No. 545.—High Court of Justice (King's Bench Division).—25th June and 2nd July, 1924.

Court of Appeal.—10th, 11th, 12th and 24th November, 1924.

House of Lords.—25th and 26th January, 1926.

Whelan (H.M. Inspector of Taxes) *v.* Henning.[1]

Income Tax, Schedule D, Case V—*Shares in foreign company.*

The Respondent was the owner of shares in a Ceylon company which for the year 1920 *declared no dividend, and for the year* 1920–21 *he therefore received no income from that source. On that ground he contended that he was not liable to be assessed*

[1] Reported K.B.D., [1924] 2 K.B. 421, C.A., [1925] 1 K.B. 387, and H.L., [1926] A.C. 293.

to Income Tax for that year on the average amount of the dividends on the shares for the three preceding years.

Held, *that, in view of the decision of the House of Lords in the case of* The National Provident Institution *v.* Brown (8 T.C. 57), *as there was no income from the shares in the year in question, there was no liability to Income Tax for that year, notwithstanding that the Respondent continued to hold the shares throughout the year.*

CASE

Stated under the Income Tax Act, 1918, Section 149, by the Commissioners for the General Purposes of the Income Tax Acts for the Division of Dorchester in the County of Dorset for the opinion of the King's Bench Division of the High Court of Justice.

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1. At a meeting of the Commissioners for the General Purposes of the Income Tax Acts for the Division of Dorchester in the County of Dorset held at the Council Chamber, Town Hall, Dorchester, on the 10th day of February, 1922, for the purpose of hearing appeals, Captain R. H. Henning (hereinafter called "the Respondent") appealed against an assessment to Income Tax in the sum of £3,424 for the year ending 5th April, 1921, made upon him in respect of income arising from shares out of the United Kingdom under the provisions of Schedule D of the Income Tax Acts, Case V.

2. The following facts were proved or admitted, viz.,

(*a*) The Respondent is a person residing in the United Kingdom who is the holder of shares in the Vincit Tea and Rubber Company, Ltd.

(*b*) The Company is incorporated in Ceylon having an issued capital of 3,300 shares of Rs.100 each fully paid (Rs.330,000).

(*c*) The Respondent is the holder of 1,000 of these shares, (Rs.100,000). He is not a Director of the Company.

(*d*) The whole of the dividends declared on the Respondent's holding have been remitted to this country.

(*e*) Up to and including the year ended 5th April, 1920, the Respondent has been assessed under Case V, Schedule D, Rule 1, on the basis of the full amount thereof on an average of the three preceding years (as directed in Case I), except in the earlier years before a three years' average was obtainable, when the assessment was determined under Rule 1 of the Rules applicable to Cases I and II, Schedule D (i.e., in the first year and second years on the actual amount declared in

the first year; in the third year on the average of the first and second years). The Respondent has no other income from Foreign Possessions assessable under Case V.

(*f*) The whole of the dividends declared having been remitted to this country no question arises under Case V, Rule 1, in respect of dividends declared but not remitted.

(*g*) The dividends have been converted from Rupees into Sterling and the actual amount of Sterling received has been brought into account.

(*h*) A return was made on the 22nd July, 1920, in the sum of £3,424, being the average of the amounts received in the three preceding years. The Respondent has since filed an amended return showing no income under Schedule D.

(*i*) For the year ended 5th April, 1921, an assessment was made upon the Respondent by the Commissioners for the Division of Dorchester in the sum of £3,424 arrived at as follows :—

Year ending	*Dividend declared.* *Rupees.*	*Dividend received.* £
5th April, 1918 ..	33,000 ..	3,730
,, ,, 1919 ..	35,000 ..	2,629
,, ,, 1920 ..	53,000 ..	3,914
		3/10,273
Average of the three preceding years ..		£3,424

(*j*) In the year 1920 the Company made a net profit of Rs.4820 but no dividend was declared, the amount being carried forward and consequently no income was remitted to the Respondent during the tax year ended 5th April, 1921.

3. Mr. Rayner Goddard appeared on behalf of the Respondent and contended :—

(i) That Case V, Rule 1, merely provides certain principles by which income has to be measured for the purposes of taxation, but that before the Respondent could be taxed there must be a taxable income.

(ii) That the computation of tax is governed by the charging section under Schedule D, paragraph 1, which provides as follows :

"Tax under Schedule D shall be charged in "respect of the annual profits or gains arising or "accruing to any person residing in the United

" Kingdom from any kind of property whatever, " whether situate in the United Kingdom or else- " where," and that therefore the tax is only leviable on income.

(iii) That in the case of *The National Provident Institution* v. *Brown (Surveyor of Taxes)*(1), [1921] 2 A.C. 222, Viscount Haldane held that " the expression Income " Tax, as used by the Legislature, was a generic " description of the tax which was levied under all " the Schedules alike, and it was not meant to be " anything but a tax on income," also that " the true meaning of the words the Legislature has " used is that the tax is intended as a matter of basic " principle to be on profits and gains forming income " in the year of assessment though not measured by " the income of that year," and that " the natural " construction of the language of the Third Case of " Schedule D appeared to be that the tax is imposed " only where there are profits and gains arising within " the year of assessment, but that the amount pay- " able is to be measured by reference only to the " profits and gains arising within the preceding year."

(iv) That in the case referred to in the last paragraph it was laid down by Lord Atkinson(2): " That Income Tax " is primarily a tax upon a real, not an imaginary, " income accruing to the taxpayer during the year of " assessment," and " that if in the year of assessment " a source of income should dry up and no income " accrue then no tax could be levied or collected in " respect of a non-existing income," and further that the average of three years as provided for in Rule 1 merely fixes the lower limit of income to be taxed and it is a measure " to be applied not however to a " vacuum or to a non-existing thing, but to an " existing thing, the amount of the profits and gains " actually arising or accruing to the taxpayer within " the year of assessment," whilst the provisions of the Income Tax Act, 1853, clearly indicate that if no profits or gains arise or accrue from one of the named sources to the person entitled during the year of assessment that person cannot be made liable to pay any Income Tax in respect of that source.

(v) That in the case of the *National Provident Institution* v. *Brown*, Lord Sumner held(3) that in a year when there is no profit the method of computation could not apply as it becomes a calculation of a sum to be paid on nothing, which meant not to be paid at all.

(1) 8 T.C. 57, at pp. 84, 85 and 86. (2) *Ibid.*, at pp. 89, 91, 92 and 93.
(3) *Ibid.*, at p. 98.

(vi) That in the case of *Tennant* v. *Smith*(1), [1892] A.C., page 164, Lord Macnaghten ruled "The duty under "Schedules D and E is payable on the 'annual "'amount.' It is a tax on income in the proper "sense of the word. It is a tax on what 'comes in' "—on actual receipts," whilst in the case of the *London County Council* v. *Attorney-General*(2), [1901] A.C. 26, the same learned Judge observed as follows: "Income Tax, if I may be pardoned for "saying so, is a tax on income. It is not meant to "be a tax on anything else," and later "In every "case the tax is a tax on income whatever may be "the standard by which the income is measured."

(vii) That had the Respondent received any income at all, however small during the year of assessment, the assessment was in order.

(viii) That the source of the Respondent's income is not the holding of shares, but the amount which by resolution of the Company is divided amongst the shareholders, and that, following the dictum of Lord Atkinson, as no income had arisen from such source or had been received by the Respondent during the year of assessment, the Respondent could not be made liable to pay Income Tax in respect of the source.

(ix) That the average income of the three preceding years cannot be deemed to be an income which in fact never existed.

4. It was contended by the Inspector of Taxes (hereinafter called the Appellant) on behalf of the Crown, (*inter alia*)—

(i) That the source of income is the holding of shares in the Company by the Respondent and that the declaration of a dividend on such shares does not constitute the source.

(ii) That the charging section under which the Respondent is liable is Schedule D, paragraph 1 (*a*) (i), and under Case V of paragraph 2.

(iii) That the Rules applicable to Case V are to be read in conjunction with the Rule applicable in Case I, and that the principles of taxation which apply to one Schedule equally apply to another as laid down in the case of *The London County Council* v. *Attorney-General*(3), [1901] A.C. 26, when it was held "That "the Income Tax Acts of 1842 and 1853 . . . . "do no more than impose a single tax on profits and "gains brought into charge by the Income Tax Acts. "There is no special or peculiar tax under each Case

(1) 3 T.C. 158, at p. 171. (2) 4 T.C. 265, at pp. 293 and 294. (3) *Ibid.*, at p. 293.

" of Schedule D and the other Schedules or their " branches whatever be the idiosyncrasies of the " methods prescribed for collection " and that Lord Haldane endorsed this ruling in the case of the *National Provident Institution* v. *Brown*(1).

(iv) That in support of this contention liability to assessment depends on the existence of the source of income in the year of assessment, i.e. the charging section of Schedule A provides the tax under such Schedule shall be charged in respect of the property in all lands, etc., in the United Kingdom, and that once the existence of the property is established such property constitutes the source, and it is liable to be assessed; similarly the charging section of Schedule B provides that tax under such Schedule shall be charged in respect of the occupation of all lands, etc., in the United Kingdom, and that once the occupation is established it constitutes the source of profit, and is liable to be assessed, whilst the charging section of Schedule E provides that tax under such Schedule shall be charged in respect of every public office or employment of profit, etc., and that, once the existence of the office or employment is established, it constitutes the source of income, and is liable to be assessed.

(v) That Case V of Schedule D has to be considered in conjunction with Cases I and II, and that once the existence of the trade, profession, employment, or vocation exists it is caught by the Rules applicable to these Cases, and liable to be assessed, and that the introduction of the word " income " in Case V does not affect the principle that the source of income, when once established, gives rise to an assessment, and that following these lines it is the practice to assess a continuing business on the average profits of the three preceding years even though during the year of assessment no profits or income may have been derived therefrom.

(vi) That Section 34 of the Income Tax Act, 1918, provides for relief in case a person sustains loss, and that if the contention of the Respondent is correct such Section has no meaning or application.

(vii) That the case of *The National Provident Institution* v. *Brown* is distinguishable from the present case, inasmuch as in the former case the source of income had ceased to exist, and laid stress on the fact that Lord Haldane in his judgment ruled(2) that " The " question is whether the source of such profits and

(1) 8 T.C. 57. (2) *Ibid.* at p. 85.

" gains must be one which continued to exist in the " year of assessment," and later " It is to be observed " that, speaking broadly at all events, the general " principle of the Acts is to make the tax apply only " to a source of income existing in the year of assess- " ment," whilst Viscount Cave (who dissented from the ruling of the other Law Lords) expressed the opinion(1) that " the taxpayer himself is the only " source of profit which need exist in the year of " assessment," and Lord Atkinson in giving judgment said(2) : " It ignores the vital fact that Income Tax " is primarily a tax upon a real, not an imaginary, " income accruing to the taxpayer during the year of " assessment." From this the Inspector of Taxes contended that a loss in trade is not imaginary income, and drew attention to the remarks of Lord Justice Warrington in the Court of Appeal (*The National Provident Institution* v. *Brown*)(3) : " Now it is " common ground that in general, according to the " scheme of the Income Tax Acts, the tax is payable " in respect of a source of income existing in the year " of assessment, and that the profits of the preceding " year, or the average of the profits of several pre- " ceding years, are respectively used merely as a " measure for the purpose of taxation of the amount " of the profits in the year of assessment."

(viii) That the word " profit " must be taken in a very broad sense and that for Income Tax purposes it includes a " loss."

5. In reply Mr. Rayner Goddard contended that Section 34 of the Income Tax Act, 1918, applies only to a loss in any trade, profession, employment or vocation, or in the occupation of lands, and it is not applicable to income under Case V.

6. In the course of the hearing the cases of *Tennant* v. *Smith*(4), [1892] A.C. 150, and *The London County Council* v. *The Attorney-General*(5), [1901] A.C. 26, were referred to and relied upon by each side.

7. Having considered the facts and contentions herein set forth, we were of opinion that the Respondent was not liable to be assessed on the average of the three preceding years, and we thereupon allowed the appeal and discharged the assessment.

8. Whereupon the Appellant immediately upon the determination of the appeal declared to us his dissatisfaction therewith as being erroneous in point of law under the Sections of the Income Tax Act, 1918, and having duly required us to state and

(1) 8 T.C. 57, at p. 88. (2) *Ibid.*, at p. 89. (3) *Ibid.*, at p. 75. (4) 3 T.C. 158. (5) 4 T.C. 265.

sign a Case for the opinion of the King's Bench Division of the High Court of Justice, this Case is stated and signed accordingly.

ALFRED POPE,
ELLENBOROUGH,
HERBERT A. GROVES,
HENRY R. T. LINDERSBY,
G. C. CREE,
The Commissioners of Taxes for the Division of Dorchester, Dorset, who heard the above Case.

EDWIN STEVENS,
Clerk to the Commissioners,
6, South Street,
Dorchester.

13*th February*, 1924.

The case was argued before Rowlatt, *J.*, in the King's Bench Division on the 25th June, 1924, when judgment was reserved.

The Attorney-General (Sir Patrick Hastings, K.C., M.P.) and Mr. R. P. Hills appeared as Counsel for the Crown, and the Respondent appeared in person.

On the 2nd July, 1924, judgment was given against the Crown with such costs (if any) as were incurred by the Respondent.

JUDGMENT.

Rowlatt, J.—In this case the Respondent was possessed of shares in a company outside the United Kingdom, income from which is taxable under Case V as profits or gains from a foreign possession. In the year of assessment (1920–1921) there was no such income, though there had been in the three previous years. He was, however, assessed in the sum of £3,424, being the average of the three preceding years. On appeal the Commissioners discharged that assessment, stating the Case which is now before me. The question is whether the Respondent's liability depends, as the Crown contends, upon the possession of the shares in the year of assessment, or, as the Respondent contends and the Commissioners decided, upon the receipt of some profit therefrom in that year. The answer to that question depends upon the true interpretation of the decision of the House of Lords in *Brown* v. *National Provident Institution*(1), [1921] 2 A.C. 222.

The Respondent unfortunately was unprovided with Counsel to argue his case before me, but I have a full statement of the contentions of his Counsel before the Commissioners. His position in view of the decision to which I have referred is that, when it is enacted in Schedule D, paragraph 1, that tax under that

(1) 8 T.C. 57

(Rowlatt, J.)

Schedule " shall be charged in respect of the annual profits or " gains arising or accruing " from the sources there mentioned (in this case a foreign possession), the subject matter of the tax is not the source of possible profits or gains, but the profits or gains themselves, and therefore the liability to taxation depends not upon the existence of such a source but upon the existence of profits or gains. This is a very clear proposition in support of which numerous passages in the judgments delivered in the Court of Appeal and in the speeches in the House of Lords were quoted to the Commissioners. The Attorney-General, however, contended that nevertheless the decision was based on the absence of a source of profits or gains and not on the absence of profits or gains themselves. He pointed out that returns for Income Tax are made early in the financial year, that the assessments are made during the summer and autumn, and that the tax is unworkable if liability depends upon the accrual of profits in the year which at the date of assessment is still incomplete and at the time for returns is only beginning. This, however, was an argument for the Crown as applicable in the case referred to as in the present and Lord Cave refers to it in his dissenting opinion. It did not prevail.

It seems to me, looking at the matter now in the light of the decision in question, that the reason why I went wrong when the case came before me was precisely this, that I approached the question from the point of view that the Attorney-General now again propounds: The Acts themselves say nothing about the existence or non-existence of sources, but the returns and assessments are made in advance. The measure of the amount is to be found in the result of previous years or their average. How then is it to be decided whether or not a return and assessment are to be made for the current year? The question in nine cases out of ten arises under Case I or Case II in respect of trades or professions, and it became a commonplace among those dealing with Income Tax that, if the trade or profession had been discontinued (a matter determinable at the beginning of the year), the liability to make a return and be assessed ceased. From this arose the notion that the cessation of liability to tax depended on the disappearance of the source of possible profits or gains as opposed to the disappearance of the profits or gains themselves, which of course necessarily also happened when the source disappeared. The test came when the question of profits from discounts arose. These do not appear to possess a source having an independent existence in the way that a trade, vocation or property has an existence, independent of the profits it may or may not produce, which can be seen at the beginning of the year. To speak of discounts as the source of profits is not to speak of a thing which may cease or continue, but is merely to describe the profits. Under these circumstances the supposed principle that liability depended upon the existence of a source

(Rowlatt, J.)

seemed to have no application, and that was the basis of my decision. I think the decision of the House of Lords has displaced the whole of this and has declared that liability depends on the existence not of sources apart from profits, but of profits, which are merely classified for measurement according to the sources named in the schedules. Lord Haldane says ([1921] A.C., at page 236) (1) : " The tax is intended as matter of basic " principle to be on profits and gains forming income in the year " of assessment, though not measured by the income of that year," and again (page 237) (2) :" The tax is only imposed where " there are profits and gains arising within the year of assessment." This seems to me quite definite and precise, but the elaborate opinion of Lord Atkinson places the matter, in my judgment, beyond any doubt at all. He says (page 243) (3) that the contention of the Crown " ignores the vital fact that " Income Tax is primarily a tax upon a real, not an imaginary, " income accruing to the taxpayer during the year of assessment." It can only be supported, he says, " by confounding the different " measures which the Statutes provide for ascertaining the " amount of the taxable income of a taxpayer with the thing to " be measured, namely, the income itself." " The Solicitor-" General," he says, " frankly admitted on behalf of the Appel-" lant that no case could be found in the books deciding that a " taxpayer, to whom no profits or gains accrued from a given " source during the year of assessment could be treated as having " received profits and gains from that source not less in amount " than those he received from it in the immediately preceding " year." With that encouragement the Attorney-General asks me to provide such a precedent in this case. " The Appellant," says Lord Atkinson (on page 244) (4), " seeks to substitute the " income of the present year for the cypher which represents the " actual income of the subsequent year."

The above extracts are taken from the preliminary remarks in Lord Atkinson's speech. He proceeds to a detailed examination of the tax and its history.

Taking first the Act of 1799, in which there was no measure provided and no classification by schedules, Lord Atkinson points out that it is clear that the taxpayer was each year obliged to pay the duty on income he received or was entitled to receive during that year. Proceeding to the Act of 1803 which introduced the schedules but provided no measure, Lord Atkinson says this(5) : " From this legislation one sees clearly what is the true " nature of Income Tax. It is a single tax divided into different " parts merely for the convenience of collection. It was a tax " assessed, levied and collected yearly on the profits and gains " arising and accruing during the year in which it was collected

(1) 8 T.C. at p. 85. (2) *Ibid.*, at p. 86. (3) *Ibid.*, at p. 89. (4) *Ibid.*, at p. 90. (5) *Ibid.*, at p. 91.

(Rowlatt, J.)

" from one or more of the sources named. If this be so, as in " my opinion it clearly is, it necessarily follows that, if in the " year of assessment a source of income should dry up and no " income accrue, then no tax could be levied or collected in " respect of non-existing income."

Lord Atkinson then proceeds to the Act of 1842, which is practically identical with that of 1806. He deals specifically with the First Case of Schedule D (trades, etc.). Speaking of the measure to be observed under that Case he says (1) it is " a measure to be " applied; not to a vacuum, or to a non-existing thing, but to an " existing thing, the amount of the profits and gains actually " arising or accruing to the taxpayer within the year of assessment." Pausing here I recall that it was most strenuously contended by the Attorney-General before me in the present case that it was impossible that, in the case of traders, the liability to assessment in the course of the year, and the obligation to make a return at the beginning, could depend upon the existence of profits in that year. But it seems to me that Lord Atkinson expressly says that it does. Proceeding to refer to the Fourth Case he again lays it down that, if the source of income dries up and nothing is received in Great Britain, no tax can be levied, and as to Case V (the one now before me) he says the income is again to be measured by the three years average, and the remarks already made by him as to Case I apply to it. Lastly, after referring to the Act of 1853, Lord Atkinson sums up the position as follows (page 250) (2) : " It would appear to me that " these provisions clearly indicate that, if no profits or gains " arise or accrue from one of the named sources to the person " entitled during the year in which the duties are to be 'charged, " ' raised, levied, collected and paid, that is, the year of assess- " ment, that person cannot be made liable to pay Income Tax " in respect of that source."

It was not suggested that the Consolidating Act of 1918 has made any difference as regards the question under discussion, and it seems to me that this appeal must clearly be dismissed with such costs, if any, as are incurred by the Respondent in person in such a proceeding as this.

The Crown having appealed against the decision in the King's Bench Division, the case came before the Court of Appeal (Pollock, *M.R.*, and Warrington and Scrutton, *L.JJ.*) on the 10th, 11th and 12th November, 1924, when judgment was reserved.

Sir Patrick Hastings, K.C., M.P., and Mr. R. P. Hills appeared as Counsel for the Crown, and Mr. Rayner Goddard, K.C., and Mr. G. M. Welsford for the Respondent.

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(1) 8 T.C. at p. 92. (2) *Ibid.*, at p. 93.

On the 24th November, 1924, judgment was given unanimously against the Crown, with costs, confirming the decision of the Court below.

JUDGMENT.

Pollock, M.R.—This is an appeal from a decision of Mr. Justice Rowlatt given on the 2nd July, 1924, whereby he dismissed the appeal of the Crown from the decision of the Commissioners for the General Purposes of the Income Tax who had discharged the assessment upon the Respondent, Captain Henning.

Captain Henning resides in the United Kingdom and is the holder of 1,000 shares in the Vincit Tea and Rubber Company, Limited. This Company is incorporated in Ceylon and has from time to time declared dividends which have been remitted to the Respondent in this country.

The question arises in reference to an assessment upon him made for the financial year ending April, 1921, under Schedule D, Case V, Rule 1, on the basis of the full amount received by way of dividend upon the shares on an average of the three preceding years, as directed in Case I, in accordance with the standard laid down in Case V.

The Respondent has no other income from foreign possessions assessable under Case V, and on the 22nd July, 1920, he made a return in the sum of £3,424 as being the average of the dividends received in the three preceding years, on which he submitted to liability for the current year of charge. In the year 1920 no dividend was declared by the Company and no income was remitted to the Respondent during the tax year ending April, 1921. The Respondent thereupon filed an amended return showing no income under Schedule D, and submits that Case V, Rule 1, merely provides certain principles by which income has to be measured, but that before he can be subject to taxation there must in the year of assessment be a taxable income.

The Respondent agrees that if he had received any income, however small, during the year of assessment, the assessment of £3,424 would be in order as the correct estimate of his income for that purpose; but that, as the whole income has totally failed, there are no profits and gains forming an income which can be made the subject of assessment, by whatever measure the income would have fallen to be assessed if it had existed.

For the Crown it is contended that Case V of Schedule D must be considered in conjunction with Cases I and II, and that once a trade, profession, employment, or vocation is found to exist, the Rules under Cases I and II apply, and there is a liability to assessment; that the words of Rule 1 of Case V

(Pollock, M.R.)

" the tax in respect of income arising from stocks and shares . . . " in any place out of the United Kingdom shall be computed," etc., are not to be construed as making the receipt of income the condition of liability; but that, when the source of income has been found and established, there is a liability to assessment whether in fact income be actually received or not. The Crown invoke the practice established of assessing a continuing business on the average profits of the three preceding years, even though during the year of assessment no profits may be derived therefrom. Counsel for the Crown further claim that, if the liability to assessment depends upon the actual receipt of income during the year of assessment, it will not be possible for the subject to make a return and the Revenue Authorities to fix the assessment upon that return, for both those operations take place in the first six or nine months of the year of assessment, while the tax is collected during the latter months of the financial year for which the assessment is made, and in which the tax is paid. Sir Patrick Hastings drew attention to the terms of the Sections 46–49 and 176 of the Act of 1842 in support of his argument as to the scheme of the Income Tax Acts, and to several Sections where " source of income " is mentioned, e.g., Section 52, which speaks of the amount of such profits and gains arising to such person from all and every the " sources charge- " able " under this Act. He also referred to the speech of Lord Macnaghten in *Colquhoun* v. *Brooks*(1), 14 A.C. 493, where at page 516 he says: " I use the expression ' source of income ' " because it is as a source of income that the Act contemplates " and deals with property and everything else that a person " chargeable under the Act may have, and the Act itself, in " Section 52, uses the expressions ' sources chargeable under " ' the Act ' and ' all the sources contained in the said several " ' Schedules ' as describing everything in respect of which the " tax is imposed."

These arguments are formidable, and if the matter were free from superior authority, I should feel bound to consider them fully, particularly in view of the opinion expressed by Lord Cave in *Brown* v. *National Provident Institution*(2), [1921] 2 A.C. at page 239. Viscount Cave's opinion however was not accepted by the majority of the House of Lords, and I see no ground for distinguishing the principle of that decision from that to be applied to the present case. The tax claimed to be charged in *Brown's* case was in respect of profits of an uncertain value not charged in Schedule A, estimated in accordance with Rule 1 of Case III " at a sum not less than the full amount of the profits or " gains arising therefrom within the preceding year "; but I am unable to find a real distinction on that ground, from the tax sought to be charged in the present case under Case V on

(1) 2 T.C. 490, at p. 508. (2) 8 T.C. 57, at p. 87.

(Pollock, M.R.)

an average of the three preceding years. Both Cases are branches of Schedule D, and under that Schedule annual profits or gains are charged though the measure of computation is not the same.

In view, however, of the importance of any decision which may appear to conflict with the system of assessing continuing businesses upon the basis of the three years' average, before the actual results of trading can be ascertained, I desire to confine my decision within the limits of the present case—namely, to an assessment falling under Case V of Schedule D where there have in fact been no profits, and that fact has been made plain by an amended return. Incidentally it may be pointed out that the possibility of correcting a return in certain cases so as to make it accord with the facts as realised originally existed under Sections 133 and 134 of the Act of 1842, and Section 24 of the Finance Act, 1907, and where a loss was sustained under Section 23 of the Customs and Inland Revenue Act, 1890, now replaced by Section 34 of the Act of 1918, and see the Third Miscellaneous Rule to Schedule D. Lord Haldane also appears on page 230(1) of *Brown's* case to hold no doubt that where a business continues that is a source in respect of which a return and assessment may be made, for the profits and gains of a continuing business are the subject of assessment; see at page 235(1).

Without further discussing the argument for the Crown, the House of Lords appears to have decided already in *Brown's* case that if a source of income dries up and no income accrues, then no tax can be levied or collected in respect of a non-existing income.

Lord Atkinson says so in terms at page 246(2), and see his words, quoted by Mr. Justice Rowlatt, at page 250(3). Lord Haldane at page 236(4) says: "It seems to me that the true "meaning of the words the Legislature has used is that the "tax is intended as a matter of basic principle to be on profits "and gains forming income in the year of assessment, though "not measured by the income of that year. If a man carries "on business by buying and discounting bills, this is, I think, "as much a source of profit as any other for the purposes of "the words employed. As in the case before us it is agreed that "there was no such source, I think that we have to assume "that there was no income on which to base the tax."

Lord Sumner at page 260(5) rejects the suggestion that the subject himself could be the source of the profit, as had been suggested by Mr. Justice Rowlatt in that case, and says that

(1) 8 T.C. 57, at p. 85. (2) *Ibid.*, at p. 91. (3) *Ibid.*, at p. 93. (4) *Ibid.*, at p. 85. (5) *Ibid.*, at p. 99.

(Pollock, M.R.)

that will not suffice to bring into operation a notional measure of computation, " no profits of the kind having been earned in " the year of charge at all."

It appears to me that the present case is covered by the reasoning to which I have referred. I venture to doubt whether the inconvenience anticipated will in fact arise, for although the House of Lords has clearly laid down that there must be profits and gains assessable in the year of assessment, they have not purported to disapprove of the system of requiring returns for assessment in ordinary course, even though the profits and gains are not realised or visible at the time it is made.

The appeal must be dismissed with costs.

Warrington, L.J.—The question in this case is whether the Respondent, Captain R. H. Henning, was liable to be assessed to Income Tax in respect of profits or gains arising or accruing to him under Case V mentioned in paragraph 2 of Schedule D of the Income Tax Act, 1918. Case V is tax in respect of income arising from possessions out of the United Kingdom. The Respondent resides in this country and is possessed of certain shares in the Vincit Tea and Rubber Company, Limited, and is entitled to receive the dividends thereon. They have been remitted to him in the United Kingdom, the Company being a company established in Ceylon. Under Rule 1 of the Rules applicable to Case V the tax in respect of income of such a nature is to be computed on the full amount thereof on an average of the three preceding years, that is to say, the three years preceding the year of assessment. In the present case the year of assessment was the year ending the 5th April, 1921. During that year the company declared no dividend. The average of the three preceding years was £3,424.

The Respondent contended that, inasmuch as he received no income from the source in question during the year of assessment, the provision as to the mode of computation did not come into operation and he was not liable to tax for that year. He relied on *Brown* v. *The National Provident Institution*(1), [1921] 2 A.C. 222.

The Commissioners accepted his contention and discharged the assessment. Mr. Justice Rowlatt took the same view, and the Crown appeal.

The contention of the Crown is that, inasmuch as in this case the possession from which the income in the preceding years has been derived continues to exist, the case is distinguishable from and is not covered by the decision in *Brown* v. *The National Provident Institution*, and that in such a case the fact

(1) 8 T.C. 57.

(Warrington, L.J.)

that in the year of assessment it does not prove to be an actual source of income is immaterial, and the taxpayer is still liable to tax computed as directed by Rule 1 under Case V.

I should mention that the Respondent originally made a return on the basis of the average of the three preceding years, but on discovering that the dividends would not be paid he made an amended return showing " no income " from the source in question. This amended return would seem to have been accepted as a sufficient return and no technical objection on this ground has been raised.

The real question is whether the decision in *Brown* v. *The National Provident Institution* covers the present case, in which, though the shares which constitute the " possession out " of the United Kingdom " do not in the year of assessment produce any income, they remain in the hands of the possessor and may thereafter again become a source of income.

I should like to say that in this judgment I propose to confine myself to the consideration of the case before me, that is to say, a case arising under Case V of Schedule D, and it must be left for another tribunal to determine the position under other circumstances and under other Cases of the same Schedule, or under other Schedules.

Brown's case arose under Case III, " Tax in respect of " profits of an uncertain value and of other income described in " the Rules applicable to this Case," and the particular income in question was profits on discounts. Under Case III the tax is to be computed on the full amount arising in the year preceding the year of assessment.

In that year the National Provident Institution made profits from dealings in Treasury Bills, that is to say, " on discounts " within the meaning of Case III, but in the year of assessment they had no transactions in Treasury Bills and therefore made no such profits. In those circumstances it was held by the majority of the House of Lords that they were not liable to be assessed under Case III. I have carefully read and considered the speeches of the three learned Lords who were the majority in that case, and I think it clear that they proceeded on the broad principle that if in the year of assessment there were no profits from a particular source there was no taxable income from that source, the existence of such income being an essential condition of the liability to tax, and that the rule referring to the profits of the preceding year only provides a measure by which the amount of the taxable income, if it exists at all, is to be ascertained.

(Warrington, L.J.)

The only distinction suggested by the Crown between the last mentioned case and the present is that in the present case the Respondent remains the possessor of the shares from which the profits, when there are any, arise. But in my opinion, bearing in mind the principle on which the House proceeded, the difference in the facts of this case from those in the case before them is no real distinction. The tax is on income, not on that which is the source of income. If there is no income from the particular source it can make no difference that there may be income from it in a succeeding year. It ceases to be a source of income in the year of assessment, and that in my opinion brings the case within the decision of the House.

It was suggested by Counsel for the Crown that, if the view I have expressed is correct, a person carrying on a trade or possessing any property from which there might or might not be income in the year of assessment could not be assessed until the expiration of that year. But I do not think this inconvenience need arise. The man might well be assessed on the hypothesis that there would be profits, leaving it to him to establish, if it were the fact, that there were no profits and that he was therefore not liable.

On the whole I think the appeal fails and should be dismissed.

Scrutton, L.J.—Captain Henning originally made a return for assessment to Income Tax under Case V of Schedule D of profits derived from shares in a Ceylon company, calculated on the average of the three preceding years. At the end of the year of assessment he asked to amend that assessment, as the Company paid no dividend in the year, and contended that, there being no profits accruing to him in the year of assessment, there was nothing to assess by the three years' average or any other rule. He relied on the recent decision of the House of Lords in *Brown's* case(1), [1921] 2 A.C. 222, a decision under Case III of Schedule D, that where there were " no profits or " discounts " in the year of assessment, you could not assess on the income of the previous year as provided by the rule of computation of Case III of Schedule D. The Commissioners accepted his contention; Mr. Justice Rowlatt affirmed their decision; and the Crown appeal to this Court.

I also am of opinion that the case is concluded here by the decision of the House of Lords in *Brown's* case. I understand the judgments of the three Lords who formed the majority to proceed on the lines that what is assessed is profits made in the

(1) Brown v. The National Provident Institution, 8 T C. 57.

(Scrutton, L.J.)

year of assessment; that if there are no profits there can be no assessment, and that the fact that if there are profits they are to be computed in accordance with an average of previous years does not enable such a computation to be made when there are no profits to assess. This appears to me to be the reasoning of the majority of the House of Lords, and I do not cite their judgments in detail. I can see no difference on this head between Case III of Schedule D, the subject matter of *Brown's* case, and Case V, the subject matter of this case. Schedule D imposes a tax " in respect of annual profits and gains." Case V of those profits is " in respect of income arising from possessions " out of the United Kingdom " assessed on an average of the three preceding years. Case III is in respect of " profits " and other " income," " computed on " the income of the previous year. If in the latter case you cannot " compute " if there is no income in fact arising in the year, so in the former case the absence of income in fact in the year prevents the statutory measure by preceding years being applied to it.

I understand the argument of Counsel for the Crown to be that this case was distinguishable from *Brown's* case, for in the latter there was no source of income in the year of assessment, no discounts having been effected, while in this case there was a source of income, though in the year no income flowed from it. In my view and I think in the view of the House of Lords, taxation under the Income Tax Acts is on " income," not on " sources of income." The title of the Act of 1842 is An Act for granting Her Majesty duties on " Profits." It is true that here and there, as in Section 23 of the Act of 1918, the expression " sources of income " is used and the assessment said to be on the " source," but this is quite inaccurate unless the expression is taken as elliptical for assessment on profits from a source.

Counsel for the Crown apprehended great difficulties from an affirmance of this decision, if they could not assess during the year, till they knew there were profits during the year. I do not share their apprehensions. If the Crown know there have been profits from a source in the preceding years, and do not know the source has ceased to flow, they may well assess according to the rules and leave the subject to show there is in fact nothing to assess in that year.

I wish however to confine my decision at present to Case V of Schedule D, the case before us, and leave other Cases or Schedules to be dealt with when they arise. The appeal should be dismissed with costs.

The Crown having appealed against the decision in the Court of Appeal, the case came on for hearing in the House of Lords before Viscount Cave, *L.C.*, and Lords Atkinson, Shaw of Dunfermline, Sumner and Carson on the 25th and 26th January, 1926, when, on the latter day, judgment was delivered unanimously against the Crown, with costs, confirming the decision of the Court below.

The Attorney-General (Sir Douglas Hogg, K.C., M.P.), the Solicitor-General (Sir Thomas Inskip, K.C., M.P.), and Mr. R. P. Hills appeared for the Crown, and Mr. Rayner Goddard, K.C., and Mr. G. M. Welsford for the Respondent.

JUDGMENT.

Viscount Cave, L.C.—My Lords, the Respondent, Captain Henning, holds some shares in a foreign company which in the three financial years ending on the 5th April, 1918, 1919 and 1920, produced substantial dividends, but in the financial year ending on the 5th April, 1921, produced no dividend. He was assessed to Income Tax under Case V, Schedule D, of the Income Tax Act, 1918, in respect of the fourth of those years, namely, the year ending 5th April, 1921. The question is whether he was properly so assessed or whether, having received no profits from the shares in the year of assessment, he was exempt from assessment in respect of those shares.

My Lords, a similar question arising under Case III of Schedule D was decided by this House in favour of the taxpayer in the case of *Brown* v. *National Provident Institution*(1), [1921] 2 A.C. 222. It has been held by Mr. Justice Rowlatt and by the Court of Appeal that the present case is governed by that decision. After carefully considering the enactments and rules relating to Case V of Schedule D, and comparing them with those relating to Case III of the same Schedule, I am unable to find any difference which prevents the case cited from being applicable in equal measure to Case V. The Attorney-General and the Solicitor-General have laid stress on certain references in the Act of 1842 and in the Act of 1918 to " sources of income " and have contended that this case is distinguishable from *Brown's* case on the ground that in *Brown's* case no continuing source of income was vested in the taxpayer, whereas in the present case the shares formed a continuing source, or at all events a potential source, of income in respect of which an assessment could be made. Your Lordships have heard the judgments in *Brown's* case read, and it does not appear to me that the judgments of the majority of the House in *Brown's* case left the door open for any such distinction. Those judgments proceeded on the broad

(1) 8 T.C. 57.

(Viscount Cave, L.C.)

principle that the tax under Case III was a tax on the profits of the year of assessment measured by, but not grounded on, the figures of the preceding year, and accordingly where there were no such profits there was nothing to which the tax could attach. That principle, which must of course be accepted as declaring the law, applies equally to Case V, with the substitution for the preceding year of the average of the three preceding years; and it is conclusive of the present case. Such differences as there are between the language of the Acts of 1842 and 1853, which governed *Brown's* case, and that of the Act of 1918, which governs the present case, are in favour of and not adverse to the application of the principle to the case now under appeal; for, whereas in the Act of 1842 the tax under Case V was described as a duty to be charged "in respect of foreign possessions," in the Act of 1918 it is referred to as a tax "in respect of the income "arising from foreign possessions." I think that *Brown's* case is fatal to this appeal.

It is only necessary to add that for myself I desire to confine my decision to cases arising under Case V of Schedule D. The question whether the same conclusions apply to Case I of Schedule D is not before your Lordships, and I express no opinion upon it.

For the reasons which I have given I am of opinion that this appeal must fail, and I move your Lordships that it be dismissed with costs.

Lord Atkinson.—My Lords, I agree.

Lord Shaw of Dunfermline.—My Lords, in the case of *Brown* v. *The National Provident Institution*(1) the noble Viscount, Lord Haldane, stated the basic principle at the end of his decision, and the decision, as I think, of the House, in this language: "The tax is intended as matter of basic principle to "be on profits and gains forming income in the year of assess-"ment, though not measured by the income of that year ". . . . . the tax is imposed only where there are profits "and gains arising within the year of assessment." I do not feel myself at liberty, therefore, to give effect to any of the arguments so carefully presented on behalf of the Crown in this case. I think *Brown's* case covers the present.

Lord Sumner.—My Lords, I agree. It is always undesirable to refine upon prior decisions of this House in order to introduce distinctions without differences, and especially is it so in tax cases. After prolonged re-examination of *Brown's* case I think the *ratio decidendi* of the judgments of the majority of the noble and learned Lords was one equally applicable to the present case and equally decisive against the imposition of tax.

(1) 8 T.C., 57, at p. 86.

(Lord Sumner.)

I should not desire it to be supposed that it is only upon the previous decision of *Brown's* case that the same conclusion could be arrived at, or that I have any doubt as to the meaning and effect of the Act of 1918 under which the present case arises. I have carefully considered all the relevant sections, with all the assistance that the Law Officers of the Crown have been able to give us, and I am of opinion that they contain no adequate or appropriate words of charge so as to make the Respondent liable to tax in this case.

Lord Carson.—My Lords, I agree.

Questions put:—

That the Order appealed from be reversed.

The Not Contents have it.

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

The Contents have it.