

TD 94/D109 - Income tax: what is the significance of the Archer Brothers principle in the context of liquidation distributions?

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Draft Taxation Determination

Income tax: what is the significance of the *Archer Brothers* principle in the context of liquidation distributions?

1. In a joint judgment, the Full High Court of Australia in *Archer Bros Pty Ltd (in vol liq) v. FC of T* (1952-53) 90 CLR 140 at 155; 10 ATD 192 at 201 observed by way of **obiter dicta**:

'By a proper system of bookkeeping the liquidator, in the same way as the accountant of a private company which is a going concern, could so keep his accounts that...distributions could be made wholly and exclusively out of...particular profits...or income...'.

2. These observations have given rise to the so-called *Archer Brothers* principle. The principle is that where a liquidator appropriates (or 'sources') a particular fund of profit or income in making a distribution (or part of a distribution), that appropriation ordinarily determines the character of the distributed amount for the purposes of section 47 and other provisions of the *Income Tax Assessment Act 1936* (the Act). Generally we accept that a liquidator may rely on the *Archer Brothers* principle, except where a specific provision in the Act produces a different result (e.g. the rules in section 160ZLA that specify the order in which different types of funds are distributed).

3. The judicial dicta quoted above refers only to the selection of particular 'profits' or 'income'. However, where a liquidator makes a distribution returning an amount representing capital actually contributed by shareholders, we accept that the principle applies even if the funds used to return the amount were from an income or profit source. We do not consider that the decision in *Glenville Pastoral Co Pty Ltd (in liq) v. FCT* (1963) 109 CLR 199 is authority for a contrary view.

Note: although we accept that the *Archer Brothers* principle is of general application, we reserve the right, in appropriate cases, to look behind the accounting entries to the substance of a distribution for tax purposes. For example, we may do so where a liquidation distribution is effected from an asset revaluation reserve but the funds distributed represent, for tax purposes, a capital gain on the disposal of the revalued asset.

4. For the *Archer Brothers* principle to operate we require that:

- (i) the company accounts have been kept so that a liquidator can clearly identify a specific profit or fund in making a distribution; and
- (ii) the liquidator actually appropriates the specific profit or fund in making the distribution, either in the accounts or in the statement of distribution.

5. It has been suggested that, for the *Archer Brothers* principle to be available, separate accounts must have been kept for each specific fund or profit in order for the liquidator's appropriations to be unequivocally from a given fund or profit. Although the maintenance of separate accounts makes it easier to identify the source of a distribution, we do not consider that separate accounts are essential if the liquidator is able to identify a fund or profit from which a distribution is made. For example, where pre-CGT non assessable profits and post-CGT capital gains have been accumulated in the same reserve, but can still be separately identified, we will accept a liquidator's nominated appropriation.

Commissioner of Taxation

8/12/94

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