

SCOBLE AND
OTHERS *v.*
SECRETARY
OF STATE
FOR INDIA.

No. 259.—COURT OF APPEAL.—13th February, 1903.

HOUSE OF LORDS.—15th June, 1903.(1)

SIR ANDREW SCOBLE AND OTHERS *v.* THE SECRETARY OF
STATE OF INDIA.

For the Judgment in the Divisional Court, *see* page 478,
supra.

(1) Reported 1903, 1. K.B. 494, and A.C. 1903, 299.

On appeal, after hearing Counsel on both sides, the Court of Appeal reversed the decision in the Court below. The following Judgments were delivered.

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JUDGMENT.

Vaughan Williams, L.J.—In our Judgment this appeal ought to succeed. I assent to a great deal that the Attorney-General has said about annuities; but it seemed to me that the outcome of this argument left him in this position:—He could not say that every annual sum which was payable under a contract was necessary and necessarily an annuity within the Income Tax Acts. It had really to be admitted that in any case in which it appeared upon the face of the contract that there was a debt existing independently of the contract which gave rise to the annual payment if the annuity or annual payment was, on the face of the contract, of such a nature that you could say on reading the contract: This is not a contract for the purchase of an annuity; it is a contract under which a debt is made payable by instalments—that the Income Tax would not apply in such a case to the whole sum payable by such annual instalments. It is not denied, but that the Income Tax Acts would apply and Income Tax be payable in respect of so much of the annual payment as was not a repayment of an instalment of the antecedent debt; it was not denied—and is not denied in the present case—that Income Tax is payable upon so much of this annual sum, the annual instalment of purchase money—payable by the Indian Government, as consists of interest. The whole question in this case is: Is Income Tax payable upon that portion of the annual payment which you can discover from the very terms of the contract is a mere payment of an instalment necessary to complete the payment of an existing debt? In my Judgment no Income Tax is payable in such a case.

Vaughan-Williams, L.J.

Now when I come to look at the clauses in this contract, clauses 22, 23, and 26, it seems to me perfectly obvious that, there having come into existence a debt payable by the Indian Government for the purchase of this railway, the Indian Government having the option, if they chose, to pay off this debt by annual payments, annual instalments, instead of paying down the gross sum, the Indian Government elected so to do, and that this annual payment (called in this contract an annuity) is really merely the payment of the purchase money of the railway by annual instalments plus interest. In my opinion there is no tax payable in respect of this annual payment in so far as it is an instalment of a repayment of the principal of a present debt. I think, under those circumstances the Judgment of Mr. Justice Phillimore was wrong, and that he ought to have given Judgment in favour of Sir Andrew Scoble and the other persons.

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Stirling, L.J.

Stirling, L.J.—I am of the same opinion. This question arises upon a contract entered into between the East India Company and the Great Indian Peninsula Railway Company in the year 1849; and it was thereby provided that at the expiration of a certain period the East India Company might give notice to the Railway Company of their intention to purchase the railway and works; and after certain other provisions it is provided that the East India Company shall be bound to pay in London for the purchase all the premises the whole amount of the value of all the shares or capital stock of the Railway Company, calculated according to the mean market value in London of such shares or stock during a certain period previous. That being provided, it is also provided by Clause 26 that in every case in which the East India Company shall become bound to repay the capital expended by the Railway Company "it shall be lawful for the East India Company, instead of paying a gross sum of money in respect of the premises, to declare, by notice to the said Railway Company in London, their option to pay an annuity to be reckoned from" a certain period, and to continue during a period which is also defined, and, in that case, such annuity shall be payable in London, the rate of interest which is to be used for calculating the annuity "being determined by the average rate of interest during the preceding two years received in London upon public obligations of the East India Company." Now the event happened and the English Government, which succeeded to the obligations of the East India Company, gave notice to exercise the option of paying an annuity. This option is one which is obviously intended for the benefit of the debtor, in this case the Government. The sum which was left to be paid was large, amounting to over £34,000,000; and, obviously it was a very great advantage to a Government—which does not generally possess capital, but exists by income alone—to have the payment of that sum provided for by moderate annual payments and of income; and accordingly that course has been adopted. The question which we have got to decide is whether in these circumstances the Income Tax is payable on the full amount of each instalment or only upon so much of it as represents income. Now the case of *Foley v. Fletcher* has been much referred to and is relied on on both sides. It seems to me that the principle which is laid down in *Foley v. Fletcher* with reference to the construction of the word "annuity" in that case has never been departed from. I think all the learned Judges who gave Judgment in that case say the same thing. For instance, Chief Baron Pollock says this, "If we were at liberty to speculate on the matter and could come to the conclusion that a part of the annual payments is the price of the convenience of getting the payment postponed, we could not say that the payments are within the Act, because a part of them consists of profit.

“The instalments are payments of money due as capital; the Act has made no provision for such case. It professes to charge profits only and we cannot say that capital is liable to the Income Tax because found in company with profits.” And Mr. Baron Bramwell says, “By an Act for granting to Her Majesty duties on profits arising from property, professions, trade and offices, it cannot be taken that the legislature meant to impose a duty on that which is not profit derived from property but the price of it.” And similar observations are made by Baron Watson, who says, “An annuity means where an income is purchased with a sum of money and the capital has gone and has ceased to exist the principal having been converted into an annuity. Annuities are made chargeable by express words. The words ‘other annual payments’ in the same section, mean payments *ejusdem generis*, viz., as profits.” And Baron Channel says, “I think that the words do not include instalments which are part of a capital sum. To hold that the instalments are liable to Income Tax would be in effect to tax that which is capital and not income”; and he says a little further on, “I am of opinion that the words ‘all annuities, yearly interest of money or other annual payments’ do not include those payments which are in respect of the purchase money of an estate and are in the nature of capital and not of income.” True it is that there are found observations in the Judgments which seem to point in an opposite direction, for example, that which has been most relied on is what is said by the Lord Chief Baron at the close of his Judgment. “If the plaintiff had sold her estate for an annuity, so calling it the annuity would have been liable to Income Tax. But she sold it for a sum which is payable by instalments, which, is therefore, not chargeable.”

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Now, as to that portion of the Judgment, it has not been followed. We have express authority in the case of the *Nizam Guaranteed Stock Railway Company v. Wyatt* (1) of the Divisional Court for saying that the mere fact that a sum is designated as an annuity is not conclusive, but that the real nature of the transaction must be looked at. Now if we look at the real nature of the transaction here, these so-called annuities are simply annual payments of equal amount, being instalments of a debt, and are made up partly of principal, partly of interest, calculated at a particular rate. On the face of the contract, therefore, it appears that each annual instalment contains principal money and a portion of interest which can be readily ascertained by a competent actuary. It seems to me, therefore, that in that state of things we are right in following the principle which I take to be laid down in *Foley v. Fletcher*—that the word “annuity,” under those circumstances, is not to be read in such a way as to make capital taxable.

(1) 2. T.C. 584.

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Now the difficulty which I certainly felt in the case arises from this : that it is said (and forcibly said) by the Attorney-General : " If that be so, then in the case of every terminable annuity which has been purchased for value the same thing occurs, and you ought, if you logically follow out the principle, to say that each annual payment of that annuity ought to be split up between capital and interest and the only portion which represents interest ought to be taxed." I feel the full force of that remark ; but it seems to me that the cases are not the same. Those are cases of purchase of annuities, where investment has been made in that form of property, and the legislature in so many words has said that that is to be taxed ; and it is recognised in this very case throughout that an annuity of that kind is taxable. And I in no way depart from that. The case to which I have referred seems to me to show that it is a different matter where it appears, on the face of the transaction, that the so-called annuity is not a thing of that kind, but simply represents instalments of an existing debt. It matters not, it appears to me, whether the debt be one which is a purchase arising from a sale, or be it the case of the repayment of a loan, in which case it is admitted by the Attorney-General that it is not the practice to tax anything except so much of the annual instalments as represent interest. For these reasons I am unable to agree with Mr. Justice Phillimore ; and I think the Appeal ought to be allowed.

Mathew, L.J.

Mathew, L.J.—I am of the same opinion. It seems to me the instalments stipulated for under this contract are not payments of an annuity within the meaning of the Act of Parliament. " Annuity," in the ordinary sense of the expression, means the purchase of an income. It generally involves the conversion of capital into income, and, reasonably enough, where the buyer places himself in that position, the Act of Parliament taxes him ; he is taken at his word, he has got an income secured in the way I have mentioned. Now has such a case any analogy whatever to the present ? It appears to me, none. Here was a sum of money, a lump sum, stipulated for in the first instance, which was to represent the capital outlay. If that money had been handed over to those who were entitled to it, it might have been invested, ought to have been invested, and probably would have been invested, and, if invested, the income of it would be taxable and not the principal sum. Now that sum representing the capital outlay is by the terms of the contract a sum that may be paid off by what is called (unfortunately) in the contract an annuity. It really meant by annual instalments. Was it intended that under the contract those to whom the money was to be payable were to be in a worse position and to get less than if the alternative were adopted by the Government ? I cannot think there was any such intention. The option to pay in that way is one which was

exercised independently of the consent of those to whom the money was payable. I think it was intended from the way the sum were arrived at under the contract—whether they were paid by annual instalments or by a lump sum—that those who were entitled to it should not pay Income Tax. I quite agree that the case of *Foley v. Fletcher*, so far as it has been encroached upon and impaired by the subsequent decision to which our attention has been called, is an ample authority for what I cannot help feeling is the perfectly reasonable conclusion to which we are invited to come in this case. I agree the Appeal must be allowed.

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Mathew, L.J.

Cripps.—It will be Appeal allowed with Judgment for £17,733 17s. 2d. (that is the right figure) and with the declaration we ask for and the costs of the Appeal and the action.

Vaughan Williams, L.J.—Yes.

Cripps.—If your Lordship pleases.

Sir R. B. Finlay, K.C., A.G. (Sir E. Carson, K.C., S.G., 15th June, 1903 and Rowlatt with him), for the Secretary of State.—The question is the meaning of the word “annuity” as used in either Schedule C or D. Income Tax would not be chargeable on the instalments of a debt. But in the present case, as soon as the option to pay by annuity was exercised by the Secretary of State, the position was the same as if the contract had been this—that if the Government resumed possession of the Railway, they should pay an annuity for the rest of the term. In the case of payment by instalments the principal money repaid would be the same from year to year. *Winter v. Mouseley*.(1) The meaning of an annuity is that the principal has gone for ever, and that it is satisfied by the periodical payments. Terminable annuities have always been taxed. *Coltness Iron Company v. Black*.(2) In any purchased annuity you can distinguish principal and interest. (*Lord Macnaghten*.—Can you say that the Company has purchased the annuity? Did not rather the Government purchase the Railway?) *Foley v. Fletcher*.(3) When once you get an annuity it cannot be analysed into its component parts.

Sir E. Carson, K.C., S.G.—The fact that the consideration for the annuity is the transfer of the Railway cannot make any real difference. If you once distinguish the component parts of an annuity, all annuities will escape taxation. Suppose a person, wanting to get a terminable annuity, buys part of this annuity from the Trustees, how is this to be distinguished from other terminable annuities? (*The Lord Chancellor*.—Might it not be that as between him and the

(1) 2 B. & Ald. 802.

(2) 1. T.C. 321.

(3) 858 1. H. & N. 769.

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Government it might be an annuity, and yet in respect of itself as between other parties, it might not be an annuity? There is no antecedent debt in the supposed case.)

Counsel for the Respondents appeared, but were not called on.

JUDGMENT.

The Lord
Chancellor.

The Lord Chancellor.—My Lords, I am not satisfied, after hearing the very ingenious arguments of the Attorney-General and Solicitor-General, that the Court of Appeal is not right in this case, and inasmuch as it is the duty of those who assert, and not of those who deny to establish the proposition sought to be established, I think the Crown must fail in the contention that this is “an annuity” within the meaning of the Act.

I do not at all say that the question is not surrounded by some difficulties. I think it is. The loose use of the word “annuity” undoubtedly renders a great many of the observations that have been made by the Attorney-General and Solicitor-General very relevant to the question under debate. Still, looking at the whole nature and substance of the transaction (and it is agreed on all sides that we must look at the nature of the transaction and not be bound by the mere use of the words) I cannot doubt that in this contract (it cannot be denied that what was done and agreed to was in that sense under a contract; but, undoubtedly, this is not the case of a purchase of an annuity, it is a case in which under powers reserved by a contract one of the parties agrees to buy from the other party what is their property) I cannot doubt, I say, that what is called an “annuity” in the contract between the parties and in the Statute was a mode of making the payment for that which, by the hypothesis on which I am speaking, had become a debt to be paid by the Government. If it was to be a debt paid by the Government, it introduces this consideration: was it the intention of the Income Tax Act ever to tax capital as if it was income? I think it cannot be doubted, both upon the language of the Act itself and the whole purport and meaning of the Income Tax Acts, that it never was intended to tax capital, as income at all events.

Under the circumstances, I think I am at liberty so far to analyse the nature of the transaction as to see whether this annual sum which is being paid is partly capital, or is to be treated simply as income, and I cannot disagree with what all the three learned Judges of the Court of Appeal pointed out, that you start upon the inquiry into this matter with the fact of an antecedent debt which has got to be paid; and if these sums, which it cannot be denied are partly in

liquidation of that debt, which is due are to be taxed as if it was income in each year in which it is being exacted, the result is that you are taxing part of the capital. As I have said, I do not think it was the intention of the Legislature to tax capital, and, therefore, the claim as against those sums fails.

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The Lord
Chancellor.

My Lords, as I have already said, I do not think it is a matter on which one can dogmatize very clearly. There is no doubt that what has been pointed out is true, that in one sense the Legislature has, in the sense in which I have used the words myself, taxed capital. Where you are dealing with Income Tax upon a rent derived from coal, you are in truth taxing that which is capital in this sense, that it is a purchase of the coal and not a mere rent. All I have to say upon that and other illustrations of the same character is this, that the Income Tax is not and cannot be, I suppose from the nature of things, cast upon absolutely logical lines, and that which justifies the exaction of the tax under these circumstances is that the things taxed have either been or have been by construction by Courts held to be what has been specifically made the subject of taxation; and my answer to an argument derived from those circumstances here is, that looking at the words here used and the word "annuity" used in the Act, I do not think that this comes within the meaning which (using the Income Tax Acts themselves as the expositors of the meaning of the word) is intended to hit at by the word "annuity" which is the only word that can be relied upon here as justifying what would otherwise be to my mind a taxation of capital.

For these reasons I come to the conclusion that, looking at it as a whole, the Court of Appeal were right in the conclusion at which they have arrived; and I, therefore, move your Lordships that this Appeal be dismissed with costs.

Lord Macnaghten.—My Lords, I am of the same opinion, and for the same reasons. I think the case is very well put in the Judgment of Lord Justice Vaughan Williams, and for the reasons given by the Court of Appeal and by my noble and learned friend on the Woolsack, I agree with the motion which has been proposed.

Lord
Macnaghten.

Lord Shand.—My Lords, I am also of the same opinion. I think the element which in a great measure enables one to determine this case is the fact that this proceeding between the parties originates with an antecedent fixed debt due by the Government, which the Government had to pay to the Railway Company. It is not disputed that the payments to be made, and which are actually being made, under the contract embrace capital and interest amounting, as they do, to the precise amount of capital and interest at the rate of £2 17s. p.r cent. stipulated for in the contract between the

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parties, though it is called an annuity, and I agree with the observation of the Solicitor-General that the use of that term is very important, still it is by no means conclusive. What is called an "annuity" in this case, in my opinion, embraces not only profits but capital; there was capital being repaid, and income paid; the income forms the proper subject of annuity; the capital does not.

In my opinion the Judgment of the Court of Appeal was right on these grounds.

Lord Davey.

Lord Davey.—My Lords, I also agree with the Judgment of the Court of Appeal. I think that this Appeal should be dismissed, and I agree with the reasons which were given for their Judgment by the learned Lord Justices who gave Judgment in the Court below.

My Lord, the one important fact which seems to me to determined this case is that for the purpose of ascertaining the amount of this annuity or so-called annuity, the principal sum, the gross sum as it is called, payable by the Secretary of State had to be ascertained. That is the foundation of the whole thing. Then the amount of the annual payment is to be ascertained, by the application to that gross sum of interest which is also ascertained under Clause 26 of the contract. That at once distinguishes it from the case which was put in argument, and which was put in one of the Judgments referred to in *Foley v. Fletcher*, the case of the purchase of an annuity. This is not that case; but this starts with a sum being due from the Secretary of State to the Company, a sum of ascertained amount, and it provides for the mode in which that sum is to be liquidated. I am, therefore, of opinion that although the annual payment is called an "annuity" it is not an "annuity" within the meaning of either Schedule C or Schedule D of the Income Tax Act, whichever may be the proper schedule applicable to it.

My Lords, I only desire to add that although I have come to this opinion, and I think this is the proper construction of that Act, I entirely agree with my noble and learned friend on the Woolsack that the case is one of difficulty owing to the language which is used in the Income Tax Act.

Lord Lindley.

Lord Lindley.—My Lords, I am of the same opinion. The difficulty which exists is attributable entirely to the ambiguity of the word "annuity." The annuity in this case is, to my mind, proved to demonstration to be nothing more than the payment by equal instalments of the purchase money for the Railway with interest at the rate of £2 17s. per cent. The annual instalments are not all profits or gains, but are in fact partly payments of principal moneys and partly only profits in the shape of interest. I cannot, with any satisfaction to myself, accept the view that this is in substance the

purchase of an annuity ; it is nothing of the sort. For those reasons, I agree.

Questions put :—

That the Judgment appealed from be reversed.

The Not Contents have it.

That the Appeal be dismissed with costs.

The Contents have it.

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