TD 95/10 - Income tax: what is the significance of the Archer Brothers principle in the context of liquidation distributions?

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Australian Taxation Office

Taxation Determination TD 95/10

This Determination, to the extent that it is capable of being a 'public ruling' in terms of Part IVAAA of the *Taxation Administration Act 1953*, is a public ruling for the purposes of that Part . Taxation Ruling TR 92/1 explains when a Determination is a public ruling and how it is binding on the Commissioner. Unless otherwise stated, this Determination applies to years commencing both before and after its date of issue. However, this Determination does not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

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. FCT* (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 what is known as the *Archer Brothers* principle. The principle is that if 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 A*rcher 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 refer only to the selection of particular 'profits' or 'income'. However, if a liquidator ostensibly distributes an amount representing capital actually contributed by shareholders, we accept that the distribution is treated as a non-dividend return of capital even if the funds used to return the amount could be traced to a receipt of income or profit. 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 result.

Note: Although we accept that the *Archer Brothers* principle is of general application, we reserve the right, in appropriate cases, to look behind accounting entries and trace the actual source of the funds distributed. For example, if a liquidator sources a distribution from an asset revaluation reserve but the source of the funds used to make the distribution was a capital gain made on the disposal of a revalued post-CGT asset of the company, we consider that the distribution would represent 'income' in terms of paragraph 47(1A)(b) of the Act, and be deemed by subsection 47(1) to be a dividend.

4. We consider that the *Archer Brothers* principle applies if:

(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) it is clear from either the accounts or statement of distribution that the liquidator has appropriated the specific profit or fund in making the distribution.

5. It has been suggested that the *Archer Brothers* principle operates only if separate accounts have been kept for each specific fund or profit so that a liquidator's appropriation from any account is unequivocally from a particular fund or profit. Although the maintenance of separate accounts makes it easier to identify the source of a distribution, and is, in our opinion, preferable from a practical point of view, we do not consider that separate accounts are essential provided the liquidator is able to identify a fund or profit from which a distribution is made. For example, if 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
20/4/95

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