HIGH COURT OF JUSTICE (CHANCERY DIVISION)—12TH, 13TH AND 28TH FEBRUARY, 1958

COURT OF APPEAL—3RD, 7TH, 8TH AND 9TH OCTOBER, 1958

HOUSE OF LORDS—23RD, 24TH AND 25TH JUNE AND 16TH JULY, 1959

Hinton (H.M. Inspector of Taxes)

v.

Maden & Ireland, Ltd.[1]

Income Tax, Schedule D—Investment allowance—" Machinery or plant " —Capital or revenue expenditure—Finance Act, 1954 (2 & 3 *Eliz.* II, *c.* 44), *Section* 16 (3).

The Respondent Company carried on the business of shoe and slipper manufacturers. It used machines which could only function when furnished with knives or lasts appropriate to the particular process. The knives and lasts were useless without the machines. Many thousands of them were in use and their life was short. A physical stock-taking being impossible owing to the large number, the Company (which made up its accounts half-yearly) charged expenditure on new knives and lasts to capital, and charged against profits one-quarter of the total cost in each of the four succeeding half-yearly accounts. Its profits had for some years been computed for Income Tax purposes on the footing that a deduction of one-sixth of such expenditure in each of the six succeeding half-years represented the best estimate of the sums expended by the Company on implements, utensils or articles employed for the purposes of its trade within Section 137 (*d*), *Income Tax Act,* 1952.

On appeal against an assessment to Income Tax under Schedule D for the year 1955–56 *the Company claimed that this expenditure qualified for an investment allowance, on the grounds that the knives and lasts were " plant or machinery " as well as being " implements or utensils " and that the expenditure was on capital account. For the Crown it was contended that the expenditure was on revenue account and that the knives and lasts were not plant or machinery. The Special Commissioners found that the knives and lasts were machinery or plant, and held that the Company was entitled to the allowance.*

Held, *that* (1) *the knives and lasts were machinery or plant ;* (2) *expenditure on the knives and lasts was capital expenditure.*

CASE

Stated under the Income Tax Act, 1952, Section 64, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the High Court of Justice.

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 2nd and 3rd April, 1957, Maden & Ireland, Ltd.

(1) Reported (H.L.) [1959] 1 W.L.R. 875; 103 S.J. 812; [1959] 3 All E.R. 356; 228 L.T. Jo. 11.

(hereinafter called " the Respondent "), appealed against an assessment made upon it for the year 1955–56 in the sum of £8,290 less capital allowances £4,836 in respect of its profits as shoe and slipper manufacturers. The sole question for our determination was whether certain expenditure incurred by the Respondent on knives and lasts in the material period qualified for an investment allowance under the provisions of Section 16 (3), Finance Act, 1954.

2. At the hearing of this appeal evidence was given before us by Mr. John Muir Layland, joint managing director of the Respondent's business, who had been concerned in the manufacture of shoes and slippers all his life, and by Mr. Vernon Harcourt Collinge, partner in the firm of J. H. Lord & Co., incorporated accountants, auditors of the Respondent. The following documents which were produced in evidence before us are attached to and form part of this Case(1):

Exhibit 1, printed accounts of the Respondent for the year ended 2nd October, 1954.

Exhibit 2*a*, accounts of the Respondent for the half year ended 3rd April, 1954.

Exhibit 2*b*, accounts of the Respondent for the half year ended 2nd October, 1954.

Exhibit 2*c*, supplementary information relating to the two foregoing half years' accounts.

Exhibit 3, summary of the knives and lasts of the Respondent as appearing in the Respondent's accounts for the half years ended 3rd April and 2nd October, 1954, respectively.

Exhibit 4, booklet illustrating and describing various machines used by the Respondent in the manufacture of shoes and slippers.

In addition to the foregoing documents certain knives and lasts were produced to us in evidence by Mr. Layland, who, with the assistance of the descriptive booklet (Exhibit 4), demonstrated to us the processes of manufacture of certain types of shoes and slippers and the functions of the said knives and lasts in these processes.

The facts found by us and admitted or proved before us are stated in the following paragraphs numbered 3 to 6 inclusive.

3. The Respondent uses a number of machines in the course of carrying on its business of shoe and slipper manufacturers.

(i) An " ideal clicking press " (Exhibit 4, page 15) for cutting upper components, fittings, etc., from leather, plastic, fabric or other materials. The cost of this machine at the material time was £423, exclusive of the cost of any knives. Its sole function is to cut the leather or other fabric to the size required for shoes or slippers and it can only function when provided with knives of the shape required for the several parts of the particular shoe. Different knives are required for uppers from those used for cutting soles, and different sets of knives are required for right and left shoes. The Respondent also uses a " revolution press " performing similar functions and depicted on page 57 of Exhibit 4, the cost of which at the material time was £1,096 if worked from a line shaft or £1,164 if used with its own motor. More upper knives are required than sole knives. But different sole knives would be needed according to the type of upper knife and material used, and also according to the type of soling material used and soling design and finish required. At any given time hundreds of knives were used in

(1) Not included in the present print.

the Respondent's factories and, though readily detachable, they are an essential and indispensable part of the cutting machines, to the extent that the machine without the knife is useless and conversely without the machine the knife is useless. Furthermore, apart altogether from the normal process of wear and tear, the Respondent constantly bought new knives whenever a new line of shoes came on the market. Some such lines, particularly in fancy shoes, involve a number of very intricately patterned knives.

(ii) After the cutting and machining together (closing) of the uppers they are transferred to a " pulling-over machine ", an example of which is depicted in Exhibit 4, page 113. This process requires an upper to be placed over the last and to be presented to the machine, which pulls the upper over the last and clenches it with six tacks. The cost of a pair of making lasts at the material time was £1 2*s*. In this process, similarly, the machine is useless without the last and conversely without the machine the last is useless.

(iii) The shoe then passes to a consol " lasting machine " for final lasting, an example of which is depicted in Exhibit 4, page 115. In this machine, as in that described in sub-paragraph (ii) above, a last, though readily detachable, is an essential and indispensable part of the machine.

(iv) The next process is the " pounding machine ", which, simulating the cobbler's action of hammering the leather flat, performs this function on the back lasted shoe, which must be secured during the process on a last of the required size and pattern.

(v) The next process, that of attaching the prepared soles by chain stitching (Blake sewing), Exhibit 4, page 139, requires no last, but in all the operations up to this stage the machines could not be used without either knives or " making lasts ".

(vi) After chain stitching (Blake sewing), the stitching channels on the sole are closed and the sole is levelled to the correct shape on a levelling machine (Exhibit 4, page 148 B). On this machine metal feet and forms, being exact replicas of the shape of the making last, are used in conjunction with the hydraulic pressure of the machine to mould the sole to the correct shape. The shoe then goes to the finishing room, where the heel is attached on a finishing last inserted. The sole and heel edges are pared and then set. If such an operation were performed without a last the shoe would lose its shape. So the different type of last known as a " finishing last " is used in conjunction with the machines, e.g. an " edge trimming machine ", depicted on page 210G of Exhibit 4.

(vii) The next processes of edge setting and heel burnishing are performed on a machine depicted at page 219 in Exhibit 4 and, as good pressure is required, a last to hold the shoe steady is still essential.

(viii) The shoe bottom is then scoured, painted and polished, on the machines depicted at pages 215, 216, 235 and 236 of Exhibit 4, and the shoe remains on the last for these processes, only leaving it after the final finishing processes.

(ix) The lasts described above thus fall into two classes, the making and the finishing lasts, the former having a metal base to enable tacks to be clenched over. Lasts are made of maple, beech or hornbeam. The Respondent attempts to use its last as long as possible, but fashions change and every change of fashion involves a change of last.

(x) Summarising the processes employed by the Respondent in carrying out its trade, it can be broadly stated that the Respondent utilises either knives or lasts (the latter making or finishing) in 90 per cent. of its manu-

facturing and finishing processes and that the machines that it uses can only function when furnished with the knives or lasts appropriate to the particular process. At the material time the Respondent in one of its factories had approximately 12,000 pairs of making lasts and 24,000 pairs of finishing lasts for a production of 1,200 dozen pairs of shoes per week. No such estimate of the number of knives in use was available to us in evidence, but one shoe might require as many as 14 knives per half pair.

(xi) The average life of upper knives is 12 months, but sole knives, subject to a 10 per cent. loss due to careless handling, have a life equal to that of the corresponding last. The average life of making lasts is three years and that of finishing lasts similar, except that the latter can sometimes be used apart from the making lasts, and they might then be used for four to five years. A greater float of lasts must be kept because the shoe stays on it for a number of processes, whereas a knife is used once only for each pair of shoes.

4. Owing to the large number of lasts and knives employed in the Respondent's business no physical stock-taking at the half-yearly dates to which its accounts are made up was possible. The Respondent therefore charged all expenditure on new knives and lasts to capital and charged against profits one-quarter of the total cost in four succeeding half-yearly accounts, on the view that an average life of two years for the combined total expenditure on knives and lasts was a fair estimate. The actual expenditure on new knives and lasts and the amount so charged against profits in the two half-years' accounts ending respectively on 3rd April and 2nd October, 1954, forming the basis of the material year 1955-56, are set out in Exhibit 3 under the headings of the five manufacturing units of the Respondent's business. Thus, the figure of £8,022 5*s*. appearing in the balance sheet at 2nd October, 1954, (Exhibit 2*b*), is the balance after crediting total additions in the half-year of £1,856 8*s*. 5*d*. and after debiting to profit and loss account a sum of £3,542 19*s*. 1*d*., being the writing off at 25 per cent. of expenditure on knives and lasts in the preceding four half-years.

5. The expenditure on knives and lasts during the basis year and the six years immediately preceding the basis year was as follows :

Half-year to			March, 1948	... ...	£2,075
„	„	„	September, 1948	... ...	£1,451
„	„	„	March, 1949	... ...	£3,706
„	„	„	September, 1949	... ...	£3,868
„	„	„	March, 1950	... ...	£4,659
„	„	„	September, 1950	... ...	£1,151
„	„	„	March, 1951	... ...	£3,527
„	„	„	September, 1951	... ...	£1,026
„	„	„	March, 1952	... ...	£5,195
„	„	„	October, 1952	... ...	£1,404
„	„	„	March, 1953	... ...	£5,131
„	„	„	October, 1953	... ...	£3,476
„	„	„	April, 1954	... ...	£4,160
„	„	„	October, 1954	... ...	£1,856

No dissection of the figures of expenditure between knives and lasts had been attempted by the Respondent, and we were satisfied that such a dissection, if not actually impossible, was not reasonably practicable.

6. The Revenue had taken the view that for Income Tax purposes the Respondent's estimate of the life of knives and lasts was too conservative, but had agreed that an average life of three years instead of two years

was reasonable. The Respondent had accepted the Revenue's contention for Income Tax purposes, and in the result a sum equal to one-sixth of the total expenditure on knives and lasts has been for a number of years allowed as a deduction in the following six half-years, as such accounts came into the computation of the Respondent's profits for Income Tax purposes. This deduction was regarded by the Revenue as the nearest practicable and just estimate of the sum expended by the Respondent " for the supply, repairs or alterations of any implements, utensils or articles employed, for the purposes of the trade ", within the meaning of Section 137 (*d*), Income Tax Act, 1952. It was common ground between the parties in this appeal that the amount so allowed for Income Tax purposes was not the sum " actually expended ", since (i) it related to expenditure incurred in the preceding six half-yearly periods and (ii) it was the result of a " straight line writing-down " on the basis of the Revenue's contention of an estimated three years' life. For the reasons hereinafter set out in paragraph 10 below, we do not consider that either the method adopted by the Respondent in making up its accounts or the variation of that method adopted by the Revenue and accepted by the Respondent for Income Tax purposes affects the issue on which we were called upon to give our determination.

7. The question for our determination was whether knives and lasts, or, in the alternative, whether either knives or lasts, were, on the evidence before us, machinery or plant within the meaning of Sections 279 and 280, Income Tax Act, 1952, and Section 16 (3), Finance Act, 1954. No issue arose before us with regard to the annual allowances " on account of the wear and tear of the machinery or plant which belonged to the Respondent and was used for the purposes of the Respondent's trade ", for, whether the expenditure on knives or lasts was properly described as expenditure on plant and machinery or not, the Revenue had allowed and the Company had accepted deductions in computing their profits arrived at by the method described in paragraph 6 above, so that in any event any claim for annual allowances would be excluded by Section 330 (1) (*a*) of the Income Tax Act, 1952. The sole issue before us was whether in addition to the said deductions the Respondent was entitled for the said year 1955–56 to an investment allowance under the provisions of Sections 16 (3), Finance Act, 1954, equal to one-fifth of the expenditure on knives and lasts on the view that such expenditure was " for the provision of new machinery or plant ".

8. It was contended on behalf of H.M. Inspector of Taxes:

(i) that the expenditure on knives and lasts incurred by the Respondent in carrying on its trade was not expenditure on capital account but on revenue account;

(ii) that on the evidence the said knives and lasts were not parts of the machines which operated them but were separate chattels;

(iii) that on the evidence the said knives and lasts were implements, utensils or articles employed for the purposes of the Respondent's trade, within the meaning of Section 137 (*d*), Income Tax Act, 1952;

(iv) that the said knives and lasts, being implements or utensils employed for the purposes of the Respondent's trade, were not plant or machinery eligible for an investment allowance, within the meaning of Section 16 (3) (*c*), Finance Act, 1954.

9. It was contended on behalf of the Respondent:

(i) that on the true construction of Sections 137, 279 and 280, Income Tax Act, 1952, and of Section 16, Finance Act, 1954, the words

" implements, utensils and articles " and " plant or machinery " were not mutually exclusive but to some extent overlapping ;

(ii) that on the evidence in this case the knives and lasts employed for the purposes of the Respondent's trade were both " implements or utensils " within Section 137 (*d*) and " plant or machinery " within Sections 279 and 280, Income Tax Act, 1952, and Section 16 (3) (*c*), Finance Act, 1954 ;

(iii) that on the evidence in this case the expenditure on knives and lasts, although they had a short life, was expenditure none the less on capital account in respect of fixed assets and not on revenue account in respect of circulating capital ;

(iv) that the said expenditure on knives and lasts was, on the evidence, expenditure on the provision of new machinery or plant within the meaning of Section 16 (3), Finance Act, 1954, and although notionally allowed to be deducted in computing profits and gains for the purpose of Income Tax was, nevertheless, by virtue of Section 16 (3) (*c*), Finance Act, 1954, to be treated as capital expenditure for the purposes of that Section ;

(v) that the Respondent was accordingly entitled to an investment allowance in respect of the said expenditure on knives and lasts for the said year 1955–56.

10. We, the Commissioners who heard this appeal, decided to allow it :

(i) We held that the words " machinery or plant " as used in Sections 279 and 280, Income Tax Act, 1952, and Section 16 (3), Finance Act, 1954, were not words of art, but on a proper construction of the Sections were to be given their ordinary meaning. So directing ourselves, we did not doubt that there might be trades employing knives and lasts in circumstances which would make it inappropriate to describe them as machinery or plant. But in the case before us we thought we should give weight to the facts (1) that the knives and lasts performed an indispensable function in the process of manufacture, (2) that in performing that function they were used, and could only be used, in conjunction with machines which themselves could perform no useful function in the said process unless used in conjunction with the lasts and knives, and (3) that, as was not disputed, the said machines themselves were machinery or plant within the meaning of the relevant Sections.

(ii) We found as a fact on the evidence that the knives and lasts were machinery or plant within the meaning of the said Sections and we held that the Respondent was entitled to the investment allowance claimed.

(iii) In coming to this conclusion we did not consider it material to decide whether the knives and lasts were " implements, utensils or articles " within Section 137 (*d*), Income Tax Act, 1952, or whether the allowances referred to in paragraph 6 of this Case were or were not made under and by virtue of that Section. In our view, even if the said allowances were made, and properly made, by virtue of Section 137 (*d*), nevertheless, having regard to the decision in *Commissioners of Inland Revenue* v. *Great Wigston Gas Co.*, 29 T.C. 197, and to the provisions of Section 16 (3) (*c*), Finance Act, 1954, that did not prevent our coming to the conclusion set out in sub-paragraph (ii) hereof.

(iv) Accordingly, we determined the assessment for the said year 1955–56 in the sum of £8,290 less £5,148 capital allowances, these being the figures agreed by the parties following our decision in principle.

11. The Appellant, immediately after 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, 1952, Section 64, which Case we have stated and do sign accordingly.

12. The point of law for the opinion of the High Court is whether, on the evidence hereinbefore set out, we were justified in holding that the Respondent's expenditure on knives and lasts was expenditure on the provision of new machinery or plant within the meaning of Section 16 (3), Finance Act, 1954, and whether our decision was right in law.

A. W. Baldwin
R. A. Furtado
} Commissioners for the Special Purposes of the Income Tax Acts.

Turnstile House,
94–99, High Holborn,
London, W.C.1.
30th October, 1957.

The case came before Vaisey, J., in the Chancery Division on 12th and 13th February, 1958, when judgment was reserved. On 28th February, 1958, judgment was given in favour of the Crown, with costs.

Mr. B. L. Bathurst, Q.C., and Mr. Alan Orr appeared as Counsel for the Crown, and Mr. G. B. Graham for the Company.

Vaisey, J.—This is an appeal from a decision of the Special Commissioners on a Case Stated, bearing date 30th October, 1957. In a sense the point in issue is one of pure fact, though it may also be regarded as involving questions of construction of the statutory provisions, or perhaps only a question as to the meaning of an expression containing two very ordinary English words—" machinery " and " plant ". The Respondents, Maden & Ireland, Ltd., are manufacturers on a large scale of boots, shoes and slippers. The Crown is the Appellant and, being dissatisfied with the decision of the Commissioners, now asks the Court to reverse it.

These, briefly, are the facts. Employed in the Respondents' business are a number of heavy, large, complicated and expensive machines, into which certain knives are inserted which, though readily detachable from them, can be considered none the less on one view as essential parts of the machines. It appears that every new line or type of shoe requires a new shape of knife. These knives wear out quickly and constantly require to be replaced. It is the great disparity in length of life between the permanent, heavy, solid machines and the readily perishable and easily worn-out knives which are put into them (but not, I understand, fixed in them) which gives rise to the problem involved in the present case. Besides the knives there are also objects called lasts without which the machines in which they are used cannot work at all, while conversely a last is absolutely useless except when placed in the appropriate machine. Many analogous cases may be suggested, such as an electric light system without bulbs, a gramophone without rotating discs, a motor car without petrol or oil, or a pipe without tobacco. The machines themselves are obviously " machinery or plant ", and the question in the case is whether the Respondents' knives and lasts, which are many thousands in number, are

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themselves machinery or plant, either in their own nature or as parts of the machines in which they are used. The Special Commissioners have in substance held that the question should be answered affirmatively in one or other of its alternative forms.

The relative facts are clearly set out in the Case, but I would read to make my judgment intelligible the substance of paragraph 3 (x) and (xi) of the Case Stated, which state, in effect, as follows. Summarising the processes employed by the Respondents in carrying out their trade, it can be broadly stated that they utilise either knives or lasts (the latter being either " making lasts " or " finishing lasts ") in 90 per cent. of their manufacturing and finishing processes, and that the machines which they use can only function when furnished with knives or lasts appropriate to the particular process. At the material time the Respondents in one of their factories had approximately 12,000 pairs of " making lasts " and 24,000 pairs of " finishing lasts " for a production of 1,200 dozen pairs of shoes per week. No such estimate of the number of knives in use was available to the Special Commissioners or to the Court in evidence, but it is stated that one shoe might require as many as 14 knives per half pair. The average life of upper knives is 12 months, but sole knives (subject to a 10 per cent. loss due to careless handling) have a life equal to that of the corresponding last. The average life of " making lasts " is three years and that of " finishing lasts " similar, except that the latter may sometimes be used apart from the " making lasts ", in which case they might be used for four to five years. A greater float of lasts must be kept because the shoe stays on it for a number of processes, whereas a knife is used once only for each pair of shoes. Photographs of the machines, or some of them, are annexed to the Case, and a specimen knife and a specimen last were produced to me at the hearing.

The contentions of the Respondents were in substance that their expenditure on maintaining the stock of knives and lasts, amounting to some £6,000 per annum, although they had a relatively short life, was expenditure none the less on capital account in respect of fixed assets and not on revenue account in respect of circulating capital, and was in fact expenditure upon the provision of new machinery or plant within the meaning of Section 16 (3) (*c*) of the Finance Act, 1954. These contentions were accepted by the Special Commissioners. While not doubting that there might be trades employing knives and lasts in circumstances not dissimilar to those of the present case which would make it impracticable to describe them as machinery or plant, the Special Commissioners relied for the conclusions to which they came on the following considerations: (*a*) that the knives and lasts performed indispensable functions in the process of manufacture ; (*b*) that in performing those functions they were used and could only be used in conjunction with machines which themselves could perform no useful function unless used in conjunction with the knives and lasts ; (*c*) that the machines themselves were machinery or plant within the meaning of the relevant provisions of the Statute. The case for the Crown was summarised as follows : first, that the Respondents' expenditure on knives and lasts in carrying on their trade was expenditure not on capital account but on revenue account, and, secondly, that the evidence showed that the knives and lasts were not parts of the machines which operated them but were separate chattels.

The enormous number of the knives and lasts compared with the comparatively small number of the machines (though that number is not expressly

stated) makes it difficult in my view to regard them as separate or separated bits either of machinery or of plant. If each machine had a complement of, say, a dozen knives or lasts the picture presented would have been very different. The point is a short one and not in my judgment very difficult, and I have myself come to the clear conclusion that the views of the Crown ought to have prevailed before the Special Commissioners and ought to prevail now before me. I think that these many thousands of constantly renewed knives and lasts are not machinery or plant and ought not to be regarded as parts of the machines, which themselves undoubtedly are machinery or plant. One knife is not " plant ", nor is one last, and thousands of knives and thousands of lasts cannot, in my judgment, be " plant " either. I think they are chattels and are properly described as " implements, utensils or articles " within Section 137 of the Income Tax Act, 1952, but in no case are they either machinery or plant.

I allow the appeal. I suppose I need only say that the assessments must be adjusted to give effect to my decision.

Mr. B. L. Bathurst.—If your Lordship pleases. Then the appeal will be allowed, and I think the right thing to do is that there ought to be an Order allowing the appeal and remitting the case back to the Special Commissioners to adjust the assessments in accordance with your Lordship's judgment?

Vaisey, J.—Yes, very well.

Mr. Bathurst.—I think that is the right method of dealing with it, my Lord.

Vaisey, J.—The matter must be sent back for these assessments to be adjusted in accordance with my judgment.

Mr. Bathurst.—Then the appeal will be allowed with costs?

Vaisey, J.—Yes.

The Company having appealed against the above decision, the case came before the Court of Appeal (Lord Evershed, M.R., and Sellers and Pearce, L.JJ.) on 3rd, 7th, 8th and 9th October, 1958, when judgment was given unanimously against the Crown, with costs.

Mr. G. B. Graham appeared as Counsel for the Company, and Mr. B. L. Bathurst, Q.C., and Mr. Alan Orr for the Crown.

Lord Evershed, M.R.—The subject-matter of this appeal is a claim by a company, Maden & Ireland, Ltd. (to which I will hereafter refer as " the taxpayer " or " the Company "), for what is called an investment allowance, under the terms of the somewhat short-lived provisions of the Finance Act of 1954. It follows that, as Mr. Bathurst observed, the onus lies upon the taxpayer to bring his case within the scope of the statutory provisions.

The taxpayer's business is that of a manufacturer of boots and shoes, upon what are called in these days mass-production methods. For those purposes the Company has installed elaborate machinery. Knives, fitted into the machines but detachable from them, cut the leather into required shapes;

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and then a very large number of lasts comes into use, upon which the cut leather is placed and there, by machine, sewn up or joined in order to make the shoes or boots of the shapes which the lasts indicate. The claim relates to the expenditure incurred by the taxpaying Company for the tax year 1955–56 on the knives so fitted into the machines and on the lasts which I have respectively mentioned.

The life of any one of these knives or of any one of these lasts is short. Some endure, no doubt, longer than others. But during the course of the argument in this Court (and, I gather, in the Court below) it has been assumed that you can take an average of three years as properly applicable to the knives and the lasts. That period is, of course, very much less than the useful life of the machines which I have mentioned and into which the knives and the lasts are fitted. Further, the number of knives and lasts used is very large indeed, running into many thousands. Finally, the individual knife is not an expensive item: it costs, we were told, 20*s.* or 21*s.*; and the individual last is not much more expensive.

The facts as to the method of production by means of these machines are very fully and, if I may say so, clearly set out in paragraph 3 of the Case Stated, and I will, if I may, treat the whole of that paragraph as incorporated in the judgment and confine myself to reading the summary of the manufacturing process (so far as relevant) which is found in sub-paragraph (x) of that paragraph:

> "Summarising the processes employed by the Respondent in carrying out its trade, it can be broadly stated that the Respondent utilises either knives or lasts (the latter making or finishing) in 90 per cent. of its manufacturing and finishing processes and that the machines that it uses can only function when furnished with the knives or lasts appropriate to the particular process. At the material time the Respondent in one of its factories had approximately 12,000 pairs of making lasts and 24,000 pairs of finishing lasts for a production of 1,200 dozen pairs of shoes per week. No such estimate of the number of knives in use was available to us in evidence, but one shoe might require as many as 14 knives".

I will also read the next sub-paragraph:

> "(xi) The average life of upper knives is 12 months, but sole knives, subject to a ten per cent. loss due to careless handling, have a life equal to that of the corresponding last. The average life of making lasts is three years and that of finishing lasts similar, except that the latter can sometimes be used apart from the making lasts, and they might then be used for four to five years."

For the purposes of the argument in this Court (and again, I gather, in the Court below and before the Commissioners) no distinction was made between the lasts and the knives. I confess that I have been a little tempted at times to think that some distinction might have been made. For example, it might have been thought that the knives could be regarded as highly expendable adjuncts to the machines, comparable in this respect to the frequently changed blades inserted into a shaving razor; whereas the lasts are more like the moulds on which and to which the shape of the manufactured products of the taxpayer's business is made. But no such distinction has been suggested in argument, and I am quite satisfied that it would be wrong now to suggest a reference back to the Commissioners with the possibility of making such a distinction. We should, therefore, treat this case (as it was treated before the learned Judge) as one in which, for relevant purposes, no proper distinction can be made between the knives on the one hand and the lasts on the other.

In paragraph 5 of the Case Stated the amounts spent on the knives and lasts over the 14 half-years up to and including the half-year to October, 1954, are set out. I shall not read the figures. The paragraph shows that in each half-year a sum which varies from a lowest sum of £1,151 to a sum, in one half-year, of appreciably over £5,000 was so spent. The figures, however, also show that within those limits there is a considerable variation in amount, the general impression left on the mind being that more is spent in the first half-year, ending March, than in the second. In the circumstances, the question which the Court has to determine is whether the sums so expended each half-year constitute capital expenditure on "machinery or plant" within the relevant statutory provisions. The learned Judge, Vaisey, J., rightly said that the point was, in the end, a short one. But there are, on examination, as Mr. Bathurst observed, two distinct points. The first is whether these knives and lasts properly fall within the meaning of the phrase I have used—"machinery or plant". The second is: assuming that they do so fall, whether the sums so spent on them constitute capital expenditure.

I turn, accordingly, to certain of the statutory provisions which must be looked at and to which our attention was most directed. I need not, I think, go into the history of the "wear and tear allowances" and "initial allowances" which all preceded the Finance Act of 1954. That is not to say that the history is irrelevant. For example, as Mr. Bathurst pointed out, the formula "machinery or plant" is first found in earlier provisions which introduced "wear and tear allowances". But I do not propose to take up time by a historical review; I make my reference to show that I have not forgotten the facts of that history. I turn to Section 279 of the Income Tax Act, 1952, which is directed to "Initial allowances". Subsection (1) says:

> "Subject to the provisions of this Act . . . where a person carrying on a trade incurs capital expenditure on the provision of machinery or plant for the purposes of the trade, there shall be made to him, for the year of assessment in the basis period for which the expenditure is incurred, an allowance"

of so much. Section 280 carries on, so to speak, the allowance in respect of such expenditure for the years subsequent to the first, and it is headed "Annual allowances":

> "Subject to the provisions of this Act, where the person carrying on a trade in any year of assessment has incurred capital expenditure on the provision of machinery or plant for the purposes of the trade, an allowance (in this Chapter referred to as 'an annual allowance') shall be made to him for that year of assessment on account of the wear and tear of any of the machinery or plant which belongs to him and is in use for the purposes of the trade".

So far, it is quite plain that the premise upon which the allowances must depend is that the expenditure on machinery or plant must have been a capital expenditure; and, by way of underlining or emphasis of that, you find the following provision in Section 330 in the same Part of the Act:

> "(1) References in this Part of this Act to capital expenditure . . . (*a*) in relation to the person incurring the expenditure . . . do not include any expenditure . . . which is allowed to be deducted in computing, for the purposes of income tax, the profits or gains of a trade".

As will appear later, on the facts of the case Mr. Graham, for the taxpayer, has felt bound to concede that, if this were a claim for an initial allowance under Section 279, then the allowances which had been made by

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way of deduction in the profit and loss account would have been fatal to his claim for such an initial allowance. But that disqualification, at any rate in its simplest form, is not applicable where the case is not a claim for an "initial allowance" but for an "investment allowance" pursuant to Section 16 of the Finance Act, 1954. That opens, in the first Sub-section, with the language:

> "In the cases provided for by this section, an allowance (in this Act referred to as an 'investment allowance') shall be made in respect of capital expenditure on new assets incurred after the sixth day of April, nineteen hundred and fifty-four."

I need not read any more of the Section for the purposes of my judgment save Sub-section (3) (*c*):

> "(3) An investment allowance equal to one-fifth of the expenditure shall be made instead of an initial allowance under Chapter II of the said Part X in respect of expenditure on the provision of new machinery or plant, and any provision of the Income Tax Acts applicable to initial allowances under that Chapter, so far as it is applicable in relation to allowances for new assets, shall apply also to investment allowances under this subsection, except that . . .—(*c*) where the expenditure on new machinery or plant is allowed to be deducted in computing profits or gains for the purposes of income tax, it shall nevertheless be treated as capital expenditure for the purposes of this subsection, if it would be so treated for the purposes of the said Chapter II but for the deduction".

Now the reference in the opening words of Sub-section (3) to the "initial allowance under Chapter II of the said Part X" is, of course, a reference to the particular Section, Section 279 of the Income Tax Act, 1952, which I read a moment ago. It is not, I think, in doubt, and cannot be in doubt, that the Parliamentary object in enacting Section 16 was, by the allowance of relief which it offered, to encourage industry to invest in the purchase of new machinery or plant. But it is equally not in doubt that a first reading, at any rate, of the Paragraph which I last read—Paragraph (*c*)—is somewhat confusing and tends to involve a circular process of thought. I must, of course, return to it hereafter, but picking it up at this stage it will be recalled that its language is:

> ". . . where the expenditure on new machinery or plant is allowed to be deducted in computing profits or gains for the purposes of income tax"

still it may qualify for the investment allowance, notwithstanding the deduction, if it would have qualified under Section 279 and stood the test but for the disqualification of Section 330. The reason why I have said that it seems to involve at first sight something of a circular argument is that in order to qualify it has got to be "capital expenditure", and it cannot be in doubt that if it is allowed as a revenue deduction then *prima facie* it never was a capital expenditure at all, Section 330 (1) notwithstanding. But I must, as I have said, come back to try to solve that problem hereafter.

On the first question—that is, was this expenditure on "machinery or plant"?—the Special Commissioners' answer was favourable to the taxpayer, but Vaisey, J., came to a contrary conclusion. The view of the Special Commissioners is to be found in sub-paragraphs (i) and (ii) of paragraph 10 of the Case Stated, which I propose to read:

> "(i) We held that the words 'machinery or plant' as used in Sections 279 and 280, Income Tax Act, 1952, and Section 16 (3), Finance Act, 1954, were not words of art, but on a proper construction of the Sections were to be given their ordinary meaning. So directing ourselves, we did not doubt that there might be trades employing knives and lasts in circumstances which would make it inappropriate to describe them as machinery or plant. But in the case before us we thought we should give weight to the facts (1) that the knives and lasts performed an indispensable function in the process

of manufacture, (2) that in performing that function they were used, and could only be used, in conjunction with machines which themselves could perform no useful function in the said process unless used in conjunction with the lasts and knives, and (3) that, as was not disputed, the said machines themselves were machinery or plant within the meaning of the relevant Sections. (ii) We found as a fact on the evidence that the knives and lasts were machinery or plant within the meaning of the said Sections and we held that the Respondent was entitled to the investment allowance claimed."

We have been referred to a very large number of cases in which problems of this general nature have arisen and to a number of judicial expressions about them. The range of those cases is wide and goes from such things as water towers at one end of the range to law reports in the library of a solicitor at the other. I hope that I shall not be thought to be neglecting the argument which brought those cases to our attention if I make no special reference to them—save just to borrow a phrase which occurred in the judgment of the Lord President (Clyde) in *Hyam* v. *Commissioners of Inland Revenue,* 14 T.C. 479, at page 486, where he used for that purpose (and the case related to the equipment of butchers' shops) the phrase " usually recurring incidents in a trading year ". That kind of phrase is no doubt useful in considering not only whether particular items are " machinery or plant " but also whether the money spent on them can properly be described as " capital " or " revenue " expenditure. We have also looked at definitions, and my brother Sellers will refer to one such definition from Wyld's Dictionary. Again, I do not propose myself to make any such reference, for while I agree that the question of the true interpretation of the words " machinery or plant " must, in the last resort, be a question of law, yet I do not think that, however many cases or dictionaries you look at, you can proceed to substitute for that short Parliamentary formula a precise set of words which will provide the answer to this problem. The words are, as the Commissioners pointed out, ordinary English words ; and I therefore think (and I do not understand this really to be disputed) that, if you give them the ordinary meaning which it would be appropriate to give in the context of a taxing Statute, then the question, in the end, is largely, if not entirely, a matter of degree, and therefore of fact.

Taking that view of the matter, I am not persuaded that in the two sub-paragraphs which I have read, sub-paragraphs (i) and (ii) of paragraph 10 of the Case, the Special Commissioners were guilty of any misdirection of themselves as to the meaning of the phrase " machinery or plant "; and, if that be so, then I think the duty of the Court *prima facie* must be to accept the conclusion, which is then a question of fact whether in truth, and in the light of all the special circumstances of this manufacturing process, the knives and the lasts can be properly described as " plant ", or, if you will, " machinery or plant ".

I am conscious, and diffident accordingly, of the fact that I am taking a different view from that which appealed to Vaisey, J. As he said, it is a short point. But, with great respect, I have formed myself a different view ; and I venture to think that the analogies which had come to his mind perhaps were not really close enough. He spoke, for example, of a motor-car without petrol, or a pipe without tobacco. I think that that kind of analogy ignores the essential fact—to which the Commissioners rightly alluded—that these knives and lasts were an essential part of the manufacturing process : indeed, the manufacturing process depended upon them. If that is so, then the circumstance that the lives of the knives and the lasts are relatively short cannot, I think, be conclusive against their being " machinery or plant ". I therefore on this point have for my part reached the conclusion—and in view

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of Vaisey, J.'s decision I can well understand that other minds might reach another conclusion—that the taxpayer has made good his submission that these knives and lasts were " machinery or plant ".

But that leaves the second question: were these sums, between £1,100 and £5,000 odd, spent half-yearly on these items, capital expenditure? That question, I confess, I have found very much more difficult, and I have been conscious of a variation of view during the course of the argument. Unfortunately, this Court has no assistance from any expressed view, either of the Special Commissioners or of the learned Judge, on this matter. Although the point was clearly put in the course of the recorded arguments to the Special Commissioners, it was not in terms decided by them at all; and, of course, having regard to the view which Vaisey, J., took it was quite unnecessary for him to pursue it. What are the facts? I state that question at once because in my judgment therein lies the real difficulty. The facts are to be found, so far as relevant, in paragraphs 4 and 6 of the Case, and I must, I am afraid, be forgiven for referring to those paragraphs fully. Paragraph 4 says this:

> " Owing to the large number of lasts and knives employed in the Respondent's business no physical stock-taking at the half-yearly dates to which its accounts are made up was possible. The Respondent therefore charged all expenditure on new knives and lasts to capital and charged against profits one-quarter of the total cost in the four succeeding half-yearly accounts, on the view that an average life of two years for the combined total expenditure on knives and lasts was a fair estimate."

I do not think it matters, but I am not satisfied that the word " succeeding " is not a mistake for " preceding ".

> " The actual expenditure on new knives and lasts and the amount so charged against profits in the two half-years' accounts ending respectively on 3rd April and 2nd October, 1954, forming the basis of the material year 1955–56, are set out in exhibit 3 . . . Thus, the figure of £8,022 5*s.* appearing in the balance-sheet at 2nd October, 1954 . . . is the balance after crediting total additions in the half-year of £1,856 8*s.* 5*d.* and after debiting to profit and loss account a sum of £3,542 19*s.* 1*d.*, being the writing off at 25 per cent. of expenditure on knives and lasts in the preceding four half-years."

Paragraph 6 reads:

> " The Revenue had taken the view that for Income Tax purposes the Respondent's estimate of the life of knives and lasts was too conservative, but had agreed that an average life of three years instead of two years was reasonable. The Respondent had accepted the Revenue's contention for Income Tax purposes, and in the result a sum equal to one-sixth of the total expenditure on knives and lasts has been for a number of years allowed as a deduction in the following six half-years, as such accounts came into the computation of the Respondent's profits for Income Tax purposes. This deduction was regarded by the Revenue as the nearest practicable and just estimate of the sum expended by the Respondent ' for the supply, repairs or alterations of any implements, utensils or articles employed, for the purposes of the trade ', within the meaning of Section 137 (*d*), Income Tax Act, 1952. It was common ground between the parties in this appeal that the amount so allowed for Income Tax purposes was not the sum ' actually expended ', since (i) is related to expenditure incurred in the preceding six half-yearly periods and (ii) it was the result of a ' straight line writing-down ' on the basis of the Revenue's contention of an estimated three years' life. For the reasons hereinafter set out in paragraph 10 below, we do not consider that either the method adopted by the Respondent in making up its accounts or the variation of that method adopted by the Revenue and accepted by the Respondent for Income Tax purposes affects the issue on which we were called upon to give our determination."

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It will, I think, be right that I should refer to the whole of paragraph (*d*) in Section 137 of the Income Tax Act, 1952, with its introduction from the opening of the Section.

> "Subject to the provisions of this Act, in computing the amount of the profits or gains to be charged under Case I"

—to take the present instance—

> "of Schedule D, no sum shall be deducted in respect of . . . (*d*) any sum expended for repairs of premises occupied, or for the supply, repairs or alterations of any implements, utensils or articles employed, for the purposes of the trade . . . beyond the sum actually expended for those purposes".

I think I am right in saying that the actual form of words "beyond the sum actually expended for those purposes" may owe something to the circumstance that previously a three years' average had been the proper method of approach in dealing with this kind of deduction; but it is, of course, apparent from what I have read that this Section is saying that, so far as deductions are concerned—that is to say, deductions for supply, repairs or alterations of implements, utensils or articles—the sum to be deducted is the sum actually so incurred; and if such deduction is made, then (as the Crown forcefully points out) that necessarily postulates of it that the deduction is, and is treated as being, a revenue expenditure.

From the language used in paragraph 6 of the Case, which I have read, and particularly the references, put as a quotation, to Section 137, it was strongly argued by Mr. Bathurst that, as a result of the agreement or arrangement made between the taxpayer and the Revenue, there was merely substituted for the actual sum spent each half-year on these knives or lasts a sum which was arrived at by an averaging process; but none the less that deduction was treated as being a deduction contemplated by and covered by Section 137 and was, therefore, essentially a revenue expense. Although (as Mr. Bathurst conceded) in the light of the language of Section 16 (3) (*c*) of the Finance Act, 1954, that fact could not be conclusive, at least it was very cogent ground for saying that the expenditure in question was not capital expenditure, and, if it was not, then of course it never came within Section 279 of the Income Tax Act, 1952, at all—that it was, in other words (reverting to the Lord President's language), expenditure on "usually recurring incidents in a trading year".

If that is the right conclusion as to the facts, then I think that Mr. Bathurst's submission would prevail. But I have not been able to conclude that the matter of fact as appears from the accounts in these two paragraphs of the Case is so simple; and I am not satisfied, on a true view of the case, that what was done was a mere substitution, for convenience or by arrangement, of an average figure for an actual figure, the average figure being treated, and known as having been treated, by the Revenue as a mere substitute for the actual expenditure mentioned in Section 137 (*d*). I would observe in the first place that (as must have been obviously known to the Revenue) the sums expended or rather the results of the sums expended, namely, the value of the knives and lasts which had been bought, was treated as a fixed capital asset. From the language which I have read in the paragraphs and which I do not repeat, what the taxpayer apparently had sought to do was this: first, to put in as a capital asset the value of these knives and the lasts, and then to deduct, by way of an allowance for depreciation or wear and tear, a sum which the taxpayer, treating their life as being two years only, calculated by taking the average of the four preceding half-yearly expenditures. The issue between the taxpayer and the Revenue

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seems to have been limited to this, that the Revenue said (and the taxpayer eventually accepted it) that two years was too short a life : therefore they substituted three. The practical result was to substitute for a figure of £3,500 odd which the taxpayer in the relevant half-yearly accounts had put in in respect of this deduction the somewhat smaller figure of £3,399. But if this was to be and intended to be a strict adoption as applicable of Section 137 (*d*) then there could have been no difficulty in inserting for the relevant half-year the actual sum expended. The formula (it will be remembered) in paragraph 6 of the Case was that

> " the nearest practicable and just estimate of the sum expended "

was—etc. I say nothing for the moment about the " justice " of what was done ; but the " nearest practicable estimate of the sum expended " surely would have been the sum in fact expended : you did not require to have a stock-taking to find out what was spent—that presumably was known. I must not in any way be taken as criticising what the Revenue authorities thought right. I am far from saying that the conclusion was not the most just result ; and I can see, from a business point of view, the disadvantage of taking considerably varying half-yearly figures, which would have meant a corresponding variation from half-year to half-year in the taxable profits. It may well be that the taxing authorities were in this respect assisting the proper, smooth running of business ; and nobody would presume to say they were going beyond their proper powers or dealing in any way wrongly in so contriving.

I have said earlier that Mr. Graham concedes none the less that, the deductions having been made as they were, that would have been fatal to him had his claim here been for an initial allowance under Section 279 of the Income Tax Act, 1952, because of the express disqualification in Section 330. But I come back, accordingly, to the somewhat obscure language of Section 16 (3) (*c*) of the Finance Act, 1954. I have already made a passing comment upon it ; and there is no doubt that expenditure was allowed to be deducted in computing profits and gains in respect of the expenditure in question. But it is quite plain that, as Mr. Bathurst concedes, the terms of the paragraph do not make that a conclusive disqualification. I have said, and repeat, that had the deduction allowed been the actual sum expended, which would have made it a direct application of Section 137 (*d*), then I think it would have been exceedingly difficult for the taxpayer to have said that the paragraph in Section 16 (3) of the Finance Act, 1954, had so remarkable and subversive an effect. I asked Mr. Bathurst what sort of case Section 16 (3) (*c*) applied to ; and it is not a question—obviously—at all easy to answer. But on the whole I propose to say that I think it was intended to apply, and does apply, at any rate to this case, in which money has been spent upon articles which I have stated to be in my judgment (right or wrong) " plant "—treated as capital expenditure by the taxpayer—appearing in the balance sheet as such ; but in respect of which an allowance was made of a character not strictly in accordance with any precise provisions of the taxing Acts but arrived at so as to give a substantially just result.

The phrase " straight line writing-down " is, I confess, novel to me, but I gather that it is one well enough known to accountants and others who deal with business or trading accounts. Its significance appears to me rather to be in relation to some form of depreciation than strictly applicable to a payment made or to a " usually recurring trading item ", to quote once more the language of the Lord President (Clyde).

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I therefore have come to the conclusion—as I have said, not without considerable doubt and some variation of opinion—that, given that my answer to the first question is right—which I must now, of course, assume—then I am not satisfied that the deductions which were made in respect of this expenditure are such as to disqualify the expenditure from being called " capital expenditure " and from being, therefore, entitled to the investment allowance. Although, as I have said, the Special Commissioners gave no express view about it, it is, I think, quite plain that that was the view which they must have accepted or *sub silentio* assumed ; and, if so, then again I get such comfort as I can from the fact that, if it be a matter of degree and of fact, then they so held.

I come in the end, therefore, to a conclusion which is favourable to the taxpayer. I think it may be that in this case fortune has smiled somewhat upon the taxpayer—though it may also be said that encouragement to produce new models of shoes and for that purpose to acquire new lasts was not outside the scope or contemplation of the 1954 Act. On the whole, therefore, in this case I think, for the reasons which I have tried to state, that the appeal succeeds and should be allowed.

Sellers, L.J.—I agree.

Within the framework of the Sections to which my Lord has referred the question has to be decided whether the taxpayer has established a qualification for the " investment allowance " in respect of the expenditure on knives and lasts in the relevant period. In that period new expenditure has been incurred on knives and lasts for the making of new models of footwear, and one essential requirement in order that the taxpayer may receive the benefit of this allowance is that it should be established that the expenditure has been on " machinery or plant ".

My Lord has referred to a definition in Wyld's Universal English Dictionary. It is in these terms, as one of the meanings of the word " plant ":

> " Complete mechanical equipment, or apparatus, machines, implements, etc., necessary for carrying on some specific industrial operation."

The dictionary by Professor Wyld (who was at one time Merton Professor of English Language and Literature at Oxford) is modern and I think that describes the ordinary modern usage of the word. It is in conformity with what Somervell, L.J., said in a Factory Act case, *Watts* v. *Enfield Rolling Mills* (*Aluminium*), *Ltd.* [1952] 1 All E.R. 1013, at page 1015,

> " The word ' plant ', I think, is one of those words the meaning of which, in its ordinary significance, is very wide. It may be cut down by its context. In certain contexts in the Factories Acts I think it means plant used by the occupier of the factory for the purposes of the processes he carries on there."

This, of course, is an industrial undertaking which is being assessed to tax, and whilst the words of the Income Tax Acts have to be considered it is appropriate, it seems to me, to look at what the industrial function was and the words commonly used in relation thereto. In the course of manufacture, in this case the manufacture of footwear, many things have to come into use—most frequently in these days some machinery and, in association with machinery, various implements, tools and equipment in order to make the machinery effective, to work in conjunction with it, and to produce the finished product. The word which is commonly used is " plant ", to describe the equipment, utensils, machinery, articles—whatever they may be—which are directly used in the process of manufacture, in the making of an article

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or part of an article. They are the tools of the trade. Whether they are to be described as " plant " or not seems to me to depend on the use to which they are put. Many things may be bought, expenditure may be made on all sorts of articles, some of which may be put to the direct process of manufacture, others of which may be used indirectly or for some other purpose. If that test is right, the conclusion does not depend on the size, the weight, the strength or the weakness, the durability or the length of serviceable use, of the particular article: it is the purpose to which it is put. Machine tools in some processes may be worthless after being used once, or may have a very short life, but if they are a vital part of the plant then, as I see it, they would be regarded as plant if they were not in fact part of the machinery.

When these particular knives are in the machine (and they are placed in and out as most machine tools, dies and so on are with a machine in use for a particular process) then for the time being they form part of the machinery or may be regarded as so doing. Such tools or articles when not in use seem to me clearly to fall within the designation of " plant ". As a qualification to that, there may be articles which might more appropriately, on a finding of fact, be regarded as tools of maintenance rather than plant itself. If one were to try to give a simple illustration, I apprehend that if one takes a furnace those commodities which go into a furnace in order to make an article, to produce the commodity which is sought to be produced, would not be described as " plant "; but the furnace, any ladles and moulds or any containers, whether they are mechanically operated or otherwise, would normally be regarded as plant relevant to the process. Viewing the matter in that way I have arrived at a different decision from Vaisey, J. It seems to me that the ground on which he based his decision, the nature and size of the knives rather than their use, is the basis of this difference of opinion.

A more difficult problem as I see it is whether the finding that the expenditure was on plant is sufficient (as the Commissioners seem to have regarded it) to justify the allowance in favour of the taxpayer. There is no direct finding that this expenditure was of a capital nature, either by the Commissioners or by Vaisey, J., who, in the view he took of the matter, was not called upon to deal with it. I find the position somewhat obscure both in the precise meaning of the relevant Section itself and in the possible application of it to the present circumstances or to any given set of facts. In order to establish that this particular expenditure was capital expenditure, a second essential requirement for the allowance, learned Counsel for the taxpayer referred to some observations of Lord Haldane in *John Smith and Son* v. *Moore,* 12 T.C. 266, at page 282:

> " My Lords, 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."

That test would give a simple line of demarcation in this case and would justify, I think, the submission made on behalf of the taxpayer. But it was submitted on behalf of the Crown that those observations of Lord Haldane stand alone in their relative simplicity and there has been a great deal of other authority on this difficult topic. Acceptable as that demarcation may

be to economists, I doubt whether Lord Haldane's observations would now be acceptable to all accountants as a complete statement of the difference between the two kinds of expenditure. As at present informed, I doubt too if it has been generally accepted as a principle in tax cases so as to give a simplicity to Revenue matters, which characteristic so far has escaped me. It would seem a simple line of demarcation to apply to any given expenditure. But I would not base my decision on this broad ground in my present state of information on the difference between capital of a fixed nature and circulating capital. In this particular case the matter, as I think and as my Lord has stated, is to be solved by the form of the Case and the facts which are found. I doubt, therefore, whether this case can be of much assistance in any other case on general principles on this aspect as to whether the taxpayer has established that this expenditure was of a capital nature.

The position as stated in the Case is somewhat obscure, and instead of developing this matter I am content to agree with what my Lord has said and accept his reasoning upon it based on the findings in paragraph 4 of the Case linked up with paragraph 6. There it does appear that the taxpayer charged the expenditure initially to capital account. They so treated it, and when the matter came for consideration the dispute between the taxpayer and the Revenue was not whether this was capital or whether it was current expenditure to be set off against the gains and profits but as to whether the period taken for the allowance for depreciation for each half-year over the period was long enough having regard to the assessed life of the knives and lasts, and instead of two years being taken, as the taxpayer submitted, the period of three years was agreed. Then the total cost was written off, as I understand it, by a depreciation which averaged out equally for each relevant half-year period and extinguished the whole capital expenditure at the end of three years. That seems to me to have sufficient elements of capital expenditure to bring it within the rather difficult conception visualised by Section 16 (3) of the Finance Act, 1954. I think it is sufficient to satisfy that Section and to entitle the taxpayer to the allowance which he claims.

I would allow the appeal.

Pearce, L.J.—I agree.

Mr. G. B. Graham.—Will your Lordships say, with costs?

Lord Evershed, M.R.—Is there any difficulty about the Order that we make?

Mr. Graham.—If your Lordships allow the appeal the result will be that the assessment in its present figure stands and it will not be necessary to go back to the Commissioners.

Lord Evershed, M.R.—Is that right, Mr. Bathurst?

Mr. B. L. Bathurst.—That appears to be right, my Lord.

Lord Evershed, M.R.—Then you ask for costs, you say, Mr. Graham?

Mr. Graham.—Yes, my Lord.

Lord Evershed, M.R.—Did you pay the costs before Vaisey, J?

Mr. Graham.—Vaisey, J., allowed the Crown's appeal, with costs, but nothing has yet in fact been paid.

Lord Evershed, M.R.—He ordered " that the costs of the Appellant "—that was the Crown—" be taxed . . . and paid by the Respondent ". You want to get rid of that. I suppose you ask that you get your costs here and below?

Mr. Graham.—Yes, my Lord.

Lord Evershed, M.R.—I think that must follow?

Mr. Bathurst.—Yes, my Lord ; I cannot oppose that. I have to ask your Lordships for leave to appeal to the House of Lords in this case. Your Lordships will remember that your Lordships are reversing Vaisey, J. It does raise difficult questions under this rather obscure Act ; and although I would hesitate to describe it as a test case—because all these cases must depend on their facts—I am instructed that there are a large number of these cases in which the authority of this case and your Lordships' decision will be very relevant, and it would be probably convenient to take this one to the House of Lords.

Lord Evershed, M.R.—The only thing that occurs to me, subject to what Mr. Graham may say, is this. If there are, as you say, a large number of cases, it is difficult for me to form a view what in pounds, shillings and pence this means to the taxpayer. It is not a vast sum.

Mr. Bathurst.—No.

Lord Evershed, M.R.—Costs get rather heavy. I do not know whether the Crown, as a matter of principle, would be disposed to make any concession about costs.

Mr. Bathurst.—If your Lordships consider the Crown should do so I have no doubt they would ; but I submit in the first place that your Lordships are reversing Vaisey, J., and——

Lord Evershed, M.R.—I am not expressing any view. I was just wondering. Sometimes the Crown say, We will not ask for costs, if the real point is not only this case. One feels that from the taxpayer's point of view the costs of the case may become disproportionate and they might even say, We had better pay : it will be cheaper in the end. It is obviously a very narrow point.

Mr. Bathurst.—My Lords, if your Lordships thought it proper we would submit to an Order that your Lordships very often make—that we would undertake not to disturb the costs here or below.

Lord Evershed, M.R.—I cannot impose it : it would not be right : but if the Crown feel that they can properly offer that——

Mr. Bathurst.—Your Lordships will give us leave to appeal on our giving such an undertaking?

Lord Evershed, M.R.—If the Crown make that offer it is obviously a rather weighty consideration.

Mr. Bathurst.—On that undertaking, my Lord?

Lord Evershed, M.R.—Yes. Mr. Graham, it is a case in which at least we have differed from the learned Judge ; and it is very obscure ; and the Crown has said that it will not seek to disturb the Order we have made as to costs. So that if you win you will get your costs in the House of Lords: if you lose you only have to pay those costs, presumably.

Mr. Graham.—Upon the offer my learned friend has made I clearly cannot oppose this application very strenuously. I would only mention that both the judgments which have been delivered in this Court have turned very much on the rather obscure findings of fact in the Case Stated, and on that basis it may not be a case suitable for the House of Lords to establish a principle. But if my friend makes the offer which he has made I cannot really oppose his application very strongly.

Lord Evershed, M.R.—Mr. Bathurst, if the Crown makes that offer—which, if I may say so, in the circumstances seems a fair and just thing to do—I think you ought to have leave so as to test the principle.

Mr. Bathurst.—I am much obliged, my Lord. On that undertaking your Lordships will give it me?

Lord Evershed, M.R.—Yes.

The Crown having appealed against the above decision, the case came before the House of Lords (Lords Reid, Tucker, Keith of Avonholm, Denning and Jenkins) on 23rd, 24th and 25th June, 1959, when judgment was reserved. On 16th July, 1959, judgment was given against the Crown, with costs (Lord Keith of Avonholm and Lord Denning dissenting).

Mr. B. L. Bathurst, Q.C., and Mr. Alan Orr appeared as Counsel for the Crown, and Mr. F. Heyworth Talbot, Q.C., and Mr. G. B. Graham for the Company.

Lord Reid.—My Lords, the Respondents are shoe and slipper manufacturers. They were assessed to Income Tax for the year 1955–56 in respect of profits of £8,290 less capital allowances of £4,836. The question in this case is whether the capital allowances should be increased to £5,148 because of expenditure which the Respondents maintain qualified for investment allowance under Section 16 of the Finance Act, 1954. The Special Commissioners decided in favour of the Respondents. Their decision was reversed by Vaisey, J., but restored by the Court of Appeal.

The Respondents' method of manufacture is described in the Case stated by the Commissioners. There are at least nine stages in the manufacture of a shoe, each performed by a different machine in conjunction with the knives and lasts which are the subject of this appeal. The first stage is cutting out from large pieces of different kinds of leather pieces of the correct shapes for the uppers, soles and other parts of the shoes. In the course of the argument it appeared that the description of this stage in the Case is somewhat misleading and no objection was taken to our being given further information about it. Pieces of the correct shape are cut out by pressing a knife on to the leather. The machine which does this is a press; the lower part of it is a flat table on which the sheet of leather is laid. Each piece is cut out by a single knife; in the case of an upper the cutting edge is heart-shaped, in the case of a sole the cutting edge is the shape of the sole. The cutting edge is the lower part of a ring of metal of the same shape. A number of these knives are arranged by hand on the sheet of leather so that as little as possible of the leather shall be wasted. Then the upper part of the machine is pressed down on them and the leather is thus cut. The knives are not parts of the machine; each knife is a separate tool or implement designed to be used in conjunction with the machine. It is stated

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in the Case that as many as 14 different knives may be used in producing the pieces of leather to be made up into one shoe. As different knives are required for right and left shoes and each size and type of shoe may require a different set of knives, it is obvious that the Respondents must have available a very large assortment of knives. It appears that each knife costs about £1. Two types of machine are used; one costs over £400 and the other over £1,000. In most of the further stages of manufacture lasts are used. These cost about £1 2*s*. per pair. For the earlier stages making lasts are used, and for the later stages finishing lasts. These lasts too are not parts of the machines. For each process a last with the pieces of leather which go to make the shoe is fed into the appropriate machine. Again, not only are different lasts necessary for right and left shoes and for different sizes, but different types of shoes require different lasts. It is stated in the Case that every change of fashion involves a change of last. It appears that about 12,000 pairs of making lasts and 24,000 pairs of finishing lasts are required for a production of 1,200 dozen pairs of shoes a week. The life of each last is about three years, though some may be used for four or five years; it is not stated whether they mostly wear out or become obsolete through change of fashion. The life of the sole knives is about the same, but upper knives only have a life of about a year.

The facts set out in the Case with regard to the Respondents' expenditure in buying knives and lasts and the way in which that expenditure has been treated for Income Tax purposes are as follows:

> "4. Owing to the large number of lasts and knives employed in the Respondent's business no physical stock-taking at the half-yearly dates to which its accounts are made up was possible. The Respondent therefore charged all expenditure on new knives and lasts to capital and charged against profits one-quarter of the total cost in the four succeeding half-yearly accounts, on the view that an average life of two years for the combined total expenditure on knives and lasts was a fair estimate. The actual expenditure on new knives and lasts and the amount so charged against profits in the two half-years' accounts ending respectively on 3rd April and 2nd October, 1954, forming the basis of the material year 1955–56, are set out in exhibit 3 under the headings of the five manufacturing units of the Respondents' business. Thus, the figure of £8,022 5*s*. appearing in the balance sheet at 2nd October, 1954, (exhibit 2*b*), is the balance after crediting total additions in the half-year of £1,856 8*s*. 5*d*. and after debiting to profit and loss account a sum of £3,542 19*s*. 1*d*., being the writing off at 25 per cent. of expenditure on knives and lasts in the preceding four half-years. 5. The expenditure on knives and lasts during the basis year and the six years immediately preceding the basis year was as follows:
>
> | | |
> |---|---|
> | Half-year to March, 1948 ... ... | £2,075 |
> | „ „ „ September, 1948 ... ... | £1,451 |
> | „ „ „ March, 1949 ... ... | £3,706 |
> | „ „ „ September, 1949 ... ... | £3,868 |
> | „ „ „ March, 1950 ... ... | £4,659 |
> | „ „ „ September, 1950 ... ... | £1,151 |
> | „ „ „ March, 1951 ... ... | £3,527 |
> | „ „ „ September, 1951 ... ... | £1,026 |
> | „ „ „ March, 1952 ... ... | £5,195 |
> | „ „ „ October, 1952 ... ... | £1,404 |
> | „ „ „ March, 1953 ... ... | £5,131 |
> | „ „ „ October, 1953 ... ... | £3,476 |
> | „ „ „ April, 1954 ... ... | £4,160 |
> | „ „ „ October, 1954 ... ... | £1,856 |
>
> No dissection of the figures of expenditure between knives and lasts had been attempted by the Respondent, and we were satisfied that such a dissection, if not actually impossible, was not reasonably practicable. 6. The Revenue had taken the view that for Income Tax purposes the Respondent's estimate of the life of knives and lasts was too conservative, but had agreed that an average life of three years instead of two years was reasonable. The Respondent had

accepted the Revenue's contention for Income Tax purposes, and in the result a sum equal to one-sixth of the total expenditure on knives and lasts has been for a number of years allowed as a deduction in the following six half-years, as such accounts came into the computation of the Respondent's profits for Income Tax purposes. This deduction was regarded by the Revenue as the nearest practicable and just estimate of the sum expended by the Respondent 'for the supply, repairs or alterations of any implements, utensils or articles employed, for the purposes of the trade', within the meaning of Section 137 (*d*), Income Tax Act, 1952. It was common ground between the parties in this appeal that the amount so allowed for Income Tax purposes was not the sum 'actually expended', since (i) it related to expenditure incurred in the preceding six half-yearly periods and (ii) it was the result of a 'straight line writing-down' on the basis of the Revenue's contention of an estimated three years' life. For the reasons hereinafter set out in paragraph 10 below, we do not consider that either the method adopted by the Respondent in making up its accounts or the variation of that method adopted by the Revenue and accepted by the Respondent for Income Tax purposes affects the issue on which we were called upon to give our determination."

In addition to this deduction from their profits the Respondents claim an investment allowance equal to one-fifth of their expenditure on knives and lasts, under the provisions of Section 16 of the Finance Act, 1954. The relevant provisions of that Section are:

"16.—(1) In the cases provided for by this section, an allowance (in this Act referred to as an 'investment allowance') shall be made in respect of capital expenditure on new assets incurred after the sixth day of April, nineteen hundred and fifty-four. . . . (3) An investment allowance equal to one-fifth of the expenditure shall be made instead of an initial allowance under Chapter II of the said Part X in respect of expenditure on the provision of new machinery or plant, and any provision of the Income Tax Acts applicable to initial allowances under that Chapter, so far as it is applicable in relation to allowances for new assets, shall apply also to investment allowances under this subsection, except that— . . . (*c*) where the expenditure on new machinery or plant is allowed to be deducted in computing profits or gains for the purposes of income tax, it shall nevertheless be treated as capital expenditure for the purposes of this subsection, if it would be so treated for the purposes of the said Chapter II but for the deduction".

Under Sub-section (1) an investment allowance can only be made in respect of capital expenditure on new assets. It is not disputed that these knives and lasts were new assets—the word "new" is used in contrast to second-hand; the contention of the Crown is that the cost of acquiring these assets was not capital expenditure. Sub-section (3) contains a further limitation: the new assets must be new machinery or plant. It is not said that the knives and lasts are machinery or parts of machinery. The Respondents say that they are plant and that is denied by the Crown. According to the contentions set out in the Case, both these points were taken by the Crown before the Commissioners, but in their decision the Commissioners do not even mention the question whether this was capital expenditure. They only deal with the question whether the knives and lasts are plant. They say:

"(ii) We found as a fact on the evidence that the knives and lasts were machinery or plant within the meaning of the said Sections and we held that the Respondent was entitled to the investment allowance claimed."

We do not know whether they thought that the expenditure being capital expenditure was so clear as not to require special mention or whether they omitted to mention it owing to some oversight. But before reaching their decision I think they must have decided in their own minds that this was capital expenditure; I find it difficult to suppose that they could have entirely overlooked the leading requirement of the Section after the point had been argued.

It is unfortunate that we do not have the Commissioners' reasons for deciding that this was capital expenditure. It is not argued that this expression

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is used in the Act as a term of art with some technical meaning, and I accept the position that this expression " capital expenditure " must be considered as an ordinary expression in un-technical English. So treating it, my first enquiry would be: what would a reasonable business man understand by the expression and would he regard this expenditure as capital expenditure or not? On that question the decision of the Commissioners would be most important. But we must do our best to interpret these words without expert assistance.

I am certainly not going to attempt a definition of capital expenditure on the one hand or of revenue expenditure on the other. Like most ordinary English words or expressions they are probably incapable of exact definition and I must look at the whole circumstances and determine as a matter of construction into which class this expenditure falls. As the first step I would ask what is the practical difference between treating an item of expenditure as capital or as revenue expenditure. I claim no expert knowledge of accountancy or of business methods, and the only practical difference that occurs to me—and none other was suggested in argument—is that if you treat a sum as capital expenditure you do not write it all off in one year or set it all against the income of one year, whereas if you treat it as revenue expenditure the whole of it is set off against the revenue of the year when it is expended. If the money has been expended on stock-in-trade and the thing bought is still there at the end of the year, you carry forward the value of the stock-in-trade at the end of the year. But these knives and lasts were not stock-in-trade and I do not know how their value at the end of the year could be carried forward in a profit and loss account if they are plant and the cost of them has been treated as revenue expenditure.

I would suppose that accounts are intended to have as close a relation as is reasonably practicable to reality. If you buy plant which still has a substantial value at the end of the year I would suppose that that value ought to be reflected somewhere in the accounts. If the cost is treated as capital expenditure there seems to be no difficulty in writing off that cost year by year as the plant wears out or becomes obsolete, but if the cost is treated as revenue expenditure I do not know what item in the next year's accounts would reflect the continuing value of the plant. I do not suggest that this distinction is or should be an inflexible rule. There may for all I know be good reasons for not following it in particular cases. But in the absence of any indication of any specialty in this case I am inclined to approach this case in that way. If that is a correct approach, then the salient facts in this case are that on the average these implements have a life of several years, that their cost has been treated by the Respondents as capital expenditure to be written off in two years, and that the Revenue has acted on the view that their average life is three years and in allowing deduction for Income Tax purposes has spread the expenditure in each year over a period of three years.

The case is complicated by the fact that deductions in respect of this expenditure have been made under Section 137 (*d*) of the Income Tax Act, 1952. This is a provision which, primarily at least, applies to revenue expenditure, and it would appear to be applicable to this expenditure because these knives and lasts were I think implements or articles supplied for the purposes of the Respondents' trade. But I do not think that this is at all conclusive, for three reasons. First, it is not at all clear that this provision was intended only to be available in the case of revenue expenditure. Secondly, Section 16 (3) (*c*) appears to recognise at least the possibility of

this provision being used in the case of capital expenditure. And thirdly, on one reading of Section 137 (*d*) its provisions were not correctly followed in making deductions in respect of this expenditure. I take these three points in turn.

At first sight, Section 137 (*f*) may appear to prohibit deductions under this Section in respect of capital expenditure, for it prohibits any deduction in respect of

> " any sum employed or intended to be employed as capital in, such trade ".

But " any sum employed as capital " may mean new capital put into the business and is not a very happy equivalent of " any capital expenditure ", and I think that it is legitimate to look at the history of this provision. Similarly worded provisions were included in the old Rule 3, which goes back at least as far as 1842. Before 1878 there was nothing in the Income Tax Acts corresponding to the modern wear and tear allowance or annual allowance in respect of capital expenditure, and unless Rule 3 applied when there was capital expenditure to replace worn out machinery or plant there was no way of getting any deduction for Income Tax purposes in respect of such expenditure. It is not disputed that in fact it was the custom to allow deductions under Rule 3 in respect of capital expenditure : an example given was the allowance of such a deduction in respect of expenditure in replacing worn out railway engines by new ones. I find it hard to believe that such a custom could have existed if Rule 3 clearly excluded all capital expenditure. Moreover, it is not disputed that this custom continued after 1878, notwithstanding the fact that thereafter capital expenditure could be the subject of an appropriate wear and tear allowance. Indeed, it is noteworthy that in the recent case of *Commissioners of Inland Revenue* v. *Great Wigston Gas Co.*, 29 T.C. 197, it was still said that there was an option to receive deductions under Rule 3 or a wear and tear allowance. Of course, the taxpayer could not have both.

Then I take Section 16 (3) (*c*) of the 1954 Act. It was not disputed, and I think that it is clear, that this provision deals with cases where there has been capital expenditure qualifying for an investment allowance, but nevertheless deductions have been allowed in respect of it under Section 137 (*d*) of the 1952 Act. This appears to me to be a statutory recognition of the practice of allowing deductions under Section 137 (*d*) in respect of capital expenditure, and to entitle the Respondents to an investment allowance if this was capital expenditure on plant, notwithstanding the fact that they have already received deductions under Section 137 (*d*). The result of getting an investment allowance is that the taxpayer gets by means of allowances or deductions more than 100 per cent. of such capital expenditure as qualifies under Section 16. In the normal case he gets investment allowance in addition to the usual allowances in respect of capital expenditure. It appears to me that the meaning and effect of Section 16 (3) (*c*) is to entitle and enable him to get more than 100 per cent. if he receives deductions under Section 137 (*d*) instead of the usual allowances.

My third reason is, I think, less important. Section 137 (*d*) prohibits the deduction of any sum expended for the purposes mentioned

> " beyond the sum actually expended for those purposes."

If this means actually expended during the accounting year, then the method adopted in this case was not in accord with the provisions of the Section, because the sums deducted were arrived at by taking into account expenditure in three consecutive years—in effect by writing off each year's expenditure over a period of three years, which is an appropriate method for capital

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expenditure. I do not in the least criticise this procedure. It was convenient, it could not cause loss to the Revenue, and it was unlikely to cause loss to the taxpayer. But it does emphasise the fact that neither party saw fit to treat this expenditure in the way in which revenue expenditure is normally treated, and it appears to me to go far to remove any presumption that expenditure in respect of which Section 137 (*d*) has been applied is revenue expenditure.

There appears to be no clear authority on this matter. The authority most strongly founded on by the Crown was the opinion of the Lord President (Clyde) in *Hyam* v. *Commissioners of Inland Revenue*, 14 T.C. 479; 1929 S.C. 384. There, shop fittings were scrapped and new fittings were purchased and a claim for a deduction under Rule 3 of the Rules applicable to Cases I and II of Schedule D of the Income Tax Act, 1918, was disallowed. Before the Rule was amended in 1926, deduction was prohibited

> "beyond the sum usually expended for those purposes according to an average of three years preceding the year of assessment",

and the Lord President really based his opinion on the fact that expenditure of this kind was not a usual expense recurring annually. It had been admitted that the shop fittings were "implements, utensils or articles" within the meaning of the Rule, but the Lord President doubted this. The passage founded on is(1):

> "The propriety, and the practice, of charging the cost of supplying 'implements, utensils, or articles employed for the purposes of the trade' to revenue must vary according to the character of the trade, and—partly perhaps—according to the financial circumstances of the trader. Trading implements, utensils, and similar articles—taking these descriptions in their ordinary connotation—have to be supplied, repaired and altered from time to time, in order to enable the trade to be carried on and profits to be earned; and in many businesses, expenditure on these things is a usual incident of their conduct and properly recurs in every year, or at least in most ordinary years, as a debt against revenue account. Take the case of a hotel or restaurant business—much table-furniture, linen, crockery, pots and pans have to be provided, and the supply of such things is a usual incident of the trade. Accordingly I think that, in a business of the kind supposed, the costs of such supply are a proper charge against revenue in the books, and a proper deduction from gross profits in terms of Sub-head (*d*) of Rule 3 for purposes of Income Tax. But, since such relatively permanent things as shop fittings must be taken to form a *species* of the *genus* 'implements, utensils, or articles employed for the purposes of the trade', it is plain that there are some kinds of 'implements, utensils or articles' the supply of which is not a usual incident (one year with another) of the conduct of the business, and in respect of which there is no sum which can be said to be 'usually expended'."

As there is no longer any reference in Section 137 to sums usually expended, the Lord President's precise ground of judgment is no longer applicable, but this is a decision that certain expenditure (apparently capital expenditure) which does not recur annually should not be allowed as a deduction under this provision. But I cannot regard this reasoning as a satisfactory criterion of whether expenditure is or is not capital expenditure. Let me suppose that a large business has 20 machines each of which lasts 20 years and that it buys a new one annually to replace one worn out. And let me suppose a small business with only one such machine; it buys a new one once in 20 years. It may be that it is proper for the large business to save a lot of calculation by treating its annual purchase as revenue expenditure and claiming under Section 137, whereas that would not be proper for the small business. But it would seem to me odd, and indeed absurd, that the Revenue should be able to say that the buying

(1) 14 T.C. 479, at p. 486.

of a new machine by the large business is not capital expenditure and carries no investment allowance, whereas the buying of a similar machine by the small business is capital expenditure carrying a right to an investment allowance. I cannot accept the view that the regularity with which a particular type of expense recurs in a particular business throws much or any light on whether it is really capital or revenue expenditure. On the material available I am of opinion that the Respondents have made out their case that this expenditure was capital expenditure, and I turn to consider whether the knives and lasts were plant within the meaning of the Section.

It is not disputed that " plant " is also used in the Act as an ordinary English word. It is not altogether an easy word to construe ; it may have a more or less extensive meaning according to its context. As a general statement of its meaning I would adopt the words of Lindley, L.J., in *Yarmouth* v. *France,* 19 Q.B.D. 647, at page 658 :

> " in its ordinary sense, it includes whatever apparatus is used by a business man for carrying on his business—not his stock-in-trade which he buys or makes for sale ; but all goods and chattels, fixed or moveable, live or dead, which he keeps for permanent employment in his business ".

I would also refer to the judgment of Uthwatt, J., in *J. Lyons & Co., Ltd.* v. *Attorney-General,* [1944] Ch. 281, at pages 286–7 :

> " I do not think that the use throughout s. 24 of the Act of the word ' plant ' as part of the phrases ' plant or machinery ' and ' machinery and plant ' has the effect of confining the meaning of the word to such plant as is used for mechanical operations or processes. Next I find it unnecessary, for the purposes of a decision in this case, to enter on the question whether any particular limitation should be placed on the general sense borne by the word ' plant ' by reason that the Act in which it appears is a rating Act. I propose to assume that no such limitation should be placed. . . . Confining my attention to trade plant, I am content to accept the general description in *Yarmouth* v. *France* that ' plant ' includes whatever apparatus or instruments are used by a business man in carrying on his business. The term does not include stock-in-trade, nor does it include the place in which the business is carried on. Whether any particular article more properly falls within ' plant ' as thus understood or in some other category depends on all the circumstances of the case."

Subject to one point, I have no doubt that these knives and lasts are plant in the ordinary sense of the word. It is true that they are numerous, small and cheap. But one trader may have to use a few large articles while another may have to use a large number of small articles, and I see no good ground for distinguishing between them as regards investment allowance. The one point is the durability of these articles. When Lindley, L.J., used the phrase " permanent employment in his business "(1), he was using it in contrast to stock-in-trade which comes and goes, and I do not think that he meant that only very long-lasting articles should be regarded as plant. But the word does, I think, connote some degree of durability, and I would find it difficult to include articles which are quickly consumed or worn out in the course of a few operations. There may well be many borderline cases, but these articles have an average life of three years, and if their cost can fairly be called capital expenditure I cannot refuse to them the description of " plant " unless the Act discloses some special reason for doing so. The word " investment " may indicate a rather longer duration than what might be sufficient in other cases. But it seems to me that machinery could not be disqualified for investment allowance because it only had a life of three years, and I see

(1) 19 Q.B.D. 647, at p. 658.

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no reason why a stricter test as to durability should be applied to plant than to machinery when the Act appears to treat them on an equal footing.

I am therefore of opinion that the Respondents are entitled to investment allowance and that this appeal should be dismissed.

Lord Tucker.—My Lords, it is common ground that in order to justify the investment allowance claimed by the Respondents it was necessary for them to prove (1) that the knives and lasts used in their business constituted machinery or plant for the purposes of Section 16 (3) of the Finance Act, 1954, and (2) that the expenditure incurred in the purchase thereof was of a capital nature. The Special Commissioners, in allowing the Respondents' appeal, expressly found that the knives and lasts were machinery or plant, and must inferentially have held the expenditure to have been of a capital nature. Vaisey, J., in allowing the Crown's appeal, held that the knives and lasts were not machinery or plant, so that the second question did not arise. The Court of Appeal agreed with the finding of the Special Commissioners on the basis that the knives and lasts were plant and held the expenditure to be of a capital nature.

I understand that all your Lordships agree with the first finding of the Court of Appeal. I am of the same opinion, for the reasons which have been stated by my noble and learned friend Lord Reid, and do not desire to add anything thereto.

The second question, upon which your Lordships are I understand divided in opinion, is, I think, much more difficult. In this connection Section 330 of the Income Tax Act, 1952, requires consideration in relation to Section 16 (3) of the Finance Act, 1954. Section 330 (1) of the former Act is, so far as material, as follows:

> " References in this Part of this Act to capital expenditure and capital sums—(*a*) in relation to the person incurring the expenditure or paying the sums, do not include any expenditure or sum which is allowed to be deducted in computing, for the purposes of income tax, the profits or gains of a trade, profession, office, employment or vocation carried on or held by him ".

Section 16 (3) of the 1954 Act has already been set out in the opinion of my noble and learned friend Lord Reid and I need not repeat it. The facts material for this part of the case are to be found in paragraphs 14 to 16 of the Case Stated and have also already been set out.

The joint effect of Section 330 of the Income Tax Act, 1952, and Section 16 (3) of the Finance Act, 1954, is, I think, to remove the disqualification for inclusion in capital expenditure attaching to sums which have been allowed by way of deduction for Income Tax in computing the profits or gains of a trade, etc. This leaves the expenditure in question to be judged free from any consideration of how it has or should be dealt with under Section 137 of the Income Tax Act, 1952. The fact that under that Section it has been allowed as a deduction is not to prejudice it in qualifying for treatment as capital expenditure for the purposes of Section 16 of the Finance Act, 1954.

My Lords, there is, as previously stated, no express finding by the Special Commissioners, but the contrary view was urged by the Crown in the first of their contentions set out in paragraph 13 of the Case Stated, and it is, I think, implicit in their decision that they must have regarded it as capital expenditure. The manner in which the taxpayer keeps his accounts is, of course, often quite irrelevant to the question how a particular item should be treated for tax purposes, but when we find, as in this case, that both the taxpayer and the Inland Revenue authorities have treated this

expenditure in the manner set out in paragraphs 4 and 6 of the Stated Case, namely by crediting the expenditure to capital account in the balance sheet and writing it off over a period of years by debiting the profit and loss account, and when no evidence is called by the Crown to say that this is not in accordance with good accountancy practice, and bearing in mind the nature and average life of the assets in question, I am of opinion that the tacit assumption of the Special Commissioners that this was an expenditure of a capital nature was fully justified, and that the appeal should accordingly be dismissed.

Lord Keith of Avonholm.—My Lords, the point in this appeal is a short one. It is whether certain knives and lasts used by the Respondents, whom I shall call " the Company ", in their trade of shoe and slipper manufacturers are machinery or plant and whether the cost of providing them falls to be treated as capital expenditure. The statutory provisions in the context of which this question has to be considered have already been explained and I do not repeat them. In the Court of Appeal and in this House the question has been dissected and examined in two parts; the nature of the assets and whether they fall to be charged against capital or revenue. To some extent this separation is inevitable, but I doubt whether it is helpful, for this reason. If at the inception of the business certain assets can properly be regarded as plant or machinery it would seem to be difficult to say that they cease to be plant or machinery when replaced or renewed. But it does not follow that the expenditure on their provision, if capital expenditure at the outset, is likewise capital expenditure on replacement.

Little, if any, attention seems to have been given to the accountancy aspect of the case before the Commissioners, apart from production of the Company's accounts, nor do the Special Commissioners expressly deal with the matter. What has been called sound accounting and commercial practice has frequently been made the basis of decision by the Courts, but the treatment by a company or individual of a particular item of expenditure in its accounts may not conform to such practice, and there are cases where the Courts have found that it does not do so. In any case, as is well known, accounts for trading purposes do not necessarily correspond to accounts for Income Tax purposes. In this case, while the views of accountants might be interesting, I doubt whether they could be conclusive, for the matter must, I think, be determined on a consideration of the statutory provisions in relation to the nature of the operations carried on by the Company.

We had a display of a sample of the knives and lasts and a demonstration of how they operated, without objection from Counsel for the Crown or challenge of the accuracy of the demonstration. From this it seems that some error or misunderstanding must have crept into the findings of the Commissioners. The knives and lasts would not seem to be attached to any machine so as to be readily detachable. The machines perform the cutting, stretching, stitching and hammering functions which might be carried out by a cobbler by hand. They in fact are just mechanical cobblers and the knives and lasts are the implements which they use, the knives being hollowed metal shapes with sharp cutting edges. It would be perfectly accurate to describe them as " implements . . . or articles employed for the purposes of the trade " within the meaning of Section 137 (*d*) of the Income Tax Act, 1952. That may not dispose of the question whether they are " machinery or plant " within the meaning of Section 279 of the same Act or Section 16 (3) of the Finance Act, 1954. The view of the

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Commissioners was that on a proper construction of these Sections the words " machinery or plant " were to be given their ordinary meaning.

" So directing ourselves,"

they say,

> " we did not doubt that there might be trades employing knives and lasts in circumstances which would make it inappropriate to describe them as machinery or plant. But in the case before us we thought we should give weight to the facts (1) that the knives and lasts performed an indispensable function in the process of manufacture, (2) that in performing that function they were used, and could only be used, in conjunction with machines which themselves could perform no useful function in the said process unless used in conjunction with the lasts and knives, and (3) that, as was not disputed, the said machines themselves were machinery or plant within the meaning of the relevant Sections."

They accordingly found as a fact on the evidence that the knives and lasts were machinery or plant within the meaning of the Sections. They seem to have considered, although they did not think it necessary to decide the fact, that the knives and lasts might also be " implements, utensils or articles " within Section 137 (*d*).

Even allowing for some error in the Commissioners' findings as to the way in which the knives and lasts functioned, I should not be prepared to say that the reasons which moved the Commissioners to find that they were machinery or plant were not equally applicable to knives and lasts functioning as described to your Lordships. They would, I think, quite properly be described as among the plant to be provided for a similar business set up for the first time, and their replacements must, I think, continue to be plant. At the same time they are, I consider, implements or articles " employed for the purposes of the trade ", expenditure on which in the course of trade can properly be chargeable as a deduction in computing profits and gains, and that in my opinion is of some importance in considering whether the money spent in replacing them is capital or revenue expenditure.

I have come to the view that in this case the expenditure on replacement should properly be treated as revenue expenditure. More upper knives are required than sole knives, and we are told that the average life of an upper knife is 12 months. The limit of life for sole knives and lasts would appear, with possible exceptions, to average three years. The Company itself in its own accounts treated its whole stock of knives and lasts as having a life of only two years and wrote off the total cost in two years. In my opinion it is quite unreal to regard constantly recurring expenditure on such articles having so short a life as capital expenditure. It can hardly be said to be expenditure on assets of an enduring nature. This to my mind is a typical case of the type referred to by the Lord President (Clyde) in *Hyam* v. *Commissioners of Inland Revenue*, 14 T.C. 479 ; 1929 S.C. 384, where he said[1] :

> " The propriety, and the practice, of charging the cost of supplying ' implements, utensils, or articles employed for the purposes of the trade ' to revenue must vary according to the character of the trade, and—partly perhaps—according to the financial circumstances of the trader. Trading implements, utensils, and similar articles—taking these descriptions in their ordinary connotation—have to be supplied, repaired and altered from time to time, in order to enable the trade to be carried on and profits to be earned ; and in many businesses, expenditure on these things is a usual incident of their conduct and properly recurs in every year, or at least in most ordinary years, as a debt against revenue account. Take the case of a hotel or restaurant business—much table-furniture, linen, crockery, pots and pans have to be provided, and the supply of such things is a usual incident of the trade. Accordingly I think that, in a business of the kind supposed, the costs of

[1] 14 T.C., at p. 486.

> such supply are a proper charge against revenue in the books, and a proper deduction from gross profits in terms of Sub-head (*d*) of Rule 3 for purposes of Income Tax."

Lord Sands, in the same case[1], took the test of considering whether the expenditure was

> "extraordinary in relation to the ordinary expenditure of the year".

It is impossible to say here that the expenditure is "extraordinary" on any view. It is just part of the ordinary expenditure incurred year after year and required for earning the profits of the business. To this may be added that the cost of the individual knives and lasts may be reckoned in shillings rather than in pounds. No doubt they have to be bought in quantity running annually into some thousands of pounds. But strictly speaking it is each knife or last that has to be considered (see *Charente Steamship Co., Ltd.* v. *Wilmot*, 24 T.C. 97), and it is somewhat fantastic to regard the expenditure of some shillings on a knife or last as capital expenditure or to suppose that when a large quantity has to be bought at one time the multiplication of what would be a revenue expense results in a capital expenditure. For the same reasons I find difficulty in supposing that Parliament intended the machinery of initial or investment allowances and annual allowances to be applied to such articles. The detailed and somewhat complex procedure prescribed by Sections 281 and 282 of the Income Tax Act, 1952, would seem quite inappropriate to such a case.

It is equally unreal to look at the matter from the purely annual point of view. The year is no doubt a convenient period and in some cases a statutory period for the making up of accounts, but there is no reason in principle why expenditure exhausted in a year should alone be treated as revenue expenditure. There must be many occasions on which it is prudent and sound commercial policy to lay in supplies of things, other than raw material of manufacture, used in a manufacturing process in quantities sufficient to last for longer than a year, and other cases where expenditure on single items which are going to endure for perhaps many years is accepted and properly accepted as revenue expenditure. Expenditure on all consumable or quickly expendable things used in industry would seem naturally to be chargeable against revenue. Nor is it always necessary to stop there. Repairs to premises or machinery may last for many years and, so long as these do not fall to be classed as improvements, are, so far as I am aware, always a charge against revenue, as is recognised indeed in Section 137 (*d*) of the Income Tax Act, 1952. Replacements generally may be said, I think, to fall into this category, and that is what the knives and lasts are here. The Company has in reality charged them against revenue. Initially charging them against capital it writes them off in two years. It may be said it charges half of them against revenue in the first year and the other half against revenue in the second year. The Company and the Revenue have reached an agreement on the amounts to be allowed as a renewals charge each year. But that does not in my opinion affect the question. It is merely a working compromise or formula to determine for the purposes of Section 137 (*d*) the actual sum expended on these renewals in any year. For my part I can see no reason why the whole sum expended in any year should not have been allowed although not exhausted in that particular year, just as I understand would be done in the case of repairs of premises or machinery. I feel at some loss because the Commissioners have not dealt with the accounting aspect of the matter, but on the evidence

(1) *Ibid.*, at p. 488.

(Lord Keith of Avonholm.)

before your Lordships I consider that the expenditure here falls to be treated as revenue expenditure.

I would allow the appeal.

Lord Denning (read by Lord Keith of Avonholm).—My Lords, in order to understand this case it is as well to have in mind the way in which a cobbler makes shoes. He cuts the leather with a knife, then shapes it round a last (which is of course a wooden model of a foot), and then hammers in the tacks. In this case, instead of a cobbler working by hand, you must envisage a series of machines which are in effect mechanical cobblers, each doing a part of the work. One mechanical cobbler is given a knife and leather: it presses down the knife and cuts the leather into the required shapes: another mechanical cobbler is given a wooden last with the leather shaped around it: it hammers down the tacks: and so forth. These machines are undoubtedly plant. They are plant used by the manufacturers in the factory. Each of the machines—each mechanical cobbler—is part of the plant. The knives and lasts too are part of the plant. When the manufacturers buy new machines, with the knives and lasts to go with them, they undoubtedly incur capital expenditure on the provision of new plant. But what is the position when the knives and lasts fall to be renewed? The manufacturers use hundreds of knives and thousands of lasts. These have a short life. They are continually having to be renewed as they wear out or fashions change. Some knives have an average life of one year, others three years. The lasts have an average life of three years. They are quite cheap; the knives cost about £1 1*s*. each, the lasts cost about £1 2*s*. a pair. The manufacturers spend about £6,000 a year on renewing them, year in and year out. What is the nature of this expenditure? Is it capital expenditure on the provision of new plant so as to qualify for an investment allowance? The Special Commissioners said nothing in particular on this point. Nor did Vaisey, J. The Court of Appeal found it difficult. Your Lordships are I believe divided in opinion.

My Lords, I cannot think that this £6,000 a year is the sort of expenditure which should qualify for an investment allowance. It is a running expense which is incurred, year in and year out, in the course of the ordinary conduct of the business. The sum actually expended can clearly be deducted in computing the profits of the business, because it is a sum expended for the supply of

> "implements, utensils or articles employed, for the purposes of the trade"

within Section 137 (*d*) of the Income Tax Act, 1952, so that the manufacturers can no doubt get 100 per cent. allowance on account of it. But I do not see that they should get an additional 20 per cent. on the ground that it is capital expenditure.

Test it this way. If this £6,000 a year were capital expenditure, the manufacturers would be entitled not only to an investment allowance on this expenditure but also to an annual allowance for wear and tear. But in order to get the annual allowance, each knife and each last would have to be treated as a separate item. Its value would have to be written down each year on a percentage basis, gradually getting less from year to year during its life—see Section 281 of the Income Tax Act, 1952; or alternatively its value would have to be written down uniformly on a straight-line basis spread over its estimated life, but this would only be allowed if the Commissioners were satisfied that proper records would be kept about it—see Section 282 of

the Income Tax Act, 1952. Neither of those methods could in practice be applied to these knives and lasts. They are too numerous, too small, too cheap and too often renewed.

Test it another way. Suppose that the manufacturers made these knives and lasts themselves. They might well have a workshop for the purpose and employ men to do the work. The cost of wages and materials would clearly be revenue expenditure which could be deducted in computing the profits of the business. There could be no suggestion that it was capital expenditure. Why should it be different because they buy them instead of making them?

Test it finally by taking some simple instances. Suppose a haulage firm has a fleet of lorries. The initial cost of the fleet is clearly capital expenditure, but the cost of renewing the tyres is revenue expenditure. Or take a hotel business. The initial cost of crockery, pots and pans and so forth is capital expenditure, but breakages run at a uniform level. The cost of replacements is revenue expenditure. Suppose a firm of builders has a carpenter's shop fitted with woodworking machines but also handsaws and chisels for the men to use. The initial cost of the machines and the tools is capital expenditure ; the machines have a long life and the cost of renewing them is a capital expenditure ; but the tools have a short life and the cost of renewing them is revenue expenditure.

I do not think that much guidance is to be obtained from the way the accounts were kept in the past. Accepting that the actual cost in each year of the knives and lasts is a revenue expense and can properly be deducted from the profits for the year, nevertheless it might well be convenient to even it out by averaging the cost over the last three years. Alternatively, if the cost was to be regarded as capital expenditure, it might well be convenient to make an annual allowance on the basis of a " straight-line " writing down on an estimated three years' life. The only thing that is perhaps significant is that there was never any claim made for an initial allowance.

My Lords, I am of opinion that the expenditure of the company on renewing knives and lasts was not a capital expenditure so as to qualify for an investment allowance, and I would allow the appeal.

Lord Jenkins (read by Lord Tucker).—My Lords, I agree with my noble and learned friends Lord Reid and Lord Tucker in their conclusion that the Respondent Company is entitled under Section 16 (3) of the Finance Act, 1954, to an investment allowance in respect of its expenditure on knives and lasts during the period relevant to its assessment to Income Tax for the year 1955–56.

In order to make good its claim to this allowance the Company had to show that the expenditure in question was " capital expenditure on new assets " within Section 16 (1), and also that it was " expenditure on the provision of new machinery or plant " within Section 16 (3). The knives and lasts were clearly new assets—see Section 16 (10) which defines " new " in relation to machinery and plant as meaning " unused and not second-hand "—and clearly also were not " machinery ". Two questions, therefore, arise in this appeal, namely (1) whether the knives and lasts were " plant " ; and (2) if so, whether the expenditure on the provision of them was capital expenditure.

I have no doubt that the knives and lasts were " plant ". On this point I am for the present purpose content to accept as a sufficient state-

(Lord Jenkins.)

ment of the ordinary meaning of the expression "plant" the words of Lindley, L.J., in *Yarmouth* v. *France,* 19 Q.B.D. 647, at page 658:

> "There is no definition of plant in the Act [the Employers' Liability Act, 1880] but, in its ordinary sense, it includes whatever apparatus is used by a business man for carrying on his business,—not his stock-in-trade which he buys or makes for sale; but all goods and chattels, fixed or moveable, live or dead, which he keeps for permanent employment in his business."

The reference to "permanent employment" in the business demands some degree of durability. This, I think, is satisfied in the present case by the life of three years attributed to making and finishing lasts, sometimes extended to four or five years in the case of the latter, and to sole knives. The upper knives are given a life of only 12 months, but the intention, no doubt, is to keep and use them for so long as they are serviceable, and I cannot regard the circumstance that they wear out in that relatively short period as investing them with so transitory a character as to take them out of the category of plant to which they would otherwise belong.

The second question, namely whether the expenditure on the provision of the lasts and knives was capital expenditure, presents more difficulty, but broadly speaking I think that subject to the requisite degree of permanence an appliance which satisfies Lindley, L.J.'s definition of plant is well on its way to attaining the status of a capital asset, the cost of providing which may be properly regarded as capital expenditure. Mr. Heyworth Talbot in his argument for the Company submitted that all expenditure on the acquisition of assets to be retained by a manufacturer for use again and again in his manufacturing operations is capital expenditure; and that this holds good whether the assets in question are acquired by way of addition to or in replacement of existing stocks. It will be seen that the definition of "capital assets" implicit in Mr. Heyworth Talbot's submission is closely akin to Lindley, L.J.'s definition of "plant". Both postulate that the assets in question should possess some degree of permanence. Lindley, L.J., speaks of goods and chattels kept by the business man for permanent employment in his business, while Mr. Heyworth Talbot speaks of assets retained by a manufacturer for use again and again in his manufacturing operations. But neither of them attempts to define the degree of permanence required, and indeed it would, as I think, be impossible to do so. I accept Mr. Heyworth Talbot's submission, not as embodying a hard and fast rule of universal application, but as providing so far as it goes a reasonably adequate guide to the solution in the present case of the question whether the expenditure on the assets here concerned, that is to say the knives and lasts, was capital expenditure for the purposes of Section 16.

The Company does not deal in knives and lasts. It acquires knives and lasts for retention and use as part of its means of manufacturing shoes and slippers. In point of function the knives and lasts resemble the machines in conjunction with which they are used, in the sense that they are not themselves a subject of the Company's trade but are kept and used until such time as they become unserviceable or obsolete, and by their use contribute to the production of the shoes and slippers in which the Company does trade. So far therefore they may be said to be assets producing income as distinct from assets representing income, and to that extent at least to be of a capital nature. The machines in conjunction with which the knives and lasts are used are admittedly capital assets. For the present purpose I see no ground for distinguishing the former from the latter in this respect apart from the small cost and relatively short life of the knives and lasts as compared with the machines. As to the cost,

if the knives and lasts had an unlimited life the fact that they cost only a matter of £1 each would not, so far as I can see, afford any ground for denying them the character of capital assets. As to length of life, if each knife or last was worn out by one day's work it would lack the element of permanence which is undoubtedly essential to the conception of a capital asset. The knives and lasts worn out by each day's work would on this supposition have no better claim to rank as capital than would be possessed by the coal consumed daily in firing the boilers in a factory where the machines were worked by steam. On the other hand, I repeat that if each knife or last endured for ever I can see no ground for holding that it would not be a capital asset.

The case, therefore, appears to me to turn in the end on the question of permanence, which is largely a question of degree. I think the element of permanence looms larger in the conception of a capital asset than it does in the conception of plant. Nevertheless, I see no reason for holding that the average life of three years possessed by sole knives and making and finishing lasts is too short to justify their acceptance as capital assets. The average life of only 12 months possessed by upper knives seems to me to be near the line, but no attempt has been made to separate these knives and the other appliances, and I do not know whether it would have been practicable to do so. In point of function there is no distinction, so far as I can see, between the upper knives and the rest. I would therefore give the upper knives the benefit of the doubt and for the present purpose treat them as possessing the requisite degree of longevity. This accords with the arrangements between the Revenue and the Company referred to in paragraph 6 of the Case, which allowed all the knives and lasts an average life of three years. So far as the question is one of fact and degree, I think the Special Commissioners must be taken to have held by implication that the expenditure here in question was capital expenditure, and I see no sufficient reason for differing from that view. I would accordingly dismiss this appeal.

Questions put :

That the Order appealed from be reversed.

The Not Contents have it.

That the Order appealed from be affirmed and the appeal dismissed with costs.

The Contents have it.

[Solicitors :—Solicitor of Inland Revenue ; Bracewell & Leaver.]