No. 625.—High Court of Justice (King's Bench Division).—15th March, 1926.

Court of Appeal.—30th June, 1926.

House of Lords.—11th July, 1927.

Constantinesco *v.* Rex.[2]

(Petition of Right.)

Income Tax—Payments by Royal Commission on Awards to Inventors for user of patent—Deduction of tax—Income Tax Act, 1918 (8 & 9 *Geo.* V, *c.* 40), *Rule* 21 (1) *of General Rules.*

An award of £70,000 *was made by the Royal Commission on Awards to Inventors on the 6th December*, 1922, *in respect of the user by the British Government subsequently to the 6th March*, 1918, *of the interrupter gear invented by the Suppliant, and on the 28th March*, 1923, *a further award of* £15,000 *was made by the Joint Commission of the said Commission and the American Commission for the Adjustment of Foreign Claims, in respect of the user by the Government of the United States of the same gear.*

Income Tax was deducted from the sums awarded before payment to the Suppliant and another, who were at all material times the joint owners of the inventions and relevant patents, but the Suppliant claimed that the said sums were capital payments in respect of which Income Tax was not payable.

Held, *that the sums received were royalties paid in respect of the user of the patent within Rule* 21 (1) *of the General Rules of the Income Tax Act*, 1918.

---

[2] Reported (K.B.D.) 42 T.L.R. 383; (C.A.) 42 T.L.R. 685; and (H.L.) 43 T.L.R. 727.

PETITION OF RIGHT.

TO THE KING'S MOST EXCELLENT MAJESTY

THE HUMBLE PETITION of George Constantinesco of "Carmen Sylva," Beechwood Avenue, Weybridge, by Messrs. Bristows, Cooke & Carpmael of 1, Copthall Buildings, E.C., his Solicitors.

SHEWETH that:

1. Your Suppliant made certain inventions relating to power transmission and interrupter gear and the said inventions were protected inter alia by British Letters Patent No. 512 of 1917 and United States Patents Numbers 1211679; 1211680; 1334280; 1373944 and Your Suppliant and Walter Haddon at all material times were the joint owners of the said inventions and the said Patents.

2. The said inventions have been used by Your Majesty's Secretary of State for War and by the Government of the United States of America for and in connection with the manufacture of munitions of war.

3. Your Suppliant by application dated December 16th, 1919, applied in respect of the use of the said inventions by Your Majesty's Secretary of State for War to the Royal Commission on Awards to Inventors, appointed by Your Majesty, for an Award under the Royal Warrant dated 19th March, 1919, appointing the said Commission.

4. The said application was heard by the said Commission and on 6th December, 1922, the following Award and recommendation was made by the said Commission:

"Claim No. 855.

"THE ROYAL COMMISSION ON AWARDS TO INVENTORS.
"APPLICATION OF MESSRS. GEORGE CONSTANTINESCO AND
"WALTER HADDON IN RESPECT OF SYNCHRONISING GEARS
"(C.C. INTERRUPTER GEARS).

"AWARD AND RECOMMENDATION.

"The Commission have settled the terms of user of this "invention as follows, that is to say, they award and "recommend that there be paid to the Applicants the sum "of £50,000 (Fifty thousand pounds) and a further sum of "£20,000 (Twenty thousand pounds) making together the "sum of £70,000 (Seventy thousand pounds) in respect of "the user by or for the service of the Crown of gears which

" as stated in Clause 7 of the Particulars of Claim herein
" dated the 16th day of March, 1919, were subsequently
" to the 6th day of March, 1918, made by any Department
" of His Majesty's Government, or by their Agents, Con-
" tractors or others in accordance with Letters Patent
" 512/1917, the number of such gears being approximately
" 27,857.

" Signed Charles H. Sargant,
" Chairman.

" P. Tindal Robertson,
" Secretary,
" Dated 6 Dec. 1922."

5. The said recommendation was accepted by Your Majesty's Treasury and on 20th December, 1922, Your Suppliant and the said Walter Haddon received a draft for £52,500 which accompanied the following letter.

" Air Ministry.
" Adastral House,
" Kingsway,
" London, W.C.2.
" 20th December, 1922.

" Air Ministry Refce. 345753/22/F.M.(B)

" SUBJECT :—

" Gentlemen,

" I am directed to transmit the enclosed draft for the sum
" of £52,500 (fifty-two thousand five hundred pounds), being
" the amount of the award of the Royal Commission on Awards
" to Inventors, £70,000, to Messrs. George Constantinesco and
" Walter Haddon, less Income Tax £17,500.

" I am,
" Gentlemen,
" Your obedient Servant,
" E. CRUICKSHANK.

" Messrs. Bristows, Cooke & Carpmael,
" 1, Copthall Buildings,
" E.C.2."

6. By Agreement in writing dated 11th day of January, 1923, between Your Suppliant and the said Walter Haddon, the President of the Air Council and the Assistant Secretary of War Department, Washington, United States of America, it was agreed that His Majesty's Royal Commission on Awards to Inventors sitting conjointly with the Commission for the adjustment of foreign claims appointed by the War Department,

United States of America, should determine the amount proper to be paid to Your Suppliant and the said Walter Haddon for the use of the said invention by the Government of the United States of America and that the decision of the said Commission should be final and conclusive.

7. In accordance with the said Agreement the said Commission heard the claim of Your Suppliant and the said Walter Haddon, and on the 28th March, 1923, a letter was written by the Secretary of the said joint Commission to the said Walter Haddon and Your Suppliant stating that the said Commission in accordance with the said Agreement of 11th January, 1923 :—

> " Awarded and determined that the amount proper to be " paid by His Majesty's Government to the Claimants in " respect of the communication to and/or user by or on " behalf of the Government of the United States of the " invention or inventions design or designs in the said " memorandum of agreement mentioned is the sum of " fifteen thousand pounds sterling."

8. The said Award was accepted by Your Majesty's Treasury and by the Government of the United States of America and the sum of £11,250 was paid by Your Majesty's Government to Your Suppliant and the said Walter Haddon, and the balance of £3,750 was paid to the Commissioners of Inland Revenue or retained by Your Majesty's Government as Income Tax.

9. The said sums of £70,000 and £15,000 were capital sums and were not annual payments or annual profits or gains

10. By Agreement in writing dated 1st June, 1921, it was agreed between Your Suppliant and Walter Haddon that their interests in the said inventions should be divided so that the said Walter Haddon and Your Suppliant became entitled to the amounts so awarded in the following proportions :—

	Suppliant.	*Walter Haddon.*
Award of £70,000	£36,000	£34,000
Award of £15,000	£7,500	£7,500
	£43,500	£41,500

and the said sums of £52,500 and £11,250 were divided in the said proportions between Your Suppliant and the said Walter Haddon.

11. Your Suppliant made application to Your Majesty's Secretary of State for Air and to the Commissioners of Inland Revenue for repayment of the sum of £10,875 deducted from his proportion of the said Awards and paid over to the said Commissioners. The said Secretary and the said Commissioners have refused to pay the sum of £10,875.

12. By reason of the premises Your Suppliant respectfully submits that there is still due and owing to him the sum of £10,875 and that Income Tax is not payable in respect of the said sum of £43,500 or any portion thereof and the said sum of £10,875 should be paid to Your Suppliant with interest thereon.

YOUR SUPPLIANT therefore humbly prays that Your Majesty may be graciously pleased to direct this Petition to be endorsed with Your Majesty's Fiat that right be done.

DATED the 23rd day of July, 1924.

CARROL ROMER,
Counsel for the Suppliant.

ANSWER AND PLEA.

To the said Petition by His Majesty's Attorney-General for and on behalf of our Lord the King delivered this 20th day of February, 1925, by the Solicitor of Inland Revenue.

SIR DOUGLAS MCGAREL HOGG, His Majesty's Attorney-General, on behalf of our Lord the King, gives the Court here to understand and be informed as follows :

1. The questions raised by this Petition relate to the deduction of £17,500 by way of Income Tax from the sum of £70,000 awarded to the Suppliant and Walter Haddon by the Royal Commission on Awards to Inventors by their award of the 6th December, 1922, and the sum of £3,750 deducted in like manner from the sum of £15,000 awarded by the said Commission sitting conjointly with the Commission for the adjustment of Foreign claims appointed by the War Department, United States, by their award dated 28th March, 1923.

2. Upon these questions the Attorney-General refers the Court to the following provisions of the Patents and Designs Act, 1907, and the Income Tax Act, 1918, and His Majesty's Royal Warrant appointing the said Commission which are respectively as follows :—

PATENT AND DESIGNS ACT, 1907.

" 29. A patent shall have to all intents the like effect as " against His Majesty the King as it has against a subject.

" Provided that any government department may, by " themselves, their agents, contractors, or others, at any " time after the application, use the invention for the ser- " vices of the Crown on such terms as may, either before or " after the use thereof, be agreed on, with the approval of " the Treasury, between the department and the patentee, " or, in default of agreement, as may be settled by the " Treasury after hearing all parties interested."

GENERAL RULES APPLICABLE TO SCHEDULES A, B, C, D AND E OF INCOME TAX ACT, 1918.

"21. (1) Upon payment of any interest of money, "annuity or other annual payment charged with tax under "Schedule D or of any royalty or other sum paid in respect "of the user of a patent not payable or not wholly payable "out of profits or gains brought into charge, the person by "or through whom any such payment is made shall deduct "thereout a sum representing the amount of the tax thereon "at the rate of tax in force at the time of the payment."

HIS MAJESTY'S ROYAL WARRANT.

"GEORGE R.I.

"George the Fifth by the Grace of God, of the United "Kingdom of Great Britain and Ireland and of the British "Dominions beyond the Seas King, Defender of the "Faith to—

"Our Trusty and Well-beloved :—

"Sir Charles Henry Sargant, Knight, one of the Judges "of our High Court of Justice (Chancery Division);

"Robert John Strutt, Esquire, Fellow of the Royal "Society (commonly called the Honourable Robert John "Strutt);

"Sir James Johnston Dobbie, Knight, Doctor of Science, "Doctor of Laws, Fellow of the Royal Society, Principal of "the Government Laboratories;

"George Lewis Barstowe, Esquire, Companion of Our "Most Honourable Order of the Bath, a Principal Clerk in "the Treasury;

"William Temple Franks, Esquire, Companion of Our "Most Honourable Order of the Bath, Comptroller-General "of Patents, Designs and Trade Marks;

"Alfred Clayton Cole, Esquire;

"Halford John Mackinder, Esquire, and

"Robert Young, Esquire.

"Greeting.

"Whereas by Section 29 of the Patents and Designs Act, "1907, it is enacted as follows, that is to say :—

(Here was inserted Section 29 of the Act set out above.)

"And whereas recently and particularly in connection "with the present war there has been an exceptional user "by the Navy, Army, Air Force, Ministry of Munitions and "other Government Departments of inventions protected "by Letters Patent.

" And whereas there may also have been the like excep-
" tional user of inventions designs drawings or processes
" which, though not protected against the Crown under the
" said Act, or otherwise may have been of such merit or
" utility as to render it proper that the inventor, author or
" owner thereof should receive some remuneration from the
" Treasury in respect of such user;

" And whereas, under the circumstances aforesaid, an
" unduly heavy burden has been cast upon the Treasury in
" relation to the settlement of the terms of user of patented
" inventions under the aforesaid Section 29 and otherwise
" under that Section and also in relation to fixing any
" proper remuneration in respect of the other matters here-
" inafter mentioned;

" And whereas we have deemed it expedient in the
" premises that a commission should forthwith issue for the
" purposes and with the powers hereinafter appearing.

" Now know ye that We, reposing great trust and con-
" fidence in your knowledge and ability, have authorised
" and appointed, and do by these presents authorise and
" appoint you the said Sir Charles Henry Sargant (Chair-
" man), Robert John Strutt, Sir James Johnston Dobbie,
" George Lewis Barstowe, William Temple Franks,
" Alfred Clayton Cole, Halford John Mackinder and Robert
" Young to be our Commissioners for the purposes and
" with the powers following, that is to say :—

" (1) In any case of user or alleged user of any patented
" invention for the services of the Crown by any Govern-
" ment Department and of default of agreement as to the
" terms of user the Commissioners, upon the application of
" the patentee and agreement to accept their determina-
" tion, may proceed to settle and may settle the terms of
" user in lieu and place of the Treasury : Provided that the
" Commissioners shall not actually award to the patentee
" any sum or sums of money whether by way of a gross sum
" or by way of royalty or otherwise which shall together
" exceed an aggregate sum of £50,000 beyond and in
" addition to any allowance the Commissioners may think
" fit to make for outlay and expenses in connection with
" the invention : But the Commissioners, if of opinion that
" the Patentee is fairly entitled to a remuneration exceeding
" the said aggregate sum of £50,000 may make a recom-
" mendation to the Treasury as to any such excess, with a
" statement of their reasons for such recommendation.

" (2) In any case where terms of user of any patented
" invention (including any terms as to selling for use,
" licensing or otherwise dealing with any article made in
" accordance therewith, or any terms as to assignment of
" an invention under Section 30 of the Act) have been agreed

" or are in course of agreement between the patentee and " any Government Department, the Commissioners may on " the application of the Treasury make any recommenda- " tion as to the giving or withholding by the Treasury of " approval of such agreement or proposed agreement, and " may assist in adjusting or determining any term or terms " of any proposed agreement as to which the parties may " not be fully agreed.

" (3) In any case of user or alleged user for the services " of the Crown by any Government Department of any " inventions, designs, drawings or processes which, though " not conferring any monopoly against the Crown or any " statutory right to payment or compensation may neverthe- " less appear from their exceptional utility or otherwise to " entitle the inventor, author or owner thereof to some " remuneration for such user (including user by way of " selling for use, licensing or otherwise dealing with any " articles made in accordance therewith) the Commissioners " may, on the request of the Treasury, enquire into the " circumstances of the case and may make a recommenda- " tion to the Treasury as to the remuneration (if any) that " is proper to be allowed therefor.

" And for the better effecting the purposes of this our " Commission, We do by these Presents authorise you to " sit in two divisions, each division consisting of such three " or more of you as the said Sir Charles Henry Sargant " shall determine : and to allocate to the two said divisions " such of the matters submitted for your consideration as " you may deem expedient.

" And We do by these Presents give and grant unto you " full power to call before you such persons as you shall " judge likely to afford you any information upon the sub- " ject of this Our Commission; to call for information in " writing; and also to call for, have access to, and examine " all such books, documents, registers and records as may " afford you the fullest information on the subject and to " enquire of and concerning the premises by all other lawful " ways and means whatsoever.

" And We do by these Presents authorise and empower " you to visit and personally inspect such places as you may " deem it expedient so to inspect for the more effectual " carrying out of the purposes aforesaid.

" And We do by these Presents will and ordain that this " Our Commission shall continue in full force and virtue and " that you Our said Commissioners may from time to time " proceed in the execution thereof, and of every matter and " thing therein contained, although the same be not con- " tinued from time to time by adjournment.

" Provided that, should you deem it expedient, the powers " and privileges hereinbefore conferred on you shall belong " to and may be exercised by any one or more of you.

" And We do further ordain that you have liberty to " report your proceedings under this Our Commission from " time to time if you shall judge it expedient so to do.

" And Our will and pleasure is that you do, from time to " time, report to the Lord Commissioners of Our Treasury, " under hand and seal, your opinions upon the matters " herein submitted for your consideration.

" Given at Our Court at *Saint James's* the " nineteenth day of March one thousand " nine hundred and nineteen in the ninth " year of Our Reign.

" By His Majesty's command,

" EDWARD SHORTT."

" ROYAL COMMISSION
" ON AWARDS TO INVENTORS."

3. The Attorney-General further gives the Court here to understand and be informed that it was agreed between His Majesty's Government and the Government of the United States of America after the declaration of War by the last-mentioned Government against Germany, that in order that the forces of the United States in France should use standard types of aircraft, that aircraft should be manufactured in the United States, and that His Majesty's Government should be responsible for the payment to all British inventors and patentees for the use and manufacture by the United States Government of the patented inventions of such British Subjects, in connection with aircraft manufactured in the United States. In pursuance of this agreement all claims by such British subjects in respect to the use of their patented inventions by the Government of the United States were submitted to the determination of the said joint Commission.

4. By reason of the foregoing the Attorney-General submits to the Court that the payments awarded by the said Royal Commission and the said Joint Commission to the Suppliant were royalties or other sums paid in respect of the user of a patent and that Income Tax was therefore properly deducted therefrom.

5. By reason of the foregoing the Attorney-General submits that there is not now due and owing to the Suppliant the alleged or any sum.

DOUGLAS MCGAREL HOGG.

The case came before Rowlatt, *J.*, in the King's Bench Division on the 15th March, 1926, when the Petition was dismissed, with costs.

Mr. Montgomery, K.C., and Mr. Carrol Romer appeared as Counsel for the Petitioner, and the Attorney-General (Sir Douglas Hogg, K.C.) and Mr. R. P. Hills for the Crown.

JUDGMENT.

Rowlatt, J.—In this case the question is whether this sum is an annual profit or gain, or whether it is a capital payment.

Now I have been referred to the Section of the Patents Act and to the form of the Claim and to the form of the Award, and so far, of course, there cannot be any doubt that these are proper materials. But I have also been referred to the proceedings before the Commission and to statements in the Report of the Commission to the Crown, to the admissibility of which exception was taken. This is not an action on the Award, but a curious inquiry as to the nature of the payment, and it seems to me that those materials were admissible in evidence. But I do not think they add to the matter. It seems to me that the claimant might very well put his claim upon a royalty basis and have it calculated upon a royalty basis and use language talking about royalty and so on without really concluding the point I have to decide. But when I look, as I think, a little deeper into what was the question at issue, I find that the question at issue was: What was to be paid, in some form or another, in respect of the user of this invention from day to day and year to year over the period in question? Mr. Constantinesco and his associate were not deprived of their patent. What they were deprived of was the power of making terms as to its use. Possibly they were deprived of the power of licensing other people, but they were not deprived of their interest in the patent. They remained (compulsorily, if you like) in the position of licensors all the time, and, so far from their having lost that position, what was happening all through the period was that this invention was earning to the patentees, for them, from day to day, the right to remuneration for the use of the invention. That was the position. Therefore I think, whatever language may have been used by Counsel before the Commission, or by the Commission themselves, it does not add to the matter. What clearly was being dealt with here was a remuneration for the use of the patent; that is to say, for the benefit from year to year of this valuable piece of property. But that does not, as I think, lead me to a conclusion. It leads me to the point to be decided, because, although what was being paid for was something which is properly paid for by means of a royalty, if I may put it that way, the question is whether this remains a royalty or whether it is a capitalised sum in lieu of a royalty. That is what I think the point is. Now you may, of course, turn payments which are

(Rowlatt, J.)

undoubtedly income into capital. There may be a charge, and you may redeem it, but the money you pay for redeeming the charge is not liable to deduction of Income Tax because the annual sums under the charge would have been. And I have not the least doubt that you may pay a lump capital sum in lieu of royalties, or to capitalise what is really a royalty, if you like to put it that way, for the use of a patent. Now has that been done? Mr. Montgomery put a case to me—an obvious case. Supposing, before the user, it is said: "Now pay £25,000"—or whatever sum the parties agree to—"and use it as much as you "like, for a definite time or for the whole length of the patent." That will clearly be a lump sum. It would not be parting with the patent, because other people might use it, but it would be clearly a capital sum, in my judgment. But see how different that is from this case. In that case the capital sum is paid, and a free hand is given to make whatever use is available of the subject matter that the party wants to make. But in this case it is afterwards; all the facts are known; the amount of the user is put in the claim, and the amount of the user is stated in the Award. Now what evidence have I got, really, that this sum is a capitalised sum? There have been three or four years of this user. The amount of the user is known. The patentee is entitled to be paid for the user of his patent all through that time, and then he is given a sum. What ground is there for saying that that is not the total sum for the actual use, as opposed to a lump sum to abolish the payment for the actual use, and capitalise it? I cannot see any materials for so deciding, and I think that this must be taken as simply a royalty for the four years, paid in this year, and that the Revenue were entitled to insist that this sum for Income Tax should be withheld. Therefore, in my judgment, the Petition fails and it must be dismissed with costs.

An appeal having been entered against this decision, the case came before the Court of Appeal (Lord Hanworth, *M.R.*, Scrutton, *L.J.*, and Russell, *J.*) on the 30th June, 1926, when judgment was given unanimously in favour of the Crown, with costs, confirming the decision of the Court below.

Mr. Montgomery, K.C. and Mr. Carrol Romer appeared as Counsel for the Appellant, and the Attorney-General (Sir Douglas Hogg, K.C.) and Mr. R. P. Hills for the Crown.

JUDGMENT.

Lord Hanworth, M.R.—We need not trouble you, Mr. Hills.

The question that we have to determine in this case is whether a sum which has been paid to an inventor for the user or the adaptation of some ingenious gear which he invented during the period of time of the War is a capital sum, or income and subject to deduction of Income Tax.

(Lord Hanworth, M.R.)

Perhaps it may be well to recall how this claim was put before the Commission who decided that the sum should be paid, and it is perhaps wise to remember that until the Patent Act of 1883 there remained in the Crown, who granted the exclusive use of a patent by its own letters patent to an inventor—the exclusive use or right or the monopoly of the patent—the right to use the patent without the assent of or without compensation being made to the patentee at all. That was decided in *Fisher* v. *The Queen*, a well-known case which is to be found in 6 Best and Smith, at page 257. But in 1883 the Section, which is now replaced by Section 29 of the Patents Act of 1907, was first introduced, and that said that a patent should have to all intents the like effect as against His Majesty the King as it has against a subject, with the important proviso that it was important for the public service and the advantage of the State and of all citizens who enjoyed the privileges and security of the State that it should be possible for a Government Department to make use of the patent, and in the proviso it is stated that any Government Department may "by themselves, their agents, contractors, or others, at any time "after the application, use the invention for the services of the "Crown on terms to be before or after the use thereof agreed on, "with the approval of the Treasury, between those officers or "authorities and the patentee, or, in default of such agreement, "on such terms as may be settled by the Treasury after hearing "all parties interested."

In the course of the War there were a large number of patents taken out which had to be used and were rightly used in the interests of public safety. Among them was this invention for which letters patent had been granted to the representative, as I understand, of Mr. George Constantinesco. The invention was an ingenious one for enabling a bullet to be fired at a time when there was a space, in front of the barrel of the gun, between the blades of the propeller of an aeroplane. The invention was largely used and was undoubtedly an important one. For the purpose of dealing with such claims as these, a Royal Commission was established, and the actual terms of the Commission are set out in the Answer and Plea of the Attorney-General to the Petition of Right of Mr. Constantinesco. It recalled that there had been exceptional user by the Navy and the Army and the Air Force and the Ministry of Munitions of the inventions and designs and processes and so on, for which, though not protected as against the Crown, the owners should receive some remuneration, and then established a system whereby the inventors could bring their claims before that Commission and obtain, if the Commission thought right, payment for the user of the invention. Accordingly a claim was put forward by Mr. Constantinesco, and that claim contains the nature and the basis on which his claim is founded. The basis on which the claim is made is for royalties, and the particulars of the alleged user by any Government Department,

(Lord Hanworth, M.R.)

and, so far as possible, the nature and extent and the period of the user were asked for in the particulars, the terms of which were no doubt issued in a printed form to the applicants before the Commission; and the reply was that in a period between 8th March, 1918, down to a date which does not appear, I think, in the answer upon the statement, but which is now given to us, namely, the 31st July, 1919, this invention was applied to no less than 27,857 gears manufactured by various factories for the purposes of the War. Particulars of the amount claimed were asked for, a sum equal to £10 per gear, being the rate of royalty reserved by the licence to the original manufacturers. Upon that, after the case had been heard, it was determined by the Commission that two large sums should be paid to the inventor. The reason why two large sums were named was this: The powers of the Commission were limited. They could not give a sum larger than £50,000. They could, if they desired to give a larger sum than that, recommend to the Treasury, stating the reasons for a larger payment, and it was left to the discretion of the Treasury to determine whether a sum outside the limit entrusted to the Commission should be given. The Commission therefore made this award: "The Commission have settled the terms of "user of this invention as follows"—then they set out the sums I have referred to—"in respect of the user by or for the service of "the Crown of the gears which, as stated in Clause 7 of the "Particulars of Claim . . . . were . . . . made by any Depart- "ment of His Majesty's Government." It appears plain from the passages in the claim to which I have referred, and the award, that what was dealt with was a sum, the totality of which was intended to cover all the cases where use had been made of the invention of Mr. George Constantinesco in respect of the 27,857 gears to which the invention had been applied during the period that I have named.

The Treasury claimed to deduct Income Tax from that payment to be made, and the first question that we have to determine is whether or not the payment so made was a sum which fell within Schedule D of the Income Tax Acts, a sum liable to tax as being part of the profits or gains made by the inventor, which are brought within the wide range of Schedule D, the words of which have been quoted to us by Mr. Montgomery. It is said that they are not a matter of annual profits or gains; that it was the payment of a capital sum. Now I agree with Mr. Justice Rowlatt that what we have to determine, and what he had to determine, is what is the substance of the matter, and that the mere statement made by the inventor that it was a capital sum or that it was an annual profit does not dispose of the matter. We have got to get at the substance of it, as has been said in so many of these cases. If it is a capital sum, then it would not be treated as an annual sum. But is it capital or is it income? I agree with Mr. Justice Rowlatt in finding no evidence at all on

(Lord Hanworth, M.R.)

which it could be claimed to be a capital sum. It appears that the compensation sought was the compensation for the use of the invention, for the repeated use of the invention, for the use of the invention during a specified period of months, for the use of the invention as applied to a specified number of gears. When you ascertain the sum, whether you ascertain it by so much per gear or whether you ascertain it by some other estimate does not appear to alter the character of the sum to be paid, which still remains a sum in respect of the use of the invention applied to those gears, the table for which was presented to the Commission by Mr. Constantinesco. Once one has determined that the nature of the payment was in respect of a user of the invention over a period of time and to a number of gears, and that it was intended to represent compensation for that particular form of user, it is stripped of all nature of capital. Mr. Montgomery has called our attention to one or two cases—and there are many of them—in which you have reached a capital sum by an estimate derived from income. The commonest case, which I put in argument, is the one in which you give so many years' purchase for a piece of land, estimating the value by the annual profit that can be made out of the land, and capitalising it at so many years' purchase; but that system has no analogy to the present case. This is a compensation paid in respect of what ought to have been paid, it may be week by week or month by month, during the time in which these gears had the invention applied to them, and during which an ever-increasing sum was totalling up, as against the Departments who were making use of the invention, in favour of Mr. Constantinesco.

It appears to me that the judgment of Mr. Justice Rowlatt is perfectly right. He has dealt with the facts. The facts appear to me to make it impossible to hold that this is a capital sum, and therefore it is a matter falling within Schedule D, from which tax is deductible.

Two other points were faintly argued before us. One was that it was not an annual profit because it was a sum paid once and for all for a particular user. The sum that has been paid, as I have pointed out, is for or in respect of the user, particulars of which were given in the claim which was put before the Commission, and we have decided more than once, and quite recently in the case of *Martin* v. *Lowry* (1), that the mere fact of its being one payment does not prevent it being annual in the sense that it is in respect of the year for which the charge on profits and gains under Schedule D is made.

Another point was suggested, that Rule 21 of the General Rules does not apply to this case; but that appears to be untenable. Rule 1 of the General Rules says: "Every body of "persons shall be chargeable to tax in like manner." The General Rules are given in the Act, and Rule 21 is this: The tax is paid

(1) 11 T.C. 297.

(Lord Hanworth, M.R.)

"upon payment of any interest of money, annuity, or other "annual payment charged with tax under Schedule D, or of "any royalty or other sum paid in respect of the user of a patent, "not payable, or not wholly payable, out of profits or gains "brought into charge". Now it is said by Mr. Montgomery that that Rule is a matter of machinery. But be it so, once one has decided that this is compensation paid in respect of the individual but ever-increasing cases where the invention has been applied to gears, then it is a sum which is paid in respect of the user of the patent upon those gears; it is a sum which I have already decided is not a capital sum but a matter of income, and Rule 21 indicates the method or manner in which the charge can be made in or upon a sum paid in respect of the user of a patent—a sum which is not strictly a royalty but which is nevertheless compensation for the user of the patent.

It appears to me upon all these grounds that Mr. Justice Rowlatt was perfectly right in his judgment and that the appeal must be dismissed with costs.

Scrutton, L.J.—I agree. The Appellant was the owner of a patented invention capable of being used in the case of aircraft carrying guns, and it was so used during the War by the Government in a specified number of instances, and thereupon the Royal Commission awarded to the inventor a sum in respect of a claim of his based upon a royalty for each of the specified number of instances. Now it seems to me that that sum was a sum paid by the Government for the use of a patent to a specified extent, the property in the patent remaining in the Appellant, and that a sum which can be described in that way is taxable as income and is not a capital payment. The Government, in paying the sum, deducted Income Tax from it, and it appears to me that such a deduction was exactly within the words of Rule 21 of the General Rules, and that it therefore follows that the appeal of the Appellant fails.

With regard to the merits, it seems obviously right that a naturalised subject of this country, who is receiving profits from the use of his invention to defend the country, should also be liable to Income Tax on those profits, the expenditure for which Income Tax is levied having been incurred to defend him and other subjects of the country.

Russell, J.—I agree. It seems to me that the suppliant here put forward a claim to be paid a sum composed of royalties at the rate of £10 on each gear made by the Government under the British patent. It appears to me, as I read the award of the Commission, that they awarded him a round sum made up of royalties upon a smaller basis.

I agree that the appeal should be dismissed.

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

Lord Hanworth, M.R.—Yes; I said so.

Notice of appeal having been given against the decision of the Court of Appeal, the case came on for hearing in the House of Lords before Viscount Cave, *L.C.*, Viscount Dunedin, and Lords Atkinson, Shaw of Dunfermline, and Carson, on the 11th July, 1927, when judgment was delivered unanimously in favour of the Crown, with costs, confirming the decision of the Court below.

Mr. Montgomery, K.C., and Mr. Carrol Romer appeared as Counsel for the Appellant, and the Attorney-General (Sir Douglas Hogg, K.C.) and Mr. R. P. Hills for the Crown.

JUDGMENT.

Viscount Cave, L.C.—My Lords, the Appellant in this case is part owner of a patented invention of great utility, which consists of a control gear enabling a machine-gun to be fired through the propeller of an aeroplane without destroying the blades. During the War the Ministry of Munitions, under the powers which had been conferred upon the Government by the Patents Act, 1907, used this invention for war purposes. The terms upon which they were to use it were not settled at the time but were, under the provisions of Section 29 of the Patents Act, to be determined, in default of agreement, by the Treasury. At the end of the War the Treasury found that they had many claims of this kind to dispose of; and accordingly a Commission was set up which was called the Royal Commission on Awards to Inventors, and that Commission was authorised to inquire into claims, both by patentees and by certain other persons, and to make an award in favour of any claimant up to £50,000 and to recommend in special cases the payment of a sum in excess of that amount. The Appellant and his partner put in their claim before the Commission, stating the period during which this invention had been used by the Crown, and the number of gears or appliances falling under the patent which had been made for the Crown, and they claimed a sum equal to £10 per gear, being, as they said, the rate of royalty reserved by the licence previously granted to certain manufacturers. The Commission awarded to the Appellant and his partner a sum of £50,000 and recommended the payment of a further sum of £20,000. The Crown paid to the Appellant and his partner those sums, amounting to £70,000, less a deduction of Income Tax on the amount, and the question is whether that tax was rightly deducted. There was a further award in respect of the use of the invention by the United States, but the question arising from that award is the same, and I need not further refer to it.

My Lords, three points are raised on behalf of the Appellant. First, it is said that the sum of £70,000 was not annual profits or gains within the meaning of the Income Tax Act but was the

(Viscount Cave, L.C.)

payment of a capital sum. I cannot agree with that contention. The payment was made in respect of the use of the invention over a period of time. The claim put in was a claim as for royalty in respect of the successive uses of the invention. In the case of patented inventions it was the practice of the Commission, as appears from their Report which has been cited on behalf of the Appellant, to take as a basis of their award a fair royalty as between a willing licensor and a willing licensee, and I have little doubt that that basis was accepted in the present case, subject, no doubt, to certain deductions. Lastly, the patent itself, that is the corpus of the patent, was not taken away from the Appellant and his partner but still remains in them. In view of all the facts I am satisfied that the sum awarded is to be treated as profits or gains, and annual profits or gains, within the meaning of the Income Tax Act.

Secondly, it is said that, assuming tax was payable on the amount, it was not right to deduct the tax under Rule 21 of the General Rules applicable to all the Schedules of the Act, because it was not a royalty or other sum payable for the use of a patented invention. But again I do not agree. It is true that the validity of the patent was not originally admitted by the Crown; but no evidence was led for the purpose of attacking it, and we were told at the Bar that the Royal Commission held it to be a good patent. I think, therefore, that the money was paid for the use of a patented invention.

Thirdly, it is said that Rule 21, which gives the power to deduct, only applies to a subject of the Crown and not to the Crown itself, and that the duty of the Crown was to pay the amount of the award in full and then to assess the Appellant to Income Tax in respect of the amount. My Lords, I am bound to say that in my view that point is not open to the Appellant in this appeal. The point was not taken in the correspondence before the Petition of Right, and indeed there are expressions in the correspondence which go to show that the only point taken on behalf of the Appellant was that no tax was payable on the amount of the award, and he nowhere claimed that the tax, if payable, was not deductible. Again, the point was not taken in the Petition of Right which received the fiat of the Attorney-General. The point taken in that Petition of Right was that £70,000 was a capital sum and not an annual payment or annual profits and gains, and that Income Tax was not payable in respect of it. That point was plainly taken, but nowhere was it suggested in the Petition of Right that the tax, if payable, was not deductible. When the Attorney-General in his answer to the Petition referred to Rule 21 of the General Rules, the Appellant allowed issue to be joined upon the facts without even then raising the point that Rule 21 did not apply to the Crown. A passage has been read from the shorthand

(Viscount Cave, L.C.)

notes with a view to showing that the point was raised before Mr. Justice Rowlatt. Having heard that passage read, I do not think that it raised with any clarity the contention which is now put forward, and accordingly Mr. Justice Rowlatt in no way dealt with the point. There is, indeed, in the judgment of the learned Master of the Rolls upon the appeal, a passage referring to Rule 21; but, so far as I can follow that passage, it appears to show that the contention now put forward was not raised or, at all events, not plainly raised before the Court of Appeal. It was raised, and in my view raised for the first time, in the Appellant's case on this appeal. In these circumstances, it appears to me that the point is taken too late and that the Appellant, who might have raised it earlier and obtained the decisions of the two Courts below upon the point, ought not to be allowed to raise it now. If your Lordships were disposed to allow any latitude in this respect—as in some cases has been done—I doubt whether you would be willing to do so in the present case, because the effect of the point now raised, if it were successful, would be that the amount in dispute must be paid to the Appellant and that, as the time for assessment has gone by, the Crown would have no remedy open to it by which to recover Income Tax, which in my view was plainly payable. Accordingly, I think it best to express no opinion upon the construction of Rule 21, but to say simply that this point is raised too late and, therefore, cannot be effective.

My Lords, for these reasons I think this appeal fails and I move your Lordships that it be dismissed with costs.

Viscount Dunedin.—My Lords, I concur. I think, on the real merits of the case, the case was scarcely arguable. This was a patent which remains this man's property. He, in the old days, got royalties for it, and those were the profits of his property. He had taken, by the Crown, the same licence of user as private persons had before, and to say that the payments which the Crown make lose their character as income and suddenly become capital is, I think, as all the Courts have understood the case, one of the most hopeless contentions I have ever heard urged at your Lordships' Bar.

As regards the other point, I hesitate to give opinions upon mere procedure points of English practice, but I do think it would be very unfortunate in a case like this if we were bound to consider now for the first time a point that was studiously—I do not mean intentionally—kept in the background by not being mentioned. There is not a trace of the point in the judgments of either Mr. Justice Rowlatt or the Court of Appeal.

Lord Atkinson.—My Lords, I concur. It appears to me clear that the sum this man was to receive for the use of his patent is not a capital sum but is a yearly sum.

(Lord Atkinson.)

With regard to the second point, I think it is a point of importance, and that makes it all the more necessary that it should be distinctly raised so as to give the opponent clear notice of the things he was intended to meet, and that we should have the advantage of having it dealt with by the different Judges in the Courts below. In this case I do not think it was raised, whether by omission or from some other cause, and for that reason I think, according to the wise and prudent practice, it should not be held to be open, and it is not open.

Lord Shaw of Dunfermline.—My Lords, I concur entirely in the opinion delivered from the Woolsack.

Lord Carson.—My Lords, upon the first and main point which has been argued I am of opinion that the sums of £70,000 and £15,000 awarded to the Plaintiff are to be treated as income arising from the user of the Plaintiff's patent by the Crown.

I desire, however, to say that, speaking for myself, I think the point as to whether Rule 21 entitled the Crown without assessment to deduct the Income Tax payable was sufficiently raised by the pleadings. The Appellant sued upon the award, and the Respondents justify the deduction under Rule 21 as entitling them to make such deduction, and upon that issue was joined, which was, I think, the usual course of pleading. However, as your Lordships are of opinion that the point is not open to the Appellant, having regard to the state of the pleadings and the absence of argument before Mr. Justice Rowlatt and the Court of Appeal, it becomes unnecessary to discuss the question whether the right of deduction imposed by Rule 21 applies to the Crown.

Questions put:—

That the Order appealed from be reversed.

The Not Contents have it.

That the Order appealed from be affirmed and this Appeal dismissed with Costs.

The Contents have it.