No. 435.—IN THE HIGH COURT OF JUSTICE (KING'S BENCH DIVISION).—
17TH JUNE AND 24TH JULY, 1919.

COURT OF APPEAL.—16TH AND 19TH APRIL AND 10TH MAY, 1920.

HOUSE OF LORDS.—24TH, 25TH AND 28TH FEBRUARY, 1ST, 3RD AND 4TH MARCH, AND 3RD JUNE, 1921.

(1) THE NATIONAL PROVIDENT INSTITUTION v. BROWN (SURVEYOR OF TAXES).
BROWN (SURVEYOR OF TAXES) v. THE NATIONAL PROVIDENT INSTITUTION.(1)

(2) THE PROVIDENT MUTUAL LIFE ASSURANCE ASSOCIATION v. OGSTON (SURVEYOR OF TAXES).(1)
OGSTON (SURVEYOR OF TAXES) v. THE PROVIDENT MUTUAL LIFE ASSURANCE ASSOCIATION.

*Income Tax, Schedule D.—Liability in respect of discount on Treasury Bills.—Income Tax Act* 1842 (5 *and* 6 *Vict. c.* 35), *Section* 100, *Schedule D, Case* III.

(1) *The National Provident Institution in the years ended 5th April*, 1916, *and 5th April*, 1917, *respectively bought at the Bank of England certain Treasury Bills, of which some were held by it until maturity, others were sold in open market during their currency and the remainder were early in* 1917 *converted into* 5 *per cent. War Loan* 1929–47, *on the terms of the prospectus issued* 11*th January*, 1917. *In the year ended 5th April*, 1918, *the Institution did not hold, or have any transactions in, Treasury Bills. In each of the years ended 5th April*, 1917, *and 5th April*, 1918, *the Institution received and paid interest, from which Income Tax was not deducted, on short loans to and from bankers. In the year ended 5th April*, 1918, *the Institution received interest on* 5 *per cent. War Loan Stock and Bonds, Income Tax being deducted from the interest on the Bonds but not from the interest on the Stock.*

(2) *The facts in the case of the Provident Mutual Life Assurance Association were similar to the foregoing, except that the Association did not in any of the years ended 5th April*, 1916, *5th April*, 1917, *or 5th April*, 1918, *receive any interest apart from dividends on War Loan from which Income Tax was not deducted before receipt. The Association also had transactions in French Treasury Bills and War Expenditure Certificates.*

*Neither the National Provident Institution nor the Provident Mutual Life Assurance Association had been assessed to Income Tax under Case* I *of Schedule D for any of the years ended 5th April*, 1916, *5th April*, 1917, *and 5th April*, 1918, *on the balance of its profits and gains.*

Held, (1) *that the whole difference between the price paid for a Treasury Bill and the sum realised by the purchaser, whether by holding the Bill until maturity or by selling it or converting it before maturity, represents a profit chargeable to Income Tax under Case* III *of Schedule D, and that no part of that profit is an accretion of capital ;*

(2) *that a profit so made constitutes income of the year in which it is received ; and*

(3) (*Viscount Cave dissenting*) *that in order to be chargeable to Income Tax for a particular year in respect of income from any source, a person must possess that source of income in that year.*

(1) Reported (K.B.D.) [1919] 2 K.B. 497; (C.A.) [1920] 3 K.B. 35; (H.L.) [1921] 2 A.C. 222.

CASES.

(1)

STATED under the Taxes Management Act, 1880, Section 59, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the King's Bench Division of the High Court of Justice.

1. At meetings of the Commissioners for the Special Purposes of the Income Tax Acts held on 22nd March and 10th June, 1918, for the purpose of hearing appeals, The National Provident Institution for Mutual Life Assurance, hereinafter called "the Institution," appealed against assessments to Income Tax in the sums of £5,422 for the year ending 5th April, 1917, and £20,566 for the year ending 5th April, 1918, made upon it by the Commissioners for the Special Purposes of the Income Tax Acts under the provisions of the Income Tax Acts.

2. The Institution is a company incorporated by Private Act of Parliament. In each of the years ending respectively 5th April, 1916, and 5th April, 1917, the Institution bought at the Bank of England certain Treasury Bills, some of which were held by it until maturity, others were sold in open market during their currency, and the remainder, being the whole of the Treasury Bills then held by the Institution, were early in the year 1917 converted into 5 per cent. War Loan 1929-1947 on the terms of the prospectus issued 11th January, 1917. In the year ending 5th April, 1918, the Institution did not hold or have any transactions in Treasury Bills. In each of the years ending respectively 5th April, 1917, and 5th April, 1918, the Institution received and paid interest from which Income Tax was not deducted, on short loans to and from bankers. In the year ending 5th April, 1918, the Institution received interest on 5 per cent. War Loan Stock 1929–1947 and Bonds, Income Tax being deducted from the interest on the bonds, but not from the interest on the stock.

3. The following particulars were furnished of the transactions referred to in the preceding paragraph—

YEAR ENDING 5TH APRIL, 1916—

Treasury Bills purchased and realised within the year—

| | Amounts Paid. | | | Amounts Received. | | | Difference. | | |
|---|---|---|---|---|---|---|---|---|---|
| | £ | s. | d. | £ | s. | d. | £ | s. | d. |
| (1) Bills held to maturity ... ... | 286,447 | 14 | 5 | 290,000 | 0 | 0 | 3,552 | 5 | 7 |
| (2) Bills sold or discounted ... ... | 374,280 | 6 | 8 | 376,150 | 12 | 8 | 1,870 | 6 | 0 |
| | | | | Total ... ... | | | £5,422 | 11 | 7 |

YEAR ENDING 5TH APRIL, 1917—

Treasury Bills purchased within or before, and realised within, the year—

| | Amounts Paid. | | | Amounts Received. | | | Difference. | | |
|---|---|---|---|---|---|---|---|---|---|
| | £ | s. | d. | £ | s. | d. | £ | s. | d. |
| (1) Bills held to maturity ... ... | 149,432 | 11 | 11 | 155,000 | 0 | 0 | 5,567 | 8 | 1 |
| (2) Bills converted into War Loan ... | 363,228 | 6 | 8 | 377,375 | 7 | 1 | 14,147 | 0 | 5 |
| | | | | Total ... | | | £19,714 | 8 | 6 |
| Interest received from Bankers on short loans ... | | | | £862 | 10 | 6 | | | |
| Interest paid to Bankers on short loans ... ... | | | | 10 | 11 | 0 | | | |
| | | | | | | | 851 | 19 | 6 |
| | | | | | | | £20,566 | 8 | 0 |

YEAR ENDING 5TH APRIL, 1918—

| | |
|---|---|
| Interest received from Bankers on short loans ... | £267 15 1 |
| Interest paid to Bankers on short loans ... ... | £947 18 7 |

5 per cent. War Loan 1929-1947—

Amounts held 5th April, 1917—

| | | | |
|---|---|---|---|
| Inscribed Stock ... ... ... ... ... | £1,004,100 | 0 | 0 |
| Bearer Bonds ... ... ... ... ... | 284,250 | 0 | 0 |
| Total ... | £1,288,350 | 0 | 0 |

Amounts held 5th April, 1918—

| | | | |
|---|---|---|---|
| Inscribed Stock ... ... ... ... ... | £1,065,000 | 0 | 0 |
| Bearer Bonds ... ... ... ... ... | 285,000 | 0 | 0 |
| Total ... | £1,350,000 | 0 | 0 |

The whole of the stock and bonds held on the 5th April, 1917, were still so held on 5th April, 1918, the increase being due to purchases made in the market. Of the amounts of Inscribed Stock held £397,250 was attributable to the conversion of Treasury Bills.

4. The Institution was not, for any of the years ending 5th April, 1916 1917 and 1918, assessed to Income Tax under Case 1 of Schedule D on the balance of its profits and gains. For the year ending 5th April, 1916, the only direct assessment made upon it under Schedule D of the Income Tax Acts was in respect of income from foreign securities. For the year ending 5th April, 1917, the first of the assessments under appeal was made upon the basis of the amount of the differences between the amounts paid and the amounts received in respect of Treasury Bills realised within the preceding year. For the year ending 5th April 1918, the second of the assessments under appeal was made upon the basis of the amount of the differences between the amounts paid and the amounts received in respect of Treasury Bills realised, together with the amount of the difference between the interest paid to and the interest received from bankers on short loans, within the preceding year. The Institution did not dispute its liability to assessment to Income Tax for the year ending 5th April, 1918, in respect of interest on short loans, on the basis of the net amount received within the preceding year, and the only questions raised by it related to its liability to assessment in respect of the differences between the amounts paid and the amount received for Treasury Bills.

5. The Treasury Bills in question were issued under the Treasury Bills Act, 1877, and the regulations contained in Treasury Minutes of 31st May, 1889, and 13th April, 1915. By the Treasury Minute of 31st May, 1889, provision is made for the inviting of tenders for Treasury Bills, for the issue of Treasury Bills with a fixed rate of interest to the Commissioners for the Reduction of the National Debt, or to such other person or persons as may be willing to buy the same, for the form of tender, and the disposal of the amount received, and in the Schedule a form of Treasury Bill is prescribed. By the Treasury Minute of 13th April, 1915, it is provided that Treasury Bills shall be issued at fixed rates of discount at the Bank of England, and that the Bills issued shall be in amounts of £1,000, £5,000 or £10,000, and shall be drawn for three, six, nine or twelve months as the case may be, that particulars of the bills offered, and the rate or rates of discount for the time being in force, shall be notified to

applicants at the Bank of England, and that the offer shall extend to the general public subject to the conditions that their Lordships reserve the right of rejecting any applications and that the rates shall be subject to variation from time to time without previous notice. The bills bought by the Institution were in the form prescribed in the Schedule to the Treasury Minute of 31st May, 1889, and were payable in some instances at three months, in others at nine months, and in the remainder at twelve months after date. Copies of the Treasury Minutes of 31st May, 1889, and 13th April, 1915, are annexed hereto and form part of this Case.(1)

6. It was contended on behalf of the Institution :—

(*a*) that the differences between the amounts paid and the amounts received for Treasury Bills were an accretion of capital, and not income or annual profits and gains chargeable to Income Tax;

(*b*) that the tax, if assessable at all, was assessable only at payment of the bills on maturity, and on the person holding them at that date, and that the bills sold or converted into War Loan during their currency should be left out of account in computing any liability on the part of the Institution;

(*c*) that in any case the assessment for the year ending 5th April, 1918, could not be maintained, as the Institution did not hold or have any transactions in Treasury Bills in that year.

7. It was contended on behalf of the Surveyor of Taxes, *inter alia*—

(*a*) that the sums in question, whether received on maturity or on sale or conversion of the bills, were profits on discounts chargeable to Income Tax under the Third Case of Schedule D of the Income Tax Acts;

(*b*) that a person is liable to Income Tax under the Third Case of Schedule D on the basis of the full amount of the profits or gains arising from the sources comprised in that Case within the preceding year, whether any profits arise to him from such sources within the year of assessment or not;

(*c*) that the Institution was in receipt of profits of a description comprised in the Third Case of Schedule D in each of the years of assessment, and was consequently chargeable to Income Tax under that Case in each of those years on the basis of the full amount of the profits or gains from any source comprised in that case within the preceding year.

8. We, the Commissioners who heard the appeal, after taking time to consider the contentions put before us, gave our determination on this appeal and on that of the Provident Mutual Life Assurance Association, which was heard at the same time, in the following terms :—

"We confirm the assessments for the year 1916–17.

"As regards the assessments for the year 1917–18, we concur in the "view put forward on behalf of the Appellants that the rule of the Third "Case of Schedule D only provides a measure of liability in respect of "profits from a source existing in the year of assessment. Not only is

(1) Omitted from the present print.

" this view supported by the analogy of the other cases of Schedule D, " but it is our practice, on application being made under Section 134 of " the Income Tax Act 1842, to amend assessments under the Third Case, " as well as under the other cases, where the source of income has ceased " in the course of the year of assessment and to grant relief for the period " of the year elapsing after the cessation of the source of income; and, " *a fortiori*, it would be inconsistent to maintain liability in full where the " source of income has ceased before the commencement of the year of " assessment while allowing partial relief where the source has ceased " during the year. Although in the present case we are not dealing with " an application under Section 134 of the Income Tax Act 1842, we think " it right to refer to our practice under that section both for the argument " which it supplies in support of our decision and because the case may " afford an opportunity for consideration by the Court of a practice which " is not directly and normally open to review upon a case stated.

" The receipt during the year of assessment of interest of money, not " being annual interest, or of interest on registered or inscribed stock of " the 5 per cent. War Loan does not, in our opinion, justify the mainten- " ance of an assessment in the amount of the profits arising from discounts " on Treasury Bills in the preceding year where no such discounts were " received or bills held or dealt in during the year of assessment. We think " that all the distinct and separate descriptions of profits comprised in " The third Case should be treated as separate sources of income and " separate subjects of assessment.

" In view of the provisions of the Sixth Case of Schedule D and the " judgments of the Court of Queen's Bench in the case of the Ryhope Coal " Company *v.* Foyer (1 Tax Cases 343) and the Judicial Committee of " the Privy Council in the case of the Commissioners of Taxation of New " South Wales *v.* Adams (106 L.T.R. 307), it appears to us that there " is *prima facie* ground for holding that classes of profits which would " in subsequent years be chargeable under the rule of the Third Case of " Schedule D are assessable in the first year in which they arise under " the rule of the Sixth Case of Schedule D. Upon this view there should " have been assessments for the year 1915–16 in respect of the discounts " on Treasury Bills, and the assessment for the year 1917–18 should be " amended so as to include the interest on War Loan received in that year " in place of the discounts on Treasury Bills received in the preceding " year; and the anomaly, alluded to by the representative of the Crown, " that upon the contention of the Appellants the Revenue would always " lose one year's tax upon profits falling within the Third Case of Schedule " D, would disappear. As, however, we were not asked to adopt this " view, and as the arguments for or against it were not put before us, " we do not consider that we should be justified in acting upon it.

" We accordingly discharge the assessment upon the Provident Mutual " Life Assurance Association Limited for 1917–18, and reduce the assess- " ment upon the National Provident Institution for that year to the sum " of £852 in respect of interest of money."

9. Immediately upon the determination of the appeal the Institution declared to us its dissatisfaction therewith as being erroneous in point of law as regards the assessment for the year ending 5th April, 1917, and the Surveyor of Taxes declared to us his dissatisfaction therewith as being erroneous in point of law as regards the assessment for the year ending 5th April, 1918, and in due course each of the parties required us to state a case for the opinion

of the High Court pursuant to the Taxes Management Act 1880, Section 59, which case we have stated and do sign accordingly.

P. WILLIAMSON, G. F. HOWE, W. J. BRAITHWAITE, } Commissioners for the Special Purposes of the Income Tax Acts.

Offices of the Special Commissioners of Income Tax,
Windsor House,
83, Kingsway,
London, W.C.2.
19th December, 1918.

(2.)

STATED under the Taxes Management Act, 1880, Section 59, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the King's Bench Division of the High Court of Justice.

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 10th June, 1918, for the purpose of hearing appeals, The Provident Mutual Life Assurance Association, hereinafter called "the "Association," appealed against assessments to Income Tax in the sums of £2,659 10*s*. for the year ending 5th April, 1917, and £8,585 for the year ending 5th April, 1918, made upon it by the Commissioners for the Special Purposes of the Income Tax Acts under the provisions of the Income Tax Acts.

2. The Association is an Insurance Company registered under the Companies Acts as an unlimited company. During the years ending 5th April, 1916, and 5th April, 1917, the Association purchased and discounted or sold during currency certain British Treasury Bills and War Expenditure Certificates, and French Treasury Bills, and also purchased a French Treasury Bill which it held to maturity. In the year ending 5th April, 1918, it did not hold or have any transactions in Treasury Bills or War Savings Certificates, but it held War Loan Stock (including 5 per cent. War Loan Stock 1929–1947) and received dividends thereon of which part was paid in full without deduction of Income Tax and the balance was paid subject to deduction of Income Tax at the source. Apart from such dividends on War Loan the Association did not in any of these three years receive any interest from which Income Tax was not deducted before receipt.

3. The following particulars were furnished of the transactions referred to in the preceding paragraph—

| | Amounts Paid. | | | Amounts Received. | | | Difference. | | |
|---|---|---|---|---|---|---|---|---|---|
| | £ | *s.* | *d.* | £ | *s.* | *d.* | £ | *s.* | *d.* |
| YEAR ENDING 5TH APRIL, 1916— | | | | | | | | | |
| British Treasury Bills purchased and sold or discounted within the year... | 334,855 | 7 | 5 | 337,514 | 17 | 11 | £2,659 | 10 | 6 |
| YEAR ENDING 5TH APRIL, 1917— | | | | | | | | | |
| British Treasury Bills purchased within or before and sold or discounted within the year ... ... ... | 340,272 | 1 | 8 | 347,469 | 2 | 0 | 7,197 | 0 | 4 |
| War Expenditure Certificates purchased and sold within the year ... | 14,400 | 0 | 0 | 14,836 | 7 | 11 | 436 | 7 | 11 |
| French Treasury Bills— | | | | | | | | | |
| (A) Purchased in October, 1915, and paid off in October, 1916 ... .. | 9,456 | 5 | 0 | 10,000 | 0 | 0 | 543 | 15 | 0 |
| (B) Purchased within or before and sold or discounted within the year... | 14,255 | 11 | 4 | 14,663 | 13 | 9 | 408 | 2 | 5 |
| | | | | | | | £8.585 | 5 | 8 |

4. The Association was not for any of the years ending 5th April, 1916, 1917 or 1918, assessed to Income Tax under the First Case of Schedule D on the balance of its profits and gains. For the year ending 5th April, 1916, no direct assessment was made upon it under Schedule D of the Income Tax Acts. For the year ending 5th April, 1917, the first of the assessments under appeal was made upon the basis of the difference between the amounts paid and the amounts received in respect of Treasury Bills discounted or sold within the preceding year. For the year ending 5th April, 1918, the second assessment under appeal was made upon the basis of the difference between the amounts paid and the amounts received in respect of Treasury Bills and War Expenditure Certificates discounted or sold or paid off within the preceding year.

5. The British Treasury Bills in question were issued under the Treasury Bills Act, 1877, and the regulations contained in Treasury Minutes of 31st May, 1889, and 13th April, 1915. By the Treasury Minute of 31st May, 1889, provision is made for the inviting of tenders for Treasury Bills, for the issue of Treasury Bills with a fixed rate of interest to the Commissioners for the Reduction of the National Debt, or to such other person or persons as may be willing to buy the same, for the form of tender, and the disposal of the amount received, and in the Schedule a form of Treasury Bill is prescribed. By the Treasury Minute of 13th April, 1915, it is provided that Treasury Bills shall be issued at fixed rates of discount at the Bank of England, and that the Bills issued shall be in amounts of £1,000, £5,000 or £10,000, and shall be drawn for three, six, nine or twelve months as the case may be, that particulars of the bills offered, and the rate or rates of discount for the time being in force, shall be notified to applicants at the Bank of England, and that the offer shall extend to the general public subject to the conditions that their lordships reserve the right of rejecting any applications and that the rates shall be subject to variation from time to time without previous notice. The bills bought by the Association were in the form prescribed in the Schedule to the Treasury Minute of 31st May, 1889, and were payable in some instances at three months, and in the remainder at twelve months after date.

6. It was contended on behalf of the Association—

(*a*) That the differences between the amounts paid and the amounts received for Treasury Bills and War Expenditure Certificates, were an accretion of capital, and not income or annual profits and gains chargeable to Income Tax;

(*b*) That the tax, if assessable at all, was assessable only at payment of the Bills and War Expenditure Certificates on maturity, and on the person holding them at that date, and that the Bills and War Expenditure Certificates sold during their currency should be left out of account in computing any liability on the part of the Association;

(*c*) That in any case the assessment for the year ending 5th April, 1918, could not be maintained, as the Association did not hold or have any transactions in Treasury Bills or War Expenditure Certificates in that year.

7. It was contended in behalf of the Surveyor of Taxes, *inter alia*—

(*a*) That the sums in question, whether received on maturity or on sale of the Bills or War Expenditure Certificates, were profits on discounts chargeable to Income Tax under the Third Case of Schedule D of the Income Tax Acts;

(b) That a person is liable to Income Tax under the Third Case of Schedule D on the basis of the full amount of the profits or gains arising from the sources comprised in that Case within the preceding year, whether any profits arise to him from such sources within the year of assessment or not;

(c) That the Association was in receipt of profits of a description comprised in the Third Case of Schedule D in each of the years of assessment, and was consequently chargeable to Income Tax under that Case in each of those years on the basis of the full amount of the profits or gains from any source comprised in that Case within the preceding year.

8. We, the Commissioners who heard the appeal, after taking time to consider the contentions put before us, gave our determination on this appeal and on that of the National Provident Institution, which was heard at the same time, in the following terms—

"We confirm the assessments for the year 1916–17.

"As regards the assessments for the year 1917–18, we concur in the "view put forward on behalf of the Appellants that the rule of the Third "Case of Schedule D only provides a measure of liability in respect of "profits from a source existing in the year of assessment. Not only is "this view supported by the analogy of the other cases of Schedule D, "but it is our practice, on application being made under Section 134 of "the Income Tax Act 1842, to amend assessments under the Third Case, "as well as under the other cases, where the source of income has ceased "in the course of the year of assessment, and to grant relief for the period "of the year elapsing after the cessation of the source of income; and, "*a fortiori*, it would be inconsistent to maintain liability in full where "the source of income has ceased before the commencement of the year "of assessment while allowing partial relief where the source has ceased "during the year. Although in the present case we are not dealing with "an application under Section 134 of the Income Tax Act 1842, we think "it right to refer to our practice under that section both for the argument "which it supplies in support of our decision and because the case may "afford an opportunity for consideration by the Court of a practice "which is not directly and normally open to review upon a case stated.

"The receipt during the year of assessment of interest of money, "not being annual interest, or of interest on registered or inscribed stock "of the 5 per cent. War Loan does not, in our opinion, justify the main-"tenance of an assessment in the amount of the profits arising from "discounts on Treasury Bills in the preceding year where no such discounts "were received or bills held or dealt in during the year of assessment. "We think that all the distinct and separate descriptions of profits com-"prised in the Third Case should be treated as separate sources of income "and separate subjects of assessment.

"In view of the provisions of the Sixth Case of Schedule D and the "judgments of the Court of Queen's Bench in the case of the Ryhope "Coal Company v. Foyer (1 Tax Cases 343) and the Judicial Committee "of the Privy Council in the case of the Commissioners of Taxation of "New South Wales v. Adams (106 L.T.R. 307), it appears to us that there "is *prima facie* ground for holding that classes of profits which would "in subsequent years be chargeable under the rule of the Third Case of "Schedule D are assessable in the first year in which they arise under the "rule of the Sixth Case of Schedule D. Upon this view there should

"have been assessments for the year 1915–16 in respect of the discounts "on Treasury Bills, and the assessment for the year 1917–18 should be "amended so as to include the interest on War Loan received in that year "in place of the discounts on Treasury Bills received in the preceding "year; and the anomaly, alluded to by the representative of the Crown, "that upon the contention of the Appellants the Revenue would always "lose one year's tax upon profits falling within the Third Case of Schedule "D, would disappear. As, however, we were not asked to adopt this "view, and as the arguments for or against it were not put before us, "we do not consider that we should be justified in acting upon it.

"We accordingly discharge the assessment upon the Provident Mutual "Life Assurance Association Limited for 1917–18, and reduce the assess- "ment upon the National Provident Institution for that year to the sum "of £852 in respect of interest of money."

9. Immediately upon the determination of the appeal the Association declared to us its dissatisfaction therewith as being erroneous in point of law as regards the assessment for the year ending 5th April, 1917, and the Surveyor of Taxes declared to us his dissatisfaction therewith as being erroneous in point of law as regards the assessment for the year ending 5th April, 1918, and in due course each of the parties required us to state a case for the opinion of the High Court pursuant to the Taxes Management Act 1880, Section 59, which case we have stated and do sign accordingly.

P. WILLIAMSON,<br>G. F. HOWE,<br>W. J. BRAITHWAITE, } Commissioners for the Special Purposes of the Income Tax Acts.

Offices of the Special Commissioners of Income Tax,
Windsor House,
83, Kingsway,
London, W.C.2.

19th December, 1918.

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The cases came on for hearing before Mr. Justice Rowlatt on the 17th June, 1919, when judgment was reserved. Sir John Simon, K.C., the Hon. W. Finlay, K.C., and Mr. A. M. Bremner appeared as Counsel for the Institution, the Hon. W. Finlay, K.C., and Mr. A. M. Bremner on behalf of the Association and the Attorney-General (Sir Gordon Hewart, K.C., M.P.) and Mr. T. H. Parr as Counsel for the Crown.

Judgment was delivered on the 24th July, 1919, in favour of the Crown, with costs, both on the Appeals and the Cross Appeals.

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## JUDGMENT.

*Rowlatt*, J.—These appeals relate to assessments to Income Tax in the case of each of the two companies in question for the years ending respectively on the 5th April, 1917, and the 5th April, 1918. The subject matter of assessment in the first of these years was the profit made during the preceding year by the purchase and realisation by sale, discounting or holding to maturity of British Treasury Bills, the purchase and realisation both having taken place during such preceding year. In the second, the subject matter was the

same with the variation in the case of both companies that some of the bills were purchased before the preceding year, though realised within it. Further, in the case of the National Provident Institution the form of realisation was that the bills were either held to maturity or converted into War Loan, none being sold or discounted in the market. In the case of the Provident Mutual Life Assurance Association, some of the bills were French Treasury Bills, and there was a small amount of War Expenditure Certificates. As regards the first year the Special Commissioners confirmed the assessments, and the point raised by the appeal of the companies is whether the profits made by the transactions in question is accretion to capital or profits and gains in the shape of discounts or interest of money within the Third Case of Schedule D. As regards the second year, the Special Commissioners discharged the assessments on the ground that in the year of assessment there were no transactions of this kind, and that there was therefore no source of income in the year of assessment to support an assessment measured in amount by the profits of the previous year. The Crown contend that this consideration is immaterial.

As regards the first point, it is clear that it is not every difference in amount between a sum payable in future and the same sum represented by cash down which is an annual profit or gain by way of discount, even though popularly the word " discount " may be used to describe it. As Sir John Simon pointed out, the difference between the cash and the credit prices of an article bought is commonly described as discount for ready money allowed by the seller, but it is not taxable as income under Case 3. So the difference between the face and the market value of a terminable debenture standing, as the phrase is, at a discount does not, when realised by holding the security till maturity, become such taxable income. Nor, it is to be hoped, will the Crown ever contend that the profit to be made by subscribing to the present Victory Bonds at 85, and holding them till they are drawn for redemption or applied in payment of death duties will be taxable income. It is true that in some cases obligations in future expressly bearing interest may command only a lower present value not merely because of the uncertain credit of the obliger, but because of the insufficiency of the rate of interest borne by the security in the view of the market at the moment. But even to this extent, the amount gained by buying and holding the security is not annual profits and gains. It is a difference in the value of the security as a whole as a marketable commodity. It seems to me that in each case one must look at the real nature of the transaction and see whether the purchase of the future obligation at a discount is really an investment of money at interest or not.

Now, in the simple case of the purchase of a Treasury Bill bearing no interest, for such a sum as with interest at such and such a rate for the currency of the bill will give the face value, I can feel no real doubt that the transaction is simply one of lending money at interest. If a twelve-months' bill for £105 is sold for £100, surely the purchaser simply lends £100 for a year at 5 per cent. If the face value is £100, and the present value has to be reached by a sum in proportion not giving a round sum in sovereigns as the result, the transaction is the same. Unfortunately the problem involved in these appeals is not confined to this simple case.

In the first place, these companies have been assessed in the second year in question not merely in respect of bills purchased and realised within the preceding year, but in respect of differences between the amount received in that year and the purchase price given before that year. On this principle, a twelve-months' bill bought in May, 1914, and paid in May, 1915, would be treated as yielding the whole of the profits and gains represented by the

discount in the year ending 1915. This cannot be right; eleven-twelfths of the amount accrued in the previous year. This is a practical matter, and cannot be treated as adjusted by compensation over a series of years. In the first place, the rate of tax may change so that it is material to be exact in determining in what year the income is taxable. Furthermore, these Treasury Bills were sold to individuals as well as to corporate bodies, and if one year is to be treated as bearing what is really one and eleven-twelfths of a year's income, the difference for Super-tax or abatement purposes may be of great importance. I am not insensible of the difficulty of treating interest accrued but not encashed as profits of the year when the question is not of taxing a trading concern on the profits shown by its balance sheet, but of taxing interest or discounts as such. Still the step must, as it seems to me, be taken. The difficulty of adjustment as between the years does not lead me to modify my view that the profit in itself is taxable as an annual profit or gain.

A more formidable complication arises where the Treasury Bill is not bought from the Government or is not held to maturity, but is either bought or sold in the market, or both. I treat the so-called conversion of a Treasury Bill into War Loan as being in substance, as it was in form, a sale to or re-discount with the Government at a price representing the original price plus the proportion of interest or discount accrued. But where a Treasury or any other bill is bought or sold in the market the price depends on the market rate for money. A person who has held the bill for, say, two months may, in a period of pressure affecting himself and the market generally, have to dispose of it at a price involving a loss of the whole or part of or of more than the interest for the time during which he held it. Conversely, in times of ease, he may sell it at a profit exceeding that interest; consequently, by the time the bill matures the bill may have passed through the hands of half a dozen persons, who have made profits out of it aggregating a larger sum than the difference between the issue price and the face value, such extra profits being, of course, exactly equalled by losses made by other holders. How is this situation to be dealt with? Is the difference between the issue price and the face value to be treated as the taxable income on the bill and all assessed on the holder at maturity, or divided among the successive holders proportionately to their periods of holding? In neither case would the solution correspond with the truth. They have not received such profits. In my judgment the matter must be dealt with (subject to an adjustment between the years as already indicated) in the way the Special Commissioners have dealt with it, that is to say, the difference between the amount paid on purchase and that received on realisation must be treated as a profit on a discount within the Second Rule of the Third Case. If any holder has made a loss, he drops out to the extent of the loss, and the aggregate of the differences received will bear tax to the Revenue, even though that aggregate exceeds the difference between the original purchase or issue price of the bill and its face value.

This disposes of the Appeals by the companies, subject only to two observations. Some of the bills in the second year, in the case of one of the companies, were French Treasury Bills with a currency, as I gather, of twelve months or less, as in the case of the British bills. Nothing was said in the course of the argument to suggest there was any distinction between British and French bills for this purpose, and I treat them, therefore, as covered by my decision. The other point is this. In the case of the same company and in the second year, some of the documents were not Treasury Bills, but War Expenditure Certificates. The case gives me no information as to the nature

of these documents, nor do I remember to have been informed of it at the Bar. I must assume that they were on the same footing for this purpose as Treasury Bills. The Appeals by the companies are therefore dismissed.

I have now to deal with the Appeals of the Crown in respect of the year ending April, 1918. There is no doubt that the general scheme of the Income Tax is that it is payable in respect of a source of income existing in the year of assessment, though the amount is often measured by the results of previous years. So far as concerns the property in or occupation of land, the mode of its collection and deduction (in the case of Schedule A) from rent necessarily involves this. Under Schedule C, and in all cases of taxation by deduction, the same principle no less necessarily applies. Under Schedule E the duty, which in the schedule of 1842 is expressed to be " upon " and in the Act of 1853 " for or in " respect of " offices and employments, is to be charged on the persons having, using or exercising the offices and employments, and there is a provision for apportionment in the case of persons quitting the office or employment within the year. The tax is clearly in respect of offices or employments held in the year of assessment, notwithstanding that under Rule 4 the perquisites may be estimated on the profits of the preceding year or on an average of the profits of the three preceding years. Under Schedule D, First and Second Cases, the duty is expressed to be charged in respect of the trade or profession, and there are in Section 134 express provisions for apportionment in respect of broken years. It is well-settled Income Tax practice that assessability depends on the existence of the trade or profession. Omitting Case III and coming to Case IV, which deals with colonial and foreign securities, the tax is to be upon the sums that have been or will be received during the year, and *ex necessitate* the source of income must exist to support the tax. Case V deals with colonial or foreign possessions. Under this case fall nowadays shares in colonial and foreign companies and interests in foreign partnerships. What was mainly in view in 1842 was probably colonial or foreign estates, as can be judged from the reference to remittances and importations. It is to be observed that the duty is to be charged in respect of the " possessions ", though it is charged on the average of the three preceding years. I put it to Mr. Parr during the argument whether he contended that a person who, at the time of the first War Loan (the interest on which bore tax by deduction) had sold foreign possessions, and brought home the money and invested it in that War Loan would be taxed twice, namely, by deduction from his War Loan interest, and also retrospectively on the three years' average profits of the possession which he had got rid of. Mr. Parr said he would not so contend. Therefore, for the purposes of this case I take it that under Case V also, assessability depends on the existence of the foreign or colonial possession. Case VI throws no more light on the matter than the only case hitherto unnoticed, namely, Case III, on which the point now before me immediately depends. I go, therefore, to that case.

This Case III, as is pointed out in the note in Dowell's Income Tax Laws, originally had reference to the duty in respect of property of an uncertain annual value, such as mines and the like, now transferred to Schedule A and governed by special rules as to the computation of the profits. Even as it stands to-day, it has reference to the taxation of lands subject to special use and provides that a further sum may be charged thereon in addition to their annual value as already assessed. It seems quite clear that neither in respect of the mines and the like, as the section originally stood, nor to-day in respect of lands specially used, could there be any tax if the property had ceased to be held.

It remains now to consider whether, under the Second Rule of Case III, there can be taxation of a simply retrospective nature in respect of the profits of the preceding year, not had recourse to by way of measure, but charged as subject matter. It is natural to suppose that the framers of the Income Tax would not desire to combine such a system with that which governs the other Schedules and Cases, especially with the system of taxation by deduction, because it would involve double taxation in the year of a change of investment. Further, even without such combination, a postponed tax like this has the inconvenience of letting the taxpayer go in the year when he has the income, and taxing him when he has parted with it, perhaps by bankruptcy, or of losing the tax altogether when the taxpayer has escaped by death. On the other hand, this may be the effect of the Statute.

It seems to me that when one considers the taxation that is imposed by the other Schedules and Cases, the principle that the duty is imposed in respect only of an existing source is really no more than an implication which arises from the terms of its imposition in each case (land, a business, an office, a permanent investment, a foreign security or possession) and from the machinery erected for its collection. There is no general enactment which expresses it. Now, in the case of public unfunded securities, discounts and interest other than annual interest, there is really no permanent source which yields these gains, nor is there anything in the machinery which gives rise to the implication I have mentioned. It seems to me that the Legislature, holding fast to the idea that these gains must be taxed somehow, has taxed them in the succeeding year rather than provide for a belated assessment in respect of the year in which they were earned. In other words, they have regarded the taxpayer himself as the only source which must exist in the year of assessment, and have taxed him upon anything which he may have made under the heads in question in the year before. It is to be remembered that this subject matter of taxation (apart from the cases where the profits would be carried into the general accounts of a banking or other business taxed under Case 1) would be in the nature of casual profits, and not of great importance. There was no contemplation in 1842 of the unhappy experiment of bringing a vast funded loan like the War Loan, 1929–1947, under the scheme of a Case dealing with profits of an uncertain value.

The Special Commissioners, as I understand, took the view that it was only because there were no dealings with Treasury Bills in the year of assessment by these companies that the assessment had to be discharged. If there had been one dealing, however small, in the eleventh month, the assessment would have stood. This seems to me unreasonable. I can see no continuance of a source of income in the circumstance that a person engages in two perfectly isolated transactions, though of the same nature, in two successive years, with an interval perhaps of twenty-two months. If a man has £10,000 on deposit at his bankers for the greater part of this year, is his liability to taxation on the interest to depend on whether next year he received, perhaps in the eleventh month, a trumpery sum for interest because a purchaser of real estate from him has delayed completion for a few days, or because a judgment recovered for £20 has carried interest under the Statute for a week or two? It seems to me that the mere statement of this criterion shows that there is in this case of such interest and of profits from discounts no source upon the continuance of which liability to Income Tax can turn. A suggestion was thrown out by the Special Commissioners in the Cases Stated that the classes of profits which would in subsequent years be chargeable under the Rule of the Third

Case are assessable in the first year in which they arise under the Rule of the Sixth Case, so that the anomaly that the Revenue would always lose one year's tax, if the liability disappeared with the source, would not arise. I do not know whether I rightly follow this suggestion, but if I understand it aright, if a man receives £1,000 from interest on short loans or discounts this year, and £10 from a similar source next year, and nothing the year after, then this year he pays on £1,000 under Case VI, next year he pays on £1,000 again under Case III, and the year after nothing, so that in all he pays tax on £2,000, having received £1,010. Conversely, if he received £10 the first year and £1,000 the next, he only pays in all on £20. I can find no solution of the problem before me in this direction.

Upon the whole, I can come to no other conclusion than that in the case of the discounts and interest of money on short loans mentioned in Rule 2 of Case III, no question of the existence of any source in the year of assessment can arise.

A good deal was naturally said during the argument as to the position of the War Loan, 1929–1947, the taxation of which has been brought under the authority of Parliament within Case III. In this case the dilemma which arises is indeed formidable by reason both of the vastness and of the nature of the subject matter. On the one hand, if there is to be no tax in respect of a year's interest unless the stock is held in a succeeding year the stock can be held tax free for every alternate year if not held in the intervening years. On the other hand, if the holding of the stock involves a hanging claim for Income Tax to fall upon the holder the year after he has parted with it, not only may he be taxed upon it (as already pointed out) after he has lost it by bankruptcy, but it is not an asset to its full face or market value in any balance sheet, unless reinforced by a suspense account provided for Income Tax. Further, if funds in settlement stand invested on such security, the hardships to tenants for life due to double taxation when upon sale or maturity of the loan the fund is transferred to a security, the interest of which is taxed by deduction or otherwise in the year of receipt, or when the income goes over on the attainment of the age of 21 years by children or otherwise, will be of the most serious character. This problem is one of the most pressing kind in cases of those numerous persons who contemplate leaving holdings in this loan as a provision for their families. I am, however, not required to deal with it on this occasion. I merely decide that in the case of profits from discounts there is no existing source to be looked for in the year of assessments in order to support the tax.

In the result the appeals of the Crown are allowed. The appeals of the companies are dismissed. The Crown will have the costs of both sets of appeals.

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Notices of Appeal having been given against the decisions of Mr. Justice Rowlatt, the cases were heard together in the Court of Appeal on the 16th and 19th April, 1920, before the Master of the Rolls (Lord Sterndale) and Warrington and Scrutton, L.JJ., when judgment was reserved. Sir John Simon, K.C., the Hon. W. Finlay, K.C., and Mr. A. M. Bremner appeared as Counsel for the Institution, Mr. A. M. Bremner on behalf of the Association, the Attorney-General (Sir Gordon Hewart, K.C., M.P.), Mr. T. H. Parr and Mr. R. P. Hills as Counsel for the Crown against the Institution, and Mr. T. H. Parr and Mr. R. P. Hills for the Crown against the Association.

Judgment was delivered on the 10th May, 1920, their Lordships holding :—

(1) that the difference between the price paid for a Treasury Bill and the sum realised by the purchaser on maturity of the Bill is not an accretion of capital but a profit on discount within the second rule of Case III of Schedule D.

Where, however, the Bill is not held until maturity, *i.e.*, in the case of sale or conversion, " the only amount that can be taxed " is the amount by which the bill has increased in value by reason " of its advance towards maturity and the consequent accrual of " interest upon it."

(2) that the profits represent income of the year in which they are received, although they may have been accruing over more than one year ; and

(3) that in order to be taxable in a particular year in respect of income from any source, a person must possess that source of income in that year.

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JUDGMENT.

*Lord Sterndale*, M.R.—This appeal from Mr. Justice Rowlatt raises two questions : Firstly, whether the Appellants are liable to be assessed to Income Tax on certain transactions in respect to Treasury Bills, and, secondly, if so, are they liable to be so assessed in the last year in question when there were in fact no transactions of the description, and they received nothing in respect of any such transactions. The Appellants were not assessed in the years in question under Schedule D in respect of the profits and gains of a business, but the Crown seeks to assess them under Case III of that Schedule in respect of profits, or income derived from profits, on discounts.

The transactions in question consist of the purchase of Treasury Bills, which are documents issued by the Government by which it undertakes to pay, on the expiration of a term fixed in the bill, a certain sum of money in consideration of a smaller sum paid down at once. The bills are therefore issued at a discount which is fixed from time to time by the Government. The rate of discount is at present 6½ per cent. ; it was a short time ago 5½ per cent. In some cases the Appellants held the bills until maturity, in some they realised them by sale and in some they converted them into War Loan. Sometimes the proceeds of the payment of the bills or of the sales were received in the same financial year as that in which the bills were purchased, and sometimes in a subsequent year. The Crown assessed the Appellants for Income Tax in respect of the amount received at the maturity of the bills in excess of the price given for them by the Appellants, and upon the profits made upon the sales in the years in which the sums were received. The first question depends upon whether this assessment can be justified under Schedule D, Case III. The first and second rules of this case are as follows. " Third Case.—The " duty to be charged in respect of profits of an uncertain annual value not " charged in Schedule A." Then the first rule is, " The duty to be charged " in respect thereof shall be computed at a sum not less than the full amount " of the profits or gains arising therefrom within the preceding year, ending " as in the first case, to be paid on the actual amount of such profits or gains " without any deduction." The second rule is, " The profits on all securities " bearing interest payable out of the public revenue (except securities before " directed to be charged under the rules of Schedule C), and on all discounts " and on all interest of money, not being annual interest, payable or paid by

"any person whatever, shall be charged according to the preceding rule in "this case."

These transactions are said to come under the words "profits on all dis- "counts". The expressions "profits on discounts" and "profits on interest" are curious, but I think they must mean, in substance, profits arising from discounts received on discounting transactions, and profits arising from interest received on securities bearing interest. The contention of the Crown is that, when the Appellants buy for £93 10*s.* a security for which at the end of a certain period they receive £100, they make a profit by having bought the security at a discount and that this is rightly described as a profit on a discount. It is further contended that the same principle applies when they sell the security at an increased price by reason of its being nearer to maturity. The Appellants, on the other hand, contend that they merely receive an accretion to their capital and not any income or annual profit or gain.

I agree with Mr. Justice Rowlatt that the case where the Appellants hold the bill to maturity is a simple one. The transaction is that the Government borrow the money paid for the bill for a certain period and pay a larger sum at the end of that period, the difference between the two sums being the amount which they pay for the accommodation. In the form in which the transaction is carried out I think the amount is a profit made by buying a security at a discount and therefore comes within the somewhat odd term, profit on a discount.

The case where the bill is sold before maturity is not so simple. If all other elements were eliminated the increased value of the bill would be regulated by the extent to which it had advanced towards maturity. But the other elements cannot be eliminated. The price of the bill in the market depends upon the state of the money market and the rise or fall in the value of money, and any increased price attributable to these causes cannot be taxed as profit on a discount. In the case of a sale, therefore, I think the only amount that can be taxed is the amount by which the bill has increased in value by reason of its advance towards maturity and the consequent accrual of interest upon it. The amount of profit arising from the fluctuation in value of money does not arise from the discount, *i.e.*, the difference between the present value and the value at maturity, and does not therefore come within the words "profit "on a discount". It might be taxed as profits arising from a business of discounting, but the Crown have deliberately elected not to assess the Appellants under this head, no doubt because in that case account would have to be taken of losses. It follows from this that the Appellants have not been assessed on a right principle in the case of sales for they have been assessed on the total profits made on the sales, and the case should go back to the Commissioners in order that the proper adjustment should be made in these cases.

It has been pointed out that in some cases the face value of the bill, or the profit on a resale, is received in a different financial year from that in which the bill was bought, and in securities of longer date than Treasury Bills, *i.e.*, War Expenditure Certificates, the interest may be accruing over three or even more financial years, but I do not think this fact presents any difficulty. The amount received is in my opinion to be taxed in the year in which it is received. Although it may be accruing over several years, it only becomes taxable income in the year in which it is received.

I think in the case where the Treasury Bills were converted into War Loan the same principle applies as in the case of sales. On the first point, therefore, subject to the amount taxable in the case of sales and conversion being adjusted, the appeal in my opinion fails.

Some discussion took place as to the possible effect of the decision in this case upon dealings in other securities, *e.g.*, Victory Loan and War Loan. I express no opinion as to these matters, they are not before us, and I have not present to my mind all the circumstances necessary for the formation of an opinion upon them. I think I ought to confine myself to deciding the case before me and not to consider any possible effect which that decision may have upon other cases. They must be decided when they arise.

The second point arises in this way. In the last year under consideration the Appellants had no transactions in discounts of any kind, either Treasury Bills or otherwise, and they contend that they ought not to be assessed in that year as there were no profits arising from the source of profits on discounts. The Commissioners upheld this contention but their decision was reversed by Mr. Justice Rowlatt. I think the Commissioners' decision was right on this point. It seems to me to be a general principle of Income Tax Law that a person in order to be taxable in a particular year must have an income arising from a source existing in that year and in order to justify this assessment the Crown must show some reason for departing from that general principle. It is admitted that if the taxation be in respect of a trade, or business, or an office, or of property the taxpayer must continue in the year of charge to carry on the trade or business or hold the office or the property. It was, however, contended for the Crown that the principle did not apply in this case because by the first rule of the Third Case the duty to be charged was computed according to the profits of the preceding year, and, therefore, if the last year was not taxed because there was no source, one year escaped taxation altogether. I do not think the first rule has this effect. The provision as to computation of profits is the same as that in respect of trades, etc., in the first rule of the First Case, and it is admitted that in that instance the trade must exist in the taxable year in order to make the taxpayer liable. I see no reason for construing the same provision in a different way in the two rules; both refer to methods of computation only, and are not directed to whether there is a taxable income or not. Besides, as pointed out in Dowell's Income Tax Laws, 7th Edition, page 300, the Third Case originally dealt with property which must have existed in the hands of the taxpayer in the taxable year in order to make him liable, and it can hardly have been intended by the insertion of the second rule to alter the effect of the first. If the first year does escape taxation, it is because the Legislature has not inserted in the second rule of the Third Case such a provision as is found in the first rule of the First Case. It is suggested by the Commissioners that the profits of the first year might be taxed under the Sixth Case. I do not think it necessary to decide that point, for even if they be not taxable it does not in my opinion show that the taxpayer can be taxed in respect of a source of income which does not exist.

The Crown, however, also contended that, even if this conclusion be correct, the Appellants should be assessed in the last year because there was in fact an existing source by reason of the fact that the Appellants had money which could have been used for discounts if they had wished to use it. I do not think this is sound. The source is money employed in transactions involving discounts and so making profits on discounts, and not money itself probably employed in something quite different. Mr. Justice Rowlatt seems to have held that the Legislature considered the taxpayer himself as the source of income, and, as he says, the Legislature must "have taxed him upon anything "which he may have made under the heads in question in the year before." I cannot find any provision to this effect unless it is to be found in the first

rule of the Third Case, and for the reasons I have already given I do not think it is to be found there.

On this second point I think the Appellants are entitled to succeed.

*Warrington*, L.J.—Three questions arise in this case: (1) Whether the difference between the amount paid to the Treasury for a Treasury Bill and the sum payable and paid at maturity is a profit in respect of which the holder of the bill is liable to be charged with Income Tax; (2) Whether the profit made by selling the bills during currency for a higher price than that paid for them is a profit in respect of which the man who receives it is liable to be charged to Income Tax; (3) Whether the subject is liable to be charged on the above heads if he has had no transactions of the nature in question in the year of assessment. The profits in question are brought into charge, if at all, under Schedule D and are to be charged annually on and paid by the persons receiving or entitled to the same.

If they are brought into charge at all they come under the Third Case as profits of an uncertain annual value not charged in Schedule A and are governed by the second rule which reads as follows: "The profits on all securities "bearing interest payable out of the public revenue (except securities before "directed to be charged under the rules of Schedule C), and on all discounts, "and on all interest of money, not being annual interest, payable or paid by "any person whatever, shall be charged according to the preceding rule in "this case."

The effect of this is that the duty is to be computed on a sum not less than the full amount of the profits within the year preceding the year of assessment.

The National Provident Institution in the year ending the 5th April, 1916, purchased Treasury Bills for a large amount, paying of course a smaller sum than the sum payable at maturity. Some they held to maturity, and received the full amount secured thereby; others they sold or discounted, receiving for those sums in excess of those paid. In the next year, the year ending the 5th April, 1917, they also purchased bills for a large amount, some of which they held to maturity, receiving a larger sum than they paid. The rest of the bills held by the Institution, whether purchased during that year or held from the previous year, were converted into War Loan for a sum exceeding the sum paid for them. In the year ending the 5th April, 1918, the Institution neither held nor had any transactions in Treasury Bills.

For the years ending the 5th April, 1917, and the 5th April, 1918, they were assessed in the full amount of the differences realised as above mentioned in the years ending the 5th April, 1916, and the 5th April, 1917, respectively. On appeal to the Special Commissioners the assessment for the first year was confirmed, but that for the second year was discharged on the ground that in that year the source of income from which the profits in the preceding year were derived did not exist, and that the profits in the preceding year are not chargeable by themselves but are only the measure for ascertaining the amount of the chargeable profits in the year of assessment. If the source of such profits did not exist in the last-mentioned year, profits in the preceding year were immaterial. The Institution appealed on the first point and the Crown on the second. Mr. Justice Rowlatt dismissed the appeal of the Institution and allowed that of the Crown. The Institution appeals.

I will take first the case in which bills are purchased and held to maturity. These are paid for under a rate of discount, either fixed by the Treasury or offered by the purchaser and accepted by the Treasury.

I agree with Mr. Justice Rowlatt that in such a case what the purchaser really receives at maturity is the sum he paid together with interest on that sum for the period of the currency of the bill. This seems to me to be either a "profit on a discount" or a profit "on interest of money not being annual "interest". The word "on" is not very appropriate in either case, but I take it to mean "resulting from" in the one case and "derived from the receipt "of" in the other, or some similar expression.

I answer, therefore, in the affirmative the first of the three questions put to myself at the opening of this judgment.

As to the second question, I can see no difference in principle between this and the first. When a holder, whether the original purchaser or not, realises during currency, he really receives a proportion of the total profit resulting from the fact that the bill was bought at a discount. It is true that that proportion may not bear an exact relation to the period of currency but may be determined by variations in the value of money, in the public credit and so forth. But it seems to me that the total of the profits received by the various sellers after deducting losses, if any, cannot exceed the difference between the price originally paid and the sum payable at maturity, and that the considerations I have referred to merely affect the distribution of that difference between the various holders. Profits made by discounting bills seem to me to rest on the same footing, and conversion into War Loan also. This last is simply a sale on certain terms fixed by the Government and investment of the proceeds. The second question therefore must in my opinion be answered in the affirmative.

I agree that the profits must be treated as profits of the year in which they are received.

The third question is, I think, one of great difficulty, and whichever way it is answered the result is not in my opinion wholly satisfactory. On the one hand, if the contention of the Institution is to prevail, profits of the nature in question in, say, the year 1916–17, would escape taxation altogether merely because there were no transactions of the particular nature in the succeeding year, unless, indeed, they would properly be taxed under the Sixth Case, on which point I prefer to express no opinion until it is directly raised and argued. On the other hand, if the view of the Crown is correct, a man who had parted with all sources of income (*e.g.*, by bankruptcy) might be assessed retrospectively on profits accruing before the happening of that event.

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 preceding years, are respectively used merely as a measure for the purpose of taxation of the amount of the profits in the year of assessment.

Excluding for the moment the case in question the general rule appears to me to apply to every Schedule and to every case under each Schedule (with the possible exception of Case VI under Schedule D) and even to cases coming under the first and third rules of Case III. If, therefore, the view of the Crown is correct the cases coming under the second rule of Case III stand (with the possible exception above mentioned) entirely by themselves and afford a single instance of retrospective taxation for the purpose of Income Tax. I think the burden is on the Crown to make out that on the construction of the Acts such an exceptional case exists.

I thought at one time that inasmuch as the general principle is founded not on any express enactment but on an implication arising from the general scheme of the Acts, the apparently casual nature of the profits in question might afford a sufficient ground for excluding the implication in their case. But on consideration I have come to the conclusion that this circumstance is not enough to support a decision in favour of so large a departure from what has hitherto been regarded as a settled principle in the application of the Acts.

As to the non-existence of the source of income in the year of assessment I agree with the decision of the Special Commissioners. It was argued before us that the source of income was the possession by the Institution of funds for investment, and that such source existed although no funds were invested in the particular manner in the year of assessment. I cannot accept this construction. I think the source to be looked for in each case is a separate source from which the profits to be charged are derived. For these reasons I agree with the other members of the Court that on this point the appeal of the Institution succeeds.

*Scrutton*, L.J.—The National Provident Institution is an Insurance Company investing its funds in various securities including Treasury Bills, and assessed to Income Tax, not on its trade as an Insurance Company, but under Case III of Schedule D on the interest on its securities. This case raises two questions. Firstly, on what principle, if at all, it should be taxed on its gains from Treasury Bills, and, secondly, whether it can be taxed on income from Treasury Bills in a year in which it holds none. A Treasury Bill is a promise by the Government to pay a fixed sum on a future day, usually three, six, or twelve months ahead, purchased by the payee for a smaller sum payable at once. The difference between the two sums is really interest on a loan of the original price by the purchaser to the Government for the period of the bill. The Government state that they will sell Treasury Bills at a rate of discount. At present they will sell a twelve months' bill for £100 for £93 10*s.*, 6½ per cent. is the rate of discount and the interest on a loan of £93 10*s.* to the Government for twelve months. Under the Act of 1842, Schedule C charged all profits arising from annuities, dividends and shares of annuities payable out of any public revenue, with a provision in Section 97 that interest payable out of the public revenue on securities issued by the Exchequer or other public office should also be charged under Schedule C, and a provision in Section 95 that small dividends under fifty shillings, otherwise chargeable under Schedule C, should be chargeable under the Third Case of Schedule D.

Schedule D in the Act of 1842 taxed profits or gains from property or trades, and its Third Case taxed profits of uncertain value not charged in Schedule A, the second rule referring to the profits on all securities bearing interest payable out of the public revenue, except securities before directed to be charged under the rules of Schedule C, which would seem to refer to Section 97 and profits on all discounts and profits on all interest of money, not being annual interest. Section 102 was an express charging section on annual interest which was not expressly mentioned in Schedule D as it then stood. When the Act of 1853 was passed "Interest" was expressly added to Schedule C, and a clause was added to Schedule D expressly charging "interest and other annual profits "and gains not charged by virtue of any of the other Schedules." What is the position then of the person who purchases, say, a six months' Treasury Bill at the rate of discount of 6½ per cent., and (1) holds it till maturity and cashes it, or (2) sells it during currency at the then market price? It appears

to me that in the first case if the form of the Treasury Bill prevents it being described as a security bearing interest because the promise to pay £100 is not to pay £100 and interest, there is clearly a "profit on a discount". The phrase is an old one, as is the next phrase, "profit on interest". They must be elliptical for "profit on (a security bought at)" or "(a transaction involv-"ing) a discount," and "profit on (a security yielding)" or "(a transaction "producing) interest", the profit being the amount of interest or discount respectively. As the effect of the transaction is that the purchaser at a price obtains at maturity his price back with an increase in fact representing interest upon it, in my opinion the real interest, though not paid under that name, is taxable as "profit on a discount" under the second rule of the Third Case of Schedule D, the amount to be assessed (subject to the point about the year of assessment) being the difference between price originally paid and amount received back.

The case where the bill is sold during currency is a little more complicated. The interest or discount is accruing proportionately to the time expired since payment, but the market price may not be simply the price paid plus a proportionate part of the interest accrued at the original rate of discount or interest. The value of money may have fallen or risen, and this may affect the price of the bill. For instance, when the Treasury increased the rate of discount from 5½ to 6½ per cent. the price of Treasury Bills would at once fall. A purchaser would not give £94 10*s*. to get £100 twelve months hence, when he could get such a security from the Treasury for £93 10*s*., and where the value of money was falling, a seller of Treasury Bills would get more than his original rate of discount or interest in the price on realization. The price therefore of a Treasury Bill would depend on two matters: (1) How much interest or discount had accrued by the progress of the bill towards maturity. (2) How much the value of the promise to pay had altered by the rise or fall of the value of money. While in taxation of a trade the latter element would be included in the profits of the trade, in my opinion in the taxation of interest or discount it is not included, for it is appreciation or depreciation of the capital sum. If the Crown taxed an insurance company or a discount house as a trade, then profits by the sale of bills during currency would be included, but then the taxpayer would deduct his working expenses and his losses. The representatives of the Crown think they do better by taxing an insurance company on the interest of its accumulated funds, and not as a trade. They may be wise to do this, but if they make this election they cannot in my view assess as interest or discount what is really a profit from buying and selling, additional to interest. The result in the present case appears to be that where the Institution has been taxed in respect of the year when Treasury Bills mature, on bills held to maturity, on the difference between amounts paid and amounts received, it is rightly taxed; but that where the Institution is taxed on bills sold or discounted within the year on the difference between amounts paid and amounts received, it is wrongly taxed, for it is being taxed not only on interest or discount, but on an amount increased by appreciation or accretion, or decreased by loss, of capital. The amount of assessment should be in the case of each bill on the amount of interest which would be received if the bill were held to maturity, reduced by proportion to the time for which the bill was held as compared with the time of full currency. For instance, a twelve months' Bill for £100 bought at £95 and sold after six months represents £2 10*s*. interest, the difference of price obtained below or above £97 10*s*. represents loss of or accretion to capital. The term "discount" as explained in the case of *Land Securities Company* v. *Farquhar* (1896, 2 Ch. 320) is I think used in the com

mercial meaning of interest on the sum secured or to be received, and not in the mathematical meaning of the sum necessary at a given rate of discount to raise the sum paid to the sum secured.

The assessment in this case on bills sold does not proceed on this basis, and should be sent back to the Commissioners to be adjusted on the principle stated. In the case of a bill bought in one year of assessment and sold or matured in another, the interest or discount falls to be taxed in the year when the profit is received, though part of it was earned but not received in a previous year.

The second point arises because the Crown contend that as the Institution made profits by discounts in the year 1917, and as by the first and second rules of the Third Case of Schedule D profits on discounts are to be computed at the amount of the gains arising therefrom in the previous year, the Crown can assess profits on discounts for the year 1918, a year in which no Treasury Bills were held and there were no profits, on the amount of the profits in the previous year 1917. The Commissioners declined to do this, taking the view that an assessment required a source of profit in the year of assessment. The learned Judge below took a different view, and appears to hold that, if under this case you have a taxpayer in a year of assessment, you may tax him for that year on any profit under Case III he made in the year before, though he has no such source of profit in the year of assessment. As he says, "In the "case of profits from discounts there is no existing source to be looked for "in the year of assessment in order to support the tax" . . . The Legislature "have regarded the taxpayer himself as the only source which must "exist in the year of assessment."

In my view on the general scheme of the Income Tax Acts, it is clear that an assessment for any year requires a taxable subject matter in that year though the conventional value of the income from that subject matter may be measured in the first instance by the average income of previous years. Under the second Section of the Act of 1853 the duties are granted yearly for and in respect of the several properties described in the Schedule, and by Section 48 of the Taxes Management Act, the year of assessment for Income Tax is from the 6th day of April to the following 5th day of April. I cannot find any trace of a right to assess for any year a taxpayer in respect of property which he does not hold at all in that year. I do not gather that it is suggested that a taxpayer can be assessed under Schedule A or B for a given year if in that year he neither owns nor occupies any land, or under Schedule D for a trade which he does not carry on at all in that year, or under E for an office which he does not hold in that year. The immediate reason suggested is that the duty to be charged under the Third Case of Schedule D is by the first rule thereunder to be computed on the profits or gains arising therefrom in the previous year; but it seems to me clear that the duty is to be charged on profits in the year of assessment, and if there are none, the opportunity for valuing them by the conventional rule of the previous year's profits never arises. Under Schedule D, Case I, indeed the duty was to be computed on an average of previous years; but it has never been suggested that this is a retrospective taxation, taxing a man on a trade not carried on in the year of assessment, on the three previous years' average.

When the first rule of the Third Case was framed in 1803 (43 Geo. III, c. 122, ss. 84, 102), it was limited to certain mines and other concerns on land, and I do not understand it to be suggested that the first rule then applied to justify an assessment when there was no mine in the year of assessment.

"Interest" was brought in in 1805 into the second rule, but I do not see that this could alter the meaning of the first rule.

Mr. Justice Rowlatt appears to have been impressed with two points. The first is that on this view, if there is a small discount in the year of assessment you will yet conventionally value it on the much larger profits of the preceding year. This is true of all conventional valuations, but I think the learned Judge must have temporarily overlooked that the taxpayer would until 1907 recover the excess back by an application under Section 133 of the Act of 1842. If he does not since 1907 recover the excess, it is because Parliament has not provided means in this case to correct the conventional valuation when it turns out to be erroneous, having by the Revenue Act of 1907, Section 24, repealed Section 133 of the Act of 1842. The learned Judge was impressed also by the contention that, if you are assessed on the profits of the previous year, you do not pay on your first year's profits, for their is no previous year, and do not pay in the next year, for there is no source of income. Personally I am inclined to think the view of the Commissioners is correct that in the first year you could be assessed under the Sixth Case of Schedule D, for these profits could not be assessed under any of the preceding rules. The question is whether interest which cannot be assessed under Case III because there are no such gains in the preceding year as required by Rule 1, is "profits "not falling under any of the foregoing rules." The learned Judge suggests that in this case the taxpayer could be assessed in both the first and second year on the profits of the first year. I think he could, but in the learned Judge's first illustration he would, until 1907, have got back in the second year the tax on £990 under Section 133 of the Act of 1842. I think the learned Judge is right in saying that in his second illustration—£10, first year; £1,000, second year; nil, third year—the taxpayer would only be taxed on £20, but this is because there seem to be no means of correcting a conventional valuation by increasing it to actual profits, though Section 133 used to give a means of correction by reducing it to actual profits. The same result undoubtedly happens under Case I of Schedule D. If a trader makes profits—first year, £2,000; second year, £4,000; third year, £6,000; fourth year, £8,000, he will be assessed for the fourth year on £4,000, the average of the three preceding years. If he suddenly stops his business at the end of the fourth year, he cannot be assessed in the fifth year at all, for there is no trade to assess, and the profits of the fourth year will escape taxation. This may be a reason for legislating, but is not one for putting a strained and impossible construction on the language of the Acts. When the learned Judge holds that "in the case of profits "from discounts there is no existing source to be looked for in the year of "assessment in order to support the tax," I cannot agree with him. I think his view is contrary to the whole scheme of Income Tax legislation, and I agree with the view of the Commissioners that a source existing during the year of assessment is necessary to support an assessment, although when so existing it is conventionally valued with reference to a previous year.

Counsel for the Crown argued that, if it was necessary to find a source of profits in the year of assessment, they could obtain it if the taxpayer had money though he did not use it at interest or discount. But the taxable matter is "discounts" and "interest on money", not the money itself. They further argued that, as there were short interest transactions which made a loss, they would do as a source of income to support conventional valuation on the previous year. Again, in my opinion, you must find profits on discounts to justify the conventional valuation of them. Parliament may or may not

have inserted provisions for correcting the conventional valuation to the real facts, but the presence or absence of such special provisions does not seem to me to affect the cardinal principle that the tax is on profits from property existing in the year of assessment, though it may be conventionally valued by reference to the profits of a preceding year, and when I find every Schedule and rule but this depending on the presence of a source of profits in the year of assessment, when I find the language of the first rule of Case III framed in 1803 at a time when it required a source of profit in the year of assessment, when I find identical language applied to other cases, such as Case I of Schedule D, which also requires profits in the year of assessment, I see no ground for supposing that in this case only you may assess a man in respect of property of which he has none during the year of assessment.

It was much discussed before us what the consequences of allowing this appeal might be on subject matters which are not before us, War Loan and Victory Loan. I prefer to reserve opinion on these matters till they come before us in proper form. It may be that Parliament has passed certain specific enactments without appreciating their consequences. That is a matter for Parliament to rectify if it can, and if it desires to. It is not the business of the Courts to form their decisions, not by construction of the statutes, but by consideration of the effect of their decisions on other subject matters. I also desire to reserve my opinion on the question whether a man who has no income at all in the year of assessment can be taxed to Super-tax because of his preceding year's income.

In my view the appeal of the taxpayer on the second point succeeds, and the assessment for the last year in which no Treasury Bills were held should be discharged.

*Lord Sterndale*, M.R.—Each party has succeeded on one part of the appeal, and I think there should be no order as to costs.

*Mr. Finlay.*—Then, my Lord, we have paid the costs below. I submit that the right order will be no costs either here or below.

*Lord Sterndale*, M.R.—No order there either.

*Mr. Finlay.*—If your Lordship pleases.

*Lord Sterndale*, M.R.—Now, what about the other case ?

*Mr. Bremner.*—It is agreed between the parties that the order made by your Lordship in the previous case which has just been delivered should govern this case also.

*Lord Sterndale*, M.R.—Very well.

*Mr. Bremner.*—So that there will be the same order.

*Lord Sterndale*, M.R.—Very well.

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Notice of Appeal having been given against the decisions in the Court of Appeal on the Appeals and the Cross-Appeals, the cases were heard in the House of Lords on the 24th, 25th and 28th February and the 1st, 3rd and 4th March, 1921, before Viscounts Haldane and Cave and Lords Atkinson, Moulton and Sumner, when judgment was reserved.

The Attorney-General (Sir Gordon Hewart, K.C., M.P.), the Solicitor-General (Sir Ernest Pollock, K.C., M.P.) and Mr. R. P. Hills appeared as Counsel for the Crown and Sir John Simon, K.C., Sir William Finlay, K.C., and Mr. A. M. Bremner on behalf of the Institution and the Association.

Judgment was delivered on the 3rd June, 1921 (varying the decision of the Court of Appeal), their Lordships holding :—

(1) That the whole difference between the price paid for a Treasury Bill and the sum realized by the purchaser, whether by holding the bill until maturity or by selling it or converting it before maturity,

represents a profit chargeable to Income Tax under Case III of Schedule D, and that no part of that profit is an accretion of capital;

(2) That a profit so made constitutes income of the year in which it is received; and

(3) (Viscount Cave dissenting) that in order to be chargeable to Income Tax for a particular year in respect of income from any source, a person must possess that source of income in that year.

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JUDGMENT.

*Viscount Haldane.*—My Lords, the Appeal and the Cross-Appeal raise questions of importance as to the scope of the Income Tax. The circumstances which give rise to these questions are, briefly stated, as follows:—In each of the financial years ending April 5th, 1916, and April 5th, 1917, which I will call the years 1915-16 and 1916-17, the Respondent Institution bought at the Bank of England Treasury Bills, maturing for payment after intervals of three, six, and nine months. These were bought at a rate of discount fixed by the Treasury. The bills bought in 1915-16 were, as to some of them, sold in 1916-17 during their currency, and as to the others of them were held until they matured and were paid off. All the bills bought in 1916-17 were held without being sold, but before the end of 1916-17, early in 1917 and before 5th April, they were converted into 5 per cent. War Loan, on terms under which each bill was credited to the Institution as investors in the War Loan at a figure representing the amount of the bill, less a discount of 5 per cent. At the end of the year 1917-18, the Institution did not hold any Treasury Bills, and had had no transactions in them in that year. In each of the years 1916-17 and 1917-18 the Institution received and paid interest on short bankers' loans, but we are asked from the Bar to assume that neither this circumstance nor the fact that they received interest on investments in War Loan affects the present question. In respect of their transactions in Treasury Bills the amounts received by or credited to the Institution exceeded the amounts paid by it for the bills by £5,422 11s. 7d. in 1915-16 and by £20,566 8s. 0d. in 1916-17. The latter amount includes a small sum representing the difference between the amounts received and paid in respect of interest on bankers' loans. The Institution was not for any of the three years ending in April, 1918, assessed to Income Tax on the balance of its profits and gains under Case I of Schedule D. For 1916-17 the first of the assessments now in question was made upon the basis of the differences between the amounts paid and the amounts received in respect of the Treasury Bills realised within the preceding year. For 1917-18 the second of the assessments was made upon the basis of the differences between the amounts paid and the amounts received in respect of Treasury Bills realised in 1916-17 together with the differences between the interest paid to and the interest received from bankers on short loans within 1916-17. As to this last item, as I have already mentioned, no question arises. The Institution did not dispute its liability to be assessed on the amount, and on the other hand it is by agreement to be looked on as a source of income wholly independent of that from which the profit on discounts arose.

My Lords, the Crown contends that the differences in controversy between the amounts paid and the amounts received in respect of the bills, whether obtained by waiting until maturity or on sale or conversion of the bills, were profits on discounts chargeable for Income Tax under the Third Case of Schedule D of the Income Tax Act. It alleges further that there is liability to the tax under that Case on the basis of the full amounts of the profits or gains arising from the sources to which the Case extends received within the

preceding year, whether any profits or gains do or do not arise within the year of actual assessment. On the other hand, it is argued for the Institution that in any event the assessment for the year ending 1918 cannot be upheld inasmuch as the Institution did not hold, or have any transactions in, Treasury Bills during that year. It is further said that, apart from this, the difference between the sum paid for a Treasury Bill and the sum received on sale or maturity is not an annual profit or gain, but an accretion to capital and is not a profit on discount within the meaning of the language of the Third Case.

My Lords, as to the year 1916-17, since there were transactions in the bills in that year the only question which arises is whether the assessment for the year should be remitted to the Special Commissioners of Income Tax, who stated the case on which all the points are raised, to eliminate the amount of any accretion to capital in the amount received for a bill due to such causes as the rise or fall in the value of money and the state of the money market, as distinguished from the difference in value by which the bill had increased by its mere advance towards maturity. The Special Commissioners thought that the whole of the transactions with the bills were transactions in discounts and that the whole of the difference realised in these transactions were profits on discounts within the meaning of the Third Case. They therefore confirmed the assessment for 1916-17 but they altered that for 1917-18 by excluding from it all sums representing profits from such transactions in 1916-17. This they did on the ground that such profits did not come within the words of the Case unless the source from which they arose, namely, discount transactions, had continued to exist in the year of charge, 1917-18. Since, as I have already stated, there were no such transactions in this year, they held that there could be no assessment of the sole kind which was attempted. As to the year 1917-18 this is the only question before the House. A third point was, indeed, at one stage in the proceedings made for the Crown, that the profits made in 1916-17 from other sources, such as the interest on bankers' loans or war loans, might count as a source continuing in 1917-18 and as satisfying for the purposes of the assessment the language of the Legislature. The Commissioners decided against the Crown on this point and, as the latter did not again raise it in the Courts below, it is agreed that your Lordships have not to decide it.

My Lords, the question, raised by the Case Stated by the Commissioners came in the first instance before Mr. Justice Rowlatt in the King's Bench Division. That learned Judge dismissed the Appeal of the Institution and allowed that of the Crown. He was of opinion that the difference between the amounts paid for the purchase of the bills and the amounts received on realization was profit on discount within the Third Case. He was further of opinion that the principle of taxation under the first two rules of this Case was to impose the tax on the taxpayer personally as a true source in the year of assessment and to impose the tax in respect of whatever he had made under the heads of the two rules in the preceding year, whether there were any other source continuing, such for example as a business, or not. Upon these points the learned Judge delivered an elaborate and closely reasoned judgment. The Court of Appeal, however, varied the decision materially. On the question indeed, whether the transactions in Treasury Bills were, generally speaking, transactions in discounts, they unanimously dismissed the Appeal and upheld the view of the Special Commissioners and Mr. Justice Rowlatt, that the profits therefrom, when truly computed, were chargeable as profits on discounts under the Second Rule of the Third Case of Schedule D of the Income Tax Acts. They held also that, in instances where the Institution had bought a bill from the Government and had held it till maturity, the whole of the accretion was rightly brought

into computation as a profit on discount, being really on the balance of interest upon a sum lent. But by a majority, Lord Justice Warrington dissenting, the Court of Appeal held that the whole of the difference between the amount contracted for and the amount received for a bill which was sold or converted into War Loan during its currency, was not necessarily taxable as a profit on a discount. The difference did not necessarily represent only a profit by way of income, but might in part represent an accretion to capital. Such an accretion might be due to the state of the money market and the rise or fall in the value of money and the rates of interest thereon by which the price of the Treasury Bill might have been caused to rise or fall without strict correspondence with its progress towards maturity. The only amount to be taxed as profit on discount in such a case was, therefore, the amount by which its value had increased merely by reason of its advance towards maturity. The assessment was, therefore, ordered to be remitted to the Special Commissioners for adjustment by elimination of the elements of profit due to accretion of capital on this principle.

My Lords, on this last question I find myself unable to agree with the view of the Court of Appeal. I see no answer to the argument as stated by Lord Justice Warrington. It is concise and I will adopt his words :—" When a " holder, whether the original purchaser or not, realises during currency, he " really receives a proportion of the total profit resulting from the fact that " the bill was bought at a discount. It is true that that proportion may not " bear an exact relation to the period of currency but may be determined by " variations in the value of money, in the public credit and so forth, but it " seems to me that the total of the profits received by the various sellers, after " deducting losses, if any, cannot exceed the difference between the price " originally paid and the sum receivable at maturity, and that the considera- " tions I have referred to merely affect the distribution of that difference " between the various holders. Profits made by discounting bills seem to me to " rest on the same footing, and conversion into War Loans also. This last " is simply a sale on certain terms fixed by the Government, and investment " of the proceeds."

My Lords, I do not think that this reasoning is really answerable. I agree too, not only with Lord Justice Warrington, but with the other members of the Court of Appeal, that the profits whatever they are in this case, must be treated as profits of the year in which they were received.

The remaining question is one of considerable difficulty. It is that of the chargeability by assessment for the year 1917-18 in which there were no transactions in bills, of the transactions during the previous year. The Court of Appeal, differing from Mr. Justice Rowlatt, thought the profits on discounts could only be charged under the Third Case of Schedule D in the year when the source of such profits still continued to exist, and that in consequence the profits on discounts of a previous year escaped taxation under that Case if in the succeeding year no such profits had been made. My Lords, this question, the most important in the Appeal brought before us, can only, I think, be answered if the principle on which the Income Tax legislation is based has been first defined, and to this principle I therefore turn. The case is governed, not by the general Income Tax Act of 1918, an Act which has superseded the older legislation, but by the Income Tax Act of 1853 and the provisions of the Act of 1842 which it kept alive. The Finance Acts of 1916, 1917 and 1918 rendered those the governing statutes for the purposes of the question before us. My Lords, in *London County Council* v. *The Attorney General* (1) (1901 A.C. 26) it was

(1) 4 T.C., 265.

decided by this House that the Income Tax Acts of 1842 and 1853, as modified by the Customs and Inland Revenue Act, 1888, 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 of Schedule D and the other Schedules or their branches, whatever be the idiosyncrasies of the methods prescribed for collection. 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. There was imposed under the Schedules no collection of taxes distinct from each other, but simply one tax with standards for assessment which varied according to the sources from which the taxable income was derived. Now the Act of 1853, as appears from its title and from Section 2, was an Act to impose an Income Tax on annual profits or gains arising from property or from some occupation.

My Lords, Schedule D of the Income Tax Act, 1853, includes as taxable profits the annual profits and gains arising or accruing to any person residing in the United Kingdom from any kind of property whatever, whether situated in the United Kingdom or elsewhere; and extends to "all interest of money, "annuities, and other annual profits and gains not charged by any of the "other schedules contained in this Act." By Section 5 the assessments are to be made under the regulations and provisions of the Income Tax Act of 1842. The Third Case of Schedule D in the latter Act is provided by Section 100. It enacts that the duty to be charged in respect of profits of an uncertain annual value not charged in Schedule A is to be as follows:—"First.—The "duty to be charged in respect thereof shall be computed at a sum not less "than the full amount of the profits or gains arising therefrom within the "preceding year, ending as in the first case, to be paid on the actual amount "of such profits or gains, without any deduction. Second.—The profits on "all securities bearing interest payable out of the public revenue (except "securities before directed to be charged under the rules of Schedule C) and "on all discounts, and on all interest of money, not being annual interest, "payable or paid by any person whatever, shall be charged according to the "preceding rule in this case." There is a third rule which provides for a charge for the tax upon the profits of dealers in cattle and milk when the annual value of the land occupied does not afford a just indication of the profits made. In such a case a return of such profits may be required for assessment, to be measured for taxation on the retrospective principle laid down in the first rule of the same case. My Lords, it was open to the Crown to have charged the Institution for Income Tax on the balance of its profits and gains under the first rule of the First Case of Schedule D. This course, for reasons that were probably sufficient, the Crown did not take. Section 102 of the Act of 1842 is the relevant charging section. It is obvious that its purpose is to impose the charge for tax upon everything within Schedule D in such a way as to sweep in interest on money not reserved or charged or payable for the period of one year. It is clear that, if the profits or gains in question come within the first and second rules of the Third Case, they are thus charged. But the question is whether they do so come, for if not no other ground for charge has been alleged before us. It is, I think, for reasons already given, clear that the sums in question are "discounts" within the second rule. The point is whether the first rule charges them. They are no doubt profits of an uncertain annual value within the meaning of the general heading of the Case. In the instance of the assessment for the year 1916–17 the Institution had the transactions I have referred to in Treasury Bills, as well as other analogous transactions,

in the preceding year, 1915–16. The operations in the bills were a source of "profits of an uncertain annual value" and these operations existed and yielded profit in the second year as well as in the first. Subject, therefore, to the other question as to the nature of the differences between the amounts paid and the amounts received in respect of the bills not being annual profits or gains at all, the question on which I have already expressed a view adverse to the contention of the Institution, it is plain that the Institution was properly assessed on such profits measured as in 1915–16. But as to the assessment for 1917–18 wholly different considerations arise. In that year there were no such transactions and consequently continuity of sources between the two years did not exist. The question is whether under such circumstances the Institution can under the words of Rule 1 be charged in respect of the amount of the profits and gains which arose within the preceding year or whether the source of such profits and gains must be one which continued to exist in the year of assessment, so that, whatever the principle of computation or measurement directed to be applied, what is assessable is only profit existing in the year of assessment. My Lords, the language of the rule measures the amount in respect of which the assessment is to be made by that of the profits and gains within the preceding year. But this does not appear to be conclusive. For the principle of retrospective measurement is one which is applied elsewhere in the Acts, limited, however, to cases in which the source of income continues to exist in the year of assessment. It is the profits and gains of a continuing business that are in such cases the subject of assessment, but the amount is measured by reference to preceding years. The first rule of Case 1 of Schedule D seems to me to be just an illustration of this principle. 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 assessment. In the instance of the Third Case itself, the third rule of the three rules seems to conform to the principle, and if the Crown is right in its construction of the second rule, the provision therein contained is accordingly not only out of harmony with the other provisions made in the third rule of the Third Case, but differs from the scheme of the Acts as appearing elsewhere. The first rule of the Third Case, if it stood without any interpretation from the second rule, should I think be construed according to the general principle I have referred to.

My Lords, it is no doubt true, as Mr. Justice Rowlatt pointed out, that the result of applying the general principle that continuation into the year of assessment is the foundation of the tax, coupled with that of retrospective measurement, will be that if there is only a very small amount of profit in the year of assessment the taxpayer may have to pay on a large amount received in the past. It is also true that if he can be assessed only on any profits made in the previous year standing alone and there is no such previous year, inasmuch as he has only begun to earn profits in the year of assessment, he escapes duty. And yet, if he ceases to earn profits after the latter year, he will escape, because in the next or third year of assessment he has earned none. I express no opinion as to whether, such a case occurring in the second year, the taxpayer could be reached under Case 6, which provides for the instances of profits not falling under any of the preceding rules. The point is not before us. For the rest, those who framed the Acts appear to have taken these chances of what Mr. Justice Rowlatt refers to occurring. 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, that 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. Reading the Income Tax Acts as a whole it appears to me that the tax is one of a single kind based, speaking broadly, on a single principle. It is imposed on existing income, however the amount to be levied is to be computed in particular instances. This, my Lords, appears to be the scheme followed out in the Acts, and I think that, if departure from it is alleged at any special point, the departure ought to be clearly demonstrated. The natural construction of the language of the Third Case of Schedule D appears to me to be that the tax is imposed only where there are profits and gains arising within the year of assessment, but that the amount payable is to be measured by reference only to the profits and gains arising within the preceding year. There is little room permissible for conjecture based merely on probabilities in a taxing statute. If I am right, the Appeal of the Crown should fail so far as the 1917–18 assessment is concerned. But I wish to add that having regard to the words employed, I have only come to this view after doubt. As to the question which arises under the 1916–17 assessment, whether the whole of the differences received by the Institution are profits, the Crown succeeds. The Cross-Appeal of the Institution directed to this point should fail.

My Lords, in the Court of Appeal it was considered that, having regard to the fact that each side had failed and that each side had succeeded on a variety of points, there should be no costs either in the King's Bench Division or in the Court of Appeal. Possibly your Lordships may think that that is the proper course to take in this case also—that there should be no costs either here or in the two Courts below.

*Viscount Cave.*—My Lords, in *Brown's* case, the questions raised on this Appeal and Cross-Appeal are conveniently stated in the Appellant's case as follows:—(1) Whether the transactions in Treasury Bills are transactions in discounts within the meaning of the second rule of the Third Case of Schedule D of the Income Tax Act, 1842, and liable to Income Tax in respect of the profits arising therefrom accordingly; (2) Assuming that the transactions in such bills are transactions in discounts for the purposes of that provision, whether, when such a bill was sold before maturity, the entire profit on the transaction should be taken into computation, or whether part should be deducted as representing an accretion of capital; (3) Whether, upon the same assumption, the profits actually arising within a year from transactions in such bills taking place in that year escape taxation if in the next year no transactions in discounts take place or, in other words, whether the principle of assessment on the amount of the profits of the preceding year laid down in the first rule of the Third Case of Schedule D assumes as a requisite of chargeability the continued existence of the same source of profits in the year of charge.

Upon the first question, which turns upon the meaning of the word "discounts" in Rule 2 of the Third Case of Schedule D of the Income Tax Act, 1842, I have no hesitation in agreeing with the decision of Mr. Justice Rowlatt and of the Court of Appeal. A Treasury Bill (of which a form is set out in the appendix to the case) [1] is a simple promise by the Treasury to pay to the holder or order a specified sum on a future date; any such bills (to quote a Treasury Minute of the 13th April, 1915) are drawn for 3, 6, 9, or 12 months as the case may be, and are issued "at fixed rates of discount" at the Bank of England.

[1] Omitted from the present print.

I am unable to see how the purchase from the Treasury of such a bill on these terms is anything but a transaction by way of discount. If it were decided otherwise, an easy way would be opened to moneylenders of evading the payment of tax on their interest on short loans. I agree that the Cross-Appeal, which relates only to this question, fails and should be dismissed. The second question, which turns on the meaning of the expression "profits on all "discounts" contained in Rule 2, presents more difficulty. The question is whether this expression includes the whole profit made by the sale of a discounted bill before maturity or only such part of that profit as is due to the advance of the bill towards maturity. Upon the whole I prefer the former view, which commended itself to Mr. Justice Rowlatt and Lord Justice Warrington. The expression "profit on a discount" is unusual, and (as Lord Justice Scrutton pointed out) is probably elliptical for "profit on a security bought at (or a "transaction involving) a discount"; and if one has once embarked on such a transaction, I think that the resulting profit, though enhanced by adventitious circumstances, is all profit on the discount. The value of a bill in the market may vary with the rise or fall of the value of money; but there is no real accretion to capital, for the amount secured by the bill remains unaltered.

I pass to the third and most difficult question; and in dealing with it I put aside the fact (referred to in the Case Stated by the Commissioners) that in the Income Tax year 1917-18 the Respondents received some small sums for interest on short loans which might have fallen within the Third Case, as this circumstance was not relied upon by the Appellants in the Court of Appeal and could not therefore be pressed in this House; and I proceed only to consider the question whether a taxpayer can be assessed to tax under the Third Case in respect of profits on discounts on the basis of the profits of that character made by him in the preceding year, although in the year of assessment no such profits have arisen. The fact that under Section 64 of the Finance Act, 1916, and Section 18 of the Finance Act, 1917, very large sums payable for interest on War Loans and Exchequer Bonds are brought within the Third Case, while it cannot alter the construction of the earlier statutes, gives greater importance to the question now to be determined.

My Lords, the sections of the Income Tax Acts under which duty is levied in respect of casual profits or profits of an uncertain value, have been stated by the noble and learned Viscount on the Woolsack; and it is unnecessary to repeat them. I agree that they are difficult to construe, and I have felt considerable doubt as to their meaning; but upon the whole I have come to the conclusion that a person who is assessable to Income Tax in any year may be assessed upon the casual profits of the previous year, even though in the year of assessment he makes no casual profits. The duty under Schedule D is not a charge on profits, but a charge upon an individual in respect of profits. It is not a collection of taxes imposed in respect of different species of profit, but one tax imposed in respect of all, and its amount depends, not on the profits received by the taxpayer in the year of assessment, but upon certain "computations", which are prescribed by the rules governing the several Cases. Under the Fourth Case, that relating to foreign securities, the computation is directed to be made on the sums received in the current year. Under the First, Second and Fifth Cases it is to be made on an average of the three preceding years; and under the Sixth Case it is to be made either on the receipts for the year or on an average as the Commissioners may direct. But under the Third Case (with which we are concerned) the duty is to be computed "at a sum not less "than the full amount of the profits or gains arising therefrom within the "preceding year", and is to be "paid on the actual amount of such profits or

"gains without any deduction". The substitution in this rule of "at" for "on" is significant, and, notwithstanding the somewhat confused language, the intention is, I think, reasonably clear that the taxpayer shall in each year be charged with duty upon the full and actual amount of the profits of this character which arose in the preceding year. In other words, the assessing officer is to shut his eyes, so far as this head of assessment is concerned, to the events or anticipations of the current year and is to look back to the preceding year and compute the duty on the figures of that year. He is to treat the profits of the preceding year as the ground and measure of assessment, and is to assess the taxpayer accordingly. A similar rule is laid down as regards Super-tax by Section 66 of the Finance (1909–10) Act, 1910, where it is provided that for the purposes of the tax, the total income of an individual from all sources "shall be taken to be the total income of the individual from all sources for the "previous year"; and although the language used in that Section is different from that used in the first rule under the Third Case, it does not appear to me that the difference is material. I would, therefore, answer the third question raised on this Appeal in the negative, and would hold (with Mr. Justice Rowlatt) that, as regards the profits comprised in the Third Case, the Legislature has regarded the taxpayer himself as the only source of profit which need exist in the year of assessment and has taxed him upon any profits of this character which he may have made in the preceding year. It has been pointed out that the contrary view leads to strange consequences. The Respondents admit that, if they had made a profit on discounts to the amount of £10 or £20 in the year 1917–18, they would have been assessable in that year upon the whole of the profits, exceeding £20,000, made in the preceding year; and yet they claim that, because no such profits were made in the year 1917–18, the large profits in the preceding year escape assessment altogether. If so, a taxpayer, if he should think fit to confine his transactions of this character to alternate years, would enjoy all his profits on such transactions without liability to tax. It has indeed been suggested that profits which so escape taxation under the Third Case might be assessed under the Sixth Case of Schedule D; but that Case is confined to annual profits and gains "not falling under any of the foregoing rules", and I do not think that this could be predicated of any profits which (like profits on discounts) are expressly brought within the rules relating to the Third Case. Further, under the Taxes Management Act, 1880, assessments for Income Tax are made during the currency of the Income Tax year, and under Section 82 of that Act the tax is payable on the first day of January, that is to say, about three months before the end of the year. The tax may, therefore, have to be assessed and paid before it can be known whether the person assessed will or will not earn profits falling within the Third Case in the Income Tax year; and if the construction for which the Respondents contend is correct, his liability to assessment will depend upon facts which may be unknown when the assessment is made. In truth, the argument for the Respondents in this case, if successful, would render the Acts wholly unworkable. It is no doubt true that, if on the true construction of a statute, not excluding a taxing statute, a lacuna or defect appears, it is no part of the duty of the Court to supply the deficiency; but in choosing between two competing constructions, each of them possible, it is not irrelevant to consider that one of them is consistent with the obvious purpose of the Act while the other would render the statute capricious or abortive.

But it is said—and I think that it is mainly upon this argument that the Court of Appeal has rested its judgment—that the Income Tax Acts proceed upon a general scheme or principle, namely, that an assessment for any year

requires a taxable subject matter in that year; and it is said that this general rule applies to every schedule except Schedule D, and to every case in Schedule D, other than Case 3 (with the possible exception of Case 6), and even to the third rule of Case 3. This may be so, but even in that case I do not think that it can be inferred that the so-called scheme or principle extends to the whole of Case 3. The matters dealt with in the other Schedules and Cases—lands, farms, annuities, trades, professions and foreign securities and possessions—have an element of continuity or recurrence; but the profits of an uncertain value classified in Case 3 are in their nature casual and intermittent, and it is not surprising that these exceptional matters should be made subject to exceptional rules. The only general scheme or principle which I can find in the Acts is that "every description of property or profits" shall somehow bear the tax.

Upon the whole I am of opinion that the argument for the Crown prevails on this point also, and accordingly that the Appeal should be allowed, and the Order of Mr. Justice Rowlatt restored, and that the Cross-Appeal should be dismissed.

In *Ogston's* case it was agreed by Counsel on both sides that this case could not be distinguished from Brown's case, and accordingly I am of opinion that it should be disposed of in the same manner.

*Lord Atkinson.*—My Lords, the National Provident Institution during the years ending 5th April, 1916, and the 5th April, 1917, respectively, embarked on the business of purchasing from the Treasury Exchequer Bills at less than their face value, and then either selling them during their currency or holding them till maturity and obtaining the amount contracted to be paid. In both these years the Institution made considerable profits out of these transactions. In the year ending the 5th April, 1918, they ceased altogether to carry on this business, and the source of their profits and gains having thus dried up, no profits or gains from this source arose or accrued to the Institution during the year so ending. The Appellant contends, however, that notwithstanding this fact, he is entitled under Schedule D, Case 3, Rules 1 and 2 of the Income Tax Act of 1842, to assess the Institution in respect of this very year for Income Tax on a sum not less than the income it had derived from this same source in the previous year, namely, the year ending the 5th April, 1917.

Putting aside for a moment the case of Super-tax, with which I shall presently deal, I may, speaking entirely for myself, say that in my opinion this contention is unsustainable. 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. It is in my view out of harmony with the whole scheme of the Income Tax code, and the principles which that code embodies. The contention can, I think, only be plausibly supported 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, the income itself. In many cases within the Income Tax Acts the amount of the taxable profits and gains arising or accruing to the taxpayer from a particular source during the year of assessment is measured at something not less than the profits and gains arising or accruing to him from that source during the immediately preceding year, or at something not less than the average income derived by him from this source during the three preceding years. But the Solicitor-General frankly admitted on behalf of the Appellant 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 same source not less in amount than those he received from it in the immediately preceding year. No authority is, therefore, available to support the Appellant's contention. It is scarcely possible to suppose that, if it were sound, it would not have been put forward and ruled upon during the 79 years which have elapsed since the Income Tax Act of 1842 was passed. In truth, the Appellant is in this case endeavouring to apply to ordinary Income Tax the principle embodied in Section 66, Sub-section (2), of the Finance Act, of 1910 for the assessment of the Super-tax. That Section provides that for the purpose of the Super-tax the total income of any individual from all sources shall be taken to be the total income of that individual from all sources for the previous year. Here the income of the previous year is not made the measure of the amount of the income of the subsequent year. It is itself treated as the actual income of the subsequent year, the year of assessment, and is taxed accordingly. So in the present case the Appellant seeks to substitute the income of the previous year for the cypher which represents the actual income of the subsequent year. There is not in the whole Income Tax code dealing with ordinary Income Tax any enactment corresponding to Section 66, Sub section (2), of the Finance Act of 1910. There is no language in the code directed to effect an object similar to that aimed at by the Legislature in the case of the Super-tax. From this I think it may safely be inferred that, if the Legislature had desired to bring about a result in the case of ordinary Income Tax similar to that brought about in the case of the Super-tax, they would, in some of the many Income Tax Acts which have been passed, have in clear and explicit language so provided. The Legislature has not done that. As, however, the Solicitor-General has resolutely pressed the above-mentioned contention on the part of the Appellant, which, if sound, would produce results of vast importance, one may be excused for analysing some of the main provisions of the principal Income Tax Acts passed since 1799 at greater length than would under other circumstances be pardonable.

The first of these, the Act of 1799 (39 Geo. 3, c. 13), by its second section provides that " there shall be raised, levied, collected, and paid annually unto " and to the use of His Majesty, his heirs, &c., upon all income arising from " property in Great Britain belonging to any of his subjects though not resident " in Great Britain and upon all income of every person resident in Great Britain " and upon that of every Body Politic, &c., whether such income shall arise " from lands, tenements, or hereditaments situated in Great Britain or else- " where, or from any kind of personal or other property or from any profession, " office, stipend, employment or trade or vocation the several rates and duties " mentioned in the Act." The machinery set up for the annual collection of these duties was roughly this :—the assessors were every year to give notice to the taxpayers of the sums claimed against them ; the taxpayers were obliged to deliver to the assessors any objections they might have to these claims (Section 28). The Commissioners named were to decide upon the validity of those objections and then assess the taxpayer accordingly. By the amending Act of the 39 Geo. 3, c. 22, substantial alterations were made in the former Act which are immaterial for the present purpose. But by neither Statute was any measure provided by which the amount of the income liable to taxation was in any case to be fixed. It is clear, therefore, from the provisions of these Statutes that the taxpayer was each year obliged to pay the duty on the income he received or was entitled to receive during that year.

Two obvious objections, however, applied to this method of collecting the tax. First, the taxpayer's income from all sources was disclosed, and next the

amount of the income to be taxed could not be ascertained till the last day of the year of assessment. To remove the first of these objections, a new method of assessment was provided by the Income Tax Act of 1803 (43 Geo. 3, c. 122). It was this :—in lieu of the taxpayer's general return of his income from all sources, the tax was divided into five parts having relation to the particular sources from which the income was derived, namely, Schedule A, dealing with the portion of the tax leviable on owners of land, including houses ; Schedule B, dealing with occupiers of land ; Schedule C, dealing with the case of fund holders, &c. ; Schedule D, dealing with the annual profits and gains arising or accruing to any person residing in Great Britain or elsewhere from any profession, trade, or vocation carried on in Great Britain or elsewhere, or arising or accruing to any person or persons whatsoever in Great Britain, from any profession, trade, employment, or vocation exercised in Great Britain, and provided that the annual amount of all these respective profits and gains should be charged at the yearly sum of one shilling for every twenty shillings of the amount thereof, and further provided that the above-mentioned duties should be charged upon every description of profits and gains not chargeable under Schedules A, B, C, and E. The amount of the income to be taxed under Schedules A and B was fixed as it is now, but as to all the other Schedules, no measure of the profit and gains arising or accruing from any of the sources mentioned was prescribed or indicated. From this legislation one sees clearly what was the true nature of Income Tax. It was 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 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 a non-existing income.

The next Income Tax Act of importance is that passed in the year 1806, but as the Income Tax Act of 1842 (5 and 6 Vict. c. 35) is practically a reprint of this Act of 1806 with some alterations and additions which are immaterial for the purposes of this case, one may safely proceed at once to the consideration of the provisions of the latter Statute. It begins, after the manner of its predecessors, by enacting that from the 5th April, 1842, there shall be charged, raised, levied, collected, and paid to Her Majesty, her heirs and successors, during the period named, the several rates and duties mentioned in the several schedules contained in the Act marked A, B, C, D, and E, respectively. In each and every one of these Schedules it is provided that the duties shall be charged yearly. In Schedules C and D it is further expressly provided that the annual profits and gains arising or accruing to any of the persons therein respectively mentioned shall be charged yearly for every twenty shillings of the amount thereof (*i.e.*, of the profits and gains) the sum of sixpence without deduction. In Schedule D itself it is enacted that the several duties mentioned therein shall be charged annually and paid by the persons or bodies who receive or are entitled to receive the same. The First Case in that schedule deals with the duties to be charged in respect of any trade, &c., and its first rule provides that the duty to be charged upon the profits and gains which the taxpayer is entitled to receive is to be computed on a sum not less than the full amount of such profits and gains of such trade on a fair and just average of the three years immediately preceding the year of assessment upon which the accounts of the trade are usually made up, or on the fifth day of April preceding the year of assessment, and shall be assessed, charged, and paid accordingly. Special provision is then made for each of these two cases :—(1) where the trade shall

have been set up within this period of three years; and (2) where the trade shall have been set up within the year of assessment. It will be observed that this average sum is a minimum. It only fixes the lower limit of income to be taxed. 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. Much less is this average sum a substitute for this non-existing thing, to be dealt with as if it had arisen or accrued to the taxpayer during the year of assessment. In the Second Case a different measure of income is provided, but the same considerations apply to it. In the Third Case of this same Schedule D, upon which the present case turns, the sum to be taxed is the amount of the profits and gains of an uncertain value. This sum, by Rule 1 of this Case, is to be computed at a sum not less than the profits and gains arising therefrom within the preceding year ending as in the First Case. Again, this computed sum is a measure, and is not a substitute for, the sum which has actually accrued. The rule ends up with this rather significant statement, that the tax is to be paid on the actual amount of such profits or gains without any deduction. It is not quite clear what these last words mean. Does "the actual amount" mean the computed amount? As the computed sum is a minimum that can hardly be so, or does it mean the amount in fact received? Whichever of the two it means, it gives no support to the contention of the Appellant that this minimum can be treated as a substitute for a cypher and used to fill a vacuum. By Rule 2 of this Case, profits on all discounts, which I presume means profits arising and accruing from all discounts, are to be charged according to this first rule. In the Fourth Case of Schedule D no measure of the sum to be taxed is provided, and the true nature of that sum is consequently made more fully apparent. The duty to be charged under this Case is to be computed on a sum not less than the full amount of the sums (so far as the same can be computed) which have been or will be received in Great Britain in the current year without any deduction. The words "will be received" are evidently introduced to get over the difficulty of having to wait till the end of the current year to make the assessment. It is obvious that in this Fourth Case, if the source of income dried up and nothing was received in Great Britain, no tax could be levied. In Case 5 the income is again to be measured by the three years' average, and the remarks I have already made as to Case 1 apply to it. The Solicitor-General contended that Rule 2 of this Case 3 of Schedule D was itself a charging enactment because of the presence in the rule of the words "shall be charged according to the preceding rule." I cannot concur in this view. Section 102 of the Act of 1842 is the charging section. It is general in its terms and applies to "all annuities, yearly interest of money, or other annual "payments", &c., and enacts that "there shall be charged for every twenty "shillings of the annual amount thereof a sum of sevenpence without deduction, "according to and subject to the provisions by which the duty in the third "case of Schedule D may be charged." This clause would be inappropriate if Rule 2 of Case 3 was a charging clause. The words "charged according to "the preceding rule" mean, I think, simply that the measure indicated in Rule 1 is to be applied to fix the minimum of the sum to be taxed, nothing more.

By the Income Tax Act of 1853 (16 and 17 Vict. c. 34) Ireland was for the first time subjected to Income Tax. Many special provisions had to be introduced into the measure to make it applicable to that country. But the main and charging part of the Statute runs on almost the same lines as does the Act of 1842. Its first section has been repealed by the Statute Law Revision Act (38 and 39 Vict. c. 66). Notwithstanding this repeal, however, it is quite

legitimate to consider the provisions of the section in the endeavour to ascertain what was the scheme and principle of the Statute of which it forms part. The section provides, as the corresponding section of the earlier Act provided, that the several rates and duties mentioned therein " shall be charged, raised, " levied, collected, and paid yearly unto and for the use of her Majesty, her " heirs", &c., and that the duties arising from the several sources enumerated shall be paid in respect of the annual profits and gains arising or accruing to any person or persons. By Section 2 it is provided that, " For the purpose of classi- " fying and distinguishing the several properties, profits, and gains for and in " respect of which the said duties are by this Act granted, and for the purposes " of the provisions for assessing, levying, and collecting such duties respectively, " the said duties shall be deemed to be granted and made payable yearly for and " in respect of the several properties, profits and gains respectively described " or comprised in the several Schedules contained in this Act marked respec- " tively A, B, C, D, and E, and to be charged under such respective Schedules ". As in the immediately preceding Act, Schedule A deals with the ownership of land ; Schedule B with its occupation ; Schedule C deals with interest, annuities, or dividends payable out of any public revenue ; and Schedule D with the annual profits and gains arising or accruing from any of the properties, professions, trades, employments, or vocations mentioned therein, and also from interest of money, annuities, and any other annual profits and gains not charged by virtue of any other Schedule contained in the Act. It then enacts that the duties to the amount mentioned shall be charged thereon. As under the other Statute, these duties are to be levied yearly. They are to be levied on the annual profits and gains arising or accruing to the person or persons entitled thereto. It would appear to me that those 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", *i.e.*, the year of assessment, that person cannot be made liable to pay any Income Tax in respect of that source. By Section 5 of this Act of 1853 it is provided that the duties by the Act granted shall be assessed, raised, levied, and collected under the regulations and provisions of the Act of 1842 and the several Acts therein mentioned or referred to, and also of any Act or Acts altering, amending, or continuing the same. For the reasons I have already mentioned, I think this Appeal wholly fails upon the main point urged by the Solicitor-General.

The Respondent relied upon a point which is made the subject of the Cross-Appeal. It is this :—that the words " on any discount " occurring in Rule 2, Case 3, do not describe or cover transactions such as those by which the Respondent made the profits admittedly made in the years ending the 5th April, 1916, and the 5th April, 1917, respectively. The words are not happily chosen, but must, I think, be taken to mean " all profits arising from discount". These words are immediately followed by the words " and on all interest of " money payable or paid by any person whatever ". The so-called Treasury Bills in form resemble much more promissory notes or I.O.U's. than ordinary bills of exchange. The specimen bill printed in the Appendix is in the following form :—

" London,__________

" This Treasury Bill entitles*__________________ or
" order to payment of______pounds at the Bank of England out of the
" Consolidated Fund of the United Kingdom on the__________.

" __________________
Secretary to Her Majesty's Treasury.

"(* If this blank be not filled in, the bill will be paid to bearer.)"

It is obvious that, if the Treasury in consideration of a loan of £100 by an instrument closely resembling this instrument contracted to pay three months after date the sum of £100 with 12 per cent. per annum interest, the holder of the instrument would at the end of the three months be entitled to receive £100, the original sum secured, plus £3 remuneration in the form of interest for the use of his money during these three months. It is equally plain that, if the Treasury in consideration of a loan of the same sum contracted to pay £103 at the end of the three months without interest, the respective parties would at the end of that period be in precisely the same position as in the first case. The Treasury would have had the use of the lender's money for three months and the lender would have got the same remuneration for its use. In fact, the only real difference between the two transactions is that in the first this remuneration would be paid to him when the principal money is repaid, and in the second that it is paid to him in advance when the principal sum is lent. This second transaction, in its essence, closely resembles the transaction which takes place between the Treasury and the Respondent, where the latter buys an Exchequer Bill at less than its face value and holds it till it is paid at maturity. The difference between the amount paid for the bill and the amount received at its maturity, it is contended by the Respondent, is not to be "profit on discount" nor yet interest, but an accretion of his capital. Sir William Finlay, however, admitted on the part of the Respondent that, if the payee of an ordinary promissory note endorsed it to his banker, receiving for it from the banker such sum as the latter may agree to give him, the transaction would amount to a discounting transaction, but contended that the difference between that transaction and the sale by the holder of a Treasury Bill consisted in this: that in the first case it was the payee not the maker of the note who sold and transferred the security. I do not think this contention is sound. The word "discount" is in Murray's English Dictionary defined, in its primary meaning, to be "an abatement or deduction from the "amount, or from the gross reckoning or value of anything," and, as used in commerce is defined to mean (1) "a deduction (usually) at a certain rate "per cent. made for payment before it is due of a bill or account, or any deduc- "tion or abatement from the nominal value or price"; (2) "a deduction from "the amount of a bill of exchange or promissory note by one who gives value "for it before it is due." The profits made by the Respondents by buying these bills from the Treasury at something less than their true face value, and selling them during their currency at an advanced price, or by keeping them till maturity when their face value was paid by the Treasury, are in my opinion "profits on discount" within the meaning of Case 3, Rule 2, of Schedule D. The Court of Appeal have, however, held that, while in the case of a Treasury Bill bought for a sum less than its face value, held until maturity and then paid by the Treasury, the difference between the two sums is a profit "made on discount" and not an accretion of capital, apparently, when one of these bills is during its currency sold by the holder at an enhanced price, the transaction is a discount transaction, but that the entire difference between the two prices is not "a profit on discount" within the meaning of the rule and that the portion of the difference which is due to the fact that the value of the bill is enhanced by its nearer approach to maturity cannot be so regarded. It might, the Master of the Rolls said, possibly be "taxed as profits on a business "of discounting" but the Crown have deliberately elected not to assess the Plaintiff under this head. With the greatest respect, I am quite unable to appreciate this distinction. When one of these bills is purchased from the Treasury, all the rights it confers are purchased with it. One of those rights

is that the holder of it can enforce payment of it by the Treasury at its maturity. When it is resold at an enhanced price that same right is purchased by the purchaser. The right is the same in quality and character on the occasion of both sales. It is true that the right may have appreciated in value by the time the second sale takes place, because the day for payment of the bill is nearer. But if the transaction of purchasing and selling such a bill be, as it has been by the Court of Appeal held rightly I think to be, a discounting transaction—otherwise no part of the difference between the two prices would be profits on discount—I utterly fail to see how the entire difference between the original price and the enhanced price, which has been obtained by and through this discount transaction, is not a "profit on discount" within the meaning of Case 3, Rule 2. Moreover, I doubt if the principle on which this distinction rests would be capable of application in practice. There is scarcely a bond of a foreign State offered for subscription or sale on the London market which is not conditioned to be redeemed on a certain specified date. There is frequently another condition added that a certain number of these bonds shall be drawn for payment annually and, when drawn, immediately paid. If one of these bonds, after having been held for a considerable time by a person who subscribed for it, should be sold for a much enhanced price, is not only the portion of the enhanced price due to the near approach of the day of payment to be deducted from the difference between the two above-mentioned sums, but, in addition, must not a sum representing the value of the vendor's chance of having his bond drawn at some of the future annual drawings and the day of payment thereby greatly accelerated be also deducted? If the dealing with this bond would be a discount transaction, as I think it would be, I am unable to see why the principle relied upon by the Court of Appeal should not be thus applied, and yet I think it would be obviously impossible to apply it.

I am of opinion that both the Appeal and Cross-Appeal fail. I think the Order appealed from should be amended by deleting the portion of it which varies the Order of Mr. Justice Rowlatt, and that, as amended, it should be affirmed and this Appeal be dismissed. It was suggested in arguments that the profits made in the year ending the 5th April, 1916, might be taxed under Case 6. I express no opinion on that point as, even if it could not be so taxed, that would not justify the taxation of a not existing thing.

*Lord Sumner*.—My Lords, the Cross-Appeal is logically the first to be disposed of, for, if the transactions which the Inland Revenue desires to charge are not taxable transactions at all, we need not discuss the conditions under which they are to be taxed. The contention is that the profits charged are not profits on discount, because they are profits on realisation of investments, which are accretions to the capital invested. Further, it is said that an investment in Treasury Bills or any similar securities may be one which locks up capital for a term of years, and consequently its release on realisation cannot result in annual profits or gains or in taxable income; an accretion after several years of investment is so much more liquid capital not so many years' annual profits aggregated; the whole gain might accrue in one year, though only realised afterwards; in any case, the transaction should be subjected to economic analysis, so that only that part of the profit which represents the consideration to the taxpayer for the use of his money may be brought into charge and not the capital advantage derived, for example, from an intermediate sale of the bill before maturity. The case has been argued as though the Second Rule of Case 3 of Schedule D either referred principally or exclusively

to dealings in Treasury Bills and similar securities, or ought to be construed as exclusive of such instruments because, at any rate in their present form, they were not in use in 1842. No doubt it is common to speak of buying or selling Treasury Bills, and to a large extent such a transaction is the converse of lending money to the Treasury at interest periodically due. The rule, however, relates to "profits" on all discounts from whomsoever made. There is no definition of discount in the Statutes, no restriction of it to transactions in use in the year 1842, no evidence of its meaning as a term of art at any time. I take it that the rule applies equally whether the lender solicits the privilege of furnishing money to the Treasury at prices which it fixes by virtue of the possession of still unsurpassed credit, or whether the borrower approaches the lender hat in hand and offers his acceptance with or without "another name" in order to obtain temporary accommodation. It includes both the transaction as between the original parties and the transaction as modified by the introduction of the bona fide holder for value. In both cases there are two economic elements, the one the value of the usufruct foregone, as measured by interim interest, and the other the risk that the money will never be repaid at all. In the case of the Treasury Bill the latter element may be said to reach its vanishing point; in the other it is probably much the most important factor in the transaction. Discount, however, is a term appropriate to its evaluation, whether it be an off chance or all but a certainty. It is all one thing, discount, whether the return to the lender is compounded of premiums for risk and interest on money in one ratio or in another. Furthermore, there is nothing to show that under this Section profits on discounts have to be analysed into a return for the use of money by way of income and a possible accretion to capital. If the acceptor comes into a fortune before the bill matures, no doubt its value increases out of all proportion to the approach of the due day, but to say that it is a case of an investment which has appreciated seems to me to be a misuse of language. The plain fact is that the discounting has been less hazardous and so more profitable than was expected. The moneylender stood out for a premium on the full risk, and gains by the risk turning out to be small. When a Treasury Bill is bought, the profit is chiefly a matter of the future value of money; but one need not go far to discover that, in the case of the Treasuries of foreign powers at least, the chance that the obligation may not be met at all enters very practically into the calculation. It is only where repayment is a certainty that the "purchase" of instruments like this can be a matter of interest only, either in the form of the interest to be paid, if the price payable for the bill is itself borrowed, or in the form of the interest which might have been earned on that price if it had not been applied to the purchase of the instrument. Mere interest can be no compensation if there is default in payment of the principal sum; and so if there is a possibility of default something more than interest is involved. Discount is the apt term to provide a consideration for both matters, and the transactions are but few in which there is absolutely no risk of a default at maturity. I see no utility in calling this an investment, a term which is quite undefined and is often applied to speculations and to purchases of chattels as well as of securities. In a sense, one who discounts a long-dated bill "invests" capital in it, but that is not the question. The real question is whether he discounts it. Unless it can be affirmed that he does not, the profits of the operation, investment or no investment, fall within this rule, and I certainly cannot affirm that the Respondent did not discount here. It is to be remembered that this is a case of a company, which carries on a business and employs its funds for and in that business. The Case Stated finds no fact to distinguish these transactions from any other business use of money.

It is not the case, as to which I say nothing, of a private person who, not in the course of any business at all, realises an investment and comes well out of it. Similarly, I see no warrant for trying to discriminate between the capital used in the transaction and the income obtained from its use. The Statute says nothing about it. To discount a bill, even a Treasury Bill, you must have money or money's worth, but whether an accountant would say that it came out of or should be debited to capital or income makes no difference to the fact of discounting. The excess of what is got back to-morrow over what is put in to-day is profit, and it is but rarely that even an economist can tell what is appreciation of capital and what is not. The Acts invite no such curious inquiry as the Court of Appeal directed on this point. I agree also that no difference arises by reason of a transfer of the bill from one holder to another, except for the purpose of determining who is to be charged, or by reason of the conversion of Treasury Bills into War Loan.

My Lords, as to the Appeal, the Inland Revenue claims to be entitled to charge duty on profits on discounts in a year in which no such profits have been earned as if they had been earned, and then to compute the amount of the duty upon these non-existent profits at a sum not less than the amount of such profits earned in the next preceding year. If this claim is to be made good, it must rest on Schedule D, Case 3, Rule 2, which is said to be the charging section, for no other words of charge can be found in the Acts to produce this result, nor do any other clauses so far strengthen Rule 2 as to make it do with their assistance what it would not be sufficient to do of itself. I agree that Rule 2, so construed, is in complete contradiction to the whole scheme of the Acts; that to make this rule an independent charging section at all is to disturb the framework of the charging and the computing sections; that, if the Crown is right, words were borrowed in 1842 from the earlier legislation substantially identical in form but wholly different in sense, and that, if so, the Legislature in 1842 gave to the Inland Revenue retrospective powers of taxation, which that department either failed to recognise or dared not use. These considerations, however, really go to the question what was the Legislature likely to mean, while the true question is what is the meaning of what it said.

It is a most wholesome rule that in taxing the subject the Crown must show that clear powers to tax were given by the Legislature. Applied to Income Tax, however, this is an ironical proposition. Most of the operative clauses are unintelligible to those who have to pay the taxes and in any case derive such clarity as they possess from the judges who have interpreted them. After the puzzle has been solved no doubt the answer seems clear and the solution is arrived at as a matter of construction. The question is always what is the meaning of the words of the Statute? If they have none there is no need to invoke the proposition that the meaning must be clear. I will therefore address myself to the construction. The duties granted in Schedule D are to extend to every description of property or profits (note this antithesis) not contained in Schedules A, B or C, and to every description of employment of profit not contained in Schedule E and are to be charged annually according to rules classified under certain cases. Case 3 is "the duty to be charged "in respect of profits of an uncertain annual value", and the first rule states how the duty to be charged in respect of such profits is to be computed. The next rule, No. 2, states how certain other profits are to be charged. They are other profits, because two of the three classes are not of uncertain annual value at all. Profits on securities bearing interest payable out of the public revenue and profits on interest of money not being annual interest are certain, and the

annual value can be calculated from the rate for a period less than a year with ease and certainty. These other profits are to be charged "according "to the preceding rule in this case", that is to say, "the duty to be charged "in respect thereof shall be computed at a sum not less than the full amount "of the profits or gains arising therefrom within the preceding year . . . "to be paid on the actual amount of such profits or gains."

Now, when a person makes such profits for a series of years and then ceases to make them, in the first year of the series he makes them without any preceding year, by the gains of which his first actual gains can be computed, and at the end of the series comes a year in which, though there is a preceding year by the gains of which to compute them, there are no actual gains of this last year to be computed. The first is the case of bill discounters in 1842; the second is the case of the Respondent Institution in the year of charge in question. If Rule 2 is a rule imposing a charge, and that charge is imposed *sub modo* as the rule directs, the charge comes to nothing, for. though the computation is possible, the payment of the charge is not; there is nothing to pay on. The rules do not say that for the purpose of payment of duty profits shall be deemed to have been made in the second of two years to the same amount as those made in the first. They say that "the" profit, that is, the profit made in the year of charge, shall be charged as if the amount of it were so and so. How can "the" profit (that is, the profit of the year of charge) be charged if there is none? If, on the other hand, Rule 2 is read as charging absolutely and not *sub modo*, which is the only possible alternative but is not in accordance with the language used, then profits (not "the" profits, but any profits of the kinds mentioned) shall be charged without restriction to the year of charge. But the computation prescribed in Rule 1 is obligatory, and charge and computation go inseparably together. Only the one mode of computation is possible. On this construction, such profits made in 1842 were charged and yet could not be charged, because they could not be computed. The same would be true, whenever a year of profit-earning followed on the heels of a barren year. Further, if there are two barren years, it is clear that the taxpayer escapes in the second year. This argument would make him escape, not because he made no profits in the second year, but because he had not set up for himself a fatal standard of comparison in the prior year. Contrariwise, if Rule 2 is an absolute charge, it charges profits, not the absence of profit; it charges profit to which a computation can be applied, resulting in a sum to be paid on something. In a year when there is no profit, how can such a computation be applied? It becomes a calculation of a sum to be paid on nothing, and I think that means not to be paid at all. These rules, it must be admitted, handle prepositions a little freely, for the first rule computes the duty "at" the full amount earned, not "on" it, but one such slip is enough; to be paid "on" the actual amount cannot be amended into to be paid "notwithstanding" the actual amount. In my opinion Rule 2 clearly means that the profits, when chargeable, shall be charged on a certain computation. Like its predecessors, the rule is a computation rule and is rather compressed. If it had been independently and fully expressed, I think it would have run thus:—"Second.—the duty to be charged in respect of the "profits on all discounts shall be computed at a sum not less than the full "amount of the profits or gains arising therefrom within the preceding year, "and when charged shall be charged accordingly."

It is said, and truly, that inconvenient results, involving loss of tax, may follow upon the conclusion that there must be some profits on discounts made in the year of charge before there can be any computation of tax on them by

reference to similar profits made in the previous year ; for example, by earning and forbearing to earn profits on discounts in alternate years a taxpayer might escape taxation on this kind of profits altogether. I am not much impressed by such an inconvenience, for this in-and-out attention to business is easier to state in theory than to carry out in practice ; nor is the whole field of making profits on discounts so large as to make this risk a very serious matter. In any case, statutory language cannot be construed by asking which construction will most benefit the Revenue. It is true that it is the subject who is taxed. He it is who has to pay, though he pays a tax charged on a particular kind of annual profits or gains made by him and not otherwise. But his mere continued existence ought not to suffice to bring into operation the previous year's profits on discounts as a measure of computing something which is purely notional, no profits of the kind having been earned in the year of charge at all. The effect would be that the taxpayer, having paid tax on the whole of his actual income for the year of charge, would have to pay out of it and really on it another tax, namely, the tax on the prior year's profits on discounts which he has not made in the year of charge at all, that is to say, he would to this extent be taxed twice over, on the ground that the Legislature had not thought it convenient to tax him at the very time when he really did make the profits on discounts. This is, I think, more than the words of the Act can bear. On the other hand, with all respect for the noble and learned Viscount, I am unable to take the view that Income Tax on profits on discounts is really charged on the profits of the year in which they are earned, but payable in the year following. We are told that all Income Tax is one. This construction tends to make Income Tax on profits on discounts a separate tax similar to Super-tax, which is contrary to the scheme of the Acts. Super-tax, on the other hand, is charged on an income which is " taken to be " the previous year's income, not merely " computed at " a sum not less than the previous year's income. As to the point on which the Court of Appeal referred the Case Stated to the Commissioners, I think the Appeal succeeds, but it should on all other points be dismissed.

*Questions put.*

IN BROWN (SURVEYOR OF TAXES) v. NATIONAL PROVIDENT INSTITUTION *et e contra.*

That the Order appealed from be reversed.

*The Not-Contents have it.*

That the Order of the Court of Appeal be varied in accordance with the agreement expressed by the majority of this House, and that, subject to such variation, the Order be affirmed and the Appeal and Cross-Appeal be dismissed.

*The Contents have it.*

That there be no costs for either party either in this House or in the Courts below.

*The Contents have it.*

In OGSTON (SURVEYOR OF TAXES) v. PROVIDENT MUTUAL LIFE ASSURANCE ASSOCIATION

*et e contra.*

That the Order appealed from be reversed.

*The Not-Contents have it.*

That the Order of the Court of Appeal be varied in accordance with the agreement expressed by the majority of this House, and that, subject to such variation, the Order be affirmed and the Appeal and Cross-Appeal be dismissed.

*The Contents have it.*

That there be no costs for either party either in this House or in the Courts below.

*The Contents have it.*

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