

National Mortgage and Agency Co. of New Zealand Vs. Inland Revenue Commissioners.

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Court : Kolkata

Decided On : Feb-11-1937

Reported in : [1938]6ITR74(Cal)

Appellant : National Mortgage and Agency Co. of New Zealand

Respondent : inland Revenue Commissioners.

Judgement :

The judgment of Lord Wright, M. R., was read by Romer, L.J. - I have read the judgments prepared and about to be delivered by my brethren Romer, L.J., and Greene, L.J. I am so fully in agreement with these judgments in every respect, both as regards reasoning and conclusions, that it is a work of supererogation to add any observations of my own. But I may perhaps say that as I read the sub-section the protean and ambiguous word 'income' as there used means the figure of income or part of income as assessed for tax purpose in either jurisdiction. The income or part of income, that is, the figure so assessed, is that on which the person has paid or become liable to pay tax within the words of the section, in the United Kingdom and in the Dominion respectively. Once it is established, on the principle expounded by my brethren, that the same part of income is assessed in the Dominion as that assessed in the United Kingdom 'double taxation' is pro tanto established, on the basis of and to the extent of the smaller assessment : the figures of assessment respectively are the material figures of income for this purpose.

ROMER, L.J. - On this appeal the Court is once more invited to consider and apply the provisions of Sec. 27(1) of the Finance Act, 1920. As the section has been recently discussed and explained by the House of Lords in the case of Assam Railways and Trading Co. v. Inland Revenue Commissioners, it becomes necessary to examine the facts and the judgments given in some detail.

The facts, so far as material for the present purpose, were as follows : The company concerned was an English company carrying on a business in India, from which business the whole of its income was (with a small exception) derived. It was controlled by its board in England and was accordingly taxed under Case I of Schedule D of the Income-tax Act, 1918, on the whole of the profits arising from its business in India. Under the rules applicable to that Case the tax on its income for the year ending April 5, 1929, fell to be computed on the company's profits for its financial year ending on March 31, 1928. The Profits so computed amounted to the sum of Pounds 18,750. Under the Indian Income-tax Act the tax for the year 1928-29 had to be computed on the profit for the same financial year, but those profits when ascertained in accordance with that law amounted only to Pounds 420,365. This was due to the following fact : (1) According to the Indian Act the sum paid by the company as interest on its debentures and amounting to Pounds 42,500 was a permissible deduction, whereas it was not so in the United Kingdom. (2) The profits derived by the company from a certain tea garden amounting to Pounds 8,343 were excluded from the Indian computation but were included in that of the United Kingdom. (3) Other divergencies between the two systems of taxation resulted in a net excess of Pounds 6,542 in the profits as ascertained in the United Kingdom over the profits as ascertained in India.

The company in due course paid United Kingdom income-tax calculated at the appropriate rate on Pounds

186,750 and paid Indian income-tax at the appropriate rate on Pounds 129,365. In these circumstances it was plain that the company was entitled to relief under Sec. 27(1). The question to be determined was as to the basis upon which such relief was to be calculated. The contention of the company was this : 'The subject of taxation both in India and the United Kingdom is the income derived from the business carried on in India during the year of assessment ending on April 5, 1929. According to the law of each country the tax on that income is ascertained by taking a notional sum that bears no relation to the actual income in fact and applying the appropriate rate to that notional sum. The fact that the notional sums are different in the two countries is immaterial. The notional sums are only brought into notional existence for the purpose of ascertaining what income-tax should be charged in the respective countries on the profits of the business earned in the year of assessment. Having served that purpose they need not be considered further. We have paid income tax for the year of assessment both in the United Kingdom and in India on precisely the same income and are entitled to relief under the section upon that footing.' It is an attractive argument and none the less so because it involves the proposition that throughout the sub section the word income means income and nothing else. Had it been accepted the company would have been entitled to be relieved to the extent of but not exceeding half the United Kingdom rate on the sum of Pounds 186,750. For the purpose of ascertaining the rate, the actual income from the Indian business would, no doubt have to be ascertained. But this should present no difficulties to a competent accountant. If any such difficulty should occur it would have to be settled by the appropriate tribunal. The actual profit having been ascertained, the Indian rate and the United Kingdom rate for the purposes of the section would be ascertained by dividing the amount paid in tax in the two countries respectively by the amount of the actual profit.

This contention on the part of the company failed, however, to find acceptance at the hands of the Commissioner for the Special purpose of the Income tax Acts, Finally J., the Court of Appeal or the House of Lord; and must now be regarded as unsound.

The Special Commissioner held that the company was entitled to relief in respect of the sum of Pounds 135,107. This sum was arrived at by deducting from sum of Pounds 186,750 the two sums of Pounds 42,500 and Pounds 8,343. They then analysed these two sums and found that, inasmuch as no debenture interest had been deducted in the United Kingdom computation and had been deducted in the Indian computation, Pounds 42,500 part of the United Kingdom taxed income had not been taxed in India. They further found that Pounds 8,343 had been included in the United Kingdom taxed income but had not been taxed in India. The reason why they did not also find that Pounds 6,542, further part of the Pounds 186,750, had not been taxed in India would seem to have been that they had not been taxed in India would seem to have been that they had not been asked to do so by the Inspector of taxes. Attention was called to this omission in paragraph 7 of the respondents case when the matter eventually came before the house of Lords. On an appeal by the company to Finally, J., that learned Judge affirmed the decision of the Commissioner and, as I read his judgment, upon the same grounds as those on which the Commissioner had proceeded.

Pausing there, it is to be observed that the question whether and to what extent income tax in this country or in India would ultimately fall on the debenture holders in respect of the interest paid to them was immaterial. Income tax on the Pounds 42,500 had been paid by the company here, and had not been paid by the company in India, and that is all that mattered. For it had been decided by the House of Lords in the Delegate case that the word paid in the section means paid and not ultimately paid.'

The decision of Finally, J., was affirmed by the court of Appeal but on somewhat different grounds. They agreed with the learned Judge in treating the sum of Pounds 186,750 as the income from the Indian business that had been taxed in the United Kingdom and not merely as notional sum arrived at for the purpose of calculating the tax to be paid on the real income for the year of assessment. They also treated the Pounds 129,365 as representing the part of the Pounds 186,750 that had been taxed in India and as representing therefore, the only part of companies income from the India business that had borne tax in both countries. They made no analysis of the two figures. They rejected, indeed the idea that any such analysis ought to be made. When we come to consider, said Lord Hanworth M. R. [102 L.J.K.B. at p. 706; (1933) 2 K.B. at p. 593],

'what is to be the relief it has to be shown by the taxpayer that on a part of the income which is his statutory income in the United Kingdom he has paid Dominion income tax for that year. Now are we to reopen and to readjust the figures in each country? Are we to set aside the items which compose the total assessable income for which the man is to be charged first in the Dominion and afterwards in the United Kingdom To my mind not so. You have to deal with the results which have been attained by following the legislative directions in each country and you have to deal with the result when the exemptions or deductions or abatements have been allowed, and you cannot scrutinise those abatements or deductions by a comparison with a different system in the other part of the Commonwealth and it falls upon the taxpayer to prove that he has paid income tax for that year in respect of the same part of the his income. The Appeal court accordingly held that the company was entitled to relief in respect only of Pounds 129,365. But as the Crown was content with the figure of Pounds 135,907 arrived at by the Commissioner the appeal was merely dismissed.

The matter was then taken to the House of lords who unanimously affirmed the decision of the court of appeal. Lord Warrington of Clyffe, in his speech, summed up the conclusions as follows (103 L.J.K.B. at p. 586; [1935] A.C. at p. 454) In the present case the part of his income on which the taxpayer has paid tax in England is Pounds 186,750. In India, he has paid tax on a smaller part numerically of the same income. This was precisely the view of the case that had commended itself to the court of Appeal. Lord Weight also agreed with that view. The Court of Appeal he said (103 L. J.K.B. at p. 587; [1935] A.C. at p. 456), in confirming (in substance) the ruling of the Special Commissioners took the view (rightly as I things) that the true amount on which relief should be given was Pounds 129,365. I would call attention to the words in substance. Later on he said (103 L.J. K.B. at p. 589; [1935] A.C. at p. 460) : On the words of the section it seems that the appellants can only show double taxation in regard to Pounds 129,365 which is part of the Pounds 186,750.' Lord Blanesburgh, Lord Atkin and Lord Thankerton agree with the judgments of Lord Warrington of Clyffe and Lord Wright.

The case seems to establish the following conclusions : (1) That the word income in the section does not mean thermal income but the statutory, or national income by means of which the tax is calculated. (2) That if this statutory income in the Dominion is Pound A and in the United Kingdom the statutory income from the same source is Pound (A plus B) relief will be given in respect of Pound A. (3) That an analysis of the two statutory income for the purpose of comparing, for example, the respective allowances for repairs or depreciation is inadmissible. It is in regard to the two latter conclusions that the view taken by the Special commissioners and Finally J. differed from that taken by the higher tribunals. The difference is one of vital importance. If the two statutory incomes are to be dissected as was done by the Special Commissioners every item appearing on the debit side in the Dominion account that does not appear on the debit side of the United kingdom account must be regarded as having born income tax in the United Kingdom and not in the Dominion and vice versa. If for, instance, in the Dominion Pounds 1000 be allowed for depreciation, and nothing for bad debts, and in the United kingdom Pounds 1000 be allowed for bad debts, and nothing for depreciation, then although the statutory incomes in the two countries might be equal (say Pounds 10,000) relief could only be given in respect of Pounds 9000. This same result would occur in case of a difference in relation to receipts of the business. The receipts of the business might in the Dominion be treated as being worth Pounds 50 less than the value at which the same receipts are brought into account in the United Kingdom. The total statutory incomes might be the same and yet relief would only be given in respect of the statutory incomes less the Pounds 50. In cases where the statutory incomes of the two countries are the incomes or average of incomes over different periods of time hopeless confusion would result. In the United Kingdom the statutory income is that of or for the year preceding the year of assessment. In the Dominion it might be that of the year of assessment. In such case no relief could be granted at all even though the statutory income in the Dominion were equal to that in the United kingdom. For no item on either side of the two accounts would be the same. The view taken by the court of Appeal and the House of lords in the Assam case would however, lead to no such difficulty. Nothing need be regarded except the two statutory incomes of the business, taking care of course to see that neither includes income from any other source. Relief will then be given to the extent of the smaller of the two sums, without inquiring into the reasons for the difference between them. The statutory

income is in such case to be treated as the taxable income for the year of assessment. Both sums must be treated as representing income derived from the same source and for the same period namely, the year of assessment. It necessarily follows that the smaller sum is a part of the larger sum, as was pointed out both by Lord Warrington of Clyffe and Lord Wright in the Assam case.

But just as it is necessary to see that the statutory incomes do not include any receipt from sources other than the business, so also it is necessary to see in each case that no profits of the business are being taxed otherwise than through the medium of the statutory income. For what has to be ascertained for the purpose of the section is how much tax has been paid by the company on its profits in this country and in the Dominions respectively.

It only remains to apply these considerations to the present case, taking for that purpose the year of assessment 1928-29. The United Kingdom statutory income from the whole of the company's business for that year was Pounds 70,017. This figure, however, included certain receipts from sources other than the business of the company in New Zealand, amounting together to Pounds 25,549, leaving the statutory income for the last mentioned business Pounds 44,468. The New Zealand statutory income was Pounds 26,592. The appellants are therefore, entitled to relief in respect of that sum. That would be the only relief to which they are entitled if under the New Zealand law the profits from the New Zealand business are only taxed by reference to the New Zealand statutory income. It appears, however, that the effect of the Land and Income tax Act 1923, of New Zealand is to exclude from the statutory income a sum equal to the interest on debentures the money secured where by has been employed in the production of the assessable income, and to tax such sum in the hands of the company. The profits of the New Zealand business are not, therefore, taxed merely by reference to the statutory incomes, but partly by reference to that income and partly by reference to the amount of interest payable in respect of its debentures. The amount taxed under this latter head is the sum of Pounds 34,779 and on this sum the company is also entitled to relief. It is true that as regards such last mentioned part of the company's profits the company has only been assessed as agents for the debenture holders; but this is immaterial. In order to get relief under the section it is sufficient for the company to show that it has paid the New Zealand tax on that part of its profits. The question in what capacity it has paid and the question whether the tax falls ultimately on the company has paid United Kingdom income tax on a part of its income namely Pounds 34,779, and has proved that it has paid Dominion tax in respect of the very same thing. In accordance with the plain words of Sec. 27(1) of the Finance Act 1920, it is entitled to relief on that sum.

For these reasons I am of opinion that both appeals should be allowed.

GREENE, L.J. - Sec. 27(1) of the Finance Act, 1920, provides as follows : 'If any person who has paid, by deduction or otherwise, or is liable to pay, United Kingdom income tax for any year of assessment on any part of his income proves to the satisfaction of the Special Commissioner that he has paid Dominion income tax for that year in respect of the same part of his income, he shall be entitled to relief from United Kingdom income tax paid or payable by him on that part of his income at a rate there on to be determined', as therein mentioned. The language of this provision appears at first sight to be reasonably clear. The first thing to consider is whether the person claiming relief is liable to United Kingdom Income tax 'on any part of his income'. His income for the purposes of the United Kingdom income tax may comprise a number of elements derived from different sources and taxable under different schedules. Any one of these elements may be a part of his income for the purposes of this limb of the subsection. The next question for consideration is whether he has paid Dominion income tax for the year in question in respect of the same part of his income. It is said that in strictness the word 'same' is necessarily inappropriate to convey the meaning intended, since income as assessed for United Kingdom income tax is a notional sum and the income on which Dominion income tax is paid cannot be the same. This to my mind presents no practical difficulty in construing the subsection, nor am I prepared to find in its language such abstruse metaphysical difficulties as were suggested in the arguments for the Crown. The subsection says that identity exists and as a practical matter I can find no difficulty in treating the assessed income which is taxed in a Dominion as being the same as that taxed in the

United Kingdom. Now even if the matter had been devoid of authority, I should have thought that the character of the identity postulated by the words the same part of his income was not difficult of ascertainment. If the income is derived from dividends on shares or interest on debentures, and it is taxed in both countries the identity is parent. If the income is derived from a business, the question is more complicated but, not in my opinion any more difficult to answer. In such a case, in order to ensure the identity which the sub section requires, the first thing to do is to see that the income taxed in the Dominion is the same as that taxed in the United Kingdom in the sense that each includes, and includes only, income (that is to say incoming profits or gains) which is common to both and any necessary adjustments of the account to ensure this result must be made. To take a single example : if an English company carries on from England business both in England and in a Dominion, its assessment here will be on the amount of the profits of the entire business. But in the Dominion it will be assessed only on the profit of the business so far as carried on in the Dominion. It is accordingly necessary in order to achieve the primary identity of the two incomes, to dissect the United Kingdom assessment and eliminate from it that portion which represents the profits of the English business. This is a perfectly simple and intelligible operation, and presents no difficulty in principle. But it will be noticed that the only matter to be eliminated from the United Kingdom or the Dominion assessment (as the case may be) are incoming profits or gains which are not common to both assessments. It is in my judgment, essential to the proper understanding of this case, to appreciate the fundamental distinction between sums which truly represent incoming profits and gains and sums which represent allowances or permissible deductions in arriving at the assessable income. For reasons which will appear later, it is only the former, which must be eliminated not the latter. But the process of arriving at the identity of the two incomes does not stop at the point where incoming profits or gains not common to both assessments have been eliminated. When this has been done, the resultant figures for the United Kingdom income and the Dominion income will in all probability be different by reason of differences in the two methods of arriving at assessable income. It must have been present to the mind of the legislature that uniformity in the method of assessing business profits is not to be found throughout the Empire. The rules for the deduction or non deduction of expenses or the allowance for wear and tear (to take some examples) which operate in the United Kingdom, may differ widely from those in force in a Dominion. And here it is necessary to see that what I may call a secondary identity is attained. It is after the elimination of incoming profits or gains which are not common to both assessments the income from the Dominion business is for the purpose of the United Kingdom assessment (let me say) Pounds 10,000 and for the purpose of the Dominion assessment Pounds 8000 it is only in respect of Pounds 8000 that the identity exists. Pounds 8000 is not the same part of the company income as Pounds 10,000 even though each figure represents an assessment in respect of the same incoming profits or gains. The relief given by the sub section is therefore to be ascertained on the footing that the only part of the business income in respect of which tax is excitable in both countries is Pounds 8000. In the converse case if the figures are reversed the only part of the company's income on which tax is excitable in the United Kingdom will be Pounds 8000 and the additional Pounds 2000 in the Dominion assessment will not entitle the company to any relief.

In support of the view expressed above, I may quote some words from the speech of the present Master of the Rolls in the *Assam* case (103 L.J.K.B. at p. 589; (1935) A.C. at p. 459). His Lordship said : It seems clear that there must be a definite part of income brought into question, and that can only be expressed in a sum of money. As income *ex vi termini* must be expressed in a sum of money, the words the same part of his income must involve a comparison between two sums of money, which prove to be the same. The contention of the appellants is to the contrary it is said on their behalf that words the same part of this income refer solely to what is called the source and that identity of amount is immaterial and does not come into question except for the purpose of ascertaining the rate of tax to be allowed for. I cannot agree with this argument. No doubt questions of source as it has been called, that is, such questions as where the income comes from, are essential to identify, so far as that aspect goes, what is taxed in the United Kingdom with what is taxed in the Dominion : but in addition the income itself that is, the amount of money, must also be identified. I think the words the same part of his income are apt to include both elements of comparison and identification.' Lord Blanesburgh (103 L.J.K.B. at p. 585; 1935 A.C. at p. 452) expresses the same view in a different way.

In order to apply these principles to the present case, it is necessary to examine shortly the facts relating to the two assessments. There are some variations in the figures in the various documents due to certain adjustments which have been made, but I will take the round sums which will readily be recognisable. The figure of the United Kingdom assessment for the year 1928-29 is Pounds 70,000. This includes, in addition to the profits of the business in New Zealand, the following items of incoming profits or gains : 1. United Kingdom profits; 2. New Zealand war Loan interest; 3. Preference Dividend; 4. Ordinary dividends on shares in 'X' amounting in round foragers to Pounds 25,000.

Now none of these items is brought into the New Zealand assessment and the first step necessary to secure identity between the two incomes is to deduct them from the United Kingdom assessment which will then give the figure of Pounds 45,000 as representing that part of the United Kingdom assessment which is exclusively referable to that part of the income which is taxed in both countries. This is what the Master of the Rolls in the Assam case described as Identification of what is taxed in the United Kingdom with what is taxed in the Dominion.' Now the New Zealand assessment in respect of that part of the income is Pounds 26,000 only, and it is in respect of this figure that what the Master of the Rolls describes as identification of the income itself, that is the amount of money exists. The result, in my opinion, is that the appellants are entitled to relief upon the basis that to the extent of the assessment of Pounds 26,000 they have paid Dominion tax upon the profits of the New Zealand business which are the same subject matter of taxation as those covered by the United Kingdom assessment as adjusted in the way which I have described. This result appears to me to accord with the language of the sub section, the construction placed upon it by the House of Lords in the Assam Case and with good sense.

Upon the view of the meaning of the sub section which I have expressed, differences between the rules prevailing in the two countries as to such matters as allowances and deductions of expenses are entirely disregarded. To take a simple example let me assume that the method of arriving at the assessable profits as a Dominion business is identical both in principle and in the matter of amount in both countries with the exception of wear and tear allowance, and gives for each country a figure of Pounds 10,000 before deducting that allowance. Let me assume then that the allowance in the United Kingdom is Pounds 750 (giving a United Kingdom assessment of Pounds 9,250) and in the Dominion Pounds 1000 (giving a Dominion assessment of Pounds 9000). The business income on which Dominion tax has been paid will be Pounds 9,000, that on which United Kingdom tax has been paid will be Pounds 9,250 and relief will be given accordingly. It is quite illegitimate in my opinion to treat the difference between the two allowances, namely Pounds 250 as in some sense a part of the business income which has not suffered tax in the Dominion and as therefore, for the purpose of the sub section to be deducted from the United Kingdom assessment under the guise of eliminating from that assessment a piece of income which has not borne tax in the Dominion. In truth, what has borne tax in the Dominion allowance over the United Kingdom allowance. Nor is the position, in my opinion any different if one of the countries makes an allowance or permits a deduction of kind not recognised in the other in the other country. Again, let me take a simple example. I will assume that all figures are identical in the two countries except that in the United Kingdom an allowance is given which is not given in the Dominion for example an allowance of Pounds 500 in respect of bad debts, giving an assessment of Pounds 9,500 and a deduction is permitted in the Dominion which is not permitted in the United Kingdom for example an allowance of Pounds 500 in respect of certain expenses of the business, giving an assessment of Pounds 9,500. The two figures which are comparable for the purpose of relief under the sub section will be Pounds 9,500 and Pounds 9,500 - not Pounds 9000 and Pounds 9000 as they would have to be if the Pounds 500 in each case were to be treated as an untaxed part of the business profits.

It is at this point that what, in my opinion, is the fallacy underlying the Crown's argument on this part of the case emerges. It is due to a failure to distinguish between two things fundamentally different namely, an incoming profit and an allowance or deduction. I have already referred to the items of incoming profit which are included in the United Kingdom assessment but not in the New Zealand assessment and shown how these must be deducted from the United Kingdom assessment for the reason that the assessment is pro tanto

referable to these items. But the Crown seeks to treat on the same basis as these items certain sums representing allowances or deductions made in New Zealand namely, (1) debenture interest (2) 5 per cent unimproved value of land allowance, amounting in round figures of Pounds 45,000. These sums it is said must be deducted from the United Kingdom assessment on the basis that the year pieces of income, not taxed in New Zealand to which pro tanto the United Kingdom assessment is referable. The result is to reduce the United Kingdom assessment to nothing or a minus quantity for the purpose of the sub section and to destroy the claim to relief. But it is to be noticed that the effect of these allowances and deductions is in itself to reduce the amount of New Zealand assessment and so to reduce the area of double taxation in respect of which the relief may be claimed. To use them again for the purpose of still further reducing that area is in my opinion wholly illegitimate.

The Crown's argument here is, in my judgment based on a misconception of the effect of the Assam decision. I have had the advantage of reading the analysis of that decision contained in the judgment which my brother Romer has just read and I entirely agree with it. I only wish to add one observation of my own. In the Assam case the appellants were endeavouring to write back into the Indian assessment two sums which had not entered into that assessment at all, one of which was an item of incoming profit not taxed in India, namely the Bogapani Tea Garden account, and the other of which was a deduction in respect of debenture interest. For the purpose of the decision in that case the difference in character of these two items was irrelevant, it was equally inadmissible to add back the one and the other to write up the Indian assessment above its true figure. But this is an entirely different thing to saying that the fact that a particular deduction is allowed in a Dominion which is not allowed in the United Kingdom can be used in order to write down the United Kingdom assessment below its true figure which is what the Crown claims to be able to do in this case.

I have so far dealt only with the New Zealand assessment in respect of business profits and for that purpose I have treated the deduction of a sum equal to the debenture interest as to what for the purpose of that assessment is in fact is, namely, a true deduction of a business expense. But the company was assessable and was in fact assessed in respect of what it paid for this interest under a different provision of the New Zealand Statute namely, Sec. 116. Under that section a company is to be the agent of the debenture holder for the purposes of the Act and is assessable in respect of interest paid to them accordingly. The appellants contend that as no deduction was permissible in respect of the debenture interest for the purposes of the United Kingdom assessment they have paid United Kingdom income tax upon it; that they have also paid New Zealand income tax upon it that the fact that under the New Zealand act this tax is chargeable under a different section is irrelevant since all that section 27(1) of the Finance act 1920, requires is that Dominion tax shall have been paid and that the fact that under the New Zealand statute they are to be deemed to have paid as agents and have in New Zealand statutory right of recovery against the debenture holder a right which is not enforceable in this country is also irrelevant. In my opinion the argument of the appellants upon this point is right. Whether or not the part of the company income in respect of which it has paid tax in the Dominion is the same as the part of its income on which it is chargeable to United Kingdom income tax is in my judgment to be decided by reference to English law alone : and the fact that for purposes of its own the New Zealand legislature has chosen to treat the sum paid away in interest as in a different tax category to that in which it is treated here cannot in my opinion affect the matter. I agree that the appeal should be allowed.

Appeal allowed.