HIGH COURT OF JUSTICE (CHANCERY DIVISION)—16TH AND 17TH DECEMBER 1968 AND 12TH FEBRUARY 1969

COURT OF APPEAL—11TH, 12TH, 13TH AND 28TH NOVEMBER 1969

HOUSE OF LORDS—15TH, 16TH, 17TH AND 18TH MARCH AND 5TH MAY 1971

Jones (H.M. Inspector of Taxes) *v.* Shell Petroleum Co. Ltd.[1]

Cropper (H.M. Inspector of Taxes) *v.* British Petroleum Co. Ltd.

Income tax—Management expenses relief—Interrelation with double taxation relief—" the amount of the tax on any sums disbursed as expenses of management "—Income Tax Act 1952 (15 *&* 16 *Geo.* 6 *&* 1 *Eliz.* 2, *c.* 10), *ss.* 350(1) *and* 425(1) *and Sch.* 16, *para.* 2.

The Respondent Companies were investment holding companies to which s. 425, *Income Tax Act* 1952, *applied. Their income consisted of* (a) *United Kingdom dividends, etc., as to which there was no question of double taxation relief;* (b) *dividends within s.* 350, *Income Tax Act* 1952, *from United Kingdom companies entitled to double taxation relief;* (c) *foreign income directly assessable subject to double taxation relief. The sums disbursed as expenses of management by one Company in the year* 1960–61 *and by the other in the year* 1958–59 *respectively exceeded the Company's income of class* (a) *but were less than its aggregate income of classes* (a), (b) *and* (c) *less charges.*

On appeal against decisions of the Inspectors of Taxes on claims to relief in respect of management expenses for the years 1960–61 *and* 1958–59 *respectively, the Companies contended that they were entitled to repayment of tax at the standard rate on the full amount of the expenses of management, subject to the relief not being in excess of the total tax paid by the Company and to account being taken, in computing the maximum amount repayable, of the provisions of s.* 350 *and of the tax credit relief allowed. For the Crown it was contended that the relief should be computed by allocating the amount of the management expenses pound for pound against the income of the Company concerned on the basis most favourable to the Company in accordance with the principle of* Sterling Trust Ltd. *v.* Commissioners of Inland Revenue (1925) 12 T.C. 868 *and repaying the tax on that income, so that where the corresponding income was a dividend within s.* 350 *the relief was restricted by s.* 350(1)(*a*) *to tax on the sum in question at the net United Kingdom rate; as regards the effect of tax credit relief due to the Company in respect of foreign income the Crown's contention before the Commissioners was replaced in the High Court by that mentioned below. The Special Commissioners upheld the Companies' contention.*

In the High Court and above the Crown contended that tax credit relief due to the Companies should be allowed before management relief was computed, and that where the corresponding income qualified for tax credit relief the rate at which management expenses relief was allowable was the standard rate as reduced by the tax credit. The Companies contended that, if their primary contention

[1] Reported (Ch.D.) [1969] 1 W.L.R. 536; 113 S.J. 167; [1969] 2 All E.R. 1158; (C.A.) [1970] 1 W.L.R. 229; 114 S.J. 91; [1970] 1 All E.R. 426; (H.L.) [1971] 1 W.L.R. 786; 115 S.J. 408; [1971] 2 All E.R. 569.

A *were rejected, s.* 350(1)(*a*) *should be construed as limiting the tax repayable only to the aggregate net United Kingdom tax attributable to the dividends received from the paying companies. In the Court of Appeal and the House of Lords the Companies contended that in the phrase in s.* 425, " *so much of the tax paid by it as is equal to the amount of the tax on any sums disbursed*", *etc.*, " *the tax on*" *meant tax at the standard rate, whereas* " *the tax paid*" *meant tax at the net* B *United Kingdom rate or after allowance of credit; alternatively, that credit in respect of class* (c) *income could be reallocated among the dividends in the manner most favourable to the taxpayer.*

Held, (1) *that the tax repayable was a proportion of the tax paid, to be ascertained by comparing the management expenses with the total investment income;* (2) *that, where the income came from sources which had borne tax at* C *different rates, there might be more than one way of calculating the repayment, and that adopted by the Crown was acceptable as a convenient agreed method;* (3) *that, in the case of tax deducted from dividends from United Kingdom companies entitled to double taxation relief, repayment was limited by reference to the paying company's net United Kingdom rate of tax.*

D

CASES

(1) *Jones (H.M. Inspector of Taxes)* v. *Shell Petroleum Co. Ltd.*

CASE

Stated under the Income Tax Management Act 1964, s. 12(5), and the Income Tax Act 1952, s. 64, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the High Court of Justice.

E 1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 2nd and 3rd February 1967 The Shell Petroleum Co. Ltd. (hereinafter called " the Company ") appealed under s. 9(5) of the Income Tax Management Act 1964 against decisions of the Inspector of Taxes on claims made by the Company for the year 1960–61 under (1) s. 425 of the Income Tax Act 1952 (which relates to claims to relief in respect of expenses of F management) and (2) para. 13 of Sch. 16 to the Income Tax Act 1952 (which relates to claims for an allowance by way of credit for foreign tax). These claims are hereinafter referred to respectively as the management expenses claim and the tax credit claim.

2. The question for our determination arose primarily in connection with the management expenses claim. The two claims are, however, in some G respects interrelated (see paras. 5 and 6 below).

3. At the hearing there was laid before us an agreed statement of facts, in which it was admitted between the parties that:

(1) Throughout the year of assessment 1960–61 the Company was a company whose business consisted mainly in the making of investments and the principal part of whose income was derived therefrom. It was accordingly H a company to which s. 425, Income Tax Act 1952, applied.

(2) The Company was charged to tax for the said year, by deduction or otherwise, upon the income described in the schedules attached hereto. The Company was not charged to tax in respect of its profits for the said year under the provisions applicable to Case I of Schedule D and could not lawfully have been so charged in respect of the income in question.

(3) During the said year the Company disbursed sums as expenses of management and as charges in the amounts described in the said schedules. The word " charges " refers to interest, annuities and other annual payments from which the Company was entitled to deduct tax under s. 169, Income Tax Act 1952, or would have been so entitled but for notices given to it by or on behalf of the Commissioners of Inland Revenue pursuant to regn. 3 of the Double Taxation Relief (Taxes on Income) (General) Regulations 1946 (S.R. & O. 1946 No. 466).

(4) The schedules attached hereto are as follows:

I. The Company's claim for relief under s. 425, Income Tax Act 1952, as submitted to the Inspector on 17th February 1965.

II. Schedule illustrating basis of the Company's claim.

III. The Inspector's analysis of the Company's claim for relief.

IV. The Inspector's calculation of the relief due to the Company.

V. The Inspector's reconciliation between schedules II and III.

Copies of the schedules attached to the said statement, numbered I to V, are annexed hereto and form part of this Case[1].

4. In 1960–61 the Company was in receipt of (1) income as to which there is no question of any double taxation relief (hereinafter referred to as " ordinary standard rate income "), (2) United Kingdom dividends with net United Kingdom rates less than the standard rate (hereinafter referred to as " net United Kingdom rate dividends ") and (3) overseas income attracting tax credit relief (hereinafter referred to as " income taxed overseas "), and disbursed as expenses of management (including subvention payments treated as expenses of management) sums which exceeded its ordinary standard rate income but were less than its total income under heads (1), (2) and (3) above.

5. The management expenses claim made by the Company for that year is set out in sch. I, and analysed by the Inspector in sch. III, of the schedules annexed hereto, and may be summarised shortly as follows:

	£		£	£	
Expenses of management	39,696,940	Income tax thereon at the standard rate (7*s.* 9*d.*)		15,382,564 maximum repayable tax	F
				£	
Ordinary standard rate income	24,678,862	Tax thereon at 7*s.* 9*d.*		9,563,059	G
Net U.K. rate dividends	11,129,673	Tax thereon at net U.K. rates		2,925,689	
			£		
Income taxed overseas	71,936,837	Tax thereon at 7*s.* 9*d.* ..	27,875,524		
		Less tax credit relief claimed	22,818,145	5,057,379	H
	107,745,372			17,546,127	
Deduct charges ..	7,181,437	*Deduct* tax applicable to charges		2,782,807	I
	£ 100,563,935			£ 14,763,320	

(1) Not included in the present print.

A The tax claimed by the Company to be repayable in such circumstances is the figure at A, subject to a ceiling of the figure at B, that is, the sum of £14,763,320, which was the maximum tax available for repayment.

On this basis the tax remaining unrelieved, after taking account of both tax credit relief (amounting to £22,818,145) and management expenses relief (£14,763,320), is nil.

B 6. The calculation set out in sch. IV of the schedules attached hereto (the Inspector's calculation of the relief due to the Company) is made on the footing that the management expenses relief should be computed by allocating sums disbursed as expenses of management pound for pound against income of the Company (in whatever way may on that basis be most favourable to the Company). The relief allowable on the management expenses and tax credit C claims is then computed on the basis that (1) where the corresponding income is a net United Kingdom rate dividend the management expenses relief is by virtue of the provisions of s. 350(1)(*a*) of the Income Tax Act 1952 required to be restricted to tax on the sum in question at the net United Kingdom rate applicable to the dividend, and (2) where the corresponding income is income taxed overseas the management expenses relief may be allowed on whatever D basis is most favourable to the Company, but so that (*a*) no tax credit relief can be allowed where United Kingdom income tax chargeable in respect of the income has been relieved by management expenses relief and (*b*) where no credit relief is allowed the assessable United Kingdom income is the net overseas income after deduction of overseas tax.

The calculation thus made may be summarised shortly as follows:

	£		£	*Maximum repayable tax* £	*Management expenses allocation* £		£
Ordinary standard rate income	24,678,862	Tax thereon at 7*s.* 9*d.*		9,563,059	24,678,862 at 7*s.* 9*d.*	=	9,563,059
Net U.K. rate dividends (Rate nil to 5*s.* 4*d.*)	5,415,387	Tax thereon at net U.K. rates ..		908,683			
(Rate 6*s.* 2*d.* to 7*s.* 5*d.*) ..	5,714,286			2,017,006	5,714,286 at rates from 6*s.* 2*d.* to 7*s.* 5*d.*	=	2,017,006
Income taxed overseas Income net of overseas tax ..	9,303,792	Tax thereon at 7*s.* 9*d.*		3,605,219	9,303,792 at 7*s.* 9*d.*	=	3,605,219
			£				
Income inclusive of overseas tax	60,823,203	Tax thereon at 7*s.* 9*d* ..	23,568,991				
		Less tax credit relief ..	21,259,122	2,309,869	£39,696,940		£15,185,284
	105,935,530			18,403,836			
Deduct charges	7,181,437	*Deduct* tax applicable to charges		2,782,807			
	£98,754,093			£15,621,029			

A The tax thus calculated to be repayable on the management expenses claim is £15,185,284, which is more than the £14,763,320 claimed by the Company as the maximum available for repayment (see para. 5 above). On this basis, however, the tax credit relief becomes £21,259,122, as against £22,818,145 claimed by the Company, and the tax remaining unrelieved, after taking account of both tax credit relief and management expenses relief, thus becomes B £15,621,029 less £15,185,284, that is £435,745, instead of nil on the basis of the Company's claim.

The question at issue between the parties was whether the management expenses relief, and therefore the tax credit relief, claimed by the Company should be computed on the basis set out in para. 5 above or on the basis set out in this paragraph, subject in either case to any minor adjustments of figures C that might be found to be necessary after this matter had been determined in principle.

7. The following cases were referred to: *Sterling Trust Ltd.* v. *Commissioners of Inland Revenue* (1925) 12 T.C. 868; *Allchin* v. *Corporation of South Shields* 25 T.C. 445; [1943] A.C. 607.

8. It was contended on behalf of the Company:

D (1) that it was charged to tax on the whole of its income by deduction or otherwise at the standard rate, viz. (*a*) to tax on United Kingdom dividends by deduction at that rate, in accordance with the provisions of ss. 184 and 185 of the Income Tax Act 1952, and, where the dividends were net United Kingdom rate dividends, the opening words of s. 350(1) of that Act, and (*b*) to tax on income taxed overseas directly at that rate, subject thereafter to any available E relief by way of tax credit;

(2) that in these circumstances the management expenses relief to which it was entitled should be computed on the basis that the tax referred to in the words " the amount of the tax on any sums disbursed as expenses of management " in s. 425(1) of the Income Tax Act 1952 was tax at the standard rate;

(3) that such relief was accordingly allowable at the standard rate on sums F disbursed as expenses of management, subject to the relief not being in excess of the tax paid by the Company, and to account being taken in computing the maximum repayable tax of (*a*) the provisions of s. 350(1)(*a*) of the Income Tax Act 1952 as to the repayment of tax deducted or authorised to be deducted from net United Kingdom rate dividends and (*b*) tax credit relief allowed;

(4) that the management expenses and tax credit claims which were made G by the Company, as set out in sch. I annexed hereto and summarised in para. 5 above, should therefore be allowed in principle and the appeal be determined accordingly.

9. It was contended on behalf of the Inspector of Taxes:

(1) that the tax referred to in the words " the amount of the tax " in s. 425(1) of the Income Tax Act 1952 is the tax on income deemed to have been H disbursed pound for pound on management expenses and not necessarily tax at the standard rate;

(2) that in the circumstances of the present case, as described in para. 4 above, the management expenses relief due should be ascertained by making an allocation of the sums disbursed as expenses of management pound for pound against income of the Company on whatever basis is most favourable I to the Company and then computing the relief due in respect of tax on the income taken to be so disbursed;

(3) that where such income is from net United Kingdom rate dividends the relief so due is by virtue of the provisions of s. 350(1)(*a*) of the Income Tax Act 1952 required to be restricted to tax on that income at the net United Kingdom rate applicable to the dividends;

(4) that where the United Kingdom tax on any income is repayable by way of relief under s. 425 no further relief by way of credit against United Kingdom tax is allowable in respect of any overseas tax paid on that income;

(5) that allocation of sums disbursed pound for pound against income of the Company accords with the scheme of the provisions contained in s. 425 of the Income Tax Act 1952, as amended by s. 19 of the Finance Act 1954, as to the carrying forward of management expenses where sums disbursed are in excess of the amount on which the Company has been charged to tax for the year in question;

(6) that the management expenses and tax credit claims made by the Company should therefore be dealt with in principle on the basis set out in sch. IV annexed hereto and summarised in para. 6 above, and the appeal be determined accordingly.

10. We, the Commissioners who heard the appeal, were of opinion that the crux of the matter was the proper interpretation of the words " the amount of the tax " in s. 425(1) of the Income Tax Act 1952. It was common ground that those words could not mean literally tax levied on disbursements as such.

As regards this question of interpretation, that section refers earlier to the claimant being " charged to tax by deduction or otherwise ", and it appeared to us that on the facts of the present case the tax there referred to should be taken to mean tax charged at the standard rate. As to the provisions of subs. (1A) of that section—the carry-forward provisions first introduced in 1954, which were referred to in argument during the hearing—it did not appear to us that these provisions were of any assistance in relation to the problem before us. We noted, however, that it would seem that on the basis contended for on behalf of the Crown the words " the amount of the tax " must in relation to income taxed overseas mean one thing if at the time when a management expenses claim was made no tax credit had been claimed and another when tax credit had been allowed.

Weighing the rival interpretations and the position generally, including the fact that there were provisions corresponding to s. 425 in s. 33 of the Income Tax Act 1918, that is, long before 1945, when provisions corresponding to s. 350 of the Income Tax Act 1952 and the tax credit provisions were first enacted, we were of opinion that the Company's contentions as to the proper interpretation of the words " the amount of the tax " in s. 425 were well founded.

We therefore held that relief should be allowed on the basis envisaged in sch. I annexed hereto and summarised in para. 5 above, and that the appeal succeeded in principle. We left figures to be agreed accordingly.

11. Figures were subsequently agreed between the parties on the basis of this decision, and on 31st July 1967 we determined accordingly that the appeal be allowed and that relief be given as follows:

Management expenses relief	£14,546,542 (tax)
Double taxation relief	£23,034,923 (tax).

12. The Inspector of Taxes immediately after the determination of the appeal declared to us his dissatisfaction therewith as being erroneous in point of law, and in due course required us to state a Case for the opinion of the

A High Court pursuant to the Income Tax Management Act 1964, s. 12(5), and the Income Tax Act 1952, s. 64, which Case we have stated and do sign accordingly.

13. The question of law for the opinion of the Court is whether our decision set out in para. 10 above is correct.

G. R. East } Commissioners for the Special Purposes of
B R. A. Furtado } the Income Tax Acts.

Turnstile House,
94–99 High Holborn,
London W.C.1
21st June 1968.

C (2) *Cropper* (*H.M. Inspector of Taxes*) v. *British Petroleum Co. Ltd.*

This case related to the appeal of the British Petroleum Co. Ltd. against the decision of the Inspector of Taxes on a claim to management expenses relief for the year 1958–59. The facts were similar to those in the foregoing case, and the contentions of the parties and the Commissioners' decision were the same as in that case.

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The cases came before Cross J. in the Chancery Division on 16th and 17th December 1968, when judgment was reserved. On 12th February 1969 judgment was given in favour of the Crown, with costs.

W. A. Bagnall Q.C. and *Patrick Medd* for the Crown.

H. H. Monroe Q.C. and *Michael Nolan Q.C.* for Shell Petroleum Co. Ltd.

E *H. H. Monroe Q.C.*, *Michael Nolan Q.C.* and *S. J. L. Oliver* for British Petroleum Co. Ltd.

The following cases were cited in argument in addition to the case referred to in the judgment: *Simpson* v. *Grange Trust Ltd.* 19 T.C. 231; [1935] A.C. 422; *Allchin* v. *Corporation of South Shields* 25 T.C. 445; [1943] A.C. 607.

F **Cross J.**—These two cases raise the question of the measure of relief from tax in respect of management expenses to which the Respondents, Shell Petroleum Co. Ltd. and British Petroleum Co. Ltd., were respectively entitled for the year 1960–61 under s. 425 of the Income Tax Act 1952 having regard to their respective claims for allowances by way of credit for foreign tax. Both Companies are investment companies, and both derived nearly all their income
G in the year in question from one or other of three sources: source A—dividends from which the paying companies had deducted United Kingdom tax at the standard rate and had themselves no claim to double taxation relief; source B—dividends paid by companies themselves entitled to double taxation relief from which United Kingdom tax had been deducted at the standard rate but in respect of which any claim to relief or repayment on account of such deduction was
H limited by s. 350(1) of the Act to the net United Kingdom rate of tax borne by the paying company; source C—foreign income in respect of which the Respondent Companies were liable to United Kingdom tax by direct assessment but were themselves entitled to double taxation relief in respect of foreign tax. The greater part of the income of Shell is derived from source C and the greater part of the income of B.P. from source B, but this difference has no bearing on
I anything which I have to decide.

(Cross J.)

Section 425(1) of the Income Tax Act 1952 is in the following terms:

> " Subject to the provisions of this section, and to the other provisions of this Part of this Act, where—(*a*) an assurance company carrying on life assurance business (whether proprietary or mutual); or (*b*) any company whose business consists mainly in the making of investments and the principal part of whose income is derived therefrom, claims and proves to the satisfaction of the Special Commissioners that, for any year of assessment, it has been charged to tax by deduction or otherwise, and has not been charged in respect of its profits in accordance with the provisions of this Act applicable to Case I of Schedule D, it shall be entitled to repayment of so much of the tax paid by it as is equal to the amount of the tax on any sums disbursed as expenses of management (including commissions) for that year."

A further subsection, (1A), was added in 1954, which runs as follows:

> " If, in the case of the year 1954–55 or any subsequent year of assessment, effect cannot be given, or cannot be fully given, to the foregoing subsection because the company has not been charged to tax for that year by deduction or otherwise, or because the sums disbursed for that year exceed the amount on which the company has been charged to tax for the year, an amount equal to the sums so disbursed, less any amount on which the company has been so charged, may be carried forward and treated for the purposes of this section as if it had been disbursed for any subsequent year of assessment".

There follows a proviso setting out in detail how the " carry-forward " is to be worked out, which I need not read. At this stage I will also read s. 350(1):

> " The amount of tax which is authorised by section one hundred and eighty-four of this Act to be deducted from any dividend shall be determined without taking into account any reduction, by reason of double taxation relief, of the United Kingdom income tax payable directly or by deduction by the company, but—(*a*) notwithstanding anything in this Act, no relief or repayment in respect of tax deducted or authorised to be deducted from any dividend shall be allowed at a rate exceeding the rate (hereinafter referred to as ' the net United Kingdom rate ') of the United Kingdom income tax payable directly or by deduction by the company after taking double taxation relief into account".

There is no doubt that the Respondents are companies to which s. 425 applies, or that they have not been charged to tax under Case I of Schedule D but have been charged to tax by deduction or by assessment under another head. Further, it was admitted before me that, in applying the section, one must first work out the tax liability of the Respondents, taking into account any double taxation relief to which they were entitled, before one proceeds to consider how much of the tax paid they are entitled to recover under the section. Finally, it was agreed that the words " tax on any sums disbursed as expenses of management " cannot be construed literally, since the management expenses might in fact have been paid out of money which had not borne tax, e.g., capital or a bank overdraft, but that the words must be taken to mean tax on such part of the taxed income of the company as is in fact equivalent to the management expenses.

The dispute between the parties centred on the words " the amount of the tax ". The contention of the Respondents was that this meant tax at the standard rate subject to the limitation introduced by s. 350(1) of the Act. The

A Crown, on the other hand, contended that one must discover what was the rate of tax effectively borne by each part of the income in question, and only allow repayment of tax on the part of the income equivalent to the management expenses at the rate appropriate to the part of the income to which one attributed the management expenses, though the Respondents were entitled in accordance with the principle laid down in *Sterling Trust Ltd.* v. *Commissioners of Inland* B *Revenue* (1925) 12 T.C. 868 to attribute the management expenses so far as possible to that part of the income which had borne tax at the highest rate.

In the year in question, the Shell figures, which are the only ones to which I will refer, were as follows. Source A: The ordinary standard rate income was £24,678,862 gross, on which tax was charged by deduction to the amount of £9,563,059. Source B: Dividends from companies entitled to double taxation C relief were £11,129,673 gross; tax was deducted from this at the standard rate, but under s. 350(1) the amount recoverable, i.e., at the net United Kingdom rates paid by the various companies in question, amounted only to £2,925,689. Source C: Income taxed abroad amounted to £71,936,837 gross; tax on that at the standard rate would have been £27,875,524, but against that there was a credit for foreign tax paid of £22,818,145, leaving a sum of £5,057,379 tax D payable by direct assessment. The total gross income was therefore £107,745,372, against which there were charges of £7,181,437 to be deducted, leaving £100,563,935. On the other hand, the maximum tax which could possibly be repaid was £17,546,127 (i.e., £9,563,059 plus £2,925,689 plus £5,057,379) less tax applicable to the charges of £2,782,807, leaving a figure of £14,763,320. The management expenses for the year were £39,696,940, income E tax on which at the standard rate would be £15,382,564, a sum greater than the maximum repayable tax.

On these figures the result, according to the Respondents, was that a sum of £14,763,320 was repayable but that the difference between that figure and £15,382,564 was irrecoverable, the " carry-forward " provisions in s. 425(1A) not applying since the management expenses did not exceed the amount on F which the Company had been charged to tax. On the Crown's approach, one allocates to the management expenses in the first instance income of the company which in fact bore tax at the standard rate, so far as it will go, and makes up the balance, first, with income which has borne tax at the next highest rate, and so on. Thus, one first attributes all the source A income—£24,678,862—to the management expenses of £39,696,940, leaving some £15,000,000 to be made up G from sources B and C. One splits up the source B income between the various companies which have paid the dividends so as to find out the net United Kingdom rate of tax borne in each case, which is the ceiling for any repayment of tax, and, similarly, if any part of the foreign income did not attract any relief but bore tax at the full rate, one would separate that from the rest where the rate of tax was reduced by the credit so as to allocate the £15,000,000 balance of H management expenses between source B and source C income in the manner most favourable to the Respondents. I will not refer to the calculations placed by the Revenue before the Special Commissioners in detail, since the Crown concede that they do not give proper effect to their own contentions as argued before me. But it is common ground that the result of applying the principle for which the Crown contends will be that, instead of the maximum repayable I tax being exhausted by the tax on the management expenses and there being a balance of tax on management expenses which will be irrecoverable, the maximum repayable tax will be somewhat greater than the total tax attributable to the management expenses.

In argument, each side agreed to illustrate its contentions by reference to hypothetical round figures for income and tax, and to disregard the complication

(Cross J.)

introduced by the source B (s. 350) income. It may perhaps be useful to give these figures at this point. Assume (*a*) a gross income of £30,000 from United Kingdom dividends and a standard rate of tax of 8*s*.; assume (*b*) a gross foreign income of £120,000, which bears foreign tax of £30,000—i.e., at a rate of 5*s*. in the pound—so that the net receipt in this country is £90,000; assume (*c*) management expenses of £60,000. On these figures the United Kingdom tax payable, apart from any relief for management expenses, would be £30,000, made up of (1) £12,000 borne by deduction from the £30,000 gross United Kingdom dividends, and (2) £18,000 paid by direct assessment on the income received from abroad. This figure is arrived at by grossing up the foreign income to its original £120,000, charging that figure notionally to tax at 8*s*., which gives £48,000, and deducting from the £48,000 the £30,000 foreign tax paid.

Coming now to the claim for management expenses, the Company's contention was that the taxpayer would be entitled on those figures to repayment of tax at 8*s*. on the £60,000 expenses (i.e., £24,000), leaving himself to bear at the end of the day tax amounting to £6,000. On the other hand the Crown's contention on these figures was that the taxpayer was entitled to be repaid (*a*) tax on £30,000 of the £60,000 management expenses at 8*s*. in the pound, that being the rate at which the United Kingdom dividends bore tax, and (*b*) tax on the balance of £30,000 management expenses at the rate at which the foreign receipts actually bore United Kingdom tax. There was some discussion before me as to whether this rate was 4*s*., which would result from relating the £18,000 tax paid to the figure of £90,000, or 3*s*., which would result from relating the £18,000 to £120,000. The provisions of Sch. 16 to the Income Tax Act 1952 are very complicated, and the point was not fully argued, so I do not propose to express any view on it. If you take a 4*s*. rate the amount repayable on the Crown's view would be £12,000 plus £6,000, making £18,000, which would leave £12,000 tax to be paid. If, on the other hand, you take a 3*s*. rate the amount repayable would be £12,000 plus £4,500, making £16,500, leaving £13,500 tax to be paid. Either figure is, of course, larger than the £6,000 payable on the Company's view.

The Commissioners decided the case in favour of the Respondents, giving the following identical reasons in each case:

> " We, the Commissioners who heard the appeal, were of opinion that the crux of the matter was the proper interpretation of the words ' the amount of the tax ' in s. 425(1) of the Income Tax Act 1952. It was common ground that those words could not mean literally tax levied on disbursements as such. As regards this question of interpretation, that section refers earlier to the claimant being ' charged to tax by deduction or otherwise ', and it appeared to us that on the facts of the present case the tax there referred to should be taken to mean tax charged at the standard rate. As to the provisions of subs. (1A) of that section—the carry-forward provisions, first introduced in 1954, which were referred to in argument during the hearing—it did not appear to us that these provisions were of any assistance in relation to the problem before us. We noted, however, that it would seem that on the basis contended for on behalf of the Crown the words ' the amount of the tax' must in relation to income taxed overseas mean one thing if at the time when a management expenses claim was made no tax credit had been claimed and another when tax credit had been allowed. Weighing the rival interpretations and the position generally, including the fact that there were provisions corresponding to s. 425 in s. 33 of the Income Tax Act 1918, that is, long before 1945, when provisions corresponding to s. 350 of the Income Tax Act 1952 and the tax credit provisions were first enacted, we were of

A opinion that the Company's contentions as to the proper interpretation of the words ' the amount of the tax ' in s. 425 were well founded. We therefore held that relief should be allowed on the basis envisaged in Sch. I annexed hereto and summarised in para. 5 above, and that the appeal succeeded in principle. We left figures to be agreed accordingly."

The comment that the Crown's argument led to one result if the management expenses claim is dealt with before any tax credit is allowed and another if it is dealt with after the allowance of tax credit seems to have resulted from a misunderstanding of the Crown's argument, for which, be it said, the Inspector rather than the Commissioners seems to have been to blame. But, however that may be, it was common ground before me that the section proceeds on the footing that all tax credits will have been allowed, and indeed that the tax exigible apart from the management expenses claim will in theory have been paid, before the management expenses claim is given effect to by a repayment of some of the tax paid.

The argument of the Respondents is simple enough. The relief given to life assurance companies and investment companies was introduced fifty years ago (see Income Tax Act 1918, s. 33), that is to say, long before there was any double taxation relief. Companies were then liable for tax at a rate fixed annually (i.e., that which has been called the " standard rate " since 1927) without liability to increase through surtax or to decrease through allowances. When, therefore, s. 33 of the 1918 Act spoke of the company having been " charged to tax " and gave it a right to have repaid to it a sum equal to the tax on a part of its income corresponding to the management expenses, it meant tax at the fixed or standard rate. The wording of the 1918 Act was reproduced in 1952 without any change, although double taxation relief had by then been introduced, and there is no warrant for now construing the words " the amount of the tax on any sums disbursed as expenses of management " as meaning no longer tax at the standard rate but tax at the rate effectively applicable to the part of the income notionally attributable to the management expenses.

The Crown rested its case mainly on the broad ground that to spread the tax on the management expenses rateably over the whole of the income is more in accord with the wording of the section and with justice and common sense than to repay tax at the standard rate regardless of whether or not the whole income bore tax at that rate. But it also relied on several minor points, which I should mention now. First, it submitted that the relief afforded by the section was not necessarily confined to incorporated bodies, since a life assurance company might in theory be an individual. This strikes me as a far-fetched argument. Next, it referred to s. 181 of the 1952 Act (which had its counterpart in earlier legislation) which gives the lessor of mineral rights a right to claim repayment of tax on management expenses in substantially the same language as that used in s. 425. A lessor of mineral rights might plainly be an individual surtax payer, and there was, so it was argued, no reason to limit the words " income tax " in that section to tax at the standard rate. That no doubt shows that a problem similar to the one which faces me may arise under s. 181. It does not itself solve the problem. Thirdly, reliance was placed on subs. (1A) of s. 425, introduced in 1954, but I cannot see that that subsection in itself helps the Crown, for it would obviously be wrong to allow the " carry-forward " provisions to extend to a case where the sums disbursed were less than the income charged to tax and the shortfall arose because the tax on the expenses at the standard rate exceeded the maximum amount of tax repayable. It can, of course, be said that the fact that the Respondents' construction can lead, and has led in this case, to such a result is an indication that it cannot be right, but that argument is not, I think, much assisted by the presence of subs. (1A).

(Cross J.)

The case, as I see it, really turns on the wording of s. 425(1) itself, and I am prepared to approach the section on the footing that it can only apply to incorporated bodies and to assume that prior to the introduction of double taxation relief the tax repaid would necessarily have been tax at the standard rate. But when the company concerned is entitled to credit for foreign tax its income received from abroad is not in fact taxed at the standard rate but at a lower rate. The grossing up of the sums received from abroad by the addition of the foreign tax paid, and the application to the gross sum of the standard rate of tax in order to obtain a figure against which credit is to be given for the foreign tax, are only steps in the ascertainment of the net United Kingdom rate at which the tax is finally paid. If the United Kingdom tax is in fact charged at different rates on different parts of this Company's income, why should one construe the words " the amount of the tax " in s. 425 as meaning, inevitably and always, tax at the standard rate? The section says that the company is to be repaid so much of the tax paid by it as is equal to the tax paid on a part of its income charged to tax equal to the sums disbursed as expenses, as though all such sums had in fact been paid out of income charged to tax. Apart from the application of the *Sterling Trust*(1) principle, the result, I would have thought, would be that one would find out the proportion which the part of the income on which tax was to be repaid bore to the total income charged with tax, and would repay that proportion of the total tax paid. If, for example, the total income chargeable to tax is £1,000, of which £500 is charged at 10 per cent., i.e., £50, and £500 is charged at 5 per cent., i.e., £25, and the expenses are £500, one would, apart from the application of the *Sterling Trust* principle, repay half the £50 and half the £25. In my judgment, therefore, the decision of the Commissioners was wrong, and I shall remit the case to them for the figures to be worked out. This may, of course, involve argument as to what the effective rate of tax on the foreign income is.

On the footing that I decided, as I have, that the Respondents' contention was wrong, I was asked by the parties to decide a point on the application of s. 350(1)(*a*), which can be illustrated by an example. Suppose that (*a*) the company's income charged to tax is £1,000, derived exclusively from dividends from a s. 350 company with a net United Kingdom rate of 4*s*., (*b*) that the standard rate is 8*s*. and (*c*) that the management expenses are £200. What repayment can be claimed? Although the United Kingdom tax actually paid by the s. 350 company was only £200, it will have deducted tax at 8*s*., i.e., £400, on payment of the dividend as directed by s. 350(1), leaving a net dividend of £600. Apart from s. 350(1)(*a*), the amount of tax which the company could reclaim under s. 425 in respect of the management expenses would be £80, for as the management expenses were one-fifth of the income the tax repayable would be one-fifth of the £400 tax paid. It was suggested on behalf of the Respondents that, though s. 425 was subject to the limitations of s. 350, that would not prevent the company in question from reclaiming £80, since £80 is less than £200, the amount of the tax actually paid by the s. 350 company. On the other hand, the Crown argued that the company in question could only recover £40. In my opinion the Crown is right. Section 350 does not say that no repayment should be allowed which exceeds the net United Kingdom tax paid, but that no repayment shall be allowed at a rate in excess of the net United Kingdom rate. If one applies the net United Kingdom rate of 4*s*. to the management expenses of £200, one gets a figure of £40.

I think that is a victory for you, Mr. Medd.

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(1) 12 T.C. 868.

Medd—My Lord, I think it is. I would ask your Lordship to allow both appeals with costs and order, as indeed your Lordship has already said, that they be remitted to the Commissioners.

Cross J.—It will have to go back. There may be an argument about what is the effect of the United Kingdom rate. You will remember that there was some dispute in which Mr. Bagnall found himself on one side, with your instructing solicitor, and Mr. Monroe was on the other.

Medd—Yes, my Lord. Possibly the simplest thing would be just to remit it to the Special Commissioners.

Cross J.—Yes, I think so. That is right, Mr. Nolan?

Nolan Q.C.—That must be right, my Lord.

The Companies having appealed against the above decision, the cases came before the Court of Appeal (Russell, Salmon and Megaw L.JJ.) on 11th, 12th and 13th November 1969, when judgment was reserved. On 28th November 1969 judgment was given unanimously in favour of the Crown, with costs.

H. H. Monroe Q.C., *Michael Nolan Q.C.* and *S. J. L. Oliver* for both Companies.

W. A. Bagnall Q.C. and *Patrick Medd* for the Crown.

Simpson v. *Grange Trust Ltd.* 19 T.C. 231; [1935] A.C. 422 was cited in argument in addition to the case referred to in the judgment.

Russell L.J.—This is the judgment of the Court.

Before the Finance Act 1915 a United Kingdom company such as Shell, whose business was that of making investments, was at a disadvantage compared with, for example, a trading concern, in that, while on the one hand it bore full income tax on its income, it could claim no relief in respect of expenses necessary to be incurred in order to earn that income: it was taxed on its gross income and not on what could fairly be regarded as its net profits of any year. An amelioration of that situation was introduced in 1915 in respect of what were described as its management expenses, in a form relevantly re-enacted in s. 425(1) of the Income Tax Act 1952, which is in the following terms:

> " Subject to the provisions of this section, and to the other provisions of this Part of this Act, where— . . . (*b*) any company whose business consists mainly in the making of investments and the principal part of whose income is derived therefrom, claims and proves to the satisfaction of the Special Commissioners that, for any year of assessment, it has been charged to tax by deduction or otherwise, and has not been charged in respect of its profits in accordance with the provisions of this Act applicable to Case I of Schedule D, it shall be entitled to repayment of so much of the tax paid by it as is equal to the amount of the tax on any sums disbursed as expenses of management (including commissions) for that year."

For many years, until the introduction of double taxation relief in respect of foreign taxation, the provision gave rise to no problems of the nature debated before us. The tax paid or suffered by the company was at the current or standard rate, and on any construction of the words " the tax on any sums disbursed " that tax was at the same rate.

The income of Shell is of three kinds: A—dividends received from United Kingdom companies the profits of which are not subject to foreign tax;

(Russell L.J.)

B—dividends received from United Kingdom companies the profits of which, owing to trading activities abroad, are subject to foreign tax and which companies have themselves claimed double taxation relief against United Kingdom income tax in connection with that foreign tax; C—dividends received from foreign companies which dividends are themselves subjected to foreign tax which is consequently withheld by the paying foreign company. In category A the tax paid by Shell under deduction is, of course, at the standard rate. In category B the situation is the same. In category C, upon Shell claiming double taxation relief, the United Kingdom tax paid or suffered is less in amount than would result from a calculation at the standard rate. Though the amount of tax paid in respect of category B is calculated at the standard rate s. 350 of the Income Tax Act 1952 (in broad terms) restricts claims to repayment of the tax paid by deduction by a ceiling, being a lower net United Kingdom rate, a rate intended to reflect the fact that in obtaining double taxation relief the distributing company has paid United Kingdom tax at a rate lower than the standard rate.

In connection with category A, whatever construction is put upon " the tax on " in s. 425(1), no problem arises: " tax paid " and " the tax on " must be both at standard rate, and the situation is as in 1915. It is when we get to categories B and C that there is difficulty. In dealing with those categories we will forget category A and assume in each case for convenience that the income of Shell is exclusively category B or exclusively category C. In so doing we remark that the amount of the management expenses is such that it is necessary to consider both those categories, the Crown accepting that upon its construction of s. 425 Shell is entitled to attribute its expenditure first to the gross income that has the highest reclaimable United Kingdom tax content, giving the highest figure or rate for " the tax on " and " tax paid ".

But before coming to these two categories it is necessary to consider the rival contentions as to the construction of " the tax on " in s. 425. Shell contend that it means, and always means, income tax at the standard rate regardless of the rate at which any part of the gross income has suffered tax—regardless of the " tax paid " if it be at a rate lower than the standard rate. (It is in fact only in category C that it might be said that tax paid was other than at the standard rate.) The Crown contends that " the tax on " is related to the tax paid on the gross income to which any particular part of the disbursements is to be attributed, so that the rate at which " the tax on " is to be calculated is the same as that for the " tax paid ". The fact that when this section was introduced in 1915 the two rates were necessarily the same and necessarily the current—later called the standard—rate does not seem to us to assist in the solution of this problem. In construing the phrase it seems to us important to start with the consideration that the introduction of the provision was clearly aimed at making the situation which should obtain in a company whose business was investment at least approach the situation that obtained in a trading concern, namely that expenses should be deducted from gross profit before a taxable net profit should be disclosed. If that were the principle to be expected from this new scheme to remove a relative disadvantage from a company such as Shell, it would involve a reflection of a system by which expenses should be deducted from gross profit in order to ascertain the proper liability to tax. The effect of such deduction would be that which is in fact contended for by the Crown in this case: £100 of expense would be matched with £100 of gross profit, relieving from tax first at the highest level of such tax and next at the next highest level of such tax.

We would approach the construction of s. 425 with this in mind, and we ask ourselves whether the language of s. 425 is such that it arrives at a different

result. It was urged upon us that " the tax " could only be the one tax known, namely income tax at the standard rate. We do not agree. It could mean that. But it could mean the tax last referred to in the section—namely " that tax " or " the tax paid by it ", which was that from which the amount of " the tax on " is to be deducted. The section does not refer to " the amount of tax "; it speaks of the amount of " *the* tax ". Nor does it say " as is equal to tax on the amount of any sums disbursed ". There is strictly of course no tax on sums disbursed. The section must refer to the tax on such gross income as is properly to be considered as having been expended as sums in disbursement of the expenses. (Of course expenses may not have been in fact paid out of income at all, but it is assumed by the section to be so since it speaks of the tax on, meaning, of course, income tax.) Again, this seems to us to relate to expenditure by the company out of income on which it has paid the tax paid by it. For Shell it was argued that if this was intended the phrase used would have been that the company was " entitled to repayment of tax paid on any sums disbursed as expenses " without all this reference to " tax on ". As a forensic point this cannot be faulted: but the fact that a different form of words could achieve more briefly a result contended for is—perhaps regrettably—an argument of little force against the contention. Nor, in our view, is the argument for Shell on s. 425 assisted by consideration of the somewhat elaborate provisions for an effective rate of tax found in para. 5 of Sch. 16 to the Income Tax Act 1952. In our judgment, on the true construction of s. 425 " the tax on " is related to " the tax paid " in respect of the gross income to be considered as having met the relevant part of the expenses, is so related so as to be calculated at the same rate as that tax paid, and is not an unvarying standard rate.

We turn next to category B. The situation here depends upon the language of s. 350 of the Income Tax Act 1952. That section deals with cases in which a United Kingdom company trading abroad has in respect of its own profit successfully claimed double taxation relief against foreign tax and distributes a dividend to Shell. The section first provides for deduction by the distributing company from Shell's dividend at the standard rate: thus, as we have said, in these cases the " tax paid " and " the tax on " are both under s. 425 at the standard rate. Section 350 then provides:

> " notwithstanding anything in this Act, no relief or repayment in respect of tax deducted [that is to say, from such a dividend] shall be allowed at a rate exceeding [the net United Kingdom rate] ".

The reason or a reason for this is of course that the United Kingdom Treasury has only received from the distributing company tax on its profits now being distributed at that net rate. That rate is stated on the dividend warrant or counterfoil and is arrived at in a manner relevant to be described under category C.

We may illustrate the contention of Shell under category B by an example which assumes for simplicity standard rate 10*s.* in £ and net U.K. rate 5*s.* in £.

	Management Expenses		*Dividends*	
	£		£	
	100		100	
" the tax on "		(i) Less at 10*s.*	50	tax paid
at 10*s.*	50	But only	25	at net U.K. rate 5*s.*
			100	
		(ii) Less at 10*s.*	50	tax paid
		But only	25	at net U.K. rate 5*s.*

(Russell L.J.)

Shell said they were content to obey the requirement of s. 350 by claiming at a rate not exceeding 5*s*., but asserted that they could nevertheless claim repayment of the whole amount of " the tax on "—that is to say £50—by claiming at the rate of 5*s*. repayment of tax paid on *both* the dividends. The Crown argued that Shell were claiming repayment at a rate of 10*s*. in the £, because that was the rate at which Shell calculated the amount of " the tax on ".

In our view the objection in law to this contention of Shell is to be found not so much in s. 350 as in s. 425. If we are correct in our view as to the purpose or design of s. 425, then Shell's contention conflicts with that purpose, for it seeks to use an expense of £100 for the purpose of offsetting tax liability in respect of £200 of gross income. If a company assessed on the profits of a trade but owning category B trade investments were to seek to use £100 of its expenses (we assume a loss on pure trading account) to claim repayment of net United Kingdom rate tax on £200 of gross income, it would not succeed. We do not consider that s. 425 in seeking to lessen the disadvantage, relative to a trading company, of a company in Shell's position, is to be construed as favouring Shell in this regard. Consequently, in our judgment, in so far as a claim in respect of management expenses is related to category B dividends, £100 of such expenses does not justify a repayment of more than the net United Kingdom rate on £100 of dividend.

We turn next to category C dividends distributed to Shell as shareholders by foreign companies, foreign tax in respect of those dividends having been under foreign law deducted at source. Again we isolate category C in relation to £100 of management expenses and assume standard United Kingdom rate 10*s*. in £. Suppose two dividends—

(i) £100 less £20 foreign tax = £80.

(ii) £100 less £30 foreign tax = £70.

If Shell did not wish to claim double taxation relief it would be charged to United Kingdom tax at 10*s*. on £80 and £70. But, having claimed such relief, Sch. 16 to the Statute, in arriving at the United Kingdom tax chargeable in respect of those dividends, requires a computation thus—

Foreign dividend no. (i)	£80	
	20	foreign tax added
	£100	
Compute at standard rate of U.K. tax on £100	£50	
Deduct	20	foreign tax
U.K. tax charged	£30	
Foreign dividend no. (ii)	£70	
	30	foreign tax added
	£100	
Compute as above	£50	
Deduct	30	foreign tax
U.K. tax charged	£20	

A In case no. (i) United Kingdom tax is, as a result of the calculation, exigible in fact at the rate of 6*s.* in the £: in no. (ii) in fact at the rate of 4*s.* Now, as we understand the argument for the taxpayer, it is as follows. First, it is said that, even if " the tax on " the £100 is to be related to the tax paid as already indicated, the only United Kingdom *rate* discoverable in the interstices of Sch. 16 is the standard rate, so that " the tax on " £100 must be calculated B as £50. But it seems to us that it matters not whether " the tax on " is at 10*s.* (£50) or at 6*s.* (£30). The position is the same, in our judgment, whichever rate is taken for " the tax on ", because for the reasons given in connection with category B we do not consider that the scope of s. 425 is such as to permit in effect relief to be claimed in respect of £100 of expenses against more than £100 of gross income; it involves no right to repayment greater than the United C Kingdom tax in fact exigible in respect of that last £100. On this basis, taking dividend no. (i) as having a reclaimable content of United Kingdom tax paid the more favourable to Shell, namely £30, that sum in the example given of these two foreign dividends is the maximum repayment of United Kingdom tax that can be claimed in respect of the £100 expenses.

It was finally suggested that the credit for foreign tax on category C D dividends could be marshalled in the manner most favourable to the taxpayer by analogy with *Sterling Trust Ltd.* v. *Commissioners of Inland Revenue* (1925) 12 T.C. 868. Thus in the two dividends stated in the example a stage in the calculation for each is reached when £50 appears as the United Kingdom tax attributable to each. But the credit for foreign tax on the two taken together is £50: by attributing the whole foreign tax credit to one dividend the other E dividend is left to suffer United Kingdom tax at the standard rate of 10*s.*— "the tax paid", the tax on the £100 of expenses is to be calculated at the same rate, and £50 of tax is recoverable. In our judgment, there is no warrant in Sch. 16 for this system of attributing foreign tax charged at one rate by, for example, country A to a dividend from, for example, country B charged at the same or any other rate, so as to achieve the suggested marshalling.

F In summary, therefore, while Shell is entitled in claiming repayment of tax paid to proceed on the assumption that gross income is attributable to disbursements on management expenses in the manner most favourable to Shell having regard to the incidence in the different items of gross income of liability to United Kingdom income tax, in neither category B nor category C may it seek repayment of tax in respect of more than £100 of gross income for any £100 G of expenses. We observe that on this basis the question whether " the tax on " is always the standard rate does not affect the result. But our opinion that it is related to " the tax paid " is a part of our general view as to the design, purpose or scope of s. 425.

We have confined our observations to the *Shell* appeal, but they apply equally to the *British Petroleum* appeal, and we dismiss both appeals.

H **Medd**—My Lord, I would ask that both appeals should be dismissed with costs.

Russell L.J.—I think that must be so.

Oliver—Yes, that must be the right order, my Lord. I am instructed, my Lord, to ask for leave to appeal to the House of Lords in both these cases.

Russell L.J.—Mr. Medd, there are only two of us here. I have taken I occasion to ask Megaw L.J. what his views on this point are. Are you both content that Salmon L.J. and I should decide this question?

Medd—Yes, my Lord. A

Oliver—Yes, my Lord.

Russell L.J.—Have you anything to say, Mr. Medd?

Medd—It is a case in which I do not think there would be any objection if your Lordship saw fit to allow it.

Russell L.J.—You may have leave to appeal to the House of Lords.

Oliver—Thank you, my Lord. B

The Companies having appealed against the above decision, the cases came before the House of Lords (Lord Hodson, Viscount Dilhorne and Lords Wilberforce, Pearson and Diplock) on 15th, 16th, 17th and 18th March 1971, when judgment was reserved. On 5th May 1971 judgment was given unanimously in favour of the Crown, with costs. C

F. Heyworth Talbot Q.C. and *Barry Pinson* for Shell Petroleum Co. Ltd.

H. H. Monroe Q.C., *Michael Nolan Q.C.* and *S. J. L. Oliver* for British Petroleum Co. Ltd.

Peter Rees Q.C. and *Patrick Medd* for the Crown.

The following cases were cited in argument:—*Simpson* v. *Grange Trust Ltd.* 19 T.C. 231; [1935] A.C. 422; *Sterling Trust Ltd.* v. *Commissioners of Inland Revenue* (1925) 12 T.C. 868; *Commissioners of Inland Revenue* v. *Frere* 42 T.C. 125; [1965] A.C. 402. D

Jones (*H.M. Inspector of Taxes*) v. *Shell Petroleum Co. Ltd.*

Lord Hodson—My Lords, I have had the advantage of reading the opinion of my noble and learned friend Lord Wilberforce, with which I agree. E

For the reasons given by him I would dismiss the appeal.

Viscount Dilhorne—My Lords, I have read the speech of my noble and learned friend Lord Wilberforce. I agree with it and do not desire to add anything.

I would dismiss the appeal.

Lord Wilberforce—My Lords, in the year of assessment 1960–61 the Shell Petroleum Co. Ltd. received income from investments in respect of which it was taxed at less than the standard rate of income tax for that year. The reason for this was that Shell was entitled to double taxation relief in respect of dividends received from foreign companies, which were subject to foreign tax; it also received dividends from United Kingdom companies which themselves were entitled to double taxation relief to which s. 350 of the Income Tax Act 1952 applied. F G

This appeal relates to Shell's management expenses for the year. Being an investment company, Shell cannot simply deduct these expenses from its investment income in the same way as trading companies which are taxed under Schedule D, Case I. What it can do is to claim relief under s. 425(1) of the Income Tax Act 1952: H

A " Subject to the provisions of this section, and to the other provisions of this Part of this Act, where—(*a*) an assurance company carrying on life assurance business (whether proprietary or mutual); or (*b*) any company whose business consists mainly in the making of investments and the principal part of whose income is derived therefrom, claims and proves to the satisfaction of the Special Commissioners that, for any year of
B assessment, it has been charged to tax by deduction or otherwise, and has not been charged in respect of its profits in accordance with the provisions of this Act applicable to Case I of Schedule D, it shall be entitled to repayment of so much of the tax paid by it as is equal to the amount of the tax on any sums disbursed as expenses of management (including commissions) for that year."

C The origin of this section is to be found in s. 14(1) of the Finance Act 1915, a provision which, there can be no doubt, was introduced to remove, or at least to mitigate, the disadvantage which investment companies and some other categories of company were under, as compared with trading companies, in respect of their management expenses.

The claim of Shell is that it is entitled to be repaid tax at the standard rate
D for the year on a sum equal to its management expenses. The Crown contends that Shell is only entitled to recover a proportion of the tax actually paid, which, as explained above, has been paid at less than the standard rate.

The whole case turns upon the construction of the subsection. Compared with some modern enactments this section may appear simplistic, but I do not think that we need to look suspiciously upon its simplicity or to inject comp-
E lexity into it to satisfy the modern taste. It is easy to forget that simple sections can give intelligible results. I think that this is the case here. The section seems to me to indicate comparison between the amount of the management expenses and the amount of the total investment income, and an ascertainment, on this basis, of how much of the tax paid is to be attributable to the management expenses. That this is the nature of the process is first shown by the words
F " so much of the tax paid by it ", and how the " so much " is to be ascertained is shown by the following words. The words " sums disbursed as expenses of management " indicate that a part of the gross revenue is to be taken equal to the management expenses—they may or may not have been paid out of it—and the tax on that part ascertained. So ascertained, this yields the amount to be repaid. I find this clear enough: no doubt the language used can be analysed
G more closely, and those in search of precision will find satisfaction in the judgment of Russell L.J., but I am content to reach the solution by the process I have indicated, making only some observations on the Appellant's argument.

In general, it would appear surprising that a taxpayer's right to repayment of income tax should be related, not to the tax he has paid, but to a standard rate which, both in respect of his income as a whole and in respect of substantial
H ingredients in it, is not the rate at which he has borne tax. To allow him to recover tax at the full standard rate might indeed result in his getting back more than the Treasury has received. Shell agrees that this result would be unacceptable, but maintains that the subsection itself avoids the consequence by use of the word " repayment ". This, it is said, shows that the right of recovery is limited to what has been paid. Perhaps this may be so, but the result is only
I achieved (if at all) by a considerable distortion of the wording: for surely " repayment of so much of the tax paid by it as is equal . . . " contemplates that the amount of the claim is less than the amount of the tax paid—not that, if it is greater, it is to be reduced to the amount paid. When a strain is imposed on words to avoid the awkward consequences of an argument, I begin to doubt

(Lord Wilberforce)

the argument. But the real contention of Shell is that when reference is made to " tax " that can only mean " tax at the standard rate ". The argument is put in two ways. First, it is said that in 1915, when the section first appeared, there was only one rate: what was later (1920) called the standard rate. " Tax " could then mean nothing else but tax at the standard rate, and this meaning adheres to the section whenever it is re-enacted. Secondly, it is said that, even though at the present time individuals, or companies, may ultimately bear tax at a lower rate, what they are charged is always tax at the standard rate, and the reduction is obtained through reliefs. Thus again " tax " means " standard rate tax ". These arguments are, in my opinion, unsound in many respects. Even if one accepts (and counsel for the Crown showed that it is disputable) that in 1915 there was only one rate of income tax, viz. " standard " rate, it does not follow that the section is immutably crystallised round this rate. A section couched in general terms often receives different applications according as the content of the generality changes. I think that if rates were in question this would be such a section. But the real answer to them, in my opinion, is that the section is not dealing with rates at all. No rate (still less, specifically " standard " rate) is mentioned, or presupposed. The repayment is not at any " rate " but is of a proportion of tax paid. No doubt when the proportion has been calculated it is possible to work out at what rate the repayment is made, but that is a very different thing from requiring the calculation to start with a rate. Similarly, even if it is the case that in charging the taxpayer it is necessary to start from a (standard) rate, that is really irrelevant. The starting point taken by the section is " the tax paid ", however the process for assessing it may be described.

I agree therefore with Cross J. and with the Court of Appeal that the appeal fails. I only add that, since Shell's income comes from various sources which bore tax at different rates, there may be more than one alternative method of calculating the tax to be repaid. One way would be by a " rule of three " calculation of the type $x = \frac{a}{b} \times c$. That accepted, for this case, by the Crown, it is one of allocation of the management expenses pound for pound to those portions of Shell's income which have borne the highest net rate of tax. I accept this as a convenient agreed method: and express no opinion as to its authenticity.

I would dismiss the appeal.

Lord Pearson—My Lords, I have had the advantage of reading the opinion prepared by my noble and learned friend Lord Wilberforce, and I agree with the reasons which he gives for dismissing the appeal.

Lord Diplock—My Lords, I have had the advantage of reading the opinion prepared by my noble and learned friend Lord Wilberforce, and I agree with the reasons which he gives for dismissing the appeal.

Cropper (*H.M. Inspector of Taxes*) v. *British Petroleum Co. Ltd.*

Lord Hodson—My Lords, I have had the advantage of reading the opinion of my noble and learned friend Lord Wilberforce, with which I agree.

For the reasons given by him I would dismiss the appeal.

Viscount Dilhorne—My Lords, I have had the advantage of reading the opinion of my noble and learned friend Lord Wilberforce, and I agree with him and for the reasons he gives that this appeal should be dismissed.

Lord Wilberforce—My Lords, in my opinion this case, in all respects but as to the figures involved, is indistinguishable from that of *Jones* v. *Shell Petroleum Co. Ltd.* already considered by this House.

The reasons given for dismissing the appeal in that case are applicable to the present, but there was one argument invoked by British Petroleum, not relied upon by Shell, with which I must deal. That relates to such portion of the Company's income as was derived from investments in United Kingdom companies with foreign interests. As regards dividends from these companies, tax had to be deducted by the paying United Kingdom company at the standard rate, but there is a proviso in s. 350(1) of the Income Tax Act 1952 that:

> " notwithstanding anything in this Act, no relief or repayment in respect of tax deducted or authorised to be deducted from any dividend shall be allowed at a rate exceeding the rate (hereinafter referred to as ' the net United Kingdom rate ') of the United Kingdom income tax payable directly or by deduction by the company after taking double taxation relief into account."

Assuming (following the decision in the *Shell* case) that s. 425 of the Act does not authorise repayment of tax in respect of management expenses at the standard rate, it is necessary to decide what limitation on British Petroleum's claim to relief is imposed by the proviso quoted. The Company's argument is that the only effect of the proviso is to limit the relief which may be claimed by reference to the total tax borne by the dividend-paying company in question. The contention of the Crown is that the relief is limited by reference to the rate of United Kingdom tax payable by the dividend-paying company directly or by deduction. In my opinion, the Crown's contention is clearly correct: it follows from the wording of the proviso, which, by contrast with s. 425, directs attention to the rate of tax rather than to the amount of tax. I find nothing illogical in this result. An illustration, by reference to some simple figures, of the way in which the proviso works is to be found in the judgment of Cross J.(1) [1969] 1 W.L.R. 536, at page 545.

In my opinion this appeal must be dismissed.

Lord Pearson—My Lords, I agree with the opinion of my noble and learned friend Lord Wilberforce, and would therefore dismiss the appeal.

Lord Diplock—My Lords, I have had the advantage of reading the opinion prepared by my noble and learned friend Lord Wilberforce, and I agree with the reasons which he gives for dismissing the appeal.

Questions put (in each case):

That the Order appealed from be reversed.

The Not Contents have it.

That the Order appealed from be affirmed and the appeal dismissed with costs.

The Contents have it.

[Solicitors:—Solicitor of Inland Revenue; Allen & Overy (for Shell Petroleum Co. Ltd.); Linklaters & Paines (for British Petroleum Co. Ltd.).]

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(1) Page 206 *ante*.