HIGH COURT OF JUSTICE (CHANCERY DIVISION)—
30TH MAY, AND 7TH AND 8TH JUNE, 1962

COURT OF APPEAL—1ST, 4TH AND 22ND FEBRUARY, 1963

HOUSE OF LORDS—10TH, 11TH AND 12TH MARCH, AND 5TH MAY, 1964

Binns, Ltd.

v.

Commissioners of Inland Revenue

Profits Tax—Gross relevant distributions—Principal and subsidiary companies—Grouping notice followed by division of subsidiary's accounting period into two chargeable accounting periods by reference to date of entry into group—Dividend declared for second period—Whether apportionable over whole accounting period—Whether retrospective division valid—Finance Act, 1937 (1 *Edw.* VIII & 1 *Geo.* VI, *c.* 54), *Section* 22 ; *Finance Act,* 1947 (10 & 11 *Geo.* VI, *c.* 35), *Sections* 35(1), 37 *and* 38.

The Appellant Company made up its accounts annually to 26*th January F Ltd. acquired the whole of the Company's issued ordinary share capital on* 28*th April,* 1953. *On* 27*th January,* 1954, *the Company declared and paid an interim dividend on its ordinary shares for the period* 28*th April,* 1953, *to* 26*th January,* 1954. *On* 6*th January,* 1954, *F Ltd. gave a grouping notice under Section* 22, *Finance Act,* 1937, *commencing with the chargeable accounting period ended* 26*th January,* 1954. *On* 28*th October,* 1958, *the Commissioners of Inland Revenue directed under Section* 38(4), *Finance Act,* 1947, *that the period of twelve months ended* 26*th January,* 1954, *should be divided into two chargeable accounting periods ended respectively* 27*th April,* 1953, *and* 26*th January,* 1954.

The Company was assessed to Profits Tax for the first of these chargeable accounting periods on the footing that the gross relevant distributions included the appropriate proportion, on a time basis, of the above-mentioned dividend. On appeal, the Company contended that this dividend should be ignored since it was paid to the principal company in respect of a period for which a grouping notice was in force.

The Special Commissioners determined the appeal in accordance with the Crown's contention.

In the Court of Appeal it was further contended by the Company that Section 38(4) *gave no power to alter retrospectively a chargeable accounting period which already existed.*

Held, *that the Commissioners' decision was correct.*

CASE

Stated under the Finance Act, 1937, Fifth Schedule, Part II, Paragraph 4, and 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 15th March, 1960, and 7th February, 1961, Binns, Ltd. (hereinafter called " the Company "), appealed against an assessment to

Profits Tax for the chargeable accounting period from 27th January, 1953, to 27th April, 1953, in the sum of £24,398 10*s.* 6*d.* (tax). The questions for our determination were, in computing the Company's Profits Tax liability for the said chargeable accounting period:

(i) whether the ordinary dividend paid by the Company (in the circumstances hereinafter appearing) in respect of the period from 28th April, 1953, to 26th January, 1954, should be ignored; and

(ii) which of the preference and preferred ordinary dividends hereinafter referred to, and how much thereof, should be taken into account.

2. The following documents were produced and admitted or proved:

(i) directors' report and accounts of the Company for the year ended 26th January, 1954;

(ii) direction by the Commissioners of Inland Revenue under Section 38(4), Finance Act, 1947, dated 28th October, 1958;

(iii) the computation by the Commissioners of Inland Revenue of the Company's Profits Tax liability for the chargeable accounting period from 27th January, 1953, to 27th April, 1953;

(iv) the Company's computation of its liability to Profits Tax for the said chargeable accounting period.

Copies of these documents are annexed hereto, marked "A", "B", "C" and "D" respectively, and form part of this Case[1].

3. The following facts were agreed by the parties:

(i) The Company carried on the trade or business of drapers, furnishers, etc., in Sunderland and elsewhere.

(ii) The accounts of the Company's trade were made up for successive periods of twelve months ending on 26th January up to and including 26th January, 1954 (Exhibit "A").

(iii) The Company became a subsidiary of House of Fraser, Ltd. (hereinafter called "the principal company"), as from 28th April, 1953; and from that date the principal company owned the whole issued ordinary share capital of the Company, other than employees' preferred ordinary shares.

(iv) Notice under Section 22, Finance Act, 1937, was given on 6th January, 1954, by the principal company in regard to the chargeable accounting period ended on 26th January, 1954, requiring that the provisions of Section 22(2), Finance Act, 1937, should apply to its subsidiary (i.e., the Company) as respects that period. This notice was effective as from 28th April, 1953.

(v) The above-mentioned ordinary dividend (see paragraph 1(i) above) amounted to £320,000 (£176,000 net, see Exhibit "A"), and was paid by the Company to the principal company on 27th January, 1954, in respect of the period from 28th April, 1953, to 26th January, 1954. It was expressly declared an interim dividend on ordinary shares for the period from 28th April, 1953, to 26th January, 1954. No dividend was paid for any part of the year ending 26th January, 1954, on employees' preferred ordinary shares.

[1] Not included in the present print.

(vi) The following preference and preferred ordinary dividends were paid by the Company.

	Gross £	s.	d.
Half-year ended 1st April, 1953			
(*a*) 6 per cent. cumulative preference shares of £1 each (free of Income Tax up to 6*s.* in the £)	26,571	7	10
(*b*) 7½ per cent. cumulative preference shares of £1 each	7,500	0	0
(*c*) 10 per cent. cumulative preferred ordinary shares of £1 each	10,000	0	0
	44,071	7	10

Similar dividends on the said three classes of preference and preferred shares were paid by the Company for the half-years ended 1st October, 1953, and 1st April, 1954. The principal company received the following dividends from the Company on its holdings of the said classes of shares.

	Gross £	s.	d.
Half-year ended 1st October 1953			
6 per cent. preference	331	9	11
7½ per cent. preference	18	15	0
10 per cent. preferred ordinary	16	13	0
	366	17	11
Half-year ended 1st April, 1954			
6 per cent. preference	563	3	6
7½ per cent. preference	64	13	9
10 per cent. preferred ordinary	65	10	0
	693	7	3

(vii) By virtue of the provisions of Section 38(4), Finance Act, 1947, the Commissioners of Inland Revenue directed that the period of twelve months from 27th January, 1953, to 26th January, 1954, should not be a chargeable accounting period, but that the periods of $3^{1}/_{30}$ months from 27th January, 1953, to 27th April, 1953, and $8\frac{29}{30}$ months from 28th April, 1953, to 26th January, 1954, should be chargeable accounting periods for the purpose of Profits Tax (Exhibit "B").

(viii) The profits of the Company as adjusted for the purpose of Profits Tax for the accounting period (i.e., the year ended 26th January, 1954), were £575,743; and the proportion of these profits for the chargeable accounting period from 27th January, 1953, to 27th April, 1953 (i.e., $3^{1}/_{30}$ months), was £145,535.

(ix) The computation by the Commissioners of Inland Revenue of the Company's Profits Tax liability (Exhibit "C") shows that, in computing the gross and net relevant distributions to proprietors for the chargeable accounting period in question (namely, $3^{1}/_{30}$ months from 27th January, 1953, to 27th April, 1953), a proportion $\left(\text{i.e.}\ \frac{3^{1}/_{30}}{12}\right)$ of the ordinary dividend of £320,000 and of the preference and preferred ordinary dividends for the year ended 1st October, 1953 (referred to in sub-paragraph (vi) hereof) was taken into account.

(x) The computation by the Company of its Profits Tax liability (Exhibit " D ") shows that, in calculating the gross relevant distributions, the ordinary dividend of £320,000 has been included and then wholly deducted and the preference and preferred ordinary dividends for the half-year ended 1st April, 1953, have not been included. The preference and preferred ordinary dividends paid for the half-years ended 1st October, 1953, and 1st April, 1954, have, however, been included in the computation; but such dividends paid to the principal company on or after 28th April, 1953, the date on which the notice under Section 22, Finance Act, 1937, became effective, have been deducted.

4. It was contended on behalf of the Company:

(i) that as the notice given by the principal company under Section 22 of the Finance Act, 1937, became effective as from 28th April, 1953, and as the said ordinary dividend of £320,000 was declared for the period 28th April, 1953, to 26th January, 1954, and was paid on 27th January, 1954, to the principal company, which was throughout the relevant period the proprietor of the whole share capital on which the said dividend was declared, the said dividend should be ignored in computing the gross relevant distributions to proprietors for the purpose of arriving at the Company's Profits Tax liability;

(ii) that the preference and preferred ordinary dividends referable to the accounting period to 26th January, 1954, are those for the half-years ended 1st October, 1953, and 1st April, 1954, respectively, and that such part thereof as was paid to the principal company should be similarly ignored in computing the Company's Profits Tax liability;

(iii) that the provisions of Section 37, Finance Act, 1947, could not be applied to the circumstances of the present case;

(iv) that the appeal should succeed.

5. It was contended on behalf of the Crown:

(i) that the said ordinary dividend of £320,000 and the said preference and preferred ordinary dividends were gross relevant distributions to proprietors within Section 35, Finance Act, 1947, for the purpose of computing the Company's liability to Profits Tax;

(ii) that Section 35, Finance Act, 1947, fell to be construed in the light of the provisions of Section 37 of the Act;

(iii) that, as the chargeable accounting period in question was not a period for which the accounts of the Company's trade had been made up, the provisions of Section 37, Finance Act, 1947, are applicable;

(iv) that the provisions of the said Section 37 are mandatory, and accordingly the gross relevant distributions to proprietors must be computed in relation to the Company's accounting period (i.e., the year ended 26th January, 1954) and apportioned on a time basis over the two chargeable accounting periods comprised in that period (namely, (*a*) from 27th January, 1953, to 27th April, 1953, and (*b*) from 28th April, 1953, to 26th January, 1954), as shown in the computation of the Commissioners of Inland Revenue (Exhibit " C ");

(v) that, in considering the provisions of Section 37, the fact that the ordinary dividend referred to in paragraph 3 (v) above was paid

in respect of a period which coincided with the chargeable accounting period from 28th April, 1953, to 26th January, 1954, is immaterial;

(vi) that the appeal should fail.

6. We, the Commissioners, who heard the appeal, gave our decision in writing as follows:

The question for our determination is whether the dividend of £320,000 gross paid on 27th January, 1954, in respect of the period from 28th April, 1953, to 26th January, 1954, should be left wholly out of account in calculating the Company's Profits Tax liability.

The Company contended that by reason of the notice given by the principal company under Section 22, Finance Act, 1937, the whole of the said dividend, having been paid to the principal company, should be ignored for purposes of Profits Tax.

The Crown, on the other hand, contended that by reason of the provisions of Section 37, Finance Act, 1947, the said dividend must be apportioned on a time basis for the two chargeable accounting periods (*a*) from 27th January, 1953, to 27th April, 1953, and (*b*) from 28th April, 1953, to 26th January, 1954.

Having carefully considered the facts and the arguments addressed to us, we are of opinion that the Crown are right in this case. It appears to us that where a chargeable accounting period is not a period for which a company's accounts have been made up, the provisions of Section 37 are mandatory as regards dividends. In this case there are two chargeable accounting periods which, when added together, cover the period of twelve months for which the Company's accounts have been made up; and we hold that, in computing the gross relevant distributions to proprietors, Section 37 requires an apportionment on a time basis of the dividend paid on 27th January, 1954, in order to arrive at the gross relevant distributions to proprietors for the two chargeable accounting periods comprised in the Company's accounting period of twelve months. Section 37 contains no reference to the period in respect of which the dividend is paid, and we hold that the fact that the dividend in the present case was paid in respect of a period which coincides with chargeable accounting period (*b*) is immaterial in considering the mandatory provisions of Section 37.

The appeal therefore fails. We leave the figures to be agreed.

As the parties were unable to agree the figures, a second meeting of the Commissioners was held on 7th February, 1961. At that second meeting the Company was not represented by Counsel. Mr. J. E. Porter, of the taxation department of House of Fraser, Ltd., attended on behalf of the Company, and we were asked to decide the following two matters:

(i) which of the preference and preferred ordinary dividends above referred to were to be treated as the gross relevant distributions for the accounting period to 26th January, 1954; and

(ii) whether such part of the said dividends as was paid to the principal company should be ignored in arriving at such gross relevant distributions.

We, the Commissioners, gave our decision as follows:

In our view, the principle of our decision relating to the ordinary dividend applies also to the preference and preferred ordinary dividends in the manner contended for by the Crown (Exhibit "C").

The appeal failed and we determined the assessment in the sum of £24,269 8*s.* 6*d.* (tax).

7. The Company immediately after the determination of the appeal declared to us its dissatisfaction therewith as being erroneous in point of law, and in due course required us to state a Case for the opinion of the High Court pursuant to the Finance Act, 1937, Fifth Schedule, Part II, Paragraph 4, and the Income Tax Act, 1952, Section 64, which Case we have stated and do sign accordingly.

8. The question for the opinion of the High Court is whether, on the facts hereinbefore set out and on a proper construction of Sections 35 and 37, Finance Act, 1947, our determination of the appeal was correct in law.

N. S. Spendlow
F. Gilbert
} Commissioners for the Special Purposes of the Income Tax Acts.

Turnstile House,
94–99 High Holborn,
London, W.C.1.

31st January, 1962.

The case came before Pennycuick, J., in the Chancery Division, on 30th May, and 7th and 8th June, 1962, when judgment was given in favour of the Crown, with costs.

Mr. F. N. Bucher, Q.C., and Mr. R. Buchanan-Dunlop appeared as Counsel for the Company, and Mr. Hilary Magnus, Q.C., and Mr. Alan Orr for the Crown.

Pennycuick, J.—This is an appeal by Binns, Ltd. (to which Company I will refer as "Binns"), from a decision of the Special Commissioners dismissing Binns's appeal against an assessment to Profits Tax for the chargeable accounting period from 27th January, 1953, to 27th April, 1953. The question is whether, in the computation of Binns's profits for that period, there should be taken into account a dividend paid by Binns on its ordinary shares in respect of the period from 28th April, 1953, to 26th January, 1954. The appeal raised a further question as to dividends paid by Binns on its preference and preferred ordinary shares, but the appeal on this point has been abandoned.

Until 28th April, 1953, Binns carried on the trade of drapers as an independent concern. Its issued capital comprised preference, preferred ordinary and ordinary shares. Its year of account ran from 27th January in each year to 26th January in the next year. On 28th April, 1953, Binns became a subsidiary of House of Fraser, Ltd. (to which company I will refer as "House of Fraser"), which acquired the whole of its ordinary shares. On 6th January, 1954, House of Fraser gave a grouping notice pursuant to Section 22 of the Finance Act, 1937, requiring that the provisions of that Section should apply to Binns in regard to the chargeable accounting period ending on 31st January, 1954, and all subsequent chargeable accounting periods. No explanation has been given as to why 31st January is specified in this notice instead of 26th January; and, for the purpose of argument,

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Mr. Magnus, who appeared for the Crown, has very sensibly accepted that the notice should be read as if it specified the date 26th January. On 27th January, 1954, Binns paid to House of Fraser a dividend of £320,000 gross on its ordinary shares, this dividend being declared as an interim dividend in respect of the period from 28th April, 1953, to 26th January, 1954, i.e., that part of the year of account from 27th January, 1953, to 26th January, 1954, during which Binns was a subsidiary of House of Fraser. On 28th October, 1958, the Commissioners of Inland Revenue gave a direction pursuant to Section 38 of the Finance Act, 1947, to the effect that the period of account of the twelve months from 27th January, 1953, to 26th January, 1954, should not be a chargeable accounting period of Binns, but that the periods of 3 and 1/30th months from 27th January, 1953, to 27th April, 1953, and of 8 and 29/30ths months from 28th April, 1953, to 26th January, 1954, should be chargeable accounting periods for the purpose of Profits Tax.

Binns claimed that in these circumstances no part of the dividend of £320,000 should be brought into account in respect of the former of the two last-mentioned chargeable accounting periods; i.e., that from 27th January to 27th April, 1953. The Crown claimed that a rateable part of the dividend, namely, 3 and 1/30th over 12, should be so brought into account. Binns's contention, as set out in the Case Stated, was as follows:

> " that as the notice given by the principal company "

—that is, House of Fraser—

> " under Section 22 of the Finance Act, 1937, became effective as from 28th April, 1953, and as the said ordinary dividend of £320,000 was declared for the period 28th April, 1953, to 26th January, 1954, and was paid on 27th January, 1954, to the principal company, which was throughout the relevant period the proprietor of the whole share capital on which the said dividend was declared, the said dividend should be ignored in computing the gross relevant distributions to proprietors for the purpose of arriving at the Company's Profits Tax liability ".

The contentions of the Crown were as follows:

> " (i) that the said ordinary dividend of £320,000 was a gross relevant distribution to proprietors within Section 35, Finance Act, 1947, for the purpose of computing the Company's liability to Profits Tax; (ii) that Section 35, Finance Act, 1947, fell to be construed in the light of the provisions of Section 37 of the Act; (iii) that, as the chargeable accounting period in question was not a period for which the accounts of the Company's trade had been made up, the provisions of Section 37, Finance Act, 1947, are applicable; (iv) that the provisions of the said Section 37 are mandatory, and accordingly the gross relevant distribution to proprietors must be computed in relation to the Company's accounting period (i.e., the year ended 26th January, 1954) and apportioned on a time basis over the two chargeable accounting periods comprised in that period (namely, (*a*) from 27th January, 1953, to 27th April, 1953, and (*b*) from 28th April, 1953, to 26th January, 1954), as shown in the computation of the Commissioners of Inland Revenue . . .; (v) that, in considering the provisions of Section 37, the fact that the ordinary dividend referred to in paragraph 3 (v) above was paid in respect of a period which coincided with the chargeable accounting period from 28th April, 1953, to 26th January, 1954, is immaterial ".

The Commissioners gave their decision in writing. After setting out the question for determination and the contentions of the respective parties, they proceeded as follows:

> " Having carefully considered the facts and the arguments addressed to us, we are of opinion that the Crown are right in this case. It appears to us that where a chargeable accounting period is not a period for which a company's accounts have been made up, the provisions of Section 37 are mandatory as regards dividends. In this case there are two chargeable accounting periods which, when added together, cover the period of twelve months for which the

Company's accounts have been made up; and we hold that, in computing the gross relevant distribution to proprietors, Section 37 requires an apportionment on a time basis of the dividend paid on 27th January, 1954, in order to arrive at the gross relevant distribution to proprietors for the two chargeable accounting periods comprised in the Company's accounting period of twelve months. Section 37 contains no reference to the period in respect of which the dividend is paid, and we hold that the fact that the dividend in the present case was paid in respect of a period which coincides with chargeable accounting period (*b*) is immaterial in considering the mandatory provisions of Section 37. The appeal therefore fails."

The significance of the question lies in the provisions relating to non-distribution relief. The same question as that raised by the present appeal was considered by Plowman, J., in the case of *T.S.S. Investments, Ltd.* v. *Commissioners of Inland Revenue*[1], 40 A.T.C. 334, where the facts were, in all relevant respects but one, similar to those here. The headnote of the case reads as follows:

"The first appellant sold its shipping business as at March 8th, 1955, but continued to carry on a trade or business within Section 19 of the Finance Act, 1937. On March 15th, 1955, it became a wholly-owned subsidiary of another company. On March 16th, 1955, it paid two dividends to its principal company. Neither dividend was expressed as payable in respect of any particular accounting period. On the same day the principal company gave a grouping notice under Section 22(1) of the Finance Act, 1937, in respect of the chargeable accounting period ending on March 31st, 1955. The company's accounts had been made up for the twelve months ended on March 31st in each year. On May 12th, 1959, the Inland Revenue made a direction, under Section 38(4) of the Finance Act, 1947, that the periods from April 1st, 1954, to March 7th, 1955, from March 8th, 1955, to March 14th, 1955, and from March 15th, 1955, to March 31st, 1955, should be chargeable accounting periods. It was contended on behalf of the appellant company that the two dividends had to be regarded under Section 35(1)(*b*) of the Finance Act, 1947, as gross relevant distributions for the chargeable accounting period in which they were made, that is to say, the period from March 15th, 1955, to March 31st, 1955. It was contended on behalf of the respondent that Section 37 of the same Act required that the dividends should be apportioned among the three chargeable accounting periods constituted by the Inland Revenue's direction. The Special Commissioners decided in favour of the respondents. *Held:* that the Special Commissioners' decision was correct."

The learned Judge in that case made a thorough review of the provisions contained in Part III of the Finance Act, 1937, "Charge of national defence contribution" (the name of the tax was subsequently changed to Profits Tax), and in Part IV of the Finance Act, 1947, "The Profits Tax. Principal changes of the law"; and he came to the conclusion that the dividend declared by the company fell to be apportioned over the whole period of account which included the several chargeable accounting periods—in that case, three—into which it was divided by the direction of the Commissioners. I propose to apply that decision here, unless it can be distinguished; and it would serve no useful purpose for me to go again over the ground which has been fully and carefully surveyed by Plowman, J.

The one significant respect in which the facts here are different from the facts in *T.S.S. Investments* is that here the dividend was declared in respect of the period 28th April, 1953, to 26th January, 1954, whereas in that case the dividend was paid in the last of the three chargeable accounting periods but was not expressed to be payable in respect of any particular period. For the present purpose this difference is, in my judgment, irrelevant. In *T.S.S. Investments* the dividend fell under Section 35(1)(*b*) of the Finance Act, 1947, and, under that paragraph, represented a distribution for the

(1) 40 T.C. 85.

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chargeable accounting period in which it was paid, i.e., the third of the three chargeable accounting periods created by the direction. Here, the dividend falls under Section 35(1)(*a*) and represents a distribution for the chargeable accounting period in respect of which it was declared, i.e., the second of the two chargeable accounting periods created by the direction. So in each case the dividend was, apart from subsequent provisions in the 1947 Act, a distribution for the broken period after the company became a subsidiary. In *T.S.S. Investments*[1], Plowman, J., applying the provisions of Section 37 of the 1947 Act, held that the dividend must be apportioned on a time basis over the whole year of account comprising the three chargeable accounting periods created by the direction. It seems to me that the same reasoning is applicable here, and that the dividend must be apportioned on a time basis over the whole year of account comprising the two chargeable accounting periods created by the direction.

Mr. Bucher, and also Mr. Buchanan-Dunlop, raised a further contention which was open to, but was not taken by, the appellant company in the *T.S.S. Investments* case. This contention is based on Section 38 of the Finance Act, 1947. Sub-section (1) of that Section reads as follows:

> "Where a notice under subsection (1) of section twenty-two of the Finance Act, 1937 (which relates to subsidiary companies) is in force—(*a*) the franked investment income, and the gross relevant distributions, of the subsidiary to which the notice relates for any chargeable accounting period shall for all purposes be included in the franked investment income and the gross relevant distributions of the principal company for the corresponding chargeable accounting period of that company; but (*b*) no franked investment income received by the principal company directly from that subsidiary, or received by the subsidiary directly from the principal company or directly from any other subsidiary of the principal company with respect to which such a notice is in force given by that company, and no distributions made by the principal company to the subsidiary, or by the subsidiary to the principal company or to any such other subsidiary of the principal company as aforesaid, shall be so included."

So it is contended that this Sub-section categorically prohibits the inclusion in the gross relevant distributions of a subsidiary company of distributions made to the principal company by the subsidiary company. In other words, there is nothing left to apportion.

It do not think this contention is well founded. By virtue of Section 37, the dividend paid by Binns in the present case is apportioned between the chargeable accounting periods 27th January, 1953, to 27th April, 1953, and 28th April, 1953, to 26th January, 1954, respectively. Only that part of the dividend which is apportioned to the later chargeable accounting period can be regarded as a distribution made where a grouping notice under Section 22 of the Finance Act, 1937, is in force; and, equally, only that part of the distribution can be regarded as paid by Binns in the capacity of subsidiary company to House of Fraser in the capacity of principal company. That part of the distribution which is apportioned to the earlier chargeable accounting period must be regarded as made where the grouping notice was not in force and where the relation of subsidiary company and principal company did not exist. It is, I think, impossible to step at this point in the Act, as Mr. Bucher invites me to do, from the fictional in Section 37 to the factual in Section 38 and to disregard for the purpose of Section 38 the apportionment of distributions required to be made under Section 37. It will be observed that the adverb with which Section 37 begins is not the purely temporal "when" but the more general "where", which

(1) 40 T.C. 85.

may be paraphrased as meaning " in the circumstances in which ". Mr. Bucher has stressed the fact that Section 38 is not expressed to be subject to the preceding Sections, but it seems to me that such words would be superfluous.

In the course of his reply, Mr. Bucher raised another contention of far-reaching importance, which was not raised in the *T.S.S. Investments* case[1] or before the Commissioners in the present case. The contention is based on Section 22 of the Finance Act, 1937, and Section 30 of the Finance Act, 1956. Section 22 (1) reads as follows[2]:

> " Where a body corporate resident in the United Kingdom is a subsidiary of another body corporate so resident (hereafter in this section referred to as ' the principal company ') the principal company may, by notice in writing given to the Commissioners of Inland Revenue before the expiration of any chargeable accounting period of the subsidiary or within six months from the end of that period or such longer time as the Commissioners of Inland Revenue may in any case allow, require that the provisions of subsection (2) of this section shall apply to the subsidiary as respects that period and all subsequent chargeable accounting periods throughout which it continues to be a subsidiary of the principal company ".

I need not read Sub-section (2). The contention is that, by virtue of Section 22 (1), a principal company, on becoming such, may give notice applicable to any chargeable accounting period—including a period ending immediately or at an interval—before the relation of principal and subsidiary companies came into existence, so long only as the notice is given within six months after the end of the period to which it is expressed to relate. This is perhaps the more literal construction of the words in the Sub-section, which cannot be construed in the light of the subsequent 1947 Act. This construction seems contrary to the apparent purpose of the Section, and, here again, Mr. Magnus for the Crown relies upon the non-temporal adverb " where ". It is unnecessary for me to decide this question of construction here for the short reason that the grouping notice given by House of Fraser is expressed to refer to the chargeable accounting period ended in January, 1954, which, by virtue of the direction under Section 38, only began on 28th April, 1953. It is, I think, impossible to treat this notice as referable to both the chargeable accounting periods into which Binns's year of account was subsequently divided by the direction.

So far as I can see, if the more literal construction of Section 22 is correct, it follows that in every case where, as here, a grouping notice is given in such terms that if the subsidiary company's chargeable accounting period had continued to correspond to its year of account the notice would have covered a period before the relation of principal and subsidiary company came into existence, the Revenue could defeat the taxpayer and effectuate the apparent purpose of the Section by a subsequent direction under Section 38. By the time the direction was given, it would be too late for a further grouping notice to be given except with the consent of the Revenue.

It was, I imagine, with a view to clearing up this confused and rather unattractive position that Section 30 of the Finance Act, 1956, was passed. Section 30 of the Act, so far as material, reads as follows:

> " (1) A grouping notice may not be given by a principal company as respects a subsidiary of it unless each of them is engaged in carrying on a trade or business, or each of them was so engaged at the beginning of the chargeable accounting period specified in the notice as the first of the periods as respects

(1) 40 T.C. 85. (2) As amended by Section 42 (4), Finance Act, 1938.

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> which the notice is to have effect; nor shall a grouping notice validly given by a principal company as respects a subsidiary of it continue in force after either of them has ceased to be so engaged or to be resident in the United Kingdom (but so that its lapsing shall not revive any previous notice which had ceased to be in force by reason of the giving thereof)."

Sub-section (2), which is the Sub-section directly in point, says:

> "The chargeable accounting period specified in a grouping notice as the first of the periods as respects which the notice is to have effect may not be a period ending before the date on which the principal company became entitled to give the notice; and if, when a grouping notice has been given, the Commissioners of Inland Revenue, under subsection (4) of section thirty-eight of the Finance Act, 1947, divide the period so specified therein, the notice shall have effect as if for the period so specified there were substituted the first of the periods into which it is divided which ends on or after that date."

Sub-section (8) says:

> "Subsections (1) and (2) of this section shall be deemed to have had effect as from the eighteenth day of April, nineteen hundred and fifty-six".

The provisions in Section 30 (2) appear to be a statement as to how the law is to stand as from 18th April, 1956, in regard to the matters stated in the Sub-section, and are no doubt designed to clear up the confusion existing under the law as it stood. I do not think it would be possible to derive from Section 30 an inference that the law must have been different in every or any particular respect before 18th April, 1956, but again I need not decide this question, since, even upon the more literal construction of Section 22, the grouping notice would not apply to the chargeable accounting period ended 27th April, 1953, as created by the direction under Section 38 of the 1947 Act.

I must, therefore, dismiss the present appeal.

Mr. Alan Orr.—My Lord, I ask that the appeal be dismissed with costs.

Pennycuick, J.—I think that must follow, Mr. Bucher?

Mr. F. N. Bucher.—Yes, my Lord.

The Company having appealed against the above decision, the case came before the Court of Appeal (Willmer, Danckwerts and Diplock, L.JJ.) on 1st and 4th February, 1963, when judgment was reserved. On 22nd February, 1963, judgment was given unanimously against the Crown, with costs.

Mr. F. N. Bucher, Q.C., and Mr. R. Buchanan-Dunlop appeared as Counsel for the Company, and Mr. Hilary Magnus, Q.C., and Mr. Alan Orr for the Crown.

Willmer, L.J.—This appeal arises out of a dispute with regard to the computation of Profits Tax due from Binns, Ltd., in relation to a short period immediately before that Company became a subsidiary of House of Fraser, Ltd. Before the Special Commissioners the issue was resolved in favour of the Crown, and by his judgment of 8th June, 1962, Pennycuick, J., upheld the decision of the Special Commissioners. Binns, Ltd., now appeals to this Court.

(Willmer, L.J.)

Binns, Ltd., carried on business as proprietor of departmental stores at various centres in the north of England and Scotland. The issued capital of the Company amounted to £1,200,198 divided as follows:

	£
6 per cent. cumulative preference shares of £1 each	620,000
7½ per cent. cumulative preference shares of £1 each	200,000
10 per cent. cumulative preferred ordinary shares of £1 each	200,000
Ordinary shares of £1 each	160,000
Employees' preferred ordinary shares of £1 each	20,198
	1,200,198

The Company's year of account ran from 27th January in each year to 26th January in the following year. On 28th April, 1953, House of Fraser, Ltd., acquired the whole of the ordinary shares of Binns, Ltd. It is, however, relevant to observe that House of Fraser, Ltd., did not, during any relevant period, hold more than a small proportion of the preference or preferred ordinary shares.

On 6th January, 1954, House of Fraser, Ltd., gave to the Commissioners of Inland Revenue a grouping notice under Section 22 (1) of the Finance Act, 1937, requiring that the provisions of Section 22 (2) of that Act should apply to Binns, Ltd., in regard to the chargeable accounting period ending on 31st January, 1954, and all subsequent chargeable accounting periods. It has been accepted that the date 31st January, 1954, is a mistake for 26th January, 1954. It is admitted that the notice was a valid notice, but it is contended by the Crown that it only became effective from 28th April, 1953, i.e., the date when Binns, Ltd., became a subsidiary of House of Fraser, Ltd. Pursuant to Section 22 (2) of the 1937 Act, the effect of the notice was that profits or losses of Binns, Ltd., arising in the chargeable accounting period to which the notice related were to be treated for the purposes of Profits Tax as if they were profits or losses arising in the corresponding chargeable accounting period of House of Fraser, Ltd.

On 27th January, 1954, Binns, Ltd., declared a dividend on its ordinary shares, such dividend being expressed to be an interim dividend in respect of the period 28th April, 1953, to 26th January, 1954. The whole of this dividend was, of course, payable to House of Fraser, Ltd., which at that time held all the ordinary shares in Binns, Ltd. Dividends were also paid on the preference shares and preferred ordinary shares on 1st April, 1953, 1st October, 1953, and 1st April, 1954, but only a small proportion of these dividends went to House of Fraser, Ltd.

A considerable time later, namely, on 28th October, 1958, the Commissioners of Inland Revenue gave a direction under Section 38 (4) of the Finance Act, 1947, to the effect

> "that the period of twelve months from the 27th January, 1953, to the 26th January, 1954, shall not be a chargeable accounting period but that the periods of 3 1/30 months from the 27th January, 1953, to the 27th April, 1953, and of 8 29/30 months from the 28th April, 1953, to the 26th January, 1954, shall be chargeable accounting periods for the purpose of Profits Tax."

The question at issue on this appeal relates to the liability of Binns, Ltd., to Profits Tax in respect of the earlier of those two periods, i.e., the period before it became a subsidiary of House of Fraser, Ltd. Binns, Ltd., contends that no part of the dividend on the ordinary shares subsequently paid to House of Fraser, Ltd., should be brought into account in relation to this earlier

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period. The Crown, on the other hand, contend that a proportionate part of the dividend paid on the ordinary shares should be allocated to this earlier period, so as to result in a net relevant distribution for this period which must be brought into account in computing the liability of Binns, Ltd., to Profits Tax.

In order fully to understand the contentions put forward on either side, it is necessary to refer briefly to the history of legislation relating to Profits Tax. In this connection I cannot do better than quote the very lucid historical survey given by Plowman, J., in the course of delivering his judgment in *T.S.S. Investments, Ltd.* v. *Commissioners of Inland Revenue,* 40 T.C. 85, at pages 91–2. The learned Judge there said:

> " By way of preface, however, I should state very shortly, and I hope accurately, the problem with which the Sections in question set out to deal. This involves, in the first place, a reference to the Finance Act, 1937. The scheme of the Finance Act, 1937, was to charge Profits Tax (or National Defence Contribution, as it was then called) on the profits of a trade or business arising in each successive chargeable accounting period. The chargeable accounting period for the purposes of Profits Tax might or might not be the same as the accounting period of the trade or business in question, depending on the operation of Section 20 (2) of the Act. In a case in which it was not the same, Section 20 (3) provided as follows:
>
> > 'Where a chargeable accounting period is not a period for which the accounts of the trade or business have been made up, such division and apportionment to specific periods of the profits and losses for any period for which the accounts relating to the trade or business have been made up, and such aggregation of any such profits or losses or any apportioned part thereof, shall be made as appears necessary to arrive at the profits arising in the chargeable accounting period.'
>
> The Finance Act, 1947, introduced a complication by providing for differential rates of Profits Tax for distributed and undistributed profits. A rate of Profits Tax of 25 per cent. was fixed, but profits which were not distributed qualified for non-distribution relief. The result was that, in addition to the existing machinery for ascertaining the profits of a company in a chargeable accounting period, it became necessary to provide machinery for ascertaining what part of such profits were to be regarded as distributed profits, and what part undistributed profits, for that period. The machinery in question was provided by Sections 34 to 37 of the Act of 1947, and it is with Sections 35 and 37 that I am particularly concerned. Section 35 (1) is in these terms:
>
> > 'Subject to the provisions of this and the next two succeeding sections, the gross relevant distributions to proprietors for any chargeable accounting period of a body corporate, society or other body, are the total distributions to the members of the body corporate, society or other body, not being distributions allowable as deductions in computing the profits of the trade or business for any period for the purposes of the profits tax, and being either —(*a*) dividends declared not later than six months after the end of that period which are expressed to be paid in respect of that period or any part thereof; or (*b*) distributions (other than dividends which, under paragraph (*a*) of this subsection, are to be treated as part of the gross relevant distributions to proprietors for any previous chargeable accounting period) made in the period'.
>
> Then the Sub-section goes on, but I do not think that I need read any more of it. Then, Section 37 is in these terms:
>
> > '(1) Where a chargeable accounting period is not a period for which the accounts of the trade or business have been made up, the gross relevant distributions to proprietors shall be computed in relation to the periods for which accounts relating to the trade or business have been made up (being periods falling wholly or partly within the chargeable accounting period) as if those periods were chargeable accounting periods, and such division and apportionment to specific periods of the amounts so computed and such aggregation of any such amounts or of any apportioned parts thereof shall be made as appears necessary to arrive at the gross relevant distributions to proprietors for the chargeable accounting period.

(2) Any apportionment under this section shall be made in proportion to the number of months or fractions of months in the respective periods.'

It will be noted that Section 37 bears a strong resemblance to Section 20 (3) of the Act of 1937, except that it is dealing with the ascertainment of gross relevant distributions to proprietors in a chargeable accounting period, and not with the ascertainments of profits in that period."

The facts in *T.S.S. Investments*[1] were similar to those in the present case except in one important respect. In that case the Commissioners of Inland Revenue had given a direction under Section 38 (4) of the 1947 Act, whereby the year in question was divided into three chargeable accounting periods. During one of these periods dividends had been paid by the subsidiary to the principal company, but such dividends had not been expressed to be paid in respect of any particular period. The dividends thus constituted distributions falling within Section 35 (1) (*b*) of the 1947 Act. In the present case, on the other hand, the dividend paid by Binns, Ltd., on the ordinary shares was expressed to be paid in respect of the period 28th April, 1953, to 26th January, 1954; it was thus a dividend falling within Section 35 (1) (*a*).

In *T.S.S. Investments* Plowman, J., decided that Section 37 of the 1947 Act applied, and that accordingly the dividends had to be computed in relation to the period for which the company's accounts were made up, i.e., as if that were a chargeable accounting period, and then apportioned over the three chargeable accounting periods established as a result of the Commissioners' direction. In the present case, Pennycuick, J., followed the decision in *T.S.S. Investments,* holding that the cases were indistinguishable notwithstanding that in the present case the dividend was expressed to be paid in respect of a particular period which was subsequently established as a chargeable accounting period by the direction of the Commissioners of Inland Revenue. He said[2]:

"In *T.S.S. Investments* the dividend fell under Section 35 (1) (*b*) of the Finance Act, 1947, and, under that paragraph, represented a distribution for the chargeable accounting period in which it was paid, i.e., the third of the three chargeable accounting periods created by the direction. Here the dividend falls under Section 35 (1) (*a*) and represents a distribution for the chargeable accounting period in respect of which it was declared, i.e., the second of the two chargeable accounting periods created by the direction. So in each case the dividend was, apart from subsequent provisions in the 1947 Act, a distribution for the broken period after the company became a subsidiary. In *T.S.S. Investments* Plowman, J., applying the provisions of Section 37 of the 1947 Act, held that the dividend must be apportioned on a time basis over the whole year of account comprising the three chargeable accounting periods created by the direction. It seems to me that the same reasoning is applicable here, and that the dividend must be apportioned on a time basis over the whole year of account comprising the two chargeable accounting periods created by the direction."

For my part, I think there is much to be said for the view that this case is distinguishable from *T.S.S. Investments,* and that there is no room for the operation of Section 37 of the Act of 1947 where, as in the present case, the dividend was expressed to be paid in respect of a particular period which, as the result of the direction given by the Commissioners of Inland Revenue, in fact became a chargeable accounting period. The dividend having actually been paid, and expressed to be paid, in respect of a period which the Commissioners of Inland Revenue themselves actually directed should be a chargeable accounting period, what room, it may be asked, is there for the fictional approach envisaged by Section 37? It is to be noted

(1) 40 T.C. 85. (2) *See* pp. 605-6, *ante.*

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that this Section requires only such apportionment to be made " as appears necessary ". I see much force in the contention that no such necessity arises where the payment of the dividend is expressed to be made in respect of a particular chargeable accounting period. I do not, however, decide the case on this ground, for in my judgment there is a broader ground on which Binns, Ltd., is entitled to succeed on this appeal. As has been already pointed out, the direction creating two chargeable accounting periods in this case was given pursuant to Section 38 (4). But it has been contended on behalf of Binns, Ltd., that Section 38 must be applied as a whole, and that when so applied it is destructive of the Crown's case. Section 38 is one of a group of Sections collected under the heading: " Provisions applicable in special cases." The special case with which Section 38 specifically deals is that of the subsidiary company. In that respect Section 38 of the 1947 Act is linked with Section 22 of the 1937 Act, and it is provided by Sub-section (6) of the former that it is to be construed as one with Section 22 of the earlier Act. Section 38 (1) of the 1947 Act provides as follows:

> " Where a notice under subsection (1) of section twenty-two of the Finance Act, 1937 (which relates to subsidiary companies) is in force—(*a*) the franked investment income, and the gross relevant distributions, of the subsidiary to which the notice relates for any chargeable accounting period shall for all purposes be included in the franked investment income and the gross relevant distributions of the principal company for the corresponding chargeable accounting period of that company; but (*b*) no franked investment income received by the principal company directly from that subsidiary, or received by the subsidiary directly from the principal company or directly from any other subsidiary of the principal company with respect to which such a notice is in force given by that company, and no distributions made by the principal company to the subsidiary, or by the subsidiary to the principal company or to any such other subsidiary of the principal company as aforesaid, shall be so included."

If I correctly understand that Sub-section, it means that distributions by a subsidiary company count as distributions by the principal company (paragraph (*a*)) except in so far as they are distributions made to the principal company itself, as in the present case, in which event they are not to be included with the distributions of the principal company, and therefore do not count at all (paragraph (*b*)). The reason for this provision was doubtless because a distribution made by a subsidiary only to the principal company was not regarded as being within the mischief against which the Statute was aimed, namely, the inflationary tendency resulting from excessive distributions to the public. In these circumstances it appears to me that the dividend in question in this case, being paid by Binns, Ltd., wholly to its principal company, was not a relevant distribution at all within the meaning of Section 38 (1). If that is right, it must follow that there could be no room for the application of Section 37 since there would be nothing to apportion. This point does not appear to have been taken in *T.S.S. Investments*[1], nor apparently in the present case when it was before the Special Commissioners. The point was, however, taken before Pennycuick, J., but was rejected by him. The learned Judge, having stated the point, said[2]:

> " I do not think this contention is well founded. By virtue of Section 37, the dividend paid by Binns in the present case is apportioned between the chargeable accounting periods 27th January, 1953, to 27th April, 1953, and 28th April, 1953, to 26th January, 1954, respectively. Only that part of the dividend which is apportioned to the later chargeable accounting period can be regarded as a distribution made where a grouping notice under Section 22 of the Finance Act, 1937, is in force; and, equally, only that part of the distribution can be

(1) 40 T.C. 85. (2) *See* p. 606, *ante*.

> regarded as paid by Binns in the capacity of subsidiary company to House of Fraser in the capacity of principal company. That part of the distribution which is apportioned to the earlier chargeable accounting period must be regarded as made where the grouping notice was not in force and where the relation of subsidiary company and principal company did not exist. It is, I think, impossible to step at this point in the Act, as Mr. Bucher invites me to do, from the fictional in Section 37 to the factual in Section 38 and to disregard for the purpose of Section 38 the apportionment of distributions required to be made under Section 37."

With all respect to the learned Judge, it seems to me that the boot is on the other leg. I do not see how it is justifiable to step from the factual to the fictional so as to apply a Section which is to be invoked only where it " appears necessary ". The distribution in question here, that is, the payment of the ordinary dividend, was in fact made at a time when Binns, Ltd., was a subsidiary of House of Fraser, Ltd., and it in fact went wholly into the pocket of the principal company. In such circumstances it seems to me to be bordering on the absurd to invent a fictional distribution during the period before Binns, Ltd., ever became a subsidiary.

I would, therefore, allow the appeal on the ground that, in all circumstances of the case, there was no necessity to apply the provisions of Section 37 so as to apportion the distribution represented by the payment of the ordinary dividend.

I must, however, refer to a further line of argument which was developed before us. It was suggested on behalf of Binns, Ltd., that the giving of the direction under Section 38 (4) constituted a wrong exercise of discretion, in that it was contrary to the policy of the Act as revealed in Section 38 (1), and that the direction should accordingly be regarded as a nullity. It was further argued that it could not in any event be competent for the Commissioners of Inland Revenue, by a subsequent direction given under Section 38 (4) of the 1947 Act, to alter an already existing chargeable accounting period which has been the subject of a valid notice properly given under Section 22 (1) of the 1937 Act. I am unable to accede to this line of argument, and on this point I find myself regretfully unable to agree with the views which will be expressed by my brethren in the judgments which they are about to deliver. For there may be cases (and so far as concerns the dividends paid on the preference and preferred ordinary shares this is one of them) where, during the first chargeable accounting period to which the notice under Section 22 (1) relates, distributions are made both before and after the date when the principal/subsidiary relationship is established. In such cases, as it seems to me, apportionment is called for so as to ascertain what proportion of the total distribution is caught by Section 38 (1) and what proportion, not being so caught, is properly to be regarded as a relevant distribution by the subsidiary. Where that situation arises—as it does in the present case in relation to the distributions in respect of the preference and preferred ordinary shares —a direction under Section 38 (4), I should have thought, is not only proper but necessary, notwithstanding the fact that it has the effect of altering an already existing chargeable accounting period which has been the subject of a notice under Section 22 (1) of the 1937 Act. That this is so is, I think, implicitly recognised by the Appellant Company itself, in that it admits that a proportion of the year's dividends paid on the preference and preferred ordinary shares must be reckoned as a gross relevant distribution attributable to the period from 27th January to 27th April, 1953 ; see the calculation submitted on behalf of the Appellant (Exhibit " D " annexed to the Case[1]).

(1) Not included in the present print.

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I do not think, therefore, that the action of the Commissioners of Inland Revenue in giving the direction which they did under Section 38 (4) can properly be criticised, or that the direction can be said to be of no effect even though it did purport to alter an already existing chargeable accounting period. This, however, does not in my view touch the question which falls for decision here in relation to the dividend on the ordinary shares which was wholly paid to the principal company. Assuming (as I do assume) that the direction given under Section 38 (4) was proper and effective, and that it did have the effect of altering the already existing chargeable accounting period, I would nevertheless allow the appeal on the ground which I have already stated.

Danckwerts, L.J.—Binns, Ltd., the Appellant Company, carried on the trade or business of drapers, furnishers, etc., in Sunderland and elsewhere. The accounts of the Company's business were made up for successive periods of twelve months ending on 26th January in each year, up to and including 26th January, 1954. House of Fraser, Ltd., acquired all the ordinary share capital of Binns, Ltd. (other than employees' preferred ordinary shares) and, as stated in paragraph 3 (3) of the Stated Case, from 28th April, 1953, Binns, Ltd., became a subsidiary of House of Fraser, Ltd., which is, therefore, " the principal company " in the terminology of the relevant Statutes. Binns, Ltd., also had two classes of cumulative preference shares and also cumulative preferred ordinary shares, but no arguments were advanced before us in reference to those shares, and they seem to me to have been treated as irrelevant for the purposes of the appeal.

On 6th January, 1954, House of Fraser, Ltd., gave what is called a " grouping notice " (which would have made the principal company responsible for Profits Tax under the relevant Statutes) in regard to " the chargeable accounting period " ending on 26th January, 1954 ; it is agreed that the reference in the notice to 31st January, 1954, is a mistake, which is to be disregarded. On 26th January, 1954, Binns, Ltd., declared a dividend amounting to £320,000 (£176,000 net) in respect of the period from 28th April, 1953, to 26th January, 1954, on the ordinary shares, which was expressed to be an interim dividend. On 27th January, 1954, the amount of the dividend was paid to the principal company.

Purporting to act under the provisions of Section 38 (4) of the Finance Act, 1947, the Commissioners of Inland Revenue directed that the period of twelve months from 27th January, 1953, to 26th January, 1954, should not be a chargeable accounting period, but that the periods (1) from 27th January to 27th April, 1953, and (2) from 28th April, 1953, to 26th January, 1954, should be chargeable accounting periods for the purpose of Profits Tax. Apparently the profits of the subsidiary Company for the year ending on 26th January, 1954, were ascertained to be £575,743, and the proportion of these profits for the earlier chargeable accounting period, i.e., 3 1/30 months, was said to be £145,535. Binns, Ltd., was assessed on that sum for an amount of £24,398 10*s*. Profits Tax. The question is whether that assessment was properly made on Binns, Ltd., which claims that, in view of the grouping notice, the profits having been paid over to the principal company should be ignored so far as Binns, Ltd., is concerned. I am afraid that I must refer to the relevant statutory provisions which, in accordance with modern taxing practice, are complicated and tiresome to understand. These are as follows.

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Section 19(1) of the Finance Act, 1937, which is the charging Section—the tax then called National Defence Contribution is now called Profits Tax (Section 44, Finance Act, 1946)—provides as follows(1):

> "There shall be charged, on the profits arising in each chargeable accounting period falling within the years of charge to the national defence contribution, from any trade or business to which this section applies, a tax (to be called the 'national defence contribution') of an amount equal to [blank] per cent. of those profits".

Section (20)(1) provides as follows:

> "(2) For the purpose of the national defence contribution, the accounting periods of a trade or business shall be determined as follows:—(*a*) in a case where the accounts of the trade or business are made up for successive periods of twelve months, each of those periods shall be an accounting period;"

—and that, I may observe, is exactly the present case—

> "(*b*) in a case where the accounts of the trade or business have been made up as aforesaid but have ceased to be so made up, the accounting periods from the end of the last period of twelve months for which they were so made up shall be such periods not exceeding twelve months as the Commissioners of Inland Revenue may determine; (*c*) in any other case the accounting periods of a trade or business shall be such periods not exceeding twelve months as the Commissioners of Inland Revenue may determine; and the expression 'chargeable accounting period' means—(i) any accounting period determined as aforesaid which falls wholly within the years of charge to the national defence contribution; and (ii) in a case where any such accounting period falls partly within and partly without the said . . . years, such part of that period as falls within those . . . years. (3) Where a chargeable accounting period is not a period for which the accounts of the trade or business have been made up, such division and apportionment to specific periods of the profits and losses for any period for which the accounts relating to the trade or business have been made up, and such aggregation of any such profits or losses or any apportioned part thereof, shall be made as appears necessary to arrive at the profits arising in the chargeable accounting period. (4) Any apportionment under the last foregoing subsection shall be made in proportion to the number of months or fractions of months in the respective periods, unless the Commissioners of Inland Revenue having regard to any special circumstances otherwise direct."

Section 22(2) provides as follows:

> "(1) Where a body corporate resident in the United Kingdom is a subsidiary of another body corporate so resident (hereafter in this section referred to as 'the principal company') the principal company may, by notice in writing given to the Commissioners of Inland Revenue before the expiration of any chargeable accounting period of the subsidiary or within six months from the end of that period or such longer time as the Commissioners of Inland Revenue may in any case allow, require that the provisions of subsection (2) of this section shall apply to the subsidiary as respects that period and all subsequent chargeable accounting periods throughout which it continues to be a subsidiary of the principal company . . . ".

That is the "grouping notice" to which I have referred.

> "(2) Where such a notice is given, the profits or losses arising in any chargeable accounting period to which the notice relates from the trade or business carried on by the subsidiary shall be treated, for the purpose of the provisions of this Act relating to the national defence contribution other than the provisions of paragraph 2 and sub-paragraph (2) of paragraph 3 of the Fourth Schedule to this Act, as if they were profits or losses arising in the corresponding chargeable accounting period from the trade or business carried on by the principal company. (3) . . . (*c*) a chargeable accounting period of a subsidiary shall be deemed to correspond to such chargeable accounting period of the principal company as the Commissioners of Inland Revenue may determine."

(1) As amended by Section 36 (2), Finance Act, 1942. (2) As amended by Section 42 (4), Finance Act, 1938.

(Danckwerts, L.J.)

Section 35 of the Finance Act, 1947, provides as follows:

> "(1) Subject to the provisions of this and the two next succeeding sections, the gross relevant distributions to proprietors for any chargeable accounting period of a body corporate, society or other body, are the total distributions to the members of the body corporate, society or other body, not being distributions allowable as deductions in computing the profits of the trade or business for any period for the purposes of the profits tax, and being either—"

and the material paragraph is:

> "(*a*) dividends declared not later than six months after the end of that period which are expressed to be paid in respect of that period or any part thereof".

Section 37 provides as follows:

> "(1) Where a chargeable accounting period is not a period for which the accounts of the trade or business have been made up, the gross relevant distributions to proprietors shall be computed in relation to the periods for which accounts relating to the trade or business have been made up (being periods falling wholly or partly within the chargeable accounting period) as if those periods were chargeable accounting periods, and such division and apportionment to specific periods of the amounts so computed and such aggregation of any such amounts or of any apportioned parts thereof shall be made as appears necessary to arrive at the gross relevant distributions to proprietors for the chargeable accounting period. (2) Any apportionment under this section shall be made in proportion to the number of months or fractions of months in the respective periods."

Section 38 provides as follows:

> "(1) Where a notice under subsection (1) of section twenty-two of the Finance Act, 1937 (which relates to subsidiary companies) is in force—(*a*) the franked investment income, and the gross relevant distributions, of the subsidiary to which the notice relates for any chargeable accounting period shall for all purposes be included in the franked investment income and the gross relevant distributions of the principal company for the corresponding chargeable accounting period of that company; but (*b*) no franked investment income received by the principal company directly from that subsidiary, or received by the subsidiary directly from the principal company or directly from any other subsidiary of the principal company with respect to which such a notice is in force given by that company, and no distributions made by the principal company to the subsidiary, or by the subsidiary to the principal company or to any such other subsidiary of the principal company as aforesaid, shall be so included. . . . (4) If at any time after the end of the year nineteen hundred and forty-six a body corporate is a subsidiary of another body corporate, there shall be made such alterations, if any, of the periods which would otherwise be chargeable accounting periods of either body corporate as the Commissioners may direct. . . . (6) This section shall be construed as one with the said section twenty-two."

Section 30(2) of the Finance Act, 1956, was also referred to, and provides as follows:

> "The chargeable accounting period specified in a grouping notice as the first of the periods as respects which the notice is to have effect may not be a period ending before the date on which the principal company became entitled to give the notice; and if, when a grouping notice has been given, the Commissioners of Inland Revenue, under subsection (4) of section thirty-eight of the Finance Act, 1947, divide the period so specified therein, the notice shall have effect as if for the period so specified there were substituted the first of the periods into which it is divided which ends on or after that date."

It is said that the object of the statutory provisions was to prevent inflation, and so where a dividend from profits was paid over to the principal company by a subsidiary, as it was not distributed to the public no inflationary effect was caused, and so in the hands of the principal company the profits were taxed (at the relevant time) at 10 per cent. instead of 25 per cent. This system has been abolished, and the present case, therefore, cannot recur, it appears.

(Danckwerts, L.J.)

Now the first thing to notice is that as the accounts of the business of Binns, Ltd., were made up for successive periods of twelve months, the present case falls within the express terms of Section 20 (2) (*a*) of the Finance Act, 1937, and under that provision each of those periods is to be an accounting period. There was, therefore, quite plainly at the date of the relevant events an " accounting period ", which is, by the same Sub-section, a " chargeable accounting period ". Paragraphs (*b*) and (*c*) (the latter of which gives the Commissioners of Inland Revenue a power to determine the accounting period) have no application. There seems no reason why any interference should be made with the plain provisions of Sub-section (2) (*a*) ; nor has Sub-section (3) any application.

It would appear, therefore, that on 6th January, 1954, the principal company was perfectly justified in giving a " grouping notice " under Section 22 (1) of the same Act in respect of the existing chargeable period of the subsidiary from 27th January, 1953, to 26th January, 1954, and thereupon the provisions of Section 22 (2) applied to that period and all subsequent chargeable accounting periods throughout which Binns, Ltd., continued to be a subsidiary of the principal company. There is no doubt that Binns, Ltd., was a subsidiary at the date of the notice. This construction seems to be supported by the provisions of Section 30 (2) of the Finance Act, 1956, if these be relevant. If the notice is effective in this way, the profits or losses arising in the chargeable accounting period to which the notice relates must, under Section 22 (2), be treated as if they were profits or losses arising in the corresponding chargeable accounting period from the trade or business carried on by the principal company. This means that the assessment made on Binns, Ltd., in the present case is wrong and cannot be supported. The dividend was, of course, declared wholly in respect of a period when Binns, Ltd., was a subsidiary. For the reasons which have been mentioned, Section 37 of the 1947 Act also had no application.

The Crown's case rests on the provisions of Section 38 (4) of the Finance Act, 1947, which, it is contended, enables the Commissioners of Inland Revenue, in an arbitrary manner, to alter the chargeable accounting period by a direction given by them in 1958, four years after the relevant period, splitting the period of the original accounting period into two parts, the first of which will be prior to the date on which Binns, Ltd., actually became a subsidiary. It was added in argument, somewhat brutally, that one result is that the notice of 6th January, 1954, will thus be invalid as regards the first period because it was not given within six months from the end of the first period ; no extension of time being offered by the Commissioners under the power permitting extension. It is somewhat startling if, by Section 38 (4), such a power is given to overturn the conditions on which a notice was given in reliance on the express provisions contained in Section 20 (2) (*a*) of the Finance Act, 1937, and payment over of the relevant dividend has been made to the principal company. It is difficult to see how business could be carried on reasonably if that is the true position. Such a construction with such retrospective effect ought not to be given to a statutory provision unless it is plain that it was intended to have that effect.

Mr. Magnus claimed that the power conferred by Section 38 (4) was unrestricted in extent and unlimited in time, and relied on the provisions in Section 38 (6) that the Section was to be construed as one with Section 22 of the Finance Act, 1937. He retreated a little from this position, I think,

(Danckwerts, L.J.)

when he admitted that, as in the case of any statutory power, this power must be exercised in a reasonable manner. Of course, one accepts without hesitation that the Commissioners of Inland Revenue and their assistants are honourable men with a desire to act in a reasonable manner; but I suspect that the excitement of the chase of the reluctant taxpayer sometimes results in an objective study of the situation being overlooked. And surely the Commissioners cannot be the uncontrollable judges of what is reasonable in given circumstances; it must be subject to the judgment of the Court. Such powers as these must, in my opinion, be regarded with careful scrutiny. In my opinion the powers conferred by Section 38(4) are not to be treated as wholly unrestricted. They must be read in their context, and with due consideration for the objects of the legislation and the purposes for which such powers have been conferred upon the Commissioners of Inland Revenue. I have come to the conclusion that where, as in the present case, the Act of 1937, by Section 20(2)(*a*), has provided a factual " chargeable accounting period ", there is no case for the application of the power conferred by Section 38(4) of the 1947 Act, and that Sub-section has no application.

In my view, the object of Section 38(4) is to enable the Commissioners of Inland Revenue to remove difficulties which arise in the working of the Act, and not to alter the effect of the Act and the actual facts to the disadvantage of the taxpayer because the suggested alteration would be more favourable to the claims of the Inland Revenue. The language of Section 38(4), moreover (as explained more fully by Diplock, L.J.), is inconsistent with such an intention. Section 37 and Section 38(1), (2) and (3) seem to me to support this result. No apportionment was required under Section 37 in the present case. Sub-sections (1), (2) and (3) of Section 38 are all based on the situation that there is a notice under Section 22(1) of the 1937 Act in force. The effect of the purported direction is to make the notice which has been duly given under the provisions of Section 22(1) irretrievably ineffective, at least in part. I do not think that was the intention of the Act, and I reach the conclusion that the direction given by the Commissioners of Inland Revenue was void and of no effect. Moreover, I think that the giving of the direction was unreasonable as an exercise of the power given by Section 38(4), and bad for this reason also. I accept that directions under the Sub-section may have to be retrospective because of difficulties in regard to the time of the actual making up of the accounts of companies; but, in my view, it is an unreasonable exercise of the power to attempt to upset the effect of a grouping notice in accordance with the Act of 1937, given four years before the direction, for the reason that it appears to give the subsidiary company an advantage of which the Commissioners of Inland Revenue wish to deprive them.

For these reasons I think that the appeal should be allowed.

The decision of Plowman, J., in *T.S.S. Investments, Ltd.* v. *Commissioners of Inland Revenue,* 40 T.C. 85, was a different case from the present arising on a different Sub-section, and I therefore make no further comment on it.

Diplock, L.J.—This is an appeal by Binns, Ltd., which is and has been since 28th April, 1953, a subsidiary within the meaning of Section 22 of the Finance Act, 1937, of House of Fraser, Ltd., which is the principal company within the meaning of that Section. It arises out of an assessment to Profits Tax on the subsidiary for the period 27th January to 27th April, 1953. The assessment to Profits Tax of the principal company for the corresponding period was not in issue.

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The accounts of the subsidiary were at all material times made up for successive periods of twelve months ending on 26th January in each year. They were in due course made up for the period 27th January, 1953, to 26th January, 1954, and were approved by the Company in general meeting in July, 1954. From the time of that approval, if not before, the period 27th January, 1953, to 26th January, 1954, was a chargeable accounting period of the subsidiary. On 6th January, 1954, a grouping notice under Section 22(1) of the Finance Act, 1937, was given by the principal company in respect of the subsidiary expressed to relate to

> " the Chargeable Accounting Period ending on [26th] January, 1954, and all subsequent Chargeable Accounting Periods ",

and on 27th January, 1954, an interim dividend expressed to be paid in respect of the period from 28th April, 1953, to 26th January, 1954, was paid to the principal company. Over four years later, on 28th October, 1958, the Commissioners of Inland Revenue, purporting to exercise their powers under Section 38(4) of the Finance Act, 1947, directed that the period from 27th January, 1953, to 26th January, 1954, should not be a chargeable accounting period of the subsidiary, but that each of the periods from 27th January to 27th April, 1953, and 28th April, 1953, to 26th January, 1954, should be chargeable accounting periods.

No point appears to have been taken before the Special Commissioners that Profits Tax in respect of the period 27th January to 27th April, 1953, was not assessable upon the subsidiary Company at all. It appears to have been common ground before them that that period was a chargeable accounting period, that the grouping notice did not apply to it, and that Profits Tax in respect of it was assessable upon the subsidiary, and not upon the principal company. The point of law taken by the subsidiary before the Special Commissioners upon which they stated a Case for the opinion of the High Court was that: (*a*) the interim dividend being expressed to be paid in respect of the period from 28th April, 1953, to 26th January, 1954, was not a distribution to the proprietors of the subsidiary for the period from 27th January to 27th April, 1953, within the meaning of Section 35(1) of the Finance Act, 1947 ; (*b*) it was not necessary to apportion it between the two periods as the Crown claimed to be entitled to do under Section 37 of that Act ; and (*c*) the subsidiary was accordingly entitled to non-distribution relief under Section 30(2) of the Finance Act, 1947, upon an amount of profits equal to that part of the dividend which the Commissioners of Inland Revenue had purported to apportion to the period 27th January to 27th April, 1953. This contention was rejected by the Special Commissioners and by Pennycuick, J. I, too, think that they were right in so doing.

Section 37 comes into operation

> " Where a chargeable accounting period is not a period for which the accounts of the trade or business have been made up ".

If the direction of 28th October, 1958, of the Commissioners of Inland Revenue was valid and effective, the subsidiary fell within the opening words of the Section, for its accounts were made up for the period 27th January, 1953, to 26th January, 1954, which, by virtue of that direction, was no longer a chargeable accounting period of the subsidiary. The Section then goes on to direct that in that event the gross relevant distributions to proprietors shall be computed in relation to the period from 27th January, 1953, to 26th January, 1954, as if that period were a chargeable accounting

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period. The dividend being expressed to be paid in respect of part of the period from 27th January, 1953, to 26th January, 1954, therefore, fell to be included in the computation of gross relevant distributions to proprietors for that period in accordance with the provisions of Section 35 (1) (*a*) of the Finance Act, 1947. At this stage of the computation directed to be made by Section 37, one has not arrived at any computation of the gross relevant distribution to proprietors for either of the actual specific chargeable accounting periods—namely, from 27th January to 27th April, 1953, or from 28th April, 1953, to 26th January, 1954—into which the Commissioners of Inland Revenue had divided the period for which the accounts of the subsidiary had in fact been made up. In order to do so it is " necessary " to apportion between those two specific periods the gross relevant distribution to proprietors for the period 27th January, 1953, to 26th January, 1954. That apportionment, which Section 37 requires to be made, is not to be made in accordance with the provisions of Section 35, but in accordance with the provisions of Section 37 (2), namely, on a time basis

> " in proportion to the number of months or fractions of months in the respective periods."

The fact that the dividend was expressed to be paid in respect of the second of the two periods is irrelevant to this apportionment. Upon the assumption, not contested before the Special Commissioners, that the subsidiary was assessable to Profits Tax in respect of the period from 27th January to 27th April, 1953, I am of opinion that they came to a correct conclusion in point of law.

Before the learned Judge, however, Counsel for the Appellant Company were permitted to raise the further point that the grouping notice applied to the period from 27th January to 27th April, 1953, as well as to the period from 28th April, 1953, to 26th January, 1954 ; and before this Court they were permitted to argue the further point that the direction of 28th October, 1958, of the Commissioners of Inland Revenue, was invalid on the grounds that Section 38 (4) of the Finance Act, 1947, gave them no power to alter retrospectively a chargeable accounting period which already existed. If either of these contentions were correct, it would follow that there should have been no assessment to Profits Tax at all made upon the subsidiary in respect of the period from 27th January to 27th April, 1953, and that its profits and gross relevant distributions should have been treated as if they were profits of the principal company, and its distributions to the principal company dealt with in the assessment of the liability to Profits Tax of the principal company in the manner provided for in Section 38 (1) of the Finance Act, 1947. If the first of these contentions were correct, the subsidiary would have been entitled to a nil assessment to Profits Tax for the period in dispute, and not merely to a reduction of its assessment by the amount of the non-distribution relief upon that part of the dividend which is all that the subsidiary claimed in its appeal to the Special Commissioners. If the second contention were correct, Section 22 (1) of the Finance Act, 1937, would prevent the Commissioners of Inland Revenue from assessing the subsidiary to Profits Tax for that particular period at all.

These two new contentions turn upon the meaning of Section 22 of the Finance Act, 1937, and Section 38 of the Finance Act, 1947, which are to be construed as one. Profits Tax is, by Section 19 (1) of the Finance Act, 1937, charged " on the profits of each chargeable accounting period

falling within " a specified period of time. It is implicit in the Act that successive chargeable accounting periods shall follow immediately upon one another, that is, that there shall be no interval of time which does not form part of a chargeable accounting period. " Chargeable accounting period " is defined by Section 20 of the Finance Act, 1937, by reference to the " accounting periods " of a trade or business, and so far as is relevant for the purposes of the present case coincides with the " accounting period " of the subsidiary. The effect of this definition before the passing of the Finance Act, 1947, was that if, and so long as, the accounts of the trade or business were made up for successive periods of twelve months, each of those periods of twelve months was a " chargeable accounting period ", but that in any other case the chargeable accounting periods were such periods not exceeding twelve months as the Commissioners of Inland Revenue might determine. It follows from these provisions that, even without the Finance Act, 1947, a chargeable accounting period until its expiration could, strictly speaking, only be inchoate, for, until the accounts of the trade or business had actually been made up for a period of twelve months immediately succeeding a previous period of twelve months for which they had been made up, it would be uncertain whether the chargeable accounting period would be that succeeding period of twelve months by virtue of Section 20 (2) (*a*) of the Finance Act, 1937, or such other period commencing at the expiration of the preceding chargeable accounting period as might be determined by the Commissioners of Inland Revenue under paragraphs (*b*) or (*c*) of that Sub-section.

Nevertheless, a taxpayer, if the accounts of his business previously had been made up for successive periods of twelve months, could be sure, before the passing of the Finance Act, 1947, that all subsequent chargeable accounting periods would be successive periods of twelve months unless he himself chose to make up his accounts for some other period. For this reason Section 22 of the Finance Act, 1937, has, in Mr. Magnus's phrase, always marched somewhat uneasily with Section 20 even before Section 38 of the Finance Act, 1947, was passed. I will first consider the position under Section 22 before the later Section came into force. It provided that a grouping notice might be given by a principal company

> " before the expiration of any chargeable accounting period of the subsidiary or within six months [originally two months(1)] from the end of that period ".

Since the notice might be given before the expiration of a " chargeable accounting period ", the latter expression must have included one which was inchoate because, although its starting date was fixed by the end of the preceding chargeable accounting period, it could only become a chargeable accounting period upon its termination, which itself depended upon the happening of an uncertain future event, namely, either the making up of its accounts for the period of twelve months from the end of the last chargeable accounting period, or (if that did not occur) then upon a determination by the Commissioners under paragraph (*b*) or (*c*) of Section 20 (2). But as the grouping notice had effect as respects the inchoate chargeable accounting period before the expiry of which the grouping notice was given,

> " and all subsequent chargeable accounting periods throughout which [the subsidiary] continues to be a subsidiary of the principal company ",

it mattered not what date would ultimately become the termination of the

(1) Amended by Section 42 (4), Finance Act, 1938.

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inchoate chargeable accounting period, for the starting date and the finishing date of the period to which the grouping notice related was fixed. By Section 22 (2)

> " the profits or losses arising in any chargeable accounting period to which the notice relates "

arising from the trade or business carried on by the subsidiary were to be treated as profits and losses of the principal company. Since " chargeable accounting period " here must also include a chargeable accounting period which was inchoate at the date of the grouping notice, it follows that the principal company was entitled to the benefit of the provisions of Sub-section (2) in (i) the first chargeable accounting period which began at the end of the last chargeable accounting period before the date of the grouping notice, whatever the length of that first chargeable accounting period might turn out to be, and (ii) all other chargeable accounting periods thereafter so long as the subsidiary continued to be a subsidiary.

Section 38 (4) of the Finance Act, 1947, gave to the Commissioners of Inland Revenue power to make

> " such alterations, if any, of the periods which would otherwise be chargeable accounting periods "

of a subsidiary as they might direct. As I have already indicated, an alteration in the anticipated length of an inchoate chargeable accounting period starting at the end of the last chargeable accounting period before the grouping notice was given would not affect the period to which the grouping notice relates. But Mr. Magnus contends that the new Sub-section gives the Commissioners of Inland Revenue power to achieve this result indirectly by creating retrospectively a chargeable accounting period starting at the end of the last chargeable accounting period existing at the date of the grouping notice and terminating more than six months before the date of the grouping notice. The grouping notice, it is then said, was given more than six months after the termination of this chargeable accounting period, which did not come into existence until after the notice had been given, and the notice was too late (not, be it noted, too early) to apply to it. This ingenious petard, which can be set to explode under its chosen target at any selected interval before it is placed in position and the fuse is lit has, we are informed, been regularly used by the Commissioners of Inland Revenue to destroy the effect of grouping notices which were valid at the time that they were given. It was used, for example, in *T.S.S. Investments, Ltd.* v. *Commissioners of Inland Revenue*, 40 T.C. 85, and no one has heretofore contested its legality. Nevertheless, I, for one, cannot accept that the simple words of Section 38 (4) of the Finance Act, 1947, have such startling consequences.

The Sub-section authorises the Commissioners of Inland Revenue to alter only " periods which would otherwise be chargeable accounting periods ". This language must be read in the light of Section 20 of the Finance Act, 1937, which determines not only what periods in the past are already chargeable accounting periods, but also what periods in the future will be chargeable accounting periods, namely: the successive twelve-monthly periods in cases falling under Section 20 (2) (*a*) or such other successive periods not exceeding twelve months as the Commissioners have determined in cases falling under paragraphs (*b*) or (*c*) of the Sub-section. Thus where Section 38 (4) of the Finance Act, 1947, speaks of " periods which would otherwise be chargeable accounting periods ", this language is apt to describe those periods in the future which, if no alteration were made, would be chargeable accounting periods by virtue of the provisions of Section 20 (2) of the Finance Act, 1937.

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Much more explicit language would, in my view, be required to authorise the Commissioners of Inland Revenue to alter a chargeable accounting period which has already expired, and in respect of which the taxpayer has incurred vested liabilities or, in the case of losses, acquired vested rights in an amount which is fixed and certain, for it is assessable although it may not yet have been assessed. But Section 38 (4) does not use the past tense at all; it contains no reference to periods which "were" or "have been" chargeable accounting periods; it does not purport to authorise the Commissioners to make or remake history. The language is in marked contrast to that used in the next succeeding Sub-section, (5), which provides in express terms for retrospective effect to be given to the revocation of a grouping notice. In my view, the Commissioners' powers under the Sub-section are limited to making alterations *in futuro,* that is to say, to making alterations in chargeable accounting periods which have not yet expired, and which are accordingly inchoate at the time of the alteration and have not yet given rise to any vested liabilities and rights. The construction which Mr. Magnus seeks to put upon the Sub-section seems to me to be contrary to the ordinary meaning of the words used and to conflict with the rule of construction that if there be an ambiguity it is to be presumed that Parliament did not intend to confer a power to destroy retrospectively rights or liabilities which have already been vested.

I turn, therefore, to the grouping notice given by the principal company on 6th January, 1954. It was expressed to be given

> "in regard to the Chargeable Accounting Period ending on [26th] January, 1954, and all subsequent Chargeable Accounting Periods."

The first chargeable accounting period to which it related was described by reference to the date on which it was anticipated that it would end instead of by reference to the date on which it had begun. This was probably done in anticipation of the Commissioners of Inland Revenue following their then current practice (which I hold to be *ultra vires*), of making a retrospective alteration in the twelve-monthly chargeable accounting period of the subsidiary laid down by Section 20 (2) (*a*) of the Finance Act, 1937; and difficult questions as to the effect of the grouping notice might have arisen if there had never been a chargeable accounting period which in fact ended on 26th January, 1954. But there was. As soon as the accounts of the subsidiary were made up for the period from 27th January, 1953, to 26th January 1954, which happened when the subsidiary's accounts were approved in general meeting, that period became "the chargeable accounting period ending 26th January, 1954", and accordingly a "chargeable accounting period to which the notice relates" within the meaning of Section 20 (2) of the Finance Act, 1937. By then it was too late for the Commissioners of Inland Revenue to alter it, and their direction of 28th October, 1958, which purported to do so, was *ultra vires* and void.

For these reasons I am of opinion that Binns, Ltd., was not liable to be assessed to Profits Tax at all for the period from 27th January to 27th April, 1953; but since it has not appealed against the whole assessment, but only in respect of a sum equal to the amount of the non-distribution relief on the proportion of the ordinary dividend which the Commissioners of Inland Revenue purported to apportion to that period, I should allow the appeal in respect of this sum only.

Mr. F. N. Bucher.—Will your Lordships allow the appeal with costs?

Willmer, L.J.—Have you anything to say on that, Mr. Orr?

Mr. Alan Orr.—I have nothing to say on that, my Lord. I am instructed to ask your Lordships for leave to appeal to the House of Lords if my clients, on conidering the judgments, should wish to take that course.

Willmer, L.J.—Have you anything to say on that, Mr. Bucher?

Mr. Bucher.—I could not resist that application, my Lord, but I would respectfully submit that consideration ought to be given as to the costs to be incurred. This is a very special case which cannot recur. The amount at stake is relatively small for such matters ; and I would respectfully submit that, if leave be given to the Crown to appeal, the Order as to costs should not be disturbed as your Lordships have given them.

Willmer, L.J.—We are not dealing with an impecunious taxpayer in this case, Mr. Bucher.

Mr. Bucher.—No, my Lord, but the amount of money involved is not large.

Diplock, L.J.—What is the amount?

Mr. Bucher.—£24,000, my Lord.

Willmer, L.J.—The amount in dispute is less than that.

Mr. Bucher.—Yes, £16,000, I think, my Lord.

Willmer, L.J.—That sounds quite a lot of money.

Mr. Bucher.—And, as I say, it is not a point which can recur.

Diplock, L.J.—Well, the point about retrospective notices, which is the basis of the majority decision, can recur.

Mr. Bucher.—The case has aspects which are of general importance to the Commissioners of Inland Revenue, but not to the taxpayer, my Lord ; and I would respectfully submit that this is a proper case in which to allow the taxpayer to have his costs up to this present hearing.

(The Court conferred.)

Willmer, L.J.—We grant leave to appeal, but with no Order in regard to costs. When I say that we grant leave to appeal, I mean that we are imposing no conditions in relation to costs in respect of the appeal. The appeal will be allowed with costs.

Mr. Bucher.—If your Lordship pleases.

The Crown having appealed against the above decision, the case came before the House of Lords (Viscount Simonds, and Lords Reid, Guest, Upjohn and Donovan) on 10th, 11th and 12th March, 1964, when judgment was reserved. On 5th May, 1964, judgment was given unanimously in favour of the Crown, with costs.

Mr. Hilary Magnus, Q.C., Mr. Alan Orr, Q.C., and Mr. P. Medd appeared as Counsel for the Crown, and Mr. F. N. Bucher, Q.C., Mr. R. Buchanan-Dunlop and Mr. Stewart T. Bates for the Company.

Viscount Simonds.—My Lords, I have been privileged to read the opinion which my noble and learned friend Lord Donovan has prepared and find that it expresses with such clarity and precision the view that I had myself formed upon the difficult questions that arise in this case that I can usefully add nothing. In my opinion, this appeal should be allowed with costs here and in the Court of Appeal and the judgment of Pennycuick, J., restored.

Lord Reid.—My Lords, the Respondent carried on business as drapers and furnishers for many years. It was its custom to make up its annual accounts on 26th January each year. It became a subsidiary of House of Fraser, Ltd., on 28th April, 1953. This case is concerned with the effect of a "grouping notice" given by House of Fraser, Ltd., to the Commissioners of Inland Revenue under Section 22 of the Finance Act, 1937, on 6th January, 1954, with regard to the Respondent. The Respondent's accounts were duly made up for the year ending 26th January, 1954, and approved in general meeting in the following July. On 27th January, 1954, the Respondent declared a dividend of £320,000 (£176,000 net) on its ordinary shares and the net sum was duly paid to House of Fraser, Ltd., which had become owner of the whole of the ordinary shares on 28th April, 1953.

The case is concerned with the effect of the provisions of the Finance Act, 1947, with regard to relief from Profits Tax in respect of undistributed profits. Broadly speaking, the effect of the 1947 Act was that a company paid Profits Tax at a lower rate in respect of that part of its profits which had not been distributed to the shareholders; but a company of which another company became a subsidiary could elect, by giving a "grouping notice", that the profits of the subsidiary should be treated as the profits of the principal company, and one effect of so electing was that any dividend paid by the subsidiary to the principal company was not to be regarded as a distribution. The reason for that seems clear. Excessive payments of dividend were regarded as contrary to the public interest because such payments were thought to promote inflation. So non-distribution relief was offered as an incentive to prevent such distribution. But payment of dividend by a subsidiary to a principal did not tend to promote inflation because the money was kept within the group of companies. From this point of view it did not matter whether money remained in the hands of the subsidiary or was paid into the hands of the principal company.

In fact no ordinary dividend at all was paid by the Respondent during the year 27th January, 1953, to 26th January, 1954. The dividend in question was only paid on 27th January, 1954, and if matters had stopped there the Respondent would have been entitled to full non-distribution relief for the whole of its accounting year 27th January, 1953, to 26th January, 1954. But for some reason which is obscure the dividend which was paid on 27th January, 1954, was expressly stated to have been paid in respect of the period 28th April, 1953, to 26th January, 1954, and the admitted effect was to throw this dividend back, for some purposes at least, into the previous accounting period. Broadly speaking, the contention of the Crown is that in the circumstances of this case the dividend paid on 27th January, 1954, must be regarded as spread over the whole of the previous accounting year of the Respondent so that a proportional part of it must be deemed to have been distributed during the period January to April before the Respondent became a subsidiary of House of Fraser, Ltd., and before House of Fraser, Ltd., owned any of the Respondent's shares. Distribution actually or notionally made during that period could not be affected by the provisions of the "grouping notice", so the Crown

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say that this notional or fictional distribution operates to deprive the Respondent of some of the non-distribution relief to which it would otherwise have been entitled. I am bound to say that this is not a contention which attracts my sympathy, but if that is the true effect of the very complicated statutory provisions which I must now examine, then, of course, the Crown must succeed.

One must begin with the Finance Act, 1937, which imposed the National Defence Contribution, which later became Profits Tax. At that stage there was no question of non-distribution relief. The only problem was to find the profit for the appropriate period, and profits were to be computed on Income Tax principles, subject to certain modifications, so the matter was relatively simple even where one company had become the subsidiary of another. In the normal case where a company made up its accounts annually, the company's financial year was to be the chargeable accounting period for this tax.

The position of a subsidiary company was dealt with by Section 22 and I quote the relevant parts:

> "Where a body corporate resident in the United Kingdom is a subsidiary of another body corporate so resident (hereafter in this section referred to as 'the principal company') the principal company may, by notice in writing given to the Commissioners of Inland Revenue before the expiration of any chargeable accounting period of the subsidiary or within two months thereafter, require that the provisions of subsection (2) of this section shall apply to the subsidiary as respects that period and all subsequent chargeable accounting periods throughout which it continues to be a subsidiary of the principal company . . . . (2) Where such a notice is given, the profits or losses arising in any chargeable accounting period to which the notice relates from the trade or business carried on by the subsidiary shall be treated, for the purpose of the provisions of this Act relating to the national defence contribution other than the provisions of paragraph 2 and sub-paragraph (2) of paragraph 3 of the Fourth Schedule to this Act, as if they were profits or losses arising in the corresponding chargeable accounting period from the trade or business carried on by the principal company."

The Commissioners had no power to require either principal or subsidiary to change their dates of making up their annual accounts, and if these were out of step, Section 22(3) merely allowed the Commissioners to determine which chargeable accounting period of the subsidiary should be deemed to correspond with a chargeable accounting period of the principal. Section 22(1) clearly assumes that each chargeable accounting period is identifiable and is unalterable by the Commissioners, and that any notice given under it (commonly called a "grouping notice") could specify the chargeable accounting period to which it refers, and could not thereafter have its effect nullified or varied by the Commissioners. The only difficulty that I can see in the application of this Section is with regard to the cases referred to in Section 20(2)(*b*) and (*c*). It is fairly obvious that the draftsman simply forgot about these cases, and perhaps that is not altogether surprising because they appear to be exceptional. But any difficulty in applying Section 22 to these exceptional cases cannot, in my opinion, affect the clear way in which it applies to the ordinary cases referred to in Section 20(2)(*a*).

The Finance Act, 1947, granted non-distribution relief, and to enable that to be calculated it was necessary to define the relevant distributions for each chargeable accounting period. For the purposes of these cases it is not necessary to distinguish between gross and net relevant distribution. Section 35 provides:

> "(1) Subject to the provisions of this and the two next succeeding sections, the gross relevant distributions to proprietors for any chargeable accounting

> period of a body corporate, society or other body, are the total distributions to the members of the body corporate, society or other body, not being distributions allowable as deductions in computing the profits of the trade or business for any period for the purposes of the profits tax, and being either—(*a*) dividends declared not later than six months after the end of that period which are expressed to be paid in respect of that period or any part thereof; or (*b*) distributions (other than dividends which, under paragraph (*a*) of this subsection, are to be treated as part of the gross relevant distributions to proprietors for any previous chargeable accounting period) made in the period . . ."

The position of a subsidiary is dealt with in Section 38 and, by virtue of Sub-section (6), this Section is to be construed as one with Section 22 of the 1937 Act. The relevant provisions of Section 38 are:

> "(1) Where a notice under subsection (1) of section twenty-two of the Finance Act, 1937 (which relates to subsidiary companies) is in force—(*a*) the franked investment income, and the gross relevant distributions, of the subsidiary to which the notice relates for any chargeable accounting period shall for all purposes be included in the franked investment income and the gross relevant distributions of the principal company for the corresponding chargeable accounting period of that company; but (*b*) no franked investment income received by the principal company directly from that subsidiary, or received by the subsidiary directly from the principal company or directly from any other subsidiary of the principal company with respect to which such a notice is in force given by that company, and no distributions made by the principal company to the subsidiary, or by the subsidiary to the principal company or to any such other subsidiary of the principal company as aforesaid, shall be so included. . . . (4) If at any time after the end of the year nineteen hundred and forty-six a body corporate is a subsidiary of another body corporate, there shall be made such alterations, if any, of the periods which would otherwise be chargeable accounting periods of either body corporate as the Commissioners may direct."

Again, there seems to me to be no difficulty in applying these provisions to the ordinary cases dealt with by Sections 20(2)(*a*) and 22 of the 1937 Act. The "grouping notice" selects which chargeable accounting period of the subsidiary is the first to which it is to apply. Then Section 35 of the 1947 Act provides that dividends expressed to be paid in respect of that period or any part of it, and dividends not expressed to be paid in respect of any period but paid during that period, are to be included in the gross relevant distributions of that period. Again, Section 35 assumes that the chargeable accounting period has already been fixed and defined, and Section 38 begins with the words:

> "Where a notice under subsection (1) of section 22 . . . is in force . . ."

and assumes that a notice is in force with regard to the period for which it was given.

The contention of the Crown is that all this is upset by Section 38(4) of the 1947 Act. It is perfectly true that the words of Sub-section (4) are quite general and would, if taken literally, entitle the Commissioners to alter any chargeable accounting period of either the principal or subsidiary, including the period for which the "grouping notice" was originally given. But it is a commonplace that general words must be read in, and controlled by, their contexts, and the contention for the Crown produces some startling consequences if it is right.

It is argued that, once a company has become a subsidiary of another, everything is in the melting pot, and that you cannot say with regard to either company that either has any definite chargeable accounting period until the Commissioners have given a direction under Sub-section (4). In this case the direction given by the Commissioners was not given until more than four years had elapsed after the Respondent became a subsidiary

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of House of Fraser, Ltd., and, be it observed, this must apply not only to non-distribution relief but also to the whole liability for Profits Tax, because Section 22 of the 1937 Act applies to the whole subject of Profits Tax, and Section 38(4) of the 1947 Act has to be construed as one with it. So it must follow, if the Crown are right, that for four years no one could say, for any purposes connected with Profits Tax, what were the chargeable accounting periods of either the Respondent or House of Fraser, Ltd.

I find it very difficult to believe that any draftsman who intended that result would have sought to achieve it merely by inserting the general words of Section 38(4), and I doubt very much whether it is necessary to read them as having so wide an effect. But if all your Lordships think otherwise I shall not dissent. There are other defects in these Sections, and the practice has apparently been to interpret this Sub-section as applying to cases like the present. No solution is really satisfactory.

Assuming that Section 38(4) applies to this case I would have been inclined to adopt the view of Willmer, L.J. But I see the force of the argument of my noble and learned friend, Lord Donovan, and if your Lordships all agree with him, again, I would not dissent. The drafting of Section 37 is peculiar, and I am far from certain about its meaning.

Lord Guest.—My Lords, the salient facts in this appeal are that on 28th April, 1953, the Respondent Company became a subsidiary of House of Fraser, Ltd. The accounting periods of the Company were for 12 months ending on 26th January in each year. On 6th January, 1954, House of Fraser, Ltd., gave a "grouping notice" under Section 22 of the Finance Act, 1937, in relation to the chargeable accounting period ending on 26th January, 1954, and for all subsequent accounting periods. On 27th January, 1954, the Company paid to House of Fraser, Ltd., an ordinary dividend of £320,000 gross, declared to be an interim dividend for the period 28th April, 1953, to 26th January, 1954. On 28th October, 1958, the Commissioners of Inland Revenue gave a direction under Section 38 of the Finance Act, 1947, that the period of 12 months from 27th January, 1953, to 26th January, 1954, should not be a chargeable accounting period, but that the two periods from 27th January, 1953, to 27th April, 1953, and 28th April, 1953, to 26th January, 1954, should be chargeable accounting periods for the purpose of Profits Tax.

The question arose in relation to the computation of the gross relevant distributions of the Company under the Finance Act, 1947, as to whether the dividend of £320,000 fell to be included in the gross relevant distributions of the Company. Pennycuick, J., affirmed the determination of the Special Commissioners in favour of the Crown, to the effect that under Section 37 of the Finance Act, 1947, the gross relevant distribution had to be computed in relation to the accounting period ending on 26th January, 1954, and to be apportioned on a time basis over the two chargeable accounting periods, with the result that the earlier portion attracted Profits Tax.

The Court of Appeal (Danckwerts and Diplock, L.JJ., Willmer, L.J., dissenting) reversed the decision of Pennycuick, J., and held that the Commissioners were not authorised to alter the chargeable accounting periods retrospectively.

The Section under which the Commissioners of Inland Revenue made their direction is Section 38(4) of the Finance Act, 1947, which I must quote *in extenso* and which reads as follows:

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> "(4) If at any time after the end of the year nineteen hundred and forty-six a body corporate is a subsidiary of another body corporate, there shall be made such alterations, if any, of the periods which would otherwise be chargeable accounting periods of either body corporate as the Commissioners may direct."

But, as the remaining statutory provisions are quoted in the speech of my noble and learned friend, Lord Donovan, I find it necessary only to narrate their purport. The charging Section for Profits Tax (originally National Defence Contribution) is Section 19 of the 1937 Act. By Section 20(1), for the purpose of Profits Tax, the profits of a trade or business in each chargeable accounting period are separately computed. Under Section 20(2) certain periods are declared to be chargeable accounting periods: (*a*) where the accounts of the trade are made up for successive periods of 12 months, each of those periods shall be a chargeable accounting period; (*b*) where the accounts have been made up for successive periods of 12 months, but have ceased to be so made up, the chargeable accounting periods from the end of the last period of 12 months shall be such periods not exceeding 12 months as the Commissioners of Inland Revenue may determine; and (*c*) in any other case, the chargeable accounting periods shall be such periods not exceeding 12 months as the Commissioners may determine. By Sub-sections (3) and (4) of this Section, where the chargeable accounting period is not a period for which the accounts of the trade have been made up, provision is made for aggregation and apportionment on a time basis of the profits and losses, so as to arrive at the profits arising in the chargeable accounting period.

Provision is made in Section 22 of the 1937 Act where a company is the subsidiary of another company (called "the principal company") for the principal company giving a notice which has come to be known as a "grouping notice" before the expiration of any chargeable accounting period of the subsidiary or within 6 months from the end of that period or such longer time as the Commissioners of Inland Revenue may allow to apply to that chargeable accounting period and any subsequent accounting periods. The effect of giving a "grouping notice" is that the profits and losses of the subsidiary in the chargeable accounting period are treated as the profits and losses arising in the corresponding chargeable accounting period of the principal company.

The Finance Act, 1947, introduced what has become known as the "two-tier" system of calculating Profits Tax. To this end, Section 35 defines the gross relevant distributions to proprietors. Section 37(1) and (2) provide as follows:

> "(1) Where a chargeable accounting period is not a period for which the accounts of the trade or business have been made up, the gross relevant distributions to proprietors shall be computed in relation to the periods for which accounts relating to the trade or business have been made up (being periods falling wholly or partly within the chargeable accounting period) as if those periods were chargeable accounting periods, and such division and apportionment to specific periods of the amounts so computed and such aggregation of any such amounts or of any apportioned parts thereof shall be made as appears necessary to arrive at the gross relevant distributions to proprietors for the chargeable accounting period. (2) Any apportionment under this section shall be made in proportion to the number of months or fractions of months in the respective periods."

It then became necessary to provide for the situation of subsidiary companies. Section 38(1), which commences with the words:

> "Where a notice under subsection (1) of section twenty-two of the Finance Act, 1937 (which relates to subsidiary companies) is in force",

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provides that certain consequences follow, *viz.*, (*a*) the gross relevant distributions of the subsidiary for any chargeable accounting period are to be the gross relevant distributions of the principal company for the corresponding chargeable accounting period of the principal, and (*b*) no distributions by the principal company to the subsidiary or *vice versa* are to be included at all.

In the Court of Appeal, Diplock, L.J., held that the direction given by the Commissioners under Section 38(4) of the 1947 Act was *ultra vires* as the Section only purported to cover chargeable accounting periods *in futuro* and did not entitle the Commissioners to alter the chargeable accounting periods retrospectively. I have had the advantage of reading the speech of my noble and learned friend, Lord Donovan, and I agree with him, for the reasons given, that the words of the Section have not the limited construction put upon them by Diplock, L.J. I also agree with my noble and learned friend in thinking that the reasons given by Danckwerts, L.J., for holding the direction invalid are not sound.

Assuming that the direction is valid, the only question is what is its effect so far as Profits Tax is concerned. In answer to the Crown's contention that the gross relevant distribution must, under Section 37 of the 1947 Act, be apportioned over the two chargeable accounting periods comprised in the direction the Respondent submitted two arguments. First, it was said that where the distribution is by a subsidiary to the principal company then, under Section 38(1) of the 1947 Act, there was no gross relevant distribution within the meaning of that Section. In this case, the distribution was made by the subsidiary to the principal after the relationship of principal and subsidiary had existed. There was consequently nothing to apportion under Section 37 as there were no gross relevant distributions. The fallacy of this argument lies, in my view, in the disregard of the opening words of Section 38(1) " where a [grouping notice] is in force ". Until the Commissioners issued their direction on 28th October, 1958, the chargeable accounting periods for the Respondent could not be finally ascertained. It is true that by virtue of Section 22 of the 1937 Act the Respondent was entitled to give a " grouping notice " with certain consequences, but the chargeable accounting period referred to therein could only be tentative until the Commissioners' views became known. In the words of Counsel for the Crown, there was, until the Commissioners' direction, " nothing on which the ' grouping notice ' could bite ". The Commissioners under Section 38(4) are given a complete discretion to alter any chargeable accounting period, which they may do " at any time " after 1946. Therefore, in the event the " grouping notice " only affected the chargeable accounting period after 28th April, 1953 (when the relationship of principal and subsidiary began). The provisions of Section 38(1) only operate " where a [grouping notice] is in force ", which I understand to mean is in force in relation to a chargeable accounting period as fixed by the Commissioners. No " grouping notice " could exist in relation to the chargeable accounting period ending 26th January, 1954, because no such chargeable accounting period in the event existed. Having regard to the wide terms of Section 38(4) I cannot see any reason why the Commissioners should not alter the chargeable accounting period contained in the " grouping notice ". I should have thought that this was one of the primary purposes of Section 38(4). It follows that Section 38(1)(*a*) operates only in relation to the gross relevant distributions subsequent to 28th April, 1953.

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The next argument submitted by the Respondent was to the effect that as the dividend was expressed to be paid for the period 28th April, 1953, to 26th January, 1954, which was a statutory chargeable accounting period as a result of the direction given by the Commissioners, no apportionment " appears necessary " under Section 37 of the Finance Act. Section 37 applies

> " where a chargeable accounting period is not a period for which the accounts of the trade or business have been made up ".

Having regard to the direction of the Commissioners, the Section applied to the subsidiary because its accounts were made up for the period 27th January, 1953, to 26th January, 1954, and the chargeable accounting period was not that period. It follows that, in view of the provisions of Section 37, it was necessary to apportion the gross relevant distributions to proprietors upon a time basis between the two chargeable accounting periods. My view, accordingly, is that the decision of Pennycuick, J., on this aspect of the matter was right. Upon the whole matter I would allow the appeal and restore the decision of the Special Commissioners.

Lord Upjohn.—My Lords, I have had the opportunity of reading the opinion which my noble and learned friend, Lord Donovan, is about to deliver and entirely agree with it.

Lord Donovan.—My Lords, this case raises a problem connected with the Respondent's liability to Profits Tax which is more easily stated than solved, and has given rise to considerable difference of judicial opinion in the Courts below. The facts lie in a narrow compass.

Binns, Ltd. (hereinafter called " Binns "), conducts what would seem to be a large and successful business as drapers, furnishers, and so on, in Sunderland and elsewhere.

On 28th April, 1953, a company known as House of Fraser, Ltd. (hereinafter called " the House of Fraser "), acquired the whole of the ordinary share capital of Binns which then became a subsidiary of the House of Fraser. It was not what is generally known as a " wholly-owned " subsidiary, for a part of the Company's preferential share capital was not acquired by the House of Fraser, but was left with its owners. The figures are immaterial. Some 9 months after the " take-over " Binns declared an interim dividend on its ordinary share capital amounting to no less than £320,000 gross (£176,000 net) which, of course, went wholly to the House of Fraser. This dividend was declared by Binns to be in respect of the period 28th April, 1953 to 26th January, 1954. The reason for the designation of this period will appear later.

Binns carried on a business the profits of which were liable to Profits Tax. This tax is under the direct management of the Commissioners of Inland Revenue (hereinafter called " the Commissioners ") who assess it and collect it. The " take-over " of Binns by the House of Fraser and the declaration of the aforesaid dividend by Binns led the Commissioners to give certain directions affecting the Profits Tax liability of Binns. It is these directions which have occasioned the present litigation.

Before stating what those directions were, it is necessary, in order to understand their effect, to say something about the legislation under which Profits Tax is levied. It is imposed by Section 19 of the Finance Act, 1937, upon the profits of trades and businesses carried on in the United

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Kingdom, or by persons ordinarily resident therein. In contradistinction to Income Tax, Profits Tax (originally called " National Defence Contribution ") is not assessed by reference to the profits of some year preceding the year when the profits actually arose. Instead, it is assessed on the actual profits of the chargeable period. Section 19 called these chargeable periods " chargeable accounting periods ": and provision had, naturally, to be made for ascertaining and determining what were to be the " chargeable accounting periods ".

In the ordinary way, trading companies make up their trading and profit and loss accounts for successive periods of 12 months. The Act of 1937, by Section 20(2), called each of these periods for which accounts were so made up " an accounting period ".

The Legislature had also to deal with cases where a business had in the past made up its accounts yearly, but for some reason had ceased to do so. In such a case the Commissioners were to take some period beginning at the terminal date of the last 12 months' account and ending on some date not more than 12 months later, and determine the period so selected as being " the accounting period " of such a business. Then there might be businesses where so far there had never been a 12 months' account, for example, because the business had only recently been started. In such a case, again, the Commissioners were to determine what period, not exceeding 12 months, should be the " accounting period " of the business for the purposes of Profits Tax. Section 20 of the 1937 Act then enacted that any " accounting period " determined as aforesaid which fell wholly within the years of charge to the tax should be a " chargeable accounting period ". The tax was imposed for 5 years only, from 1st April, 1937, so that these were originally the years of charge. The tax has followed precedent, however, by being still with us.

It will thus be seen that where (as would normally be the case) a business had made up its accounts for successive periods of 12 months, then, while it continued to do so, those periods were the " accounting periods ", and the Commissioners had no power to alter them. But in the case of all other businesses, the Commissioners were given power to determine what should be the accounting periods. I have summarised, I hope sufficiently, the effect of Section 20(2)(*a*), (*b*) and (*c*) of the Finance Act, 1937.

The Commissioners might exercise this power in such a way that a " chargeable accounting period " did not correspond to any period for which the company had made up its accounts. Suppose, for example, that a company started business on 1st April, 1937, and made up its first accounts for the 9 months ended 31st December, 1937. For the second year of its life the company made up its accounts for the 12 months to 31st December, 1938. Such a case would fall within Section 20(2)(*c*) of the Act of 1937, and the Commissioners could determine the " accounting period ". If they determined that it should be the first 12 months of the life of the business, that is from 1st April, 1937, to 31st March, 1938, then the " accounting period " would be a period for which accounts were not made up. How were the profits for this " accounting period ", then, to be ascertained? The Act supplied the answer in Section 20(3) and (4) by saying, in effect, " the company has made up a 9 months' account to 31st December, 1937, and a 12 months' account to 31st December, 1938. Aggregate the profits shown in these two accounts,

apportion that aggregate 'as appears necessary' on a time basis over the whole 21 months, and then find out the proportion attributable to the 12 months ended on 31st March, 1938".

The Legislature then went on in the 1937 Act to make special provision regarding subsidiary companies. It gave the principal company the right to give a notice (called in practice a "grouping notice") to the Commissioners requiring that the profits or losses of the subsidiary company in the chargeable accounting period to which the notice related, and in all subsequent chargeable accounting periods while it remained such a subsidiary, should be treated as the profits or losses of the principal company in the "corresponding chargeable accounting period" of the principal company. The notice had to be given to the Commissioners before the expiration of

> "any chargeable accounting period of the subsidiary or within two months thereafter"

(Section 22(1)). It will be seen at once that this time limit could lead to difficulties in cases coming under Section 20(2)(*b*) and (*c*) of the 1937 Act, that is to say, cases where the Commissioners had the power to determine what were to be the "accounting periods" of a business and, therefore, its "chargeable accounting periods". For in the nature of things this determination might come much longer than two months after the end of the chargeable accounting period to which it related. No doubt in order to meet this situation, the time limit was later altered to

> "six months from the end of that period or such longer time as the Commissioners may in any case allow"

(Finance Act, 1938, Section 42(4)). It was also necessary to make some provision as to what chargeable accounting period of the subsidiary should correspond to a chargeable accounting period of the principal company. This was left to be determined by the Commissioners (Section 22(3)(*c*), Finance Act, 1937).

Profits Tax began in 1937 at the rate of 5 per cent. upon the chargeable profits. It was raised by the Finance Act, 1947, to the rate of 12½ per cent. The same Act provided, however, that if the distribution of profits to the proprietors for any chargeable accounting period were less than the chargeable profits for such period, then the Profits Tax chargeable upon the undistributed profits of the period was to be 5 per cent. only. This result was effected by Section 30(2) of the Finance Act, 1947, reading, so far as relevant, thus:

> ". . . if . . . the net relevant distributions to proprietors . . . for any chargeable accounting period are less than the profits thereof for that period chargeable to the profits tax, the amount chargeable by way of the profits tax in respect of that period shall be reduced by an amount equal to seven and a half per cent. of the difference."

In this way what has been called the "two-tier arrangement" was introduced. A considerable inducement was provided to leave profits in the business instead of distributing them to the proprietors. The object at the time was to curb inflation. "Net relevant distributions" were defined in the Act of 1947 as being a certain specified proportion of the "gross relevant distributions" (see Section 34(2)); and "gross relevant distributions" were defined in Section 35. For present purposes it is enough to quote an extract from Section 35(1):

> "Subject to the provisions of this and the two next succeeding sections, the gross relevant distributions to proprietors for any chargeable accounting period

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> of a body corporate . . . are the total distributions to the members of the body corporate . . . being either—(*a*) dividends declared not later than six months after the end of that period which are expressed to be paid in respect of that period or any part thereof; or (*b*) distributions (other than dividends . . .) made in the period . . ."

Section 30(3) of the Finance Act, 1947, went on to provide that if the net relevant distributions to proprietors for any chargeable accounting period were *greater* than the profits for that period chargeable to Profits Tax, then the excess of such distributions should bear additional tax at the rate of 7 per cent., subject to a ceiling of liability which need not be here elaborated.

The relief for non-distribution provided by Section 30(2) was called " reliefs for non-distribution ": the charge on excess distributions was called " distribution charges " (Section 30(4)).

The rates of Profits Tax, distribution reliefs and distribution charges varied over the years until the " two-tier arrangement " was abolished by the Finance Act, 1958, Section 25. For the periods with which the present appeal is concerned, the rate of Profits Tax was 22½ per cent.: and the rate both of non-distribution relief and distribution charge was 20 per cent.

This " two-tier arrangement " brought fresh problems in its train, and I deal first with one, which was general to all businesses where the chargeable accounting period was *not* a period for which the accounts of the trade or business had been made up. Suppose that a business made up accounts from 1st April, 1947, to 31st December, 1947, and then made up the succeeding accounts for 12 months ending 31st December, 1948. It declared an interim dividend on 1st March, 1948, of £1,200 without expressing the dividend to be paid in respect of any particular period. This would be a case where for Profits Tax purposes the chargeable accounting period would be determined by the Commissioners (Section 20(2)(*c*) of the Finance Act, 1937). Suppose those Commissioners fixed the chargeable accounting period as being the 12 months 1st April, 1947, to 31st March, 1948. The question then arises, is the whole or only some part of the dividend of £1,200 paid on 1st March, 1948, to be treated as a distribution in this chargeable accounting period?

The procedure to be followed in such a case is prescribed by Section 37 of the Finance Act, 1947. It is this. First, compute the distributions in relation to periods for which accounts *have* been made up and which fall wholly or partly within the chargeable accounting period. In the example taken, accounts were made up, *inter alia,* for the 12 months to 31st December, 1948, and the dividend of £1,200 was paid in this period. Then treat the 12 months to December, 1948, *as if it were a chargeable accounting period.* Then apportion the £1,200 " as appears necessary " to arrive at the distribution for the *actual* chargeable accounting period, that is, the 12 months 1st April, 1947, to 31st March, 1948, in proportion to the number of months in " the respective periods ". The periods for comparison are thus the 12 months 1st January, 1948, to 31st December, 1948, which is to be treated " as if " it were a chargeable accounting period, and the 12 months 1st April, 1947, to 31st March, 1948, which is the actual chargeable accounting period. The dividend having been paid on 1st March, 1948, $\frac{1}{12}$th of it should be apportioned to the *actual* chargeable accounting period, leaving $\frac{11}{12}$ths to be dealt with subsequently.

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Perhaps the important thing to notice at this stage is that while, in the example I have taken, the dividend of £1,200 was declared and paid on 1st March, 1948, the effect of Section 37 is (at least at first sight) to treat it as *not* being a distribution falling wholly within the actual chargeable accounting period ending on 31st March, 1948, though it was in *fact* wholly paid in that period.

The "two-tier" system also called for further special provisions regarding subsidiary companies. These are to be found in Section 38 of the Finance Act, 1947, and so far as were relevant may be summarised thus: (1) gross relevant distributions of the subsidiary were to be included in the gross relevant distributions of the principal company for the corresponding chargeable accounting period of that company, but (2) no distributions made by the subsidiary company to the principal company were to be so included. These provisions are to apply, however, only where a "grouping notice" under Section 22(1) of the Finance Act, 1937, was in force.

Thus, in the present case, it would look at first sight as if the whole dividend of £320,000 paid to the principal company, the House of Fraser, by its subsidiary, Binns, on 27th January, 1954, would not be treated as a gross relevant distribution of either company. This, again, is an understandable provision, since a dividend passing between subsidiary and principal and not reaching the outside public would not have the inflationary effect which the Legislature at the time desired to avoid.

Section 38(4) proceeded to enact that if at any time after the end of 1946 a body corporate is a subsidiary of another body corporate

> "there shall be made such alterations, if any, of the periods which would otherwise be chargeable accounting periods of either body corporate as the Commissioners may direct."

Binns became a subsidiary of the House of Fraser on 28th April, 1953. The latter company gave a "grouping notice" to the Commissioners on 6th January, 1954. This notice required that the provisions of Section 22(2) of the Finance Act, 1937, should apply to Binns in regard to the chargeable accounting period ending on 26th January, 1954, and all subsequent chargeable accounting periods. At this time Binns made up its accounts yearly to 26th January, so that *prima facie* each 12 months ending on that date was both "the accounting period" and the "chargeable accounting period" for the purposes of Profits Tax—see Section 20(2)(*a*) of the Finance Act, 1937. The effect of giving the "grouping notice" was to require the Commissioners to treat the profits or losses of Binns for the chargeable accounting period to which the notice related, and for all subsequent chargeable accounting periods while it remained such a subsidiary, as being the profits or losses of the House of Fraser for the corresponding chargeable accounting period of the House of Fraser.

There was then a delay of over $4\frac{1}{2}$ years which remains unexplained. On 28th October, 1958, the Commissioners, purporting to act under Section 38(4), determined that the period of 12 months from 27th January, 1953 to 26th January, 1954 (which was Binns's normal accounting year, and for which it had made up its accounts) should *not* be a chargeable accounting period: but that that 12 months should be divided into two accounting periods thus: (1) the period of $3\frac{1}{30}$ months from 27th January, 1953 to 27th April, 1953; (2) the period of $8\frac{29}{30}$ months from 28th April, 1953

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to 26th January, 1954. It will be remembered that Binns became a subsidiary of the House of Fraser on 28th April, 1953 : so that the first of these chargeable accounting periods runs to the day before that happened, and the second continues from the first day of such relationship. It is admitted that Binns expected such a direction from the Commissioners, it being the usual practice in cases of such a " take-over ". Indeed, it was in anticipation of such a direction that the interim dividend later paid by Binns on 27th January, 1954, was expressed to be paid for the period 28th April, 1953 (the day of the " take-over "), to 26th January, 1954, so as to secure that it should be excluded from the calculation of gross relevant distributions. Section 38(1) of the Finance Act, 1947, enacts, it will be recalled, that where a " grouping notice " is in force, distributions made by a subsidiary to its principal are to be left out of account when computing the latter's gross relevant distributions.

The Commissioners, however, having directed that there should be these two chargeable accounting periods, proceeded to apportion the dividend of £320,000 between them on a time basis. The result was that a fraction of this dividend, that is, $3\frac{1}{80}$ over 12, was treated as a distribution by Binns before it became a subsidiary company, and thus the relief for non-distribution was materially less than Binns expected for this chargeable accounting period. The difference amounts to some £20,000.

As might be expected, Binns objected. The whole of the dividend of £320,000 had gone to its principal, the House of Fraser ; and, indeed, had been expressed to be payable for a period during the whole of which the House of Fraser had been its principal. Why, therefore, should not the saving provision of Section 38(1) of the Finance Act, 1947, apply? The answer of the Commissioners was that an apportionment of the dividend was required by the terms of Section 37 of the Finance Act, 1947.

The Company appealed to the Special Commissioners, contending that as the dividend had been expressed to be paid for a particular period, during all of which Binns had been a subsidiary, no part of the dividend could be treated as a gross relevant distribution by Binns, and that Section 37 was inapplicable to the circumstances of the case. The Special Commissioners rejected this contention. So, also, did Pennycuick, J., to whom the Company appealed by way of Case Stated. Before him, however, the Company took an additional point ; namely, that Section 38(1) in terms prohibited the inclusion in the gross relevant distributions of a subsidiary of a distribution made by it to its principal. This new contention also failed. Upon appeal to the Court of Appeal, the Company took still a further point, which it expressed in the requisite notice to the Crown as follows :

> " . . . that in the circumstances of this case it was wrong and capricious for the [Commissioners] to make the direction under Section 38(4) Finance Act 1947 made by them on 28th October 1958 in as much that such a direction would defeat the purpose of Section 38(1)(b) of that Act."

In the Court of Appeal the Company succeeded.

Willmer, L.J., upheld the contention of Binns that, since the dividend was paid to its principal company, the House of Fraser, Section 38(1) of the Finance Act, 1947, operated to exclude the dividend as a gross relevant distribution of either company. Danckwerts, L.J., took the view that the direction of the Commissioners under Section 38(4) of the Finance Act, 1947, by which two chargeable accounting periods were brought into being, was null and void : or, in the alternative (so it would appear), was of

no effect as being an unreasonable exercise of the Commissioners' powers under Section 38(4). Diplock, L.J., considered that the same direction was null and void, as being *ultra vires* the Commissioners.

No Lord Justice upheld the original contention of the Company when before the Special Commissioners, namely, that the designation of a particular period as being the period for which the dividend was paid was conclusive and ousted the need for any apportionment; though Willmer, L.J., was attracted by the argument. It is right to say also that he disagreed with the grounds adopted by Danckwerts and Diplock, L.JJ., for allowing the appeal.

It will, I think, be convenient to deal with those grounds first.

Danckwerts, L.J., said(1), after examining the relevant statutory provisions:

> "I have come to the conclusion that where, as in the present case, the Act of 1937, by Section 20(2)(*a*), has provided a factual 'chargeable accounting period', there is no case for the application of the power conferred by Section 38(4) of the 1947 Act, and that Sub-section has no application."

Later, however, in his judgment he said(1):

> "I accept that directions under the Sub-section [Section 38(4)] may have to be retrospective because of difficulties in regard to the time of the actual making up of the accounts of companies; but, in my view, it is an unreasonable exercise of the power to attempt to upset the effect of a grouping notice in accordance with the Act of 1937, given four years before the direction, for the reason that it appears to give the subsidiary company an advantage of which the Inland Revenue wish to deprive them."

The first part of this extract from the judgment of the learned Lord Justice is not easy to reconcile with his view expressed earlier, that a direction under Section 38(4) could not disturb an accounting period determined by the provisions of Section 20(2)(*a*) of the Finance Act, 1937. I will, however, deal with this aspect of the matter in a moment.

The second ground, namely, unreasonableness, on which the learned Lord Justice found, I fear I cannot support. I see nothing unreasonable in making the last chargeable accounting period of a company, while it is still an independent company, terminate on the last day of its life as such, and in making the next chargeable accounting period begin on the first day of its life as a subsidiary company. Indeed, it is admitted that the Company expected this to happen; and neither before the Special Commissioners nor before Pennycuick, J., was any contention of unreasonableness put forward. I can, if I may respectfully say so, understand the considerations which moved Danckwerts, L.J. The formation of two chargeable accounting periods led to the reduction of relief for non-distribution and, on the face of it, this looks a harsh result. But if it is simply the result of the relevant provisions once the Commissioners have decided to make two chargeable accounting periods, I do not see how they can be said to have been unreasonable. It is not suggested that in exercising their powers under Section 38(4) they were acting in bad faith, or took into account irrelevant considerations, or failed to take into account considerations which were relevant. It seems to me that the only way in which the direction under Section 38(4) can be impugned is to say that the Commissioners had no legal power to make it—a view which the learned Lord Justice also took, and which Diplock, L.J., shared. To this I now turn.

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(1) *See* p. 618, *ante*.

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Dealing with Section 38(4), Diplock, L.J. said(1):

> "In my view the Commissioners' powers under the Sub-section are limited to making alterations *in futuro*, that is to say, to making alterations in chargeable accounting periods which have not yet expired, and which are accordingly inchoate at the time of the alteration, and have not yet given rise to any vested liabilities and rights. The construction which Mr. Magnus seeks to put upon the Sub-section seems to me to be contrary to the ordinary meaning of the words used, and to conflict with the rule of construction that if there be an ambiguity, it is to be presumed that Parliament did not intend to confer a power to destroy retrospectively rights or liabilities which have already been vested."

In taking this view, the learned Lord Justice was much influenced by the words of Section 38(4)—"*which would otherwise be* chargeable accounting periods"—words which, in his opinion, connoted chargeable accounting periods in the future and no others. But it has to be remembered that the Commissioners will be considering these Profits Tax problems long after the end of the company's own domestic accounting period—in the present case apparently it was four years and more afterwards. It seems to me that it is a perfectly natural use of language at that moment to say "Now what *would be* the chargeable accounting periods in this case if we, the Commissioners, make no direction under Section 38(4)?" In other words, the language is quite apt to apply to periods in the past as well as in the future. If this were not so, it is difficult to see how Section 38(4) is to work at all. How can the Commissioners make directions for future accounting periods before they have the company's accounts and know the material facts? Furthermore, since they already have a discretion as to chargeable accounting periods under Section 20(2)(*b*) and (*c*) of the Act of 1937, what is left for this new discretion to operate upon except cases coming within Section 20(2)(*a*) and possibly Section 22(3)(*c*)?

> "A statute is designed to be workable",

said Lord Dunedin in *Whitney* v. *Commissioners of Inland Revenue*(2):

> "and the interpretation thereof by a Court should be to secure that object, unless crucial omission or clear direction makes that end unattainable"

([1926] A.C. 37, at page 52). Looking at the terms of Section 38(4) I find them to be quite general and unambiguous. To give them full effect is not to deprive Binns of any vested rights or liabilities, since those rights and liabilities are dependent upon the way in which the Commissioners operate the Sub-section. In my opinion, they were entitled thereunder to give the direction which in fact they gave on 28th October, 1958. On this aspect of the case I find myself in agreement with Willmer, L.J.

I come next to what was the sole contention of Binns before the Special Commissioners, namely, that the designation of the dividend of £320,000 as being payable for the period 28th April, 1953, to 26th January, 1954, of itself prevented the apportionment of any part of the dividend to any other period. This contention was rejected both by Pennycuick, J., and by Diplock, L.J., and I agree with this conclusion, and with their reasoning.

That leaves the contention which found favour with Willmer, L.J., namely, that since the dividend of £320,000 was paid at a time when Binns was a subsidiary and was paid wholly to its principal, which had earlier served a "grouping notice", then by Section 38(1)(*b*) of the Finance Act, 1947, the dividend was not to be treated as a gross relevant distribution at

(1) *See* p. 623, *ante*. (2) 10 T.C. 88, at p. 110.

all, and that accordingly there was nothing to apportion under the terms of Section 37. This view admittedly has its attractions, for it is based on what in fact occurred. But after careful consideration, I have come to the conclusion that the true construction of Section 38 leads inevitably to a different result.

I do not think, as Counsel for the Crown suggested, that in coming to the view he did, Willmer, L.J., overlooked the fact that Section 38 applied only where a " grouping notice " was in force, and not to all cases where the subsidiary and principal relationship existed. Indeed, in this part of his judgment he quotes Section 38 *verbatim*. Nor do I agree with the contention at first put forward on behalf of the Crown, that no " grouping notice " is " in force " until a chargeable accounting period is created upon which it can have effect. Counsel for the Crown himself contracted the width of this contention when it was pointed out that the " grouping notice " had the effect of inducing the Commissioners to take the action they did under Section 38(4). Nevertheless, it remains true to say (and this I think is really the Crown's contention) that Section 38 has to be operated at a time when the chargeable accounting period affected is in being, and it is then operated for the purpose of discovering what are the gross relevant distributions of the principal company in that period. To find out what these are one has to go back to Section 35 of the Act, which makes both that Section and Sections 36 and 37 applicable for determining what are the gross relevant distributions of a company for any chargeable accounting period. In the present case, the chargeable accounting periods were not periods for which accounts of the business had been made up, and the terms of Section 37 therefore applied. When the mandatory terms of that Section were obeyed an apportionment of the dividend became necessary, and yielded the result that the gross relevant distribution for the purposes of Section 38 was less than the amount which the House of Fraser actually received. The balance remained a gross relevant distribution of Binns and thus diminished the relief for non-distribution which it could obtain. The words in Section 37

> ". . . and such . . . apportionment . . . shall be made as appears necessary . . ."

do not mean simply as appears necessary in the light of the facts, but as appears necessary when the express directions of Section 37 as to the computation of the gross relevant distributions have been given effect. Indeed, it is difficult otherwise to see when an apportionment would ever be necessary, for distributions to proprietors would always be made upon some date or another, and the contention of Binns seems to involve that such date would of itself settle the question as to the period in which the distribution was made. For these reasons, I regret that I am unable to share Willmer, L.J.'s conclusion in favour of Binns upon this point. No doubt this result appears somewhat harsh, but the truth is, in my opinion, that a gross relevant distribution for the purposes of Section 38 connotes the sum, and nothing more, yielded by those provisions of the Act prescribing how it is to be calculated.

A further contention of the Company was that the " grouping notice " given by the House of Fraser on 6th January, 1954, applied just as much to the first of the two accounting periods later determined by the Commissioners under Section 38(4) as to the second. The first such period was the three months and one day immediately before Binns became a subsidiary of the House of Fraser, and Counsel for the Company quoted

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Section 30(2) of the Finance Act, 1956, as showing, by implication, that a " grouping notice " might be given, before that Section came into operation, which would embrace a period before the subsidiary and principal relationship came into being. For the Crown this was not denied. The answer of the Crown to the contention was, however, that it was not open on the language of the " grouping notice " itself, and that in any event that notice was given more than six months after the end of the accounting period in question, that is, 27th April, 1953, and that the Commissioners were not prepared to extend the time. The contention of the Company (which, if correct, would expunge all liability to Profits Tax upon Binns for the first of the two chargeable accounting periods in question) was put to Pennycuick, J., but rejected by him, and I think rightly. In the Court of Appeal it became absorbed, apparently, by the wider contention that the direction under Section 38(4) was invalid, and was thus not separately considered.

During the argument before your Lordships my noble and learned friend, Lord Reid, raised the question of the possible effect of a direction under Section 38(4) upon a " grouping notice " already given. Thus the direction might specify an accounting period ending more than six months before the date of the " grouping notice "—an interval which would invalidate the notice, unless the Commissioners granted an extension of time. Counsel for the Crown admitted that such a situation could arise and said that the discretion given to the Commissioners to extend the time for a " grouping notice " was intended to meet it. Nevertheless, in such a case the rights granted to principal and subsidiary in the matter of Profits Tax by Section 22(2) of the 1937 Act would become subject to the Commismissioners' discretion, contrary to the language of that provision. This, indeed, is an unsatisfactory feature of this legislation. It no doubt arises from the circumstance that delay inevitably occurs before the Commissioners are in possession of all the accounts and information they require before deciding whether to make any, and if so what, alterations in the chargeable accounting periods pursuant to Section 38(4) : but the difficulty is not incapable of remedy. Counsel for Binns claimed that it gave further support to his argument that no direction under Section 38(4) could alter a chargeable accounting period determined under the provisions of Section 20(2)(*a*) of the Finance Act, 1937. I have already given my reasons for not accepting this argument. Section 20(2)(*a*) is of general application to all trades and businesses ; Section 38(4) is of special application to businesses carried on by a subsidiary company ; and in those cases is, I think, paramount. This particular imperfection is not enough, in my opinion, to justify a different construction.

I have reached the conclusion that this appeal should succeed and the judgment of Pennycuick, J., be restored.

Questions put :

That the Order appealed from be reversed, and that the judgment of Pennycuick, J., be restored.

The Contents have it.

That the Respondent does pay to the Crown their Costs here and in the Court of Appeal.

The Contents have it.

[Solicitors :—Baileys, Shaw & Gillett ; Solicitor of Inland Revenue.]