

Wales Vs. Tilley.

Wales Vs. Tilley.

SooperKanoon Citation : sooperkanoon.com/864808

Court : Kolkata

Decided On : May-18-1942

Reported in : [1943]111TR1(Cal)

Appellant : Wales

Respondent : Tilley.

Judgement :

Their Lordships took time for consideration.

May 18. - LORD GREENE, M.R. - By an agreement of June 28, 1937, the remuneration which the appellant had been receiving as managing director of his company was increased from Pounds 2,000 to Pounds 6,000 a year, and in the event of his ceasing from any cause whatsoever to be managing director, the company agreed to pay him, as an from the date of cessation, a pension of Pounds 4,000 a year for ten years, reckoned from the same date. There was no agreement between the parties as to the period for which the appellant should serve and his tenure of office could have been, as it sill can be, terminated by either party at any time on whatever may be reasonable notice. The language of the clause relating to the pension is obscure, and questions might have arisen whether the pension was payable after the death of the appellant if he were to die during his service, or after its cessation. By clause 1 of an agreement of April 6, 1938, the appellant released the company from its obligation to pay him the pension. Clauses 2 and 3 were as follows : '2. Mr. Tilley hereby agrees to serve

the company as managing director as from the date of these presents at a reduced salary of two thousand Pounds per annum. 3. In consideration of the premises the company will pay to Mr. Tilley the sum of forty thousand Pounds by two equal installments, the first of which shall be paid on April 6, 1939.'

The Special Commissioners discharged an assessment made under Schedule E in respect of the sum of Pounds 40,000 payable under the 1938 agreement, holding that it was a payment in commutation of the companys liability under the 1937 agreement to pay pension and increased salary, and that it was not income in the hands of the appellant. Lawrence, J., reversed this decision, holding that the payment was expressly made in consideration of the appellants agreement to serve at a reduced salary. Part of the Pounds 40,000 he considered to be payable in commutation of the pension, but he held that as the pension would have been assessable under Schedule E, a sum payable in commutation of it would also be assessable under the same schedule. As will be seen, I agree with the conclusion of Lawrence, J., but I respectfully dissent from his view that a sum paid in commutation of a pension is necessarily assessable under Schedule E. The case of *short Bros., Ltd. v. Inland Revenue Commissioners* cited by Lawrence, J., does not, in my opinion, support his proposition. Indeed, the Attorney-General on behalf of the Crown did not attempt to support this part of the reasoning of the learned Judge. He preferred to argue that the pension was deferred remuneration, and that the acceptance during the service of a sum in commutation to it was the acceptance of present, in place of deferred, remuneration. If the agreement of 1938 had dealt with nothing but the appellants salary as managing director, reducing the annual amount and providing of payment of a lump sum in consideration of his acceptance of the reduction, there would, in my opinion, have been no difficulty in the case. If a man agrees to serve in consideration of a lump sum and no periodical salary or a small periodical salary, the lump sum is just as much remuneration and taxable as such as a periodical salary or a large periodical salary would have been (*Prendergast v. Cameron*). Indeed, the only real argument that was presented on behalf of the appellant on this aspect of the case consisted of an endeavour to draw a distinction between a lump sum paid at the beinning of the service and a sum paid, as in the present case, in consideration of an agreement to continue to serve for a reduced salary. There is no substance in this

distinction. If a man who is serving at a salary of Pounds 1,000 a year agrees to serve for a reduced salary in consideration of a lump sum, he is merely commuting his salary, and a sum so accepted in commutation of salary can in its nature be nothing but salary. The commutation merely substitutes one form of remuneration for another. It is, in effect, remuneration payable in advance and it is quite fallacious to speak of it as a special payment. Indeed, I am unable to understand how a sum paid as remuneration can ever be capital in the sense that it escapes taxation, since remuneration as such is the subject-matter of tax under Schedule E whatever form it takes. The analogy of cases such as the sale by an annuitant of his annuity for a lump sum is a false one since the quality of remuneration is absent from the payment.

The real difficulty in the case arises by the introduction into the agreement of the provisions relating to the pension. If the agreement had merely provided for the surrender of the pension in consideration of a present payment, with no reference to or connection with present or future services, I do not think that the sum received would have been taxable under Schedule E since it would not have been remuneration or salary of services. It would have been nothing more nor less than commutation of a pension, and a pension is in itself a distinct taxable subject-matter. It was admitted by the Attorney-General that a sum received in commutation of a pension effected after the termination of the service is not taxable. But he maintained that the case is different where the commutation takes place during the continuance of the service, and that a sum paid then must necessarily be regarded as remuneration for service rendered and to be rendered. I do not think that this view is correct. It would, of course, be possible for an employee to agree to give up his future pension rights in consideration of a present addition to his salary, and in that case the addition would be remuneration and taxable as such, notwithstanding that it originated in a surrender of pension rights. The question whether a sum received in consideration of the surrender of future pension rights is or is not remuneration must, as it appears to me, depend upon the true construction of the agreement by which the transaction is effected. If the sum received is by way of an addition to remuneration, in the form either of an increase in periodical salary or of a lump sum, it is taxable; if it is not so received, but is merely received, but is merely paid by way of commutation of a future

pension, without reference to or connection with the service, it would not, I think, be taxable. The game result would, I think, have followed in the present case if the agreement had been framed in two distinct parts : one an agreement to serve at a reduced salary in consideration of sterling Pounds x, the other an agreement to give up the pension rights in consideration of Pounds y. In that case the sum y Pounds could not, as it appears to me, have been described as remuneration for services.

It was argued on behalf of the appellant that if the whole Pounds 40,000 does not escape taxation, it ought to be regarded as referable in part to the acceptance of a reduced salary and in part to a commutation of future pension rights and apportioned accordingly. I was impressed by this argument, but on consideration I am unable to accept it. The question, as I see it, turns upon the actual language of the agreement. The parties themselves have made no attempt to apportion the Pounds 40,000, no doubt because of the practical difficulty of doing so when the commencing date of the pension was unascertainable and an actuarial valuation accordingly impossible. Instead, they have chosen to treat the 40,000 Pounds, as an indivisible sum paid 'in consideration of the premises.' The consideration is thus agreed to be an entire non-severable consideration, the whole of which is referable to the agreement to serve at a reduced salary just as much as to the agreement to give up the pension rights. It may well be that an apportionment might properly be made if, for example, a lump sum were paid in consideration of an agreement to serve and of the sale of a piece of land by the employee to his employer. In such a case the land would be capable of valuation, and the parties must be presumed to have known it, and the agreement for sale would have no connection with the agreement to serve. But here one of the considerations for the entire sum is expressed to be the agreement to serve, and as the parties have so agreed I do not think that an apportionment is permissible, since it would involve rewriting the contract. It was argued by counsel for the appellant that the present case is covered by the decision in *Dewhurst v. Hunter*. I did not obtain any legal assistance from the elaborate discussion of that decision which took place before us. It was a very special case and the contract did not contain peculiarities of the contract which are found in the present case, to which I have referred. As I have said, this case, in my opinion, falls to be decided on the terms of the bargain which

the parties have themselves made, which is, in essential respects, different from that in Dewhursts case, and counsels argument for the appellant that the facts of the present case are in all essentials indistinguishable from those in Dewhursts case is one that I cannot accept. I would dismiss the appeal.

MACKINNON, L.J. - Lawrence, J., has held that the appellant is liable to pay Income-tax under Schedule E of the Finance Act, 1918, upon the Pounds 20,000 paid to him by the company on April 6, 1938, and upon the Pounds 20,000 so paid on April 6, 1939. In other words, each of these sums was 'an annuity, pension, or stipend.....in respect of salaries, fees, wages, perquisites, or profits...for the year of assessment.' The special case sets out the agreements of December 19, 1921, and of March 31, 1937. I need only remark of the latter that it is obvious that the provision in it for the payment of Pounds 4,000 a year for ten years from the date of Mr. Tilley's ceasing to be a director involves a nice question of construction, namely, what, if any, are the rights of his executors or administrators if he should die (a) while he is still managing director, or (b) after he has ceased to be managing director, but when only some of the annual sums of Pounds 4,000 have been paid. The 1938 agreement provided (1) that the company should be released from the obligation to pay the Pounds 4,000 a year, 'pension' for ten years; (2) that Mr. Tilley should serve the company as managing director at a salary of Pounds 2,000 a year instead of Pounds 6,000; no period for such service is fixed, so presumably it would be for a reasonable time; and (3) that the company should pay him Pounds 20,000 on April 6, 1938, and Pounds 20,000 on April 6, 1939. The date 'April 6' is perhaps not without significance in a case about Income-tax.

The problem is whether these two sums of Pounds 20,000 are taxable in the two years of receipt under Schedule E. If I were not assisted, or embarrassed, by decision of the House of Lords which are reported, I should think the answer was 'Yes', as was held by Lawrence, J. Each Pounds 20,000 must have been paid partly in consideration of Mr. Tilley accepting for the future Pounds 2,000 a year salary in place of the Pounds 6,000 a year he was entitled to under the 1937 agreement, and partly in consideration of his releasing the company from the obligation under that agreement to pay him Pounds 4,000 a year for ten years. As regards the first sort of consideration, if a servant were entitled to Pounds 10 a

week, and on April 6 he agrees, in consideration of Pounds 520 paid down, to serve for a year for nothing, the Pounds 520 would pretty clearly be an annual receipt within Schedule E. So if a servant has an annual salary of Pounds 2,000 and in consideration of Pounds 20,000 paid down he agrees to serve for ten years AFC for nothing. And if, as here, he is entitled to be paid Pound Pounds 6,000 a year for an unspecified time, and in consideration of Pounds x paid down he agrees to serve for a reasonable time for Pounds 2,000 a year instead of Pounds 6,000 a year, I should think the Pounds x would be in the same position.

So far as each Pound 20,000 was in consideration for the surrender or abolition of the right to the 'pension' in futuro, the position may not be so clear. No doubt, if a man had, under an endowment policy, a right to be paid Pound x a year by a insurance company and he sold or surrendered this right to the insurance company for a lump sum, that lump sum would not be taxable under Schedule E. But why would it not be so Not, I think, from any characterisation of the sum as 'capital' rather than 'income', but because the annual sum he was to receive, and was surrendering, was not 'an annuity, stipend, or pension in respect of salaries, fees, wages, or profits.' That being so, the lump sum received by was of commutation could not be within that category. The question, as I see it, is whether the so-called 'pension' is within that category, i.e., payment by way of salary or wages for services rendered. If it is, then I should think the lump sum payable in presenti for its satisfaction is also within that category. If the 1937 agreement had remained in force, and the ten sums of Pound 4,000 had been paid, I should myself have thought that each of them, in its year of receipt, would be taxable under Schedule E as an 'annuity, stipend, or pension, in respect of salaries, fees, wages, or profits.' Each would be, in effect, deferred remuneration for services rendered in the past. And if that be so I should think that the lump sum agreed to be paid in advance in satisfaction or commutation such deferred remuneration would also be within the Schedule E.

This, as I have said, would be my view if there were no reported cases to assist, or perhaps embarrass, me. But there are two such cases, Dewhurst v. Hunter and Cameron v. Prendergast. Both are decisions of the House of Lords. The former was decided by three votes to two; the latter was the unanimous decision of five

noble Lords, of whom none were participants in the former. So far as the two sums of Pound 20,000 were paid in consideration of Mr. Tilley agreeing to serve for Pound 2,000 a year in place of Pound 6,000 a year, the decision in *Cameron v. Prendergast* seems clear authority that the amount so paid is taxable under Schedule E. It is to be observed that *Cameron*, like *Tilley* in this case, did not agree so to serve for any fixed period of time. But so far as the two sums of Pound 20,000 in this case were paid in consideration of the surrender of the prospective right to the Pound 4,000 a year pension, the decision in *Dewhurst Case* seems to me to make it very difficult, if not impossible, to hold that that part of the Pound 20,000 is taxable under Schedule E, for I cannot think that there is any essential difference between the sum which *Dewhurst* would have been entitled to under article 109 and the sums which *Tilley* would have been entitled to under his 1937 agreement. *Dewhurst* would have got a lump sum and *Tilley* would have got ten annual payments. But I do not see how that difference can alter the nature of their respective gains; and if a prepayment in satisfaction of *Dewhurst's* prospective right was not within Schedule E, I have great difficulty in seeing how the prepayment in satisfaction of *Tilley's* prospective right can be. If a single payment has been made for two sorts of consideration, one of which does make part of the sum taxable, while the other does not, the Commissioners would have to ascertain how much of the total sum fell within each category. Suppose, for example, a director received Pound 10,000 from his company; it is found to have been paid under a resolution of the Board 'that Mr. A be paid Pound 10,000 in satisfaction of his claims (a) for his fees for last year as a director (b) in payment for his patent No. - which he has assigned to the company.' Obviously the Commissioner would have to analyse the Pound 10,000 and find how much was payable under (a) and therefore was taxable.

In these circumstances I should be inclined to think that this case must go back to the Commissioners for them to find how much of the two sums of Pound 20,000 was paid in consideration of the reduction of his salary (with a direction that the sum so found is taxable under Schedule E) and how much was paid in consideration of the surrender of his right to the Pound 4,000 a year 'pension' (which sum would not be so taxable). I realise that this would be a difficult problem, by reason of (a) the doubtful effect in law of Mr. *Tilley's* death, which I

mentioned above, and (b) that the agreement of 1938 fixes no period for his service at the reduced salary. But if the law requires the Commissioners to ascertain a fact I doubt if the difficulty of performing their task can relieve them of the duty. My own inclination, therefore, is to think that the case ought to be sent back to the Commissioner in this way. But I can pretend to no disappointment at finding that my brethren think this view is incorrect, and that this appeal should be dismissed, for that is the result I should certainly have arrived at upon my own view of the law if I were happily oblivious of the existence of Dewhurst case and free from the constraint of attempting loyally to follow it.

GODDARD, L.J. - In my opinion, the question in this case depends for its solution on the true meaning and effect of the agreement of April 6, 1938. It has now been decided by the House of Lords in *Cameron v. Prendergast* that if a lump sum is paid to a director to induce him to continue to serve the company, either for no salary or at a reduced rate of salary, that payment is a profit of his office and is taxable. It is as though, instead of agreeing to serve, say, for five years at Pound 1,000 per annum, he agreed to serve for five years for one payment of Pound 5,000. If, however, a director is entitled to receive on the termination of his office a fixed sum or a pension, and he compromises that right by acceptance of a smaller sum, then *Dewhurst's* case decides that the sum he receives is not income, nor, according to the view expressed by Lord Atkin in that case, is to be regarded as received under or from the contract of employment.

In the present case Mr. Tilley was, under the agreement of June 28, 1937, entitled to a total salary of Pound 6,000 while he served as managing director, and to a pension of Pound 4,000 for ten years payable from the date when he ceased to hold his office. The agreement contained no provision as to the period for which he was to serve as managing director; the appointment could be determined by either side at any time, though presumably only upon reasonable notice. By the 1938 agreement Mr. Tilley, in consideration of Pound 40,000, to be paid in two installments, released the company from its obligation to pay him a pension and agreed to serve the company from the date of the agreement at a reduced salary of Pound 2,000. Again, no period was fixed during which he was to serve. In my opinion, had the agreement been one under which Mr. Tilley agreed to commute

his pension for Pound x and also to accept a reduced salary in consideration of a payment of a lump sum, on the authority of the cases above referred to the result would have been that the sum representing the commutation of the pension would not have attracted tax, while that which represented or was taken in lieu of the larger salary would have been taxable. But that is not, in my opinion, the true result of the agreement. The consideration is entire, and Mr. Tilley covenants to continue to serve the company for Pound 40,000 plus two thousand a year, instead of Pound 6,000 per annum plus the prospect of a pension. I am, therefore, unable to avoid the conclusion that the Pound 40,000 was remuneration for serving as a director, and I do not see that remuneration can ever be capital. There was, as it seems to me, a very good reason why the sum was not allocated partly to the reduction in salary and partly to the commutation of pension. As no one could say when the pension would become payable, it would be impossible to calculate its present value, apart, moreover, from the question that might arise on the construction of the classes granting the pension, whether, for instance, it would inure to the benefit of Mr. Tilley's estate if he died before ten years had elapsed, or had died while he was still in office. There is one point, however, on which I am not sure that I fully understand the judgment of Lawrence, J. If he meant that whenever a pensioner commutes a pension the sum received by way of commutation is taxable as income, as at present advised I do not agree with him; nor am I able to see that it makes any difference whether the commutation takes place before or after the pension has become payable. Schedule E charges pensions and annuities as specific things, in addition to charging profits arising from office, and if a commuted pension or annuity were taxable as income in the year that the sum was received, I cannot understand why it should make any difference whether the calculation and payment take place while the pensioner is still in the service of the granter or not. Nor does it seem to me to be right to say, as the Attorney-General submitted, that a pension must be deferred remuneration. Whether it be paid as a matter of contract or voluntarily, it may be a reward for or an inducement to render long service. For instance, an employer may pay all his clerks of a certain grade Pound 5 a week and be willing to pay no more. If he promises a pension of Pound 2 a week after thirty years service I do not see that this would be an inducement to them to remain in his employment, or, if paid

voluntarily, a recognition of long and faithful service. I agree with the Master of the Rolls that the appeal should be dismissed.

Appeal dismissed.

Leave to appeal to House of Lords.

SooperKanoon - India's Premier Online Legal Search - sooperkanoon.com