Friday, November 12.

FIRST DIVISION.

[Exchequer Cause.

INLAND REVENUE *v.* HENDERSON.

Revenue — Income Tax — Interest on Jus Relictæ—Interest of Money—Income Tax Act 1842 (5 *and* 6 *Vict. cap.* 35), *sec.* 100, *Schedule D, Third Case — Income Tax Act* 1853 (16 *and* 17 *Vict. cap.* 34), *sec.* 2, *Schedule D.*

Some years after her husband's death a widow obtained decree for (*a*) the balance of her *jus relictæ*, towards which partial payments had been made by her husband's trustees, and (*b*) interest at 4½ per cent. on the various amounts outstanding from time to time, beginning with the date of her husband's death. The trustees during the whole period paid income tax on the whole revenue of the trust, and the interest decerned for was ultimately paid to the widow in a lump sum without deduction of income tax. *Held* that the widow was assessable to income tax on the sum paid as interest at the rate of tax then current.

Lees' Trustee v. *Inland Revenue*, 1916 S.C. 188, 53 S.L.R. 156, *followed.*

Mrs Helen Mary Macdiarmid or Henderson, *respondent*, appealed to the Commissioners for the General Purposes of the Income Tax Acts for the County of Aberdeen against an assessment made on her under Schedule D for the year ending 5th April 1919 on the sum of £341 in respect of untaxed interest. The Commissioners having found that the interest in question had been paid to the respondent out of sources already taxed sustained the appeal and discharged the assessment. Against that decision S. L. Sweet, Inspector of Taxes, appealed.

The Case stated — "The following *facts* were admitted or proved :—(*a*) In an action raised in the Court of Session on 21st January 1914 by the respondent against the trustees of her deceased husband John Henderson, retired builder and valuator, who resided at No. 12 Rubislaw Den North, Aberdeen, for payment of her *jus relictæ*, the Lord Ordinary on 12th July 1917 decerned against the said trustees for payment to the respondent of the sum of £394, 13s. (being the balance of the respondent's *jus relictæ*), and interest at the rate of 4½ per centum per annum upon (1) the sum of £4394, 13s. from 6th November 1912, the date of the death of respondent's husband, to 10th March 1914; (2) the sum of £894, 13s. from 10th March 1914 to 17th December 1914; and (3) the sum of £394, 13s. from 17th December 1914 to the date of payment of that sum, under deduction from the amount of such interest of such amount of income tax thereon, if any, as was deductible and retainable by the trustees under the Acts relative to income tax. Reference is made to the report of said decision in 1916, 2 S.L.T. 292. (*b*) The said interest, which amounted to £341, was paid to the respondent on or about 14th August 1917. No income tax was deducted therefrom by the trustees on payment of said sum to the respondent."

Argued for the appellant—The finding of the Commissioners had no evidence to support it. Further, it was irrelevant, for the whole income of the trust had paid tax. Payments out of that income might well be subject to pay tax. The payment to the respondent was not of the nature of a payment to a beneficiary under a trust, neither was it by way of damages. *Jus relictæ* was a claim of debt burdening the moveable trust estate, and giving no right to claim any specific items thereof, and no doubt being exigible only if there was moveable estate free of ordinary debts — *Cameron's Trustees* v. *Maclean*, 1917 S.C. 416, 54 S.L.R. 355; *M'Murray's Trustees* v. *M'Murray*, 1852, 14 D. 1048, *per* Lord President M'Neill at p. 1053, and Lord Ivory at p. 1054. Legitim was in the same position, and interest on both was due irrespective of whether or not the trust estate was earning interest and its amount—*Bishop's Trustees* v. *Bishop*, 1894, 21 R. 728, 31 S.L.R. 590, which must be regarded as overruling *M'Intyre* v. *M'Intyre's Trustees*, 1865, 3 Macph. 1074. Such being its nature, interest was payable *ex lege* upon *jus relictæ*. Even on legacies interest was payable—*May's Trustees* v. *Paul*, 1900, 2 F. 657, 37 S.L.R. 470. Consequently the payment in question was within the words of the statute either as profits or gains or as interest on money. The method of assessment was right, for until decree the payment was illiquid. The case was completely covered by *Lees' Trustees* v. *Inland Revenue*, 1916 S.C. 188, 53 S.L.R. 156. The payment was not one of damages. *Carmichael* v. *Caledonian Railway Company*, 1870, 8 Macph. (H.L.) 119, *per* Lord Westbury at p. 131, 7 S.L.R. 666, was referred to.

Argued for the respondent—The payment in question was not of the interest, though it was so called, but was damages, and damages were capital and not subject to tax — Bell's Prin., sec. 32; *In re National Bank of Wales*, [1899] 2 Ch. 629, *per* Wright, J., at 651; *Dunn* v. *Chalmers*, 1898, 25 R. 688, *per* Lord M'Laren at p. 689, 35 S.L.R. 537. Alternatively the trustees simply held the respondent's fund for her until they paid it over, and in place of her paid the tax on the interest or profits it earned. The widow was entitled to share in profits which her *jus relictæ* earned after her husband's death—*Ross* v. *Masson*, 1843, 5 D. 483; *Gilchrist* v. *Gilchrist's Trustees*, 1889, 16 R. 1118, 26 S.L.R. 639. Consequently the trustees having paid tax on the whole trust income had paid any tax exigible from the respondent. In any event the tax should not be imposed for more than three years back, for that was the limit for entertaining claims of relief. Further, the assessment ought to be year by year at the rate current in each year—*In re Craven's Mortgage*, [1907] 2 Ch. 448, *per* Warrington, J.

At advising—

LORD PRESIDENT—The respondent's husband died in 1912. She claimed her *jus relictæ*. The settlement of her claim led to litigation between her and her husband's

trustees. The litigation began in 1914, and payments to account were made during its dependence. The litigation ended in 1917 in a decree in her favour for the balance of the capital of the *jus relictæ* as finally adjusted, and for interest which was fixed by the Court at 4½ per cent. per annum on the various amounts outstanding from time to time, beginning with the date of her husband's death. This interest was paid to the respondent in 1917 (along with the principal sum decerned for) without deduction of income tax. The appellant now claims to assess this interest to income tax under section 2 (Schedule D) of the Income Tax Act 1853, and the rules relating to the Third Case of Schedule D of the Income Tax Act 1842.

It is settled that the words "all interest of money" occurring in the third paragraph of Schedule D of the Income Tax Act 1853, section 2, cover interest whether annual or not—*Leeds Benefit Building Society* v. *Mallandaine*, [1897] 2 Q.B. 402. Accordingly the fact that the sum paid to the respondent in 1917 in name of interest was not payable to her termly for a year or years is immaterial if it was "interest of money" within the meaning of the schedule.

In *Lees' Trustees* v. *Inland Revenue*, 1916 S.C. 188, 53 S.L.R. 156, a decree had been pronounced in 1911 against the representatives of a deceased trustee for recovery of sums which had been lost to the trust through the negligence of the deceased trustee a number of years before. The decree covered the capital of the funds and interest at 3½ per cent. per annum from a date which—for present purposes—may be identified with the date when the funds were lost. The defenders did not pay up till 1913. In that year they paid both the capital of the funds which had been lost, together with the taxed expenses, as decerned for, and also (*a*) a sum arrived at by calculating interest at 3½ per cent. per annum on the capital of the funds since the date when they were lost to the trust, and (*b*) a further sum arrived at by calculating interest at 5 per cent. per annum on the amount of the decree for taxed expenses. The judgment in the case which affirmed the liability of the payee to assessment in respect of both of the latter sums makes no distinction between the two, although Lord Johnston expressed the opinion that "where a pursuer recovers damages with interest from the date of decree" the interest in that case is not chargeable to income tax, because it is part of the damages. This opinion has no bearing on the present case, which arises with regard to proceedings for the recovery, not of reparation, but of the debt legally due to a widow *jure relictæ*. Nor indeed does the present case raise any question regarding the chargeability to income tax of the usual interest at 5 per cent. payable on a sum comprehended in a decree of court, from the date of such decree during non-payment. But as regards the sum which was arrived at in *Lees'* case by calculating interest at 3½ per cent. per annum on the capital of the lost funds the ground of the decision was that that sum was the adopted measure of "recompense to the creditor for being deprived of the use of his money," or the "surrogatum for that [income] which ought" (but for the deprivation of the trustees of possession of part of the trust capital) "to have termly reached the hands of the trustees and to have been applied by them as income." Such measure of recompense for being deprived of the use of money, and such surrogatum for income not received, was held to be "interest of money" within the meaning of Schedule D (as that schedule stands under the Acts of 1842 and 1853).

It does not seem material to inquire into the ratio of the rule which gives a widow interest on the amount of her *jus relictæ* from the date of her husband's death at 5 per cent., or—according to modern practice—at a rate conformable to the returns yielded by her deceased husband's estate, It is enough to say that she is a creditor of the estate, not a beneficiary under her husband's trust. Adverting to Lord Fraser's three categories in *Blair's Trustees* v. *Payne*, 1884, 12 R. 104, 22 S.L.R. 54, the interest is due to her *ex lege*, since it is neither *ex pacto* nor *ex mora*—at least so far as regards the time necessarily consumed by the process of ascertaining the amount of the free residue and by the deliberations of the widow on the problem of her election. Such being the position, the interest in the present case seems to me to fall within the comprehensive definition adopted in *Lees' Trustee* v. *Inland Revenue*—either as the measure of recompense for being deprived of the use of money, or as a surrogatum for income not received. It is remarkable that there should be so little authority with regard to the wide scope of chargeability under the Acts of 1842 and 1853, which the decision in *Lees' Trustee* discloses. But the precedent of *Lees' Trustee* was unchallenged at the discussion of the present case; it is binding and must be followed. The present case shares with *Lees' Trustee* the peculiarity that the rate of interest was not fixed, and could not even have been known, until the Court modified it at 3½ per cent.

The Commissioners expressed their judgment as one on the facts, and held that the interest had been paid to the respondent out of sources already taxed. It may well be—although it is not among the facts narrated as proved in the case—that the trustees paid all the income tax chargeable on the income of the deceased's estate. But that circumstance affords no evidence that the interest paid to a creditor on the capital sum of a debt due to such creditor has already been charged with the tax due upon it.

I think we have no alternative but to sustain the appeal.

LORD MACKENZIE—It is sufficient for the determination of the present question to note that what the widow has been held by the Court entitled to receive is payment of interest upon a debt, not a share of the trust income. She has paid no tax upon this, and has no title to maintain any plea which the trustees might urge. The inter-

est is interest on "money," and falls directly under the language of section 2, Schedule D, of the 1853 Act. The *jus relictæ* (although in this case it was specially bequeathed — see 1916, 2 S.L.T. 292) is a debt due at the husband's decease, and bears interest *ex lege* from that date until payment at a rate to be fixed by the Court. It is in the same position as legitim. The widow is a creditor, though postponed as in a question with ordinary creditors. The interest received on the trust estate bears no necessary relation to the rate of interest allowed on the debt. There is no case in which the claim for interest has been held to be elided because the estate was non-productive, although such a possible defence is referred to by Lord Cowan in *M'Intyre's Trustees* (3 Macph. 1074). The interest on the *jus relictæ* is not of the nature of damages, for the element of wrongful withholding is absent. It is none the less of the nature of interest because it is peculiar in this respect that it is not instantly demandable.

These considerations are sufficient for the disposal of the present case. It only remains to say that the decision in the case of *Lees' Trustee* is directly applicable. The soundness of that judgment was not disputed in the argument. In my opinion the determination of the Commissioners is wrong.

LORD SKERRINGTON—There are no facts found proven in this Stated Case which support the view which the respondent's counsel asked us to accept, viz., that the sum of £341 received by a widow in name of interest on her *jus relictæ* was not really interest but was damages. So far as appears it was what it bore to be—interest which as we all know is due *ex lege* upon a widow's *jus relictæ*. I reserve my opinion upon the question whether interest is exempt from taxation under the Income Tax Acts merely because the liability to pay arises *ex mora*, viz., in respect of the wrongous withholding of the capital.

The other ground upon which the determination of the Commissioners was supported was that upon which they themselves proceeded, viz., that the interest in question had been paid to the respondent out of sources already taxed. That involves a question of fact, but the Solicitor-General told us that for the purposes of this case we might assume that Mr Henderson's trustees had duly paid income tax upon the whole revenue of the trust. One might have expected that in settling with the widow the trustees would have deducted the income tax which they had paid. When one examines the decree, however, it becomes apparent that this matter was not overlooked, because it reserves to the trustees any right which they may have to deduct income tax. No such deduction was made. No doubt the trustees were advised that this income was not yearly income, and that accordingly they could not deduct the tax. At any rate the respondent successfully asserted her right to receive in full what she was awarded by the Court viz., interest at 4½ per cent. upon the various balances due to her from time to time. This was hard upon the persons interested in the residue of Mr Henderson's estate, but that is no reason why the respondent should obtain a benefit to which she is not otherwise entitled. It might have been different if in the adjustment of the interest account the parties had proceeded upon a different footing and had awarded her one-half or one-third of the free income received by the trustees. In that case it might have been argued that she had already paid income tax by way of deduction and that she ought not to be compelled to pay a second time. I think that the Commissioners' decision is bad in law and that their determination falls to be reversed.

LORD CULLEN — The provision of the income tax statutes here in question brings under taxation "interest of money." It expresses no distinction as to the footing on which the interest has accrued, whether *ex contractu* or otherwise. In the present case the interest sought to be taxed is the subject of a judicial decree which constituted the capital amount of the respondent's legal claim for *jus relictæ* on the estate of her deceased husband, together with interest thereon during the non-payment. The interest is mainly for the period prior to the date of decree and to a small extent for the period thereafter. As the authorities stand the respondent's claim was a claim of debt, and the interest payable *ex lege* on the capital amount thereof would seem, therefore, to fall within the words of the statute. The respondent's argument to the contrary appears to me to be met by the case of *Lees' Trustee* v. *Inland Revenue*, 1916 S.C. 188, 53 S.L.R. 156, which was not challenged and is binding. The interest decerned for was not defined as a *pro rata* share of, or as payable out of, the income of the trust estate, but was interest at the rate of 4½ per cent. payable to the respondent *qua* creditor. It was paid to her in full, and it follows from the decision above cited that it is taxable in her hands as the appellant contends.

The Court reversed the decision of the Commissioners and remitted to them to assess the respondent.

Counsel for the Appellant—The Solicitor-General (Murray, K.C.) — R. C. Henderson. Agent—Stair A. Gillon, Solicitor of Inland Revenue.

Counsel for the Respondent—Wark, K.C. —Scott. Agents—J. & J. Galletly, S.S.C.