they may have the insurance money instead of the timber and, in my judgment, they must treat that money in the same way as they would have treated the timber, namely, as an item in their trading account." Those are the words of Mr. Justice Rowlatt. It appears to me that they are right, and therefore that the appeal fails.

I would like to add one more word because it appears to me that the case is one which is clearly open to review by the Court. The Special Commissioners, somewhat curiously, appear to have made a finding in paragraph 12 (1) which, so far as I can read it, appears to me to be in direct conflict with the evidence as stated in paragraph 8 of Mr. F. W. Gower. Why they set the evidence out in the Case if they did not accept it I cannot imagine. There was no evidence called on the other side, we are told, and Mr. Gower's evidence is this: ". . . the normal commercial method of dealing with monies recovered by a trader under a policy of insurance in respect of stock destroyed by fire was to include the actual amount received in the accounts as an ordinary trading receipt in the same way as the proceeds of an ordinary sale of stock". That is the evidence as it stands. Upon that, without any comment from the Commissioners other than that it purports to be a satisfactory statement, the Commissioners say: "We are satisfied that the sum . . . . . recovered from the insurance companies does not represent a trade receipt". I find some difficulty as to what evidence there was upon which the Commissioners could come to that conclusion, having regard to the evidence which they themselves have set out in the Case Stated. However, I make that observation by the way. It certainly shows that the Commissioners appear to have dealt with a matter which must be a matter of law, namely, the proper way in which, in a trading account, the insurance money is to be dealt with. For the reasons I have given I think that it forms an ordinary

(1) See page 375 ante.



**(Lord Hanworth, M.R.)**

item in respect of the circulating capital of the trading company which has to be brought into the trading account and dealt with at its true value, and not at an artificial value, based upon the mode in which they estimate, for certain purposes, their book values of the timber actually in stock.

For those reasons I think the appeal fails and must be dismissed with costs.

**Sargant, L.J.** — With great respect to the arguments of Mr. Maugham and Mr. Latter it seems to me that this is a very plain case. We have to consider whether, in computing under the Rules applicable to Schedule D, Case I, the balance of the profits or gains of this Company during the year or during the three years, this large sum of over £400,000 received from the insurance companies under the policies of insurance against fire is to be taken as being one of the gains to be brought into account. The facts are really beyond dispute.

The Company, trading as a timber company, in the ordinary course of business insured its timber against loss or damage by fire. That was an ordinary trade outgoing allowed for, of course, in the trading account. Fire is an event which has to be taken into account as an ordinary risk of a company of this kind, and in consequence of the insurance this very large sum was recovered. To my mind, on the face of the transaction itself, the whole of the amount so recovered is clearly an amount which ought to be brought in. It is an ordinary receipt in this sense, not that it occurs every year or regularly at stated periods, or anything of that kind, but that it is a receipt which would ordinarily be received in case the risk insured against should happen. A great deal has been made, or attempted to be made, of Rule 3 (*k*). To my mind really that Rule does not affect the matter in any way. I do not think there is any real doubt about the effect of the Rule. The words of the Rule are: "any sum recoverable under an insurance or contract of indemnity"; that is to say, it is one of the items in respect of which there shall be no deduction. It seems to me that head (*k*) assumes that there has been a loss and that the loss is one which is wholly or partially covered by an insurance or contract of indemnity; and the effect of the words seems to me quite clear, namely, that to the extent to which the loss is met by the sum recoverable under the contract of indemnity or insurance, the loss is not chargeable in the ascertainment of profits and balance of profits. To my mind the broad meaning of those words is, so far as it goes, rather against the Appellants than in their favour because, broadly speaking, I think the words mean that the amount recoverable in such a case is to take the place of the asset lost, so far as the amount recoverable

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goes. What is said by the Appellants is that you must take account not of the actual sum recovered, but only of the book value, in the Company's books, of the timber destroyed, and that as regards any excess of the amount recovered over the book value, that is a mere windfall and is not to be accounted for at all. I fail to follow that argument altogether. To my mind the book value of the timber in the Company's books has nothing at all to do with the amount of the loss or with the amount which has been recovered in respect of the loss. That amount is a gain of the Company in the course of its business no less than the sale price of the timber would have been if the timber had been sold in the course of ordinary sales during the continuance of the Company's business; and in estimating the balance of the profits or gains which the Company has to bring into account for the purposes of Income Tax, the amount of the excess of the sum recovered over the book value of the timber in the Company's books has to be brought into account just as fully and completely as if there had been a sale in the ordinary course of business at that price, in which case it is conceded by the Appellants that the full amount of the difference between the sale price and the book value in the Company's books would have had to be brought into account. I agree that the appeal should be dismissed.

**Lawrence, L.J.—I agree.**

The Appellants contend that the difference between the book value of the timber and the amount paid by the insurance companies is not a trading receipt but is in the nature of a windfall, and in support of that contention they rely mainly upon Rule 3 of the Rules applicable to Cases I and II in Schedule D. Their contention is that Rule 3 (*k*) negatives the idea of bringing in the insurance money as one of the items of receipt, and that what has to be brought in is the book value of the stock which has been burnt, and that the excess over that value is not a trading receipt and does not stand on the same footing as the proceeds of sale of the stock. In my opinion that contention is not well-founded. The effect of Rule 3 (*k*) in my judgment is that, in arriving at the balance of profits or gains there has to be no deduction in respect of a loss which is covered by insurance to the extent by which that loss is so recovered. But that in no way negatives the idea that if the true value of the stock burnt is received from the insurance companies, that receipt is a receipt in the ordinary course of the Company's business. I agree, of course, that a fire is not an ordinary incident in a trading business; but if it does occur I think the receipt from the insurance company is an ordinary receipt in that it is a receipt which an ordinary trader generally stipulates for in case his stock is burnt. I agree with

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Mr. Justice Rowlatt that the insurance money ought to be treated, for the purposes of ascertaining the balance of profits or gains, as an ordinary trading receipt in the same manner as the proceeds of the sale of the stock would have had to be treated had the stock been sold.

I agree that the appeal fails and ought to be dismissed.

**Mr. Hills.**—The other appeal against the Commissioners of Inland Revenue will also be dismissed?

**Lord Hanworth, M.R.**—That follows in both cases, does it not, Mr. Latter?

**Mr. Latter.**—Yes, my Lord.

**Lord Hanworth, M.R.**—Then in both cases the appeal will be dismissed with costs.

**Mr. Latter.**—If your Lordship pleases.

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The Company having appealed against this decision, the cases came before the House of Lords (Lord Buckmaster, Viscount Dunedin and Lord Warrington of Clyffe) on the 22nd February, 1929, when judgment was given unanimously in favour of the Crown, with costs, confirming the decision of the Court below.

Mr. H. P. Macmillan, K.C., Mr. A. M. Latter, K.C., and Mr. C. King appeared as Counsel for the Company and the Attorney-General (Sir T. Inskip, K.C.) and Mr. R. P. Hills for the Crown.

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#### JUDGMENT.

**Lord Buckmaster.**—My Lords, the Appellants are timber merchants who carry on their business at Stratford, near London. In August, 1921, they had a large quantity of timber stored upon their premises, and on the 8th of that month a fire broke out and destroyed a considerable quantity of the Appellants' goods. The goods had, in the due course of their business, been insured, and as the result of the insurance the Appellants received £477,838 from the insurance companies. But the timber had stood in their books and balance sheets as representing the figure of £160,824, and accordingly the Appellants sought to bring only that latter figure in for the purposes of assessment to Income Tax, while the Inland Revenue authorities asserted that they were bound to bring in the larger sum.

**(Lord Buckmaster)**

The accounts of the Appellants' business are set out and they show that the ordinary method of accounting is followed. They bring in on the debit side of their balance sheet the stock-in-trade they have at the beginning of the year, the amount they purchase, the various charges that they incur in connection with it, and, on the other side, their sales and their stock-in-trade at the end of the accounting period. It therefore follows that if, in the place of stock-in-trade that was brought forward on the credit side they introduced this £477,000, there would be a large sum of profit which would be liable to assessment for tax. In point of fact the way in which they sought to bring it in was by entering the figure merely under the head of "Timber destroyed at estimated cost prices" at the lower sum of £160,000.

My Lords, the Special Commissioners thought that they were right in that course: Mr. Justice Rowlatt and the Court of Appeal have unanimously thought that they were wrong.

The Appellants seek to fortify their argument by a consideration of the Rules that apply to Schedule D under the Income Tax Act, 1918. They point out that under that Schedule the tax is to apply to a trade and is to be computed on the amount of the profits and gains of the trade; and they say that whatever was received in relation to this fire was not a profit or gain of the trade, but that it was something received from the insurance, that the real business that they were carrying on was not that of insuring the timber, but its purchase and its sale. Further they say that by Sub-head (*k*) under Rule 3 of the Rules applicable to Cases I and II there is an express provision that there shall not be deductible from the profits and gains any sum recoverable under an insurance or contract of indemnity, and they suggest that that means that by implication there is a prohibition against bringing in on the other side the moneys that are received under such a contract. My Lords, I am quite unable to take that view. All that Sub-head (*k*) does is to prevent them from bringing in a loss which they have incurred that is covered by insurance, when, in fact, the amount of that loss is capable of being recovered by the policy monies that they may receive; it goes no farther than that, and so far as it does extend, it is, I think destructive of that part of the argument of the Appellants, which consisted in saying that if they were bound to bring in the moneys that they received from the insurance company on the one hand they could bring in the equivalent amount of losses on the other; this Sub-section, which is in language not specially ambiguous, has expressly provided that they shall not do anything of the kind.

There remains this question: Ought the total amount of these insurance moneys to be regarded as part of the profits and gains

**(Lord Buckmaster)**

of the trade? My Lords, in my opinion they ought, and for this reason: What has happened has been this, that the timber which the Appellants held has been converted into cash. It is quite true it has been converted into cash through the operation of the fire, which is no part of their trade, but loss due to it is protected through the usual trade insurances, and the timber has thus been realised. It is now represented my money, whereas formerly it was represented by wood. If this results in a gain, as it has done, it appears to me to be an ordinary gain—a gain which has taken place in the course of their trade—none the less because, as Mr. Macmillan put it, and as I think Sir John Simon before him appears to have put it, it is no part of a timber merchant's business to trade in fires. I think that a few words in the judgment of Lord Justice Sargant express the whole matter in a sentence, and to them it is unnecessary to add anything more. He says<sup>(1)</sup>: "To my mind the book value of the timber in the Company's books has nothing at all to do with the amount of the loss or with the amount which has been recovered in respect of the loss. That amount is a gain of the Company in the course of its business no less than the sale price of the timber would have been if the timber had been sold in the course of ordinary sales during the continuance of the Company's business; and in estimating the balance of the profits or gains which the Company has to bring into account for the purposes of Income Tax, the amount of the excess of the sum recovered over the book value of the timber in the Company's books has to be brought into account just as fully and completely as if there had been a sale in the ordinary course of business at that price."

My Lords, for these reasons I think that this Appeal should be dismissed.

**Viscount Dunedin.**—My Lords, I agree. In these Income Tax Act cases one has to try, as far as possible, to tread a narrow path, because there are quagmires on either side into which one can easily be led, and I think into one of these quagmires we were tempted to be led when the argument turned upon the question of what you were entitled to debit or not. I do not think this case has anything to do with debiting losses. The whole point is that the business of the Company is to buy timber and to sell timber, and when they sell timber they turn it into money. This particular timber was turned into money, not because it was sold, but because it was burned and they had an insurance policy over it. The whole question comes to be whether that is a turnover in the ordinary course of their business. I think it was. They had that amount of timber, which they got rid of and for which they got

(1) See page 381 *ante*.

**(Viscount Dunedin)**

a certain price, and then they could begin again. The more times you have a turnover, that is to say, the more sales you can get, provided that you are carrying on business at remunerative prices, the better for you. The result of this fire was that they got rid of so much timber and got the insurance money at that figure, and that seems to me precisely in the same position as if they got rid of it by giving it to a customer. If that is so, that is exactly the view of Mr. Justice Rowlatt, and I think he arrived at the right result.

**Lord Warrington of Clyffe.**—My Lords, I agree, and I have nothing to add except to say that to me, at all events, it is some comfort to think that the decision we are giving is in accordance with the commercial practice, because I notice that the chartered accountant who alone gave evidence on the point says that in his experience as a chartered accountant extending over twenty years the normal commercial method of dealing with moneys recovered by a trader under a policy of insurance, in respect of stock destroyed by fire, was to include the actual amount received in the accounts as an ordinary trading receipt in the same way as the proceeds of an ordinary sale of stock.

*Questions put :*

In *J. Gliksten and Son, Ltd. v. J. H. Green (H.M. Inspector of Taxes)*.

That the judgment appealed from be reversed.

*The Not Contents have it.*

That this appeal be dismissed with costs.

*The Contents have it.*

In *J. Gliksten and Son, Ltd. v. Commissioners of Inland Revenue*.

That the judgment appealed from be reversed.

*The Not Contents have it.*

That this appeal be dismissed with costs.

*The Contents have it.*

[Solicitors :—The Solicitor of Inland Revenue ; Messrs. Ward, Perks and Terry.]

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