P.C.
GDT

24, 1965

IN THE PRIVY COUNCIL

No. 53 of 1964

ON APPEAL

FROM THE HIGH COURT OF AUSTRALIA

BETWEEN:

MOBIL OIL AUSTRALIA LIMITED
(formerly called Vacuum Oil
Company Proprietary Limited)
(Appellant) Appellant

80963

- and -

10 THE COMMISSIONER OF TAXATION OF
THE COMMONWEALTH OF AUSTRALIA
(Respondent) Respondent

CASE FOR THE RESPONDENT

RECORD

INTRODUCTION

1. This is an appeal (pursuant to special leave granted by Her Majesty in Council on the 3rd day of July 1964) from a majority judgment of the Full High Court of Australia dated the 25th day of February 1964, disallowing an appeal p.134
20 by the Appellant from a judgment given on the 8th day of May 1961, by Taylor J. sitting in the original jurisdiction of the High Court of Australia. By his judgment Taylor J. disallowed pp.104-116
Appeals by the Appellant taxpayer against an assessment and an amended assessment of income tax and social services contribution for the year of income ended the 30th day of June 1953. pp.116,117

2. The question in issue is whether the Respondent Commissioner of Taxation wrongly
30 disallowed, pursuant to the Income Tax and

Social Services Contribution Assessment Act 1935-1953, as a deduction from the Appellant's assessable income for the year in question, the sum of £192,701, that being the aggregate of amounts claimed as deductions during the relevant year which were said to have been expended in or in connexion with the Appellant's activities to secure sites for the exclusive sale of the Appellant's products.

3. In considering the facts giving rise to this question it is necessary to refer to the manner in which the Appellant conducted its business prior to and up to relevant year in issue. At all material times the Appellant was engaged in the business of selling and distributing motor spirit and allied products to service station operators (who in turn sold the products to the public) in competition with other suppliers of such products. For some years prior to 1951 sales were made to service station operators mainly through "multi-pump" stations at which were installed tanks and pumps belonging to different competing oil companies and to which motor spirit was supplied by each of competing companies whose tanks and pumps were installed at any particular service station. Each operator thus offered to the public a choice of a number of different brands of motor spirit. The pumps and tanks remained the property of the oil companies concerned, and were subject to the right of the service station operator to give notice (one month) for them to be removed. In practice, the tanks were not removed, as there was in existence a trade convention by which a company which had received notice of removal would make its existing tanks on a particular site available to its successor. In August 1951 one of the Appellant's competitors - The Shell Company of Australia Ltd. - announced its intention to introduce immediately "a solo site scheme" whereby it would supply its products only to service station operators who purchased their requirements exclusively from it. Shortly after this move the Appellant put into operation a similar scheme for which it had by that time made tentative plans and all the other competing oil companies put into operation similar schemes.

4. The Appellant eventually decided that it would provide substantial financial inducements to service station operators at selected sites to obtain trading ties with those operators. The

Appellant accordingly did provide substantial financial benefits in return for agreements by service station operators to sell the Appellant's products exclusively. The Appellant provided dual benefits to operators. One form of benefit was by cash payments which are referred to below. The other was by the expenditure of a sum of money in minor structural improvements and additions, in driveway alterations, in painting and, in appropriate cases, the provision of a lubratorium. The amount which is in issue in this appeal, and which was expended in the year in question on the abovementioned items, other than the cash payments, represents £121,299 out of the total amount of £192,701 in issue, and is made up as follows:-

Alterations to concreting of driveways	£29,558
Structural alterations and repairs to buildings	78,239
Purchase and installation of plant and Equipment	4,900
Other miscellaneous expenditure	8,602
	£121,299

As Taylor J. found, expenditure on these items by the Appellant was one of the inducements held out by the Appellant to operators to join in the solo marketing scheme, and was part of the deal made with operators. The other form of inducement above referred to was by direct money payment to each operator, said to be made pursuant to one of two types of agreement termed "SS1-B" and "SS1-C" Agreements. Each provided inter alia that the operator would execute the Appellant's "Trading Agreement". By the "Trading Agreement" the operator agreed to buy from the Appellant exclusively all motor fuels intended by him for re-sale at his service station and that he would not sell from his service station any motor fuels except as should have been bona fide purchased by him from the Appellant. The Trading Agreement provided a specified period for its duration and that it should continue to run from the expiry of that period until determined by six months' notice in writing. It was the Trading Agreement which provided for the Appellant to make the minor structural improvements

p.116 ll.13-15

pp.192-198

and additions, the driveway alterations, the painting and the provision of a lubratorium above referred to and it was accordingly pursuant to the terms of the Trading Agreements that the above-mentioned sum of £121,299 was expended by the Appellant. This was part of the deal with the operator. But as above stated the operator also obtained the benefit of a direct money payment. Payments were said to be made pursuant to one or other of the two abovementioned forms of agreement, namely the "SS1-B" and "SS1-C" Agreements. Provisions of the "SS1-B" and "SS1-C" Agreements which were substantially similar in terms were in substance as follows:-

pp.192-198

(a) a covenant against the operator selling or disposing of the premises or of his business without first offering it to the Appellant on the terms and conditions of any proposed sale;

(b) a covenant that, in the event of the rejection of any offer made to the company under the preceding covenant, the operator would not sell or dispose of the premises or of the business unless the Appellant should approve of the proposed purchaser and unless that person should execute the company's form of trading agreement for a period of not less than the unexpired portion of the period currently fixed;

(c) a covenant that unless and until he should have disposed of the premises or business in conformity with the agreement the operator would remain personally in occupation of the premises;

(d) a covenant granting the Appellant the sole and exclusive advertising rights in relation to all parts of the garage or service station for the fixed period.

The most important manner in which the "SS1-B" and "SS1-C" contracts differed from each other were as follows:-

pp.192-195

(i) The "SS1-B" contract recited that the service station operator had requested the Appellant to lend him a specified sum of money and that the Appellant had agreed to do so on terms set out. The service station operator covenanted to repay the amount of the loan together with interest by equal monthly instalments comprising both principal and interest; the Appellant covenanted to pay the service station operator a specified sum of

money each month, a payment which, at the option of the Appellant, might be made by crediting the operator in the Appellant's books with the amount payable to him. In fact the amount of these monthly payments to be made by the Appellant to the service station operator was calculated so as to coincide precisely with the amount of the monthly payments of principal and interest which the service station operator had covenanted to make in repayment of the loan made to him. Many more "SS1-B" agreements were entered into than "SS1-C" agreements. The amount claimed to be expended by the Appellant pursuant to the "SS1-B" contracts during the year ended the 30th June 1953 was £57,265.

(ii) The "SS1-C" contract differed from the "SS1-B" contract in that it contained no provision for the loan of money by the Appellant to the operator nor did it provide for monthly payments to the operator by the Appellant; it made provision for annual payments by the Appellant to the service station operator over a fixed period of years so long as the service station operator observed the covenants of the contract and the trading agreement. Otherwise it contained provisions generally similar to those of the "SS1-B" contract. The amount expended by the Appellant pursuant to the "SS1-C" contracts during the year ended the 30th June 1953 was £9,637. pp.196-198

(iii) The sum of £4,500, being the balance of the sum of £192,701, was for legal expenses paid in introducing the "solo site" scheme, it being agreed by the Appellant and the Respondent that this sum be deemed to be attributed to the other items of expenditure proportionately and that it should be treated as deductible or not according as such items were treated.

In summary the following sets out how the sum of £192,701 claimed as a deduction is made up :

(a)	Payments paid pursuant to the Trading Agreements:	£121,299
(b)	Payments said to be paid pursuant to SS1-B agreements:	57,265
(c)	Payments paid pursuant to SS1-C Agreements:	9,637
(d)	Legal costs expended in relation to the introduction of the solo site scheme	4,500
		£192,701

5. The payments amounting to £121,299 made pursuant to the Trading Agreements were lump sum payments. In the case of both the "SS1-B" and "SS1-C" Agreements the total amount paid to each service station operator was the amount necessary to induce the operator to give a trade tie to the Appellant. The price which it was necessary from time to time to pay to obtain a tie was determined by the degree of competition for each site between the oil companies.

p.114 ll.13-19 6. As Taylor J. found, a "gallonage" factor, i.e. the gallonage of motor spirit sold or which might be sold from the site, played no part in determining the amount to be paid in any case. The Appellant when it wished to secure access to any particular site, was "forced to pay the price that attracted the reseller". When a deal took place the price was determined by the degree of competition for the site in question. At no time did the "gallonage" factor determine what should be paid.

7. As to the total amount of £192,701 which the Appellant claims to be an allowable deduction for income tax purposes under the four heads set out above, the Appellant contends that the amounts represent deductible outgoings chargeable to revenue. The Respondent on the other hand contends that none of the amounts claimed is deductible. The Respondent contends inter alia that the payments claimed to have been made pursuant to the "SS1-B" contracts were not in fact made or were not outgoings in fact and that the only payments made were the so-called loans and further that whatever payments were made were not deductible because they were outgoings of capital or of a capital nature or were alternatively

not deductible by reason of Section 260 of the Income Tax and Social Services Contribution Assessment Act. As to all the other payments the Respondent contends that the payments were outgoings of capital or of a capital nature and were not deductible. Further as to all the amounts claimed as deductions by the Appellant, the Respondent contends that they are not outgoings incurred in gaining or producing assessable income nor were they necessarily incurred in carrying on a business for the purpose of gaining or producing such income. As to moneys expended on repairs the Respondent contends that they are not deductible by reason of Section 53(2) of the Act.

Statutory Provisions

8. The sections of the Income Tax and Social Services Contribution Assessment Act (hereinafter referred to as "the Act") most material to the present case are :

(a) the definition of "allowable deduction" in Section 6(1) which is as follows:

"'allowable deduction' means a deduction allowable under this Act".

(b) the definition of "assessable income" in Section 6(1) which is as follows:

"'assessable income' means all the amounts which under the provisions of this Act are included in the assessable income".

(c) the definition of "taxable income" in Section 6(1) which is as follows :

"'taxable income' means the amount remaining after deducting from the assessable income all allowable deductions".

(d) Section 17 which is as follows:

"17. Subject to this Act, income tax and social services contribution at the rates declared by the Parliament shall be levied and paid for the financial year which commenced on the first day of July, One thousand nine hundred and fifty, and for each financial year thereafter, upon the taxable income derived during the year of

income by any person, whether a resident or a non-resident".

(e) Section 25 (1) which is as follows :

"25(1) The assessable income of a taxpayer shall include :

(a) where the taxpayer is a resident -

the gross income derived directly or indirectly from all sources whether in or out of Australia;.....

which is not exempt income".

(f) Section 51 (1) which is as follows:-

"51 (1) All losses and outgoings to the extent to which they are incurred in gaining or producing the assessable income, or are necessarily incurred in carrying on a business for the purpose of gaining or producing such income, shall be allowable deductions except to the extent to which they are losses or outgoings of capital, or of a capital, private or domestic nature, or are incurred in relation to the gaining or production of exempt income".

(g) Section 53 which is as follows:-

"53 (1) Expenditure incurred by the taxpayer in the year of income for repairs, not being expenditure of a capital nature, to any premises, or part of premises, plant, machinery, implements, utensils, rolling stock, or articles held, occupied or used by him for the purpose of producing assessable income, or in carrying on a business for that purpose, shall be an allowable deduction.

(2) Expenditure incurred upon repairs to any premises or part of premises not so held occupied or used shall not be an allowable deduction."

(h) Section 260 which is as follows:-

"260. Every contract, agreement, or arrangement made or entered into, orally or in writing, whether before or after the commencement of this Act,

shall so far as it has or purports to have the purpose or effect of in any way, directly or indirectly -

(a) altering the incidence of any income tax;

(b) relieving any person from liability to pay any income tax or make any return;

(c) defeating, evading, or avoiding any duty or liability imposed on any person by this Act; or

(d) preventing the operation of this Act in any respect,

be absolutely void, as against the Commissioner, or in regard to any proceeding under this Act, but without prejudice to such validity as it may have in any other respect or for any other purpose."

The Respondent's General Contentions

9. The following are basic features of the three forms of payments made by the Appellant.

(a) Payments pursuant to the Trading Agreements - £121,299

(i) The payments were lump sum payments made once and for all.

(ii) In return for the payments the Appellant secured an exclusive trading tie by the operator.

(iii) The payments were used to make capital improvements to the operator's premises.

(iv) The payments were not determined by the gallonage of petrol sold or to be sold from the site.

(b) Payments said to be pursuant to the "SS1-B" Agreements - £57,265

(i) The only real payment was of the lump sum which was not really a loan but an outright payment conditional upon performance of the agreement by the operator. At the most it was defeasible, in part only,

in the event of non-performance. The so-called periodic repayments by the operator and the so-called counterpayments by the Appellant were not really payable and were not in fact really made.

(ii) The amounts claimed as deductions were not losses or outgoings at all.

(iii) An unsuccessful attempt was made to spread the payments for tax purposes.

p.113 11.9-13 (iv) Alternatively, as Taylor J. held, the amounts the Appellant covenanted to pay the operator periodically constituted the payment of a lump sum by instalments.

(v) Alternatively by reason of Section 260 of the Act, the payment was a lump sum payment of the amount of the so-called loan and the other provisions of the agreements relating to payments were absolutely void as against the Respondent.

(vi) In return for the payments the Appellant secured an exclusive trading tie by the operator.

(vii) The amount of the total payment was in each case determined solely by competition for the site between the competing oil companies.

(viii) The payments were not determined by gallonage of motor fuels sold or to be sold from the site and were not equivalent to trade rebates or discounts.

(c) Payments pursuant to the "SS1-C" Agreements - £9,637

(i) In each case it was a lump sum paid by instalments.

(ii) In return for the payment the Appellant secured an exclusive trading tie by the operator.

(iii) The amount of the total sum was in each case determined solely by competition for the site between the competing oil companies.

(iv) The payments were not determined by

gallonage of motor fuels sold or to be sold from the site and were not equivalent to trade rebates or discounts.

10. All forms of payments and agreements involved the following essential characteristics:-

(a) The securing of retail outlets for the sale of the Appellant's products.

(b) The exclusion of the sale of any competitor's products at the site.

(c) The assurance that the Appellant's petrol tanks and pumps would remain on the site.

(d) Advertising rights for the Appellant on the site.

11. Further:

(a) The expenditure did not constitute ordinary incidents of the conduct of the Appellant's business.

(b) The whole of the expenditure was for the acquisition of capital assets bringing into existence a new trading or business structure - a change from one involving the use of multiple pump service stations, with liability to lose tanks, and competition on the site, to one of tied stations, fewer of them, elimination of competition on the site and exclusive advertising. The trade ties thus obtained were capital assets of an enduring nature.

(c) The expenditure resulted in the exclusion of competition from other oil companies on the sites of the tied service stations, which resulted in security of outlets at least for a number of years and possibly indefinitely; this advantage was of an enduring nature.

(d) The expenditure was not related in any real sense to purchases made from the Appellant; there was no obligation on the service station operator to purchase any required amount of motor spirit or gallonage, the determining factor being the amount of competition for a specific site; the expenditure was therefore not in the nature of a rebate or discount on purchases.

(e) The expenditure constituted the buying off of competition.

(f) The Appellant by the payments obtained an enlargement of its goodwill, an enduring benefit.

(g) The payment in each case was in the hands of the service station operator a receipt of a capital nature, and as it also conferred an enduring benefit upon the Appellant it was capital expenditure.

12. What the Appellant did was in effect to acquire by means of substantial payments exclusive outlets for the sale of its products. In considering whether or not the payments were capital payments, the basic considerations are the character of the advantage sought, the manner in which it is to be used, relied upon or enjoyed and the means adopted to obtain it (compare Dixon J. in Sun Newspaper Ltd. v. Federal Commissioner of Taxation 61 C.L.R. 337 at 363). In the present case all these considerations lead to the conclusion that the payments were capital payments. The character of the advantage sought and the manner in which it was to be used, relied upon or enjoyed were the obtaining of sites for the exclusive sale of the Appellant's products and ties with operators thereon; the means adopted were financial payments. The basic consideration is that the Appellant was buying these enduring benefits by financial payments. The fact that there was intense competition between oil companies for sites demonstrates that the ties were of considerable value. The fact that the price paid was determined by the competition for each site is also relevant as showing that the payments were not in the nature of rebates or discounts. In applying Section 260 to the "SS1-B" agreements, the Appellant's motives or reasons may be relevant to the question whether the device adopted of periodical payments and counter-payments was done for any of the purposes specified in that Section. But fundamentally, in determining whether the payments were of capital or a capital nature, the determining factor is the consideration that the Appellant purchased the enduring benefit of tied sites for the exclusive sale of its products.

13. All the payments were actually equivalent to purchasing the freehold of selling sites and are comparable to the following other capital expenditure by the Appellant:-

(a) During the year in question, the Appellant purchased sites for service stations for £866,678. p.94 ll.33-35

(b) During the year in question the Appellant made genuine loans to secure ties amounting to £1,289,250. p.91 ll.4-7

14. The payments and the agreements involved the bringing into existence of assets or advantages for the enduring benefit of the Appellant within the meaning of Viscount Cave's statement in British Insulated and Helsby Cables Ltd. v. Atherton (1926) A.C. 205 at 213.

(a) The agreements were in most instances for periods of 5 years or more, in some cases for 10 years. Of 258 "SS1-B" agreements 99 were for 10 to 15 years, 137 for between 5 and 9 years and of the remaining 22 all but one were for 3 years at least. pp.38 & 39 pp.213-221

(b) "Enduring" in this context does not mean "that the advantage which will be obtained will last forever"; see per Taylor J, in B.P. Australia Limited v. Commissioner of Taxation citing Latham C.J. in Sun Newspaper Ltd. v. Federal Commissioner of Taxation 61 C.L.R. 337 at 355.

(c) The tie for the payment held to be a capital payment in Strick v. Regent Oil (1964) 1 W.L.R. 1166 was for 10 years.

(d) The benefit here obtained was of a more definite character and more readily identifiable as such than the asset or advantage recognized by Viscount Cave as enduring in the Helsby Cables case (1926) A.C. 205, where the benefit was the goodwill of employees resulting from the establishment of a fund for their benefit - see per Taylor J. in B.P. Australia Limited v. Commissioner of Taxation.

(e) In any event the lump sum payments pursuant to the trading agreements for the capital improvements to the sites were made once and for all and were not recurring. Even so far as the "SS1-B" and "SS1-C" agreements are concerned, once a site had become tied to the Appellant the benefits were likely to endure indefinitely. Thus for example in a country town an oil company would often not need more

than one site. Once a situation emerged in which each of the major companies had its own site, it would not be likely to be interested in acquiring a further site and accordingly the tied operator would tend to remain tied after his original agreement had run out. He would be unlikely to be able to obtain any consideration from any other company and, if he did not continue to take supplies from the company to which he was originally tied, he would be in the danger of losing his whole business. Accordingly, the oil company to which he was originally tied would be in the stronger position and he would be wanting to remain with it. Thus, the benefits resulting from the original payments would be enduring.

p.103
pp.222-235

(f) The evidence of so called renewals of agreements in later years does not establish recurrence because those later agreements were in a different form and are not renewals in a true sense. The benefits of the original agreements endured beyond their terms.

(g) Other examples of capital payments for advantages for limited periods are to be found in the following cases and judgments:-

Henriksen v. Grafton Hotel (1942) 2 K.B. 184 (C.A. - The tenant of a hotel covenanted with the landlord to pay all charges which might be imposed in respect of the licences. Charges in respect of monopoly value imposed in respect of the re-grant of the licences for 3 years were held capital in nature and not deductible. Du Parcq LJ. said at pages 195-6:-

"It is true that the period for which the right was acquired in this case was three years and no more and a doubt may be raised whether such a right is, of 'enduring benefit' or 'of a permanent character'. These phrases, in my opinion, were introduced only for the purpose of making it clear that the 'asset' or 'right' acquired must have enough durability to justify its being treated as a capital asset..... 'Permanent' is indeed a relative term and is not synonymous with 'everlasting'. In my opinion the right to trade for three years as a licensed victualler must be regarded as attaining to the dignity of a capital asset .....".

In Sun Newspapers Limited v. Federal Commissioner of Taxation (1938) 61 C.L.R. 337 at page 362, Dixon J. said :

".....the lasting character of the advantage is not necessarily a determining factor. In John Smith & Son v. Moore (1921) A.C. 13, the coal contracts which Lord Haldane and Lord Sumner thought were acquired at the expense of capital had a very short term".

United Steel v. Cullington 23 T.C. 71 (C.A.) Payment to close down steel mills for 10 years held a capital payment.

15. By the payments and agreements the Appellant acquired or added to its "profit yielding subject" - per Dixon J. in Sun Newspaper Case 61 C.L.R. at 360 citing Lord Blackburn in United Collieries v. Inland Revenue Commissioners 1930 S.C. 215 at 220; 12 T.C. 1248 at 1254.

16. The payments and agreements involved the acquisition of goodwill of sites or the enlarging of the Appellant's goodwill. Payment for the acquisition or enlargement of goodwill is a capital payment. Here the Appellant's goodwill was enlarged through the establishment of a large number of service stations selling and advertising only the Appellant's brand of petrol. Compare:-

Compare:-

United Steel v. Cullington 23 T.C. 71 - Payment of £180,000 to a competitive company to close down for 10 years held to be a capital payment.

Collins v. Joseph Adamson (1938) 1 K.B. 477 - Purchase price of another company to close it down held a capital payment.

Sun Newspaper Ltd. v. Federal Commissioner of Taxation 61 C.L.R. 337. Payment for the purchase of a competing newspaper company to close it down held a capital payment. The Respondent relies upon the whole of the reasons for judgment of Dixon J. in this leading case.

17. The payments and agreements were made for the purpose of the removal or prevention of trade competition on the site or to buy off opposition of other trade competitors on a site and were accordingly capital payments. The competition and opposition here bought off were the competition and opposition of other companies' products being sold at the sites.

Compare:-

Associated Portland Cement v. Kerr 27 T.C. 103 -

Lump sum payment to directors with expert knowledge to prevent them competing held a capital payment.

Collins v. Joseph Adamson (1938) 1 K.B. 477 above referred to.

Sun Newspaper Ltd. v. Federal Commissioner of Taxation 61 C.L.R. 337 above referred to.

18. The transactions in the present case may be regarded as joint ventures between the Appellant and the re-sellers for the selling of petrol secured by money payments. Payments for such purpose are essentially capital in nature.

Boyce v. Whitwick Collieries 18 T.C. 655 where there was a joint adventure in the supply of water to the Council.

19. The correctness of the decisions of Taylor J. and of the majority of the Full High Court are, it is submitted, strongly reinforced by the reasons of the Court of Appeal in the recent decision in Strick v. Regent Oil Company Limited (1964) 1. W.L.R. 1166. The following summary of the facts of that case is taken from the judgment of Lord Denning M.R. at pages 1172 to 1173 of the report:

"There are three large suppliers of petrol in this country - Shell, Esso and Regent. Since the war there has been intense competition between them. Each of these three great companies has sought to get the owners of garages or filling stations to sell its brand of petrol only and not to sell the brands of others. Each seeks to get the retailer to sell its brand of petrol exclusively. The competition is so intense that they call it an 'Exclusivity war'. The retailers have not been slow to take advantage of this war between the giants. They have bid the one against the other. They ask each of the big companies: 'What will you pay me if I tie myself to your products?' In the early stages the inducement held out by each company was a simple rebate. The company would offer the retailer a rebate of a farthing or thereabouts on every gallon of petrol if he would promise to sell its brand to the exclusion of all others. The retailer would tie himself to the company offering the most rebate. Competition forced the rebates up. The next stage was that instead of a rebate the company

paid a sum in advance to the retailer each year according to the estimated gallonage for the coming year. So the retailer received cash in hand at the beginning of the year, and then at the end of the year the figure was adjusted up or down according to the gallonage actually supplied. The retailer would tie himself to the company offering the best advance payment. The third stage was, that instead of an advance for one year, the company paid a lump sum in advance for five or six years ahead; and this was adjusted up or down afterwards according to the gallonage sold. That was the stage reached in Bolam's case, (1956) 37 T.C. 56, where Danckwerts J. held that these advance payments made by a company were payments of a revenue nature. They were not capital expenditure. They could be deducted by the company in calculating its profits for tax purposes.

We have now reached a further stage. Some of the retailers have taken even greater advantage of their bargaining position. They have extracted from the oil companies a sum in advance which is not to be returned in any circumstances, and furthermore, in such a form that the retailers hope it will not be taxable in their hands. This form is known as 'lease-sub-lease'.

I will describe it by reference to one of the cases. FIRST, THE LEASE. Green Ace Motors Ltd. owned a garage and filling station in the Norwich Road, Ipswich. On June 11, 1956, Regent paid Green Ace Motors the sum of £5,000 which was described as 'paid by way of premium.' In return, Green Ace Motors demised to Regent the garage and filling station for 10 years from 13th May, 1955, at a rent of £1 a year. The £5,000 was calculated in this way:- It was estimated that Green Ace Motors would, during the 10 years, sell 1,200,000 gallons of petrol, and that the rebate on that gallonage would be at about 1d. a gallon. That comes to £5,000 over the 10 years. SECONDLY, THE SUB-LEASE. On the same day, 11th June 1956, Regent sublet the property back again to Green Ace Motors. They sub-demised it for 10 years less three days from the 13th May, 1955, at a rent of £1 a year. This sub-lease contained a specific covenant which tied Green Ace Motors to Regent. They covenanted that during the term of the sub-lease they would buy all

their requirements of motor fuels from Regent and they would not sell any fuel except that supplied by Regent. They covenanted also to keep the premises open for the supply of fuel and not discontinue business or reduce the number of pumps. They could only assign the premises if they got a responsible person who would covenant to observe the tie. THIRDLY, ADDITIONAL PAYMENT. On the same day, the 11th June 1956, Regent agreed that if during the 10 years Green Ace Motors bought from them more than 1,200,000 gallons, they would pay or allow by way of rebate a penny a gallon on every gallon over 1,200,000. In other words, if Green Ace Motors sold MORE than the estimated gallonage they were to receive extra payment. But there was no provision for any adjustment if they sold LESS than the estimated gallonage. There was no provision for a repayment of any part of the £5,000. Regent made similar agreements with the other owners of garages, but usually for longer terms of years and bigger payments. In some cases the sum paid was not described as a 'premium' but just as a 'sum'".

The case was heard before Mr. Justice Pennycuick who reversed the decision of the Special Commissioners of Income Tax that the payments were of a revenue nature. His Lordship held that the payments were of a capital nature. On appeal, the Court of Appeal consisting of Lord Denning M.R., Danckwerts LJ. and Diplock LJ. held unanimously (confirming Pennycuick J.) that the payments were of a capital nature. Lord Denning M.R. at pages 1174 to 1175 said:-

"Even if one looks at the transaction in a business sense one gets the same result. The payment was made so as to acquire an exclusive out-put for Regent's oil for a term of years. This was an asset of a permanent nature which would bring in revenue throughout the term".....

"Regent make a payment once and for all. In return they get an advantage which is of enduring benefit to them. It brings in revenue to Regent week after week, and month after month, from the petrol they supply to the retailer. I have no doubt this advantage is a capital asset and the payment for it is capital expenditure" .....

"These lump sums were not rebates. True it is they were calculated on the estimated gallonage,

but the measure of a thing is not to be confused with the thing itself. The yardstick is different from the cloth which it measures. We must look at these lump sums as they really were, payments for a permanent asset in the shape of an exclusive output of Regent's product, and as such they were capital payments."

Danckwerts LJ. at pages 1175 to 1176 said :-

"In two cases the lump sum is described as a 'premium' but in the other cases it is simply referred to as a sum of money".....

"The real purpose of the transactions is, of course, to secure a tie in the sense that the retailer and his petrol station are restricted to sale of Regent's products. This is an asset of commercial value in the fierce competition between the rival oil companies."

Diplock LJ. at pages 1176-1178 said :-

"But this is a case in which the substance follows from the form. The purpose of acquiring the interest in land, the head lease, was that there might be attached to it by means of the sub-lease to the dealer covenants by the dealer under which he would be compelled for the duration of the lease (which varied in the cases under consideration from five to 20 years) to buy his petrol exclusively from the taxpayer, Regent.

.....

"It seems to me plain that it was a capital sum expended to secure an advantage of enduring benefit during the period of the head lease."

.....

"What matters is whether or not they were moneys which were expended to obtain an enduring benefit for the trade, even though the benefit related only to a small part of the trade.

The reason I think that the commissioners have misunderstood or misapplied those citations is because in the next sentence they go on to say this :

'In our opinion these questions' - that is to say the questions they had extracted from

> Atherton's and Van den Berghs' cases - 'had to be answered having regard to the whole nature, extent and scope of Regent's trade, including the fact that the payments in question were not expected to secure an increase in Regent's share of the oil trade but only to maintain it.'
>
> With the greatest respect that was an irrelevant consideration. If a trader acquires a capital asset in order to carry on trade to produce his stock-in-trade or to enable him to sell it, it matters not whether he does it in the hopes of extending his business or of maintaining that business."

20. (a) The expenditure amounting to £121,299 made by the Appellant pursuant to the Trading Agreements, was for one of the following four purposes:-

(i) alterations to concreting of driveways,

(ii) structural alterations and repairs to buildings,

(iii) purchase and installation of equipment, and

(iv) miscellaneous expenditure.

(b) These payments were non-recurring and of lump sums made by the Appellant either to the service station operator or the contractor who did the work. They were clearly payments of lump sums to secure a tie.

(c) Further they were for structural alterations and they are accordingly of a capital nature. Two decisions support this submission - Boyce v. Whitwick Colliery Company Limited (1934) 18 T.C. 655 and Ounsworth v. Vickers Limited (1915) 3 K.B. 267. The first was a case in which a colliery and a council agreed that the colliery should supply the council with water for thirty years and the council should pay the colliery per annum one thirtieth of the cost of capital works erected by the colliery, the property in the work to pass to the colliery at the end of the thirty years period. The council sought to deduct the payment of one-thirtieth of the amount per annum as outgoings of revenue. The Court of Appeal held that they were capital payments made on the premises of another person. In Ounsworth's Case Rowlatt J. held that where a harbour authority had neglected the maintenance of a channel open to all shipping, and the respondents a shipbuilding firm undertook in conjunction with the harbour authority

to dredge the channel and paid the cost of part of such dredging, such expenditure was capital expenditure carried out on a site which the respondent did not own.

(d) In so far as the payments were for repairs, as they were for repairs on premises not held occupied or used by the Appellant, Section 53(2) makes them not deductible. Likewise the provisions of Sections 54 to 62 of the Act dealing with depreciation strongly suggest that money spent on plant or the making of structural improvements can never be an allowable deduction under Section 51 or otherwise, although in certain cases depreciation can be claimed.

(e) In so far as this expenditure amounting to £121,299 is clearly capital, so also are the payments associated with the "SS1-B" and "SS1-C" agreements, because the dual benefits to each operator thereby involved were part of the deal with him.

21. So far as the "SS1-B" agreements are concerned, Taylor J. held that what each agreement provided for was the payment of a lump sum by instalments. In the case of the "SS1-C" agreements he held that the periodical payments for which this class of agreement provided was simply an appropriate annual part of a lump sum agreed upon as the "price" of the trading advantages which it secured to the Appellant. Such payments, even where there is a break clause in the event of breach or termination, are still capital payments despite the fact they are paid by instalments. See:- p.113 ll.9-13 p.115 ll.26-34

United Steel v. Cullington 23 T.C. 71 (C.A.) A payment of £180,000 to close down steel works spread over 10 years by monthly instalments was held to be a capital payment. The payments were terminable in certain circumstances on breach (see page 80).

Green v. Favourite Cinemas 15 T.C. 390. A premium payable by quarterly instalments with a break clause was held to be a capital payment. The fact that the payment had a relation to earnings was held irrelevant (page 384).

Doncaster Amalgamated Collieries v. Bean 1 A.E.R. 642 (H.L.) Payment of the cost of

drainage works over 30 years by instalments was held a capital payment (see particularly per Lord Simon at page 645).

Boyce v. Whitwick Collieries 18 T.C. 655 (C.A.) Payment by the Council to the colliery of 1/30th of the cost of works per annum spread over 30 years was held none the less a capital payment.

Commissioner of Inland Revenue v. Adam (1928) S.C. 738; 14 T.C. 34 (Court of Session). Payment by cartage contractors of £3,200 by half yearly instalments of £200 each over 8 years in consideration of the right to deposit earth on land owner's land held a capital payment (cited with approval in Green v. Favourite Cinemas.)

Henriksen v. Grafton Hotel (1942) 2 K.B. 184 (C.A.). The payment there held to be a capital payment was £570 payable in 3 instalments of £190 per annum.

22. The Appellant claims that the payments were recurring and that this suggests that the payments were not capital payments. However -

p.103
pp.222-235

(a) Agreements in later years were in a different form and were not renewals in any true sense.

(b) In any event recurrence is not a test; it is no more than a consideration, the weight of which depends upon the nature of the expenditure (see per Dixon J. in Sun Newspaper case cited by Taylor J. in B.P. Australia Ltd. v. Commissioner of Taxation.)

(c) It has been authoritatively decided that if a payment is otherwise capital in nature the fact of recurrence does not alter its character. See :-

Hinton v. Maden and Ireland Ltd. 38 T.C. 391. A shoe and slipper manufacturer purchased knives and lasts which were necessary to the conduct of its business. Thousands of them were purchased and they had a short life each. None the less the purchase price was held to be a capital payment.

Rorke v. Commissioner of Inland Revenue

39 T.C. 194. It was held that payments by a company engaged in open cast mining to land owners for the right to enter upon their land as compensation for diminution in the value of the land were capital outgoings despite the inevitable necessity for recurring payments to other land owners once the land was exhausted. (See particularly at page 207). See also Stow Bardolph Gravel Co v. Poole 35 T.C. 459 and Knight v. Calder Grove Estates 35 T.C. 447.

(d) So far as "SSl-B" Agreements are concerned, the reason why the alleged payments were spread over the years was that the agreements provided expressly for cross payments or book entries month by month. The claims for deduction were spread over a series of years by reason of the terms of the very agreements.

23. Taylor J. decided, and the evidence clearly established, that the gallonage factor played no part in determining the amount to be paid in any case. The Appellant when it wished to secure access to any particular site was "forced to pay the price that attracted the reseller." When a "deal" took place the "price" was determined by the degree of competition for the site in question. As Taylor J. found, "It appeared clearly enough what was meant was that as competition increased it was possible by a series of ex post facto calculations to relate the 'prices' demanded and agreed upon to a rate per gallon which varied from .3 per penny per gallon to over 1½d. per gallon. But at no time did the 'gallonage' factor determine what should be paid." Further there was no obligation on the service station operator to purchase any required amount of petroleum products or gallonage and at no time did the gallonage factor determine what should be paid. The evidence was that in 1952 the Appellant's officers were prohibited by internal policy from putting the price on a gallonage basis. p.114 11.13-24 p.114 1.42 - p.115 1.2

These considerations all lead to the conclusion that the payments were capital in nature and not in the nature of trade rebates or discounts. See:-

Glenborg Union Fireclay Co. v. Inland Revenue Commissioner 12 T.C. 427 at 464 per L. Buckmaster. Green v. Favourite Cinemas Ltd.

15 T.C. 390 at 394. Strick v. Regent Oil (1964) 1 W.L.R. 1166 at 1175. The decision in Bolam v. Regent Oil (1956) 37 T.C. 56 is clearly distinguishable and was so regarded by the High Court. The payments there involved were the equivalent of a rebate and were related specifically to an amount calculated on the estimated amount of gallonage of petrol to be supplied during the currency of the agreement.

24. The decision of the High Court in Dickenson v. Commissioner of Taxation 98 C.L.R. 460 also supports the correctness of the decision of Taylor J. and the majority of the Full High Court in the present case. In that case, the question at issue was the assessability to a service station operator of two sums of £2,000 each combining to form one receipt of £4,000 from the Shell Company of Australia Ltd. Whilst the form of the agreements used was not the same as those under consideration in this appeal, it is submitted the purpose of them was the same. The Full Court held the payments made by the Shell Company when received by the service station operator were of a capital nature and did not form part of the operator's taxable income. It is acknowledged that the character in which a payment is received by the recipient does not conclude the character in which it is paid by the payer, but it is submitted that it is significant that the High Court held that these payments when received were capital receipts, and the characterisation of the payments is also very significant for the present appeal. Dixon J. said at page 474 "It may be that in a sense the sum of £4,000 was compensatory for the loss of future profits which the restriction might involve. It may be that it was meant as present payment by way of incentive to promote sales of the product derived from the single source. But if either or both of these elements formed part of the rationale of the payment, it amounted to a capitalisation of these elements." At page 491 of the report, Kitto J. expressed the view that "the ultimate result which the Shell Company sought was, of course, an increase in the sale of its products; but the actual transaction with which we are concerned was confined almost entirely to the exclusion of competitors from that part of the trade in petroleum products which would be done at the appellant's garage"; and at page 492 he remarked that it did not seem possible to regard the two payments made by the Shell Company as amounting to a rebate in advance against the price of the petroleum products to be purchased by the appellant. Again at page 482 Williams J. said

that "it was no doubt mainly to secure a monopoly for its products at that station that Shell paid the £4,000".

25. In a recent decision of Your Lordships' Board, Commissioner of Taxes v. Nchanga Consolidated Copper Mines Limited (1964) 1 A.E.R. 208 at page 212; (1964) 2 W.L.R. 339 at page 345 Your Lordships in discussing the tests to be applied for deciding whether expenditure is made on behalf of revenue or capital said:

> "These phrases are of course used with intended reference to earlier judicial decisions that distinguish between capital and income for the purposes of assessing profit. Since a question of capital or income is always capable of giving rise to a question of law, such a form of argument is unavoidable in any legal system that governs itself by appeal to precedent. Nevertheless, it has to be remembered that all these phrases, as for instance, 'enduring benefit' or 'capital structure' are essentially descriptive rather than definitive, and, as each new case arises for adjudication and it is sought to reason by analogy from its facts to those of one previously decided, a court's primary duty is to inquire how far a description that was both relevant and significant in one set of circumstances is either significant or relevant in those which are presently before it."

The Respondent respectfully submits that when the decisions of the majority of the Full High Court and Taylor J. are looked at in this appeal, it is clear that their Honours' judgments were in accordance with these statements of Your Lordship's Board.

26. So far as the "SS1-B" payments are concerned Section 260 of the Act produces the result that they are capital outgoings. If they had been lump sum payments they would clearly have been capital outgoings. The device of loans with repayments was obviously adopted to endeavour to achieve the result that the payments would be deductible. Both the purpose and the effect of the "SS1-B" agreements is to relieve the Appellant from liability to pay income tax (Section 260 (b)) or defeat, evade or avoid the liability to pay tax (Section 260(c)) or prevent the operation of the

Act (Section 260(d)). Accordingly the whole of the so-called loans are capital outgoings which are not deductible, the remainder of the payment provisions are void as against the Respondent and no portion of the periodical payments is deductible. See Newton v. Federal Commissioner of Taxation 1958 A.C. 450; Hancock v. Federal Commissioner of Taxation 108 C.L.R. 258.

27. In any event the payments claimed as deductions by the Appellant do not come within the first part of Section 51(1) of the Act. They were not outgoings incurred in gaining or producing the Appellant's assessable income and were not necessarily incurred in carrying on a business for the purpose of gaining or producing such income. What the Appellant did was to make payments to acquire a favourable position from which to earn income or to enter into arrangements that would yield income. This does not fall within any part of the opening language of Section 51(1).

Judgments of the High Court of Australia in this Appeal.

pp.104-116 Judgment of Taylor J.

In the present case the primary Judge, Taylor J. decided in favour of the Respondent. The hearing of this case before His Honour followed immediately after the hearing by His Honour of an appeal by B.P. Australia Limited against its assessment for income tax for the year of income ended on the 30th day of June 1952, in respect of similar deductions claimed for payments to service station operators, which formed part of the consideration for the operators' undertaking that they would for a fixed term of years deal exclusively in brands of petroleum products approved by B.P. Australia Limited and other marketers known as the "Independent Group" of which it was a member and partly in making payments to other marketers of petroleum products for the purpose of adjusting as between B.P. Australia Limited and other marketers, known as the "Independent Group", and of which it was a member, the total amounts paid by each member to service station operators. His Honour in his reasons for judgment in the present case made reference to his reasons for judgment in the appeal by B.P. Australia Limited in which he had delivered judgment on the same day and applied to the facts in the present case conclusions arrived at by him in that appeal. It will therefore be

necessary to refer to His Honour's remarks in that case, as well as commenting on his reasons in the present case.

29. In the B.P. Australia Limited Case His Honour said:- B.P. Record pp.164-178

(1) After stating the facts and analysing the various forms of agreements he described the purpose and effect of such agreements as being to secure a reselling outlet for the products of B.P. and those of the co-operating companies. B.P. Record p.171 ll.36-41

(2) That such an arrangement amounted to a trade tie, which was of considerable value to B.P. Australia Limited as there was intense competition among companies in the trade for "strategic" sites and that was the vital factor in determining how much should be paid to secure a particular site. B.P. Record p.171 l.42 - p.172 l.3.

(3) That it was inevitable that B.P. Australia Limited had to incur the expenditure because of the Shell Company's announcement, but this was not of much help in solving the problem whether the expenditure which was actually incurred was of a revenue or capital nature. B.P. Record p.172 ll.30-39

(4) He rejected the submission that the circumstances of the trade became such as to make payments of the character in question ordinary incidents of B.P. Australia Limited's business. He also rejected the contention that the payments should be characterized as revenue expenditure solely on the ground that the changed trading conditions made multiple outlays necessary to secure trade ties and referred to the statement of Dixon J. (as he then was) in Sun Newspapers Limited v. The Federal Commissioner of Taxation 61 C.L.R. 337 that "Recurrence is not a test, it is no more than a consideration the weight of which depends upon the nature of the expenditure." B.P. Record p.173

(5) He rejected the Appellant's submission that the language of Viscount Cave in British Insulated and Helsby Cables Ltd. v. Atherton (1926) A.C. 205 did not apply, as the expenditure was not made with a view to bringing into existence any asset or advantage for the enduring benefit of the Appellant's trade. He observed:-

"But the contention does much less than justice to those arrangements ..... In B.P. Record p.173 l.49 - p.174 l.39

terms, the contractual arrangements did not bind any service station operator to purchase any, or any stated quantity of, motor spirit from the appellant though it is beyond doubt that it was contemplated that purchases would be made and the operator's promise to increase the sales of C.O.R. products to the best of his ability proceeds on this basis. But the real substance of the arrangements is to be found in the exclusion from sale on the subject premises of brands of motor spirit other than those approved of by the appellant. To the extent specified in the contract an operator was bound to suffer 'a substantial or enduring detraction from pre-existing rights'. Dickenson v. Federal Commissioner of Taxation (1958) 98 C.L.R. 460 at p.492. The appellant did not, of course, succeed to these rights but it seems clear to me that it did obtain a great deal more than the contention under consideration acknowledges. First of all, it was implicit that the payment in each case was intended to secure that the appellant's pumps and tanks should remain on the subject premises undisturbed for the period agreed upon. Secondly, it was implicit that the appellant's product would be sold on the site for that period and finally, by the stipulation that no brands of motor spirit other than those approved by the appellant should be sold on the site, substantial freedom from competition on each selected site was secured to the appellant for periods extending from three to ten years. To say, as the appellant does, that this was neither an asset nor an advantage for the enduring benefit of its trade would be, in my view, to give the lie to a great number of decisions since Viscount Cave's dictum was first promulgated".

(6) He said further that although the value of the tie in relation to any particular site bore some relation to its trading potential, there could be no doubt that the amounts expended were determined by the intensity of the competition and the lump sums which were paid were laid out by one or other of the competitors to secure the resultant advantage for periods of years. He said :-

B.P. Record p.175 ll.27-32

"If there were nothing more in the case I should entertain no doubt that expenditure so made by the Appellant was expenditure of a capital nature in spite of the fact that there was a multiplicity of payments during the relevant year."

(7) He then rejected B.P. Australia Limited's submission that the payments made by it represented trade rebates or discounts because the Company took into account the "gallonage" factor in deciding what amount it thought economical to expend to secure a tie. He examined the Company's claim in this regard and found that although "gallonage" was one of the factors in determining whether any particular proposal should be entertained the "gallonage" factor played no greater part than this and he found on the evidence that the lump sums paid were not paid either in form or substance as the equivalent of trade rebates or discounts. The quantum of each payment was determined by reference to the competition between the oil marketers. The payments which were made had no real relation to gallonage. He concluded therefore that the decision in Bolam v. Regent Oil Co. Ltd. 37 T.C. 56 was not applicable. The payments were lump sums for the purpose of securing trade ties for a period of years and the amount paid was a capital outgoing for the purpose of obtaining the resultant advantage.

B.P. Record pp.175-177

30. In the present case His Honour said :-

(1) After reviewing the facts and analysing the substance of the three types of agreement pursuant to which payment had been made by the Appellant he rejected the argument that the payments constituted ordinary marketing costs properly attributable to the Appellant's trading account.

pp.104-111

(2) He said that the payments in question and the circumstances in which they were made indicated a close parallel to the B.P. Case: indeed the facts were such that if it were concerned merely with lump sum payments made once and for all in each particular case it would be sufficient to say that for the reasons given in the B.P. Case the appeal should be dismissed.

p.111 ll.31-40

(3) However he went on to say that that was not the fact and that some attention needed to be given to the circumstances in which the expenditure was incurred by the Appellant. He then set out the three heads of expenditure made pursuant to the agreements in issue.

p.111 ll.40-42

p.111, l.43 - p.112, l.9

(4) In respect of the payments pursuant to

p.113, ll.9-19 the "SS1-B" contracts, he said it was clear that what each agreement provided for was the payment of a lump sum by instalments. It was beyond doubt that the amount of the advance in each case was not in any way measured by the service station operator's desire to borrow a specified sum of money, nor was, so far as the operator was concerned, the Appellant in the market to lend money.

He said :

p.113, ll.19-32

> "What the appellant wished to do was to secure trading ties for fixed periods and in the circumstances of the trade as it existed at the relevant time it became necessary to expend large sums of money to secure these advantages. What it was necessary from time to time to pay to secure these advantages was determined by the degree of competition for each site. And the amount of the advance in each case was determined not by the operator's need for some specified amount of borrowed capital but solely by the 'price' which competition made it necessary for the appellant to pay for the advantages which it wished to secure."

p.113 ll.32-40 However, he said the Appellant was not prepared to pay in advance and unconditionally a lump sum for a trade tie, extending over a period of years, but was prepared to pay the same by instalments spread over the relevant period and in the meantime to make available to the service station operator

p.113 ll.46-49 an amount equal to the lump sum involved. He then said the amounts payable under the "SS1-B" contracts were in no way related to or dependent upon the quantity of petrol which might be purchased by any operator. He then rejected the Appellant's submission that the amounts paid were based on a "gallonage" factor. He said :

p.114 ll.14-19

> "But it is beyond doubt that this factor played no part in determining the amount to be paid in any case. In fact the appellant when it wished to secure access to any particular site, was 'forced to pay the price that attracted the reseller'".

Others of His Honour's findings on this aspect are set out or referred to above in this Case.

p.115 ll.17-37 (5) In respect of the payments pursuant to the "SS1-C" contracts His Honour said that the agreements provided for the making of an annual

payment to the operator in respect of each period of twelve months during which the operator remained personally in occupation of the service station and as such were not distinguishable from payments under the "SS1-B" contracts. He said:

> ".....but it is, I think, again clear from the evidence that the periodical payments for which this class of agreement provided was simply an appropriate annual part of a lump sum agreed upon as the 'price' of the trading advantages which is secured to the Appellant. That being so I can see no real distinction between moneys paid under that form of contract and moneys paid under contracts in the form SS1-B". p.115 ll.28-37

(6) He then said that the fact that the Appellant made the payments under both forms of contract by instalments did not distinguish the present case from the B.P. Case and that the amounts so paid out were not deductible for the purposes of ascertaining the Appellant's taxable income. p.115 l.38 - p.116 l.5

(7) He reached the same conclusion in respect of the sum which was expended by the Appellant on structural alterations and the supply of plant in converting service stations to conform to the minimum requirements of the Appellant. He said :

> "The evidence showed that expenditure of this character was undertaken as 'part of the deal' made with operators who became parties to SS1-B and SS1-C agreements. It was, in fact, one of the inducements held out to operators to join in the solo marketing scheme ..... Such expenditure must, in my opinion, be regarded as expenditure of a capital nature." p.116 ll.10-21

(8) He said that the legal expenses must share the same fate, and thus characterized all of the expenditure in issue as of a capital nature and disallowed the appeal. p.116 ll.28-32

JUDGMENTS IN THE FULL COURT

31. In the Full Court there was a division of opinion. The majority consisting of McTiernan, Windeyer and Owen JJ. held that the deductions claimed were incurred on account of capital and pp.121-134 p.122 pp.124-125 pp.125-134

were properly disallowed, and dismissed the appeal. The then Chief Justice Sir Owen Dixon and Kitto J. took a contrary view and held that the deductions were incurred on account of revenue and should have been allowed by the Respondent and they would have allowed the appeal.

pp.121-122
pp.123-124

32. The Respondent in this case instituted an appeal to the Full Court, as did B.P. Australia Limited, and those appeals came on for hearing before the Full Court constituted by the Judges mentioned in paragraph 31 herein. The appeal by the Appellant in this case was heard first and the appeal by B.P. Australia Limited followed thereafter. Certain of their Honours in giving separate reasons for judgment in each of the two appeals made reference to their reasons for judgment in the other of these appeals for the purpose of adopting the whole or portion of these reasons.

pp.121-122

33. The decision of the then Chief Justice (who dissented).

(1) His Honour stated that the appeal was governed by the same considerations as governed the appeal of B.P. Australia Limited, his reasons in which he referred to, and said that the expenditure in question was made on behalf of revenue.

(2) His Honour said :

p.122 ll.14-19

> "It appears to me clearly expenditure incurred in the process of marketing the commodity and to be expenditure which is not made once for all, but is likely to be repeated, and not to be sufficiently identified as outside the ordinary conduct of business".

B.P. Record p.186 ll.41-45

(3) In the B.P. Case His Honour after reviewing the facts stated the actual nature and amount of the expenditure was more important in determining its character than the motives which led those who made the expenditure to adopt a particular form or course of business.

(4) In the B.P. Case His Honour said that the changes in the conduct of the Appellant's selling business seem to be of a more or less enduring character but he went on to say that as he understood the matters in issue the company was engaged in its activities to obtain a definite market among the public by one means or another and was doing so in

the course of conducting its business of disposing of petrol which it was able to acquire or import. He said :-

> "I do not think it was acquiring a capital asset or doing any more than so conducting its business on revenue account as to increase it and make as certain as it could that its business was continuing and also would continue, if possible, to expand. For my part I cannot think that all the course adopted changed the character of the transactions of the company from those of a continual attempt to establish its product in a consumers' market and to meet all the obstacles which arose in a long and rather troubled period to obtaining a reputation for its product".

B.P. Record p.190 ll.1-12

His Honour did not think there was any specific expenditure in increasing any element in the profit earning instrument under the company's control. Accordingly His Honour thought the appeal should be allowed.

B.P. Record p.190

It is respectfully submitted that His Honour's judgment is in error for the reasons given throughout this Case and because:-

(a) His Honour overlooked the basic consideration which was stressed by Taylor J. that the objective or the purpose being to sell the company's products, that objective could have been achieved by way of capital payments or by way of revenue payments.

(b) He confined his decision to the question of objective which was to sell the company's products, but he did not give consideration to the mode of achieving the objective nor to the lasting benefit achieved.

(c) He erred in saying the objective or purpose of the selling of the company's products demonstrated that the payments were revenue payments.

(d) He erred in confining himself to looking at what was the business activity of the company and saying that the company wanted to extend or maintain its business or sales and not going on to consider the means by which the company achieved this objective and what benefit the company thereby achieved : such as was it a permanent or enduring benefit?

(e) He failed to advert at all to the real purpose of the transactions, that is, that they were to secure a tie, in the sense that the retailer and his service station were restricted to the sale of the company's products. This was an asset of commercial value particularly in the light of the fierce competition which prevailed between the rival oil companies. That is, he failed to look at the aspect of the advantage obtained - the obtaining of goodwill or the buying off of competition, and he failed to appreciate that this was an enduring advantage.

(f) He failed to appreciate that the acquisition of solo sites amounted to a complete reorganisation and change in the structure of the Appellant's trade.

B.P. Record p.189 11.5-8

(g) His statement in the B.P. Case that "There is no dispute that the sum represents expenditure in advancing or promoting the sales of petrol nor indeed that an increased volume of selling business followed" is not correct because it was contended that the payments did not fall within the first part of Section 51 (1) and the evidence did not justify a conclusion that an increased volume of selling business followed.

p.122

34. The decision of McTiernan J. (one of the majority)

McTiernan J. agreed in all respects with the views expressed by Taylor J. and said that the findings of fact were supported by the evidence; that Taylor J. correctly applied the criteria laid down in the decided cases for distinguishing between payments on income and capital accounts respectively.

pp.123-124

35. The decision of Kitto J. (who dissented)

B.P. Record pp.191-197

(1) His Honour stated that the reasons he gave in the B.P. Case applied in substance to the present case, and said there were only two additional matters he wished to comment on to re-inforce his conclusion in that case.

(2) In the B.P. Case His Honour stated that the choice to be made in describing the expenditure in question was -

B.P. Record p.191 11.22-24

(a) as expenditure "upon establishing replacing and enlarging the profit yielding subject, the profit making machine," or

(b) as expenditure "though unusual, for a purpose falling within the conduct of the trade". B.P. Record p.191 ll.28-29

(3) He said the first view could be supported either by regarding the expenditure by the Appellant as the purchase of freedom from competition on a particular site or as the cost of purchasing or equipping itself with a new market in the place of one which had been destroyed or was being destroyed by the actions of competitors, it being assumed that once a service station ranged itself with an oil company it would be likely to remain with that company more or less permanently. His Honour rejected these two bases. B.P. Record p.191 l.37

(4) He rejected the first basis because he said the Appellant was not eliminating competition in order to create a more favourable situation in which to carry on its trade but on the contrary the undertaking given by the service station operator was only the negative side of the substantial positive advantage which the Appellant obtained namely that the Appellant would secure the particular sales which would be necessary for the satisfaction of the service station's requirements of the period. Thus the expenditure was part and parcel of the business of effecting sales of its products and was prima facie part of the cost of selling the goods and not a capital expenditure. B.P. Record p.192 l.41

(5) As to the second basis His Honour said that the change in the wholesale trade in motor spirit from the old system of multiple pump service stations to the new "solo" system meant that every oil company if it wanted to sell motor spirit to service stations in the future, had to accept the necessity of spending money, not at the beginning once and for all, but at the beginning and from time to time, to ensure it would receive from as many service stations as possible the whole of their orders for limited periods. The expenditure by the oil company to get its quota of stations during the months in which the market was in the throes of arranging itself initially, was simply part of the expenditure to which that B.P. Record p.193 l.42

company's participation in the new system committed it as a regular feature of its selling activities. The advantage obtained was not a new market, not a new framework within which to carry on trade for the future, nor was it an addition to goodwill by the buying off of competition, but was the practical assurance of receiving bundles of orders for motor spirit in the future. Thus "gallonage" was not a governing factor in deciding or fixing the amount of expenditure, but only a factor to be taken into account with the monopoly obtained, in fixing the amount to be paid in the cost of obtaining orders for the spirit to be supplied during the relevant term of the agreement. Thus such a sum paid was from an accounting point of view a marketing cost in the securing of orders.

B.P. Record p.197 l.30

(6) His Honour for these reasons held that the outgoings in the B.P. Case were not of a capital nature but were of the nature of trading expenses to be allowed for in the ascertainment of the profits from the carrying on of the Appellant's business.

(7) His Honour, as stated, said there were two additional matters in the present case which re-inforced his conclusion in the B.P. Case.

p.123 l.23

(8) The first was the evidence of the need as "a continuing operation" to obtain new and renewed agreements with operators and the need to accede to the giving of concessions in the form of money payments to such operators which was part of the process of getting the business of selling the goods, under the newly accepted method of trading; therefore cost of the concessions must be taken into account in ascertaining the profit from the business.

(9) The second was that the amounts paid periodically to the operators, monthly under the SS1-B agreements and yearly under the SS1-C agreements, were not instalments of a principal sum, but were rewards by the Appellant to the operators for their due performance of the agreements during any relevant month or year. He said:

p.124 ll.9-14

"The Appellant had embarked upon a course of securing orders by making payments to its

customers and every payment that it made must necessarily, it seems to me, be regarded as having diminished the profit from the orders obtained".

(10) Accordingly His Honour held that the outgoings in question were not of a capital nature and should have been treated as allowable deductions in the assessment of the Appellant's tax. p.124 ll.15-18

It is respectfully submitted that His Honour's judgment is in error for the reasons given throughout this Case and because -

(a) He decided that recurrence of payments to service station operators was significant. Recurrence is not a test, it is no more than a consideration the weight of which depends on the nature of the expenditure. Further, the amounts paid pursuant to the "SS1-B" and "SS1-C" agreements in the year in question only amounted to £66,902 out of a total expenditure of £192,700 claimed as a deduction. In any event the benefits obtained under the "SS1-B" and "SS1-C" agreements endured for indefinite periods and the later agreements were not really renewals because they were on different terms. In any event recurrence does not point against the conclusion that the payments were of a capital nature.

(b) He overlooked the significance of the fact that far the greater portion of the payments made were lump sums to secure and tie service station operators and they were also payments used for capital purposes namely to produce alterations in the structural set-up of other persons' premises and the purchase of equipment for operators' sites.

(c) He did not give due weight to the fact that the moneys expended were for ties which were enduring benefits, in the sense of permanent assets in that once a service station became tied it would tend to continue to remain so, as once a site was acquired in a settled area in competition with other oil marketers, the resellers' advantage had disappeared.

(d) Decisive circumstances to which His Honour did not give proper significance were

that :

(i) by the acquisition of sites valuable rights were acquired for the sale of the Appellant's products to the exclusion of the sale of competitors' products on those sites;

(ii) the acquisition of sites amounted to the buying off of competition for a period of years;

(iii) the acquisition of sites gave the Appellant freedom from the competition of competitors' products being sold on the sites and this amounted to a complete re-organisation of and change in the structure of the Appellant's trade;

(iv) by the acquisition of sites the Appellant obtained the goodwill of the selling sites and thus enlarged its goodwill by having service stations selling only its products.

(e) In failing to recognise the significance of the enduring benefits obtained from the payments, he overlooked the significance of Viscount Cave's dictum approved by Latham C.J. in Sun Newspapers Ltd. v. Federal Commissioner of Taxation 61 C.L.R. at page 355, that "enduring" does not mean "that the advantage which will be obtained will last forever".

pp.124-125 36. The decision of Windeyer J. (one of the majority)

(1) His Honour was of the opinion that the conclusion reached by Taylor J. was correct and said that he also had read the remarks of Owen J. and agreed with his examination of the facts. Consequently he did not analyse the transactions which the Appellant adopted for obtaining the advantage it gained by the expenditure of the moneys in question but said :

p.124 ll.32-40 "In a business sense, and using the language of 'merchandising' it seems to me that, in each case, it obtained for a period and in a selected locality an assured 'outlet' to consumers for its products. Having regard to the competitive character of the trade in which it was engaged and to the whole of the circumstances, I think that the expenditure was of a capital nature."

(2) His Honour then referred to his reasons in the B.P. Case and adopted them for the purposes of this Appeal. In that case he said he agreed with Taylor J's. decision and wished to say very little.

B.P. Record pp.198-199

(3) In the B.P. Case after referring to decided cases on the question of whether expenditure is capital or revenue he said :

(a) "The character of a questioned item of expenditure must, I think, depend primarily upon its purpose. Regard ought therefore to be had to what it was sought to acquire and to the relation of that to the taxpayer's undertaking or business ..... In other words it was what the particular taxpayer got for his money, rather than how he got it, that is important."

B.P. Record p.199 11.3-12

(b) He agreed with Taylor J. that the payments were made to secure for the agreed period a reselling outlet for the Appellant's products.

B.P. Record p.199 11 20-23

(c) The Appellant met a new situation in trading by setting up a system of tied service stations and by such arrangements obtained, for a substantial period, "and I would suppose with a prospect of renewal thereafter something that was to become a part of the structure, organisation or frame-work within which, and by means of which, the Appellant carried on its business. He accordingly dismissed the appeal.

B.P. Record p.199 11.43-47

37. The decision of Owen J. (one of the majority)

pp.125-134

Owen J. did not refer to the B.P. Case and after reviewing the facts and analysing the various agreements dismissed the Appellant's appeal.

(1) His Honour said the payments made varied from station to station and it was the original intention of the Appellant to determine the amount to be paid under

p.128 1.43 - p.129 1.12

"SS1-B" and "SS1-C" agreements by estimating the probable number of gallons of its petrol likely to be resold at the sites it acquired.

p.129 11.30-35 His Honour agreed with Taylor J. that the "estimated" gallonage for any particular service station was no more than a factor and no doubt an important factor in deciding what sum it would be economically sound to lend or pay to a particular service station operator.

p.129 11.26-29 His Honour found at no time did the Appellant's arrangements with operators provide for a rebate or discount on the price of the petrol supplied.

p.130 1.49-p.131 1.3 (2) His Honour held that the transactions were real transactions intended to be and in fact carried out according to the terms of the documents.

p.132 11.15-29 (3) His Honour was of the opinion that the fact that it became necessary to obtain trade ties in order to secure outlets did not assist in characterizing the nature of the exoenditure, as the establishment of a "solo site" system might be by the purchase of service stations which would obviously be of a capital nature or it may take the form of a rebate on the price of petrol supplied, which might be regarded as chargeable against revenue.

p.132 11.32-43 (4) His Honour said that the difficulty in characterizing an outgoing as being on capital or revenue account lay in the fact that no definite criterion has been or can be laid down which would enable that question to be answered with certainty in all circumstances. He said a number of tests have been suggested none of which could be conclusive; they were no more than indications of the category into which a particular outgoing should be placed.

p.132 1.44 - p.133 1.14 (5) His Honour then referred to the dictum of Dixon J. (as he then was) in the Sun Newspaper Case 61 C.L.R. 337 at pages 359-363 and said in considering the test questions of degree must inevitably arise. However, he considered that one important test was "the character of the advantage sought and in this its lasting qualities may

play a part" (as per Dixon J. in Sun Newspaper Case supra).

(6) Although His Honour thought all the outgoings in the present case were of a recurring nature he said :

"But when an examination is made of the character or nature of the advantage gained by the appellant by the making of all these payments, the balance seems to me to tilt in favour of the view that the outgoings were of a capital nature. The expenditure on structural and the like improvements to service stations was made in return for the operator's undertakings to deal exclusively in the appellant's products and give it exclusive advertising rights on the station site for a substantial period of time. The monthly payments under the SS1-B agreements and the annual payments under the SS1-C agreements were made in return for the carrying into effect of those undertakings in respect of the periods for which those payments were made. The advantages thus obtained were of a continuing and not of a transient nature. The purpose or effect of the expenditure seems to me to have been to add valuable, even if intangible, assets of a lasting character to the appellant's profit earning organization." p.133 l.34 - p.134 l.7

(7) His Honour accordingly agreed with Taylor J. and dismissed the appeals. p.134 ll.8-17

38. CONCLUSION

The Respondent therefore submits that the decision of Taylor J. and the Full Court of the High Court was correct and should be affirmed for the following among other

R E A S O N S

(1) The reasons of the majority of the Full Court and Taylor J. were right and the reasons of Dixon C.J. and Kitto J. were incorrect.

(2) The decisions of the majority of the Full Court and Taylor J. are in accordance with well established and well known principles

laid down by the decisionsof Your Lordships' Board, the House of Lords and the High Court of Australia.

(3) The decisions of the majority and Taylor J. accord with the reasoning of Your Lordship's Board in the Nchanga Case.

(4) The reasoning in the recent decision of the Court of Appeal in Strick v. Regent Oil strongly supports the correctness of the decision of the majority in the Full High Court and of Taylor J.

(5) The payments for alterations to driveways, structural alterations, repairs to buildings and the purchase of plant totalling £121,299 (being by far the greater portion of the payments) were all lump sum payments payable in advance with no refund to be made, as part of a deal to secure and tie a service station operator for a period of years and were enduring benefits in the sense of permanent benefits in that once a service station operator became tied to the Appellant he would tend to continue to remain tied and were payments expended on capital outlays on the operator's site.

(6) The Appellant by all the payments acquired valuable rights to have retail outlets for a period of years at least, plus the exclusion of the sales of any of its competitors' products and the assurance that its tanks and pumps would remain on the sites, and advertising rights.

(7) These rights were enduring for the periods agreed upon and were likely to continue to endure thereafter.

(8) Such benefits or rights are clearly the obtaining of capital advantages and are within the concept of Viscount Cave's dictum in the Helsby Cables Case.

(9) The payments were not paid as the equivalent of trade rebates or discounts on gallonage sold or to be sold and as such were distinguishable from the payments in Bolam's Case where the payments were adjusted up or down to the gallonage sold.

(10) The quantum of the payments made fluctuated with the competition for a particular site, and the strategic nature of the site determined the quantum of the payment.

(11) The payments involved the acquisition of goodwill of sites. The Appellant acquired the goodwill of reselling sites which enlarged its goodwill generally.

(12) The payments were for the purpose of the removal or prevention of trade competition on the site or to buy-off opposition of other trade competitors on a site.

(13) Recurrence of payments is not a test, it is no more than a consideration, the weight of which depends upon the nature of the expenditure. In any case the majority of payments being for improvements were not renewed being payments made once and for all and there was no renewal in any true sense of any of the agreements. p.103 pp.222-235

(14) In any event "recurrence" (if there was recurrence in the true sense) does not point against the conclusion that the payments were of a capital nature, particularly when the benefit obtained and the means of obtaining it are looked at.

(15) The alleged payments pursuant to the "SS1-B" agreements were either payments of lump sum payments under the guise of loans or were not outgoings at all or alternatively were lump sums paid by instalments and on any view were capital outgoings.

(16) Alternatively the payments pursuant to the "SS1-B" agreements were capital payments by reason of Section 260 of the Act.

(17) The payments pursuant to the "SS1-C" agreements were lump sums payable by instalments.

(18) All expenditure was made by the Appellant in increasing the profit earning structure, organization or framework under its control.

(19) So far as the payments were for repairs they were not deductible by reason of Section 53(2) of the Act.

(20) None of the payments fell within the first part of Section 51 (1) of the Act.

C.I. MENHENNITT

R.L. GILBERT

No.53 of 1964

IN THE PRIVY COUNCIL

O N A P P E A L

FROM THE HIGH COURT OF AUSTRALIA

B E T W E E N

MOBIL OIL AUSTRALIA LIMITED (formerly called Vacuum Oil Company Proprietary Limited) (Appellant) — Appellant

and -

THE COMMISSIONER OF TAXATION OF THE COMMONWEALTH OF AUSTRALIA (Respondent) — Respondent

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CASE FOR THE RESPONDENT

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