HIGH COURT OF JUSTICE (CHANCERY DIVISION)
17TH, 18TH AND 19TH MARCH, 1959

COURT OF APPEAL — 2ND, 5TH AND 6TH OCTOBER, 1959

HOUSE OF LORDS — 2ND AND 3RD MAY, AND 21ST JUNE, 1960

Abbott

v.

Philbin (H.M. Inspector of Taxes) [1]

Income Tax, Schedule E—Emolument of office—Option to purchase shares —Whether benefit assessable for year when option was granted or year of exercise.

The Appellant was the secretary of a company which decided to grant options over 250,000 *of its ordinary shares to certain executives of the company and its subsidiaries. By a letter dated 6th October,* 1954, *he was offered the option at a price of* £1 *for every* 100 *shares to purchase* 2,000 *shares at the market price then ruling, namely* 68*s.* 6*d. per share. The option was to be non-transferable and to expire after ten years or on the earlier death or retirement of the Appellant. The next day the Appellant wrote accepting this offer and enclosing his cheque for* £20. *Because of the need to obtain Treasury consent to the issue of the shares, the option certificate, though stating that the option had been granted on 6th October,* 1954, *was not issued to the Appellant until 6th May,* 1955.

On 28th March, 1956, *the Appellant applied for and was allotted* 250 *shares at the option price of* 68*s.* 6*d. per share. The market price was then* 82*s. A sum equal to the difference between the current market price and the amount paid for the shares (plus a proportionate part of the price of the option) was included in an assessment to Income Tax under Schedule E made upon the Appellant for the year* 1955–56.

On appeal to the Special Commissioners, the Appellant contended (a) *that a right of property representing money's worth and inherently capable of realisation was vested in him forthwith by the contract of option, and that this right was to the extent of any excess in value over the price paid assessable under Schedule E for the year* 1954–55, *and* (b) *that any excess in value of the shares when issued over the price paid for them was not an emolument of his employment but represented an appreciation in the value of property owned by him. The Special Commissioners, considering that they were bound by the decision in* Forbes's Executors *v.* Commissioners of Inland Revenue, 38 T.C. 12, *dismissed the appeal.*

Held, *that the benefit of the option contract was a perquisite which fell to be taxed only in the year* 1954–55.

Forbes's Executors *v.* Commissioners of Inland Revenue, 38 T.C. 12, *over-ruled.*

[1] Reported (Ch. D.) [1959] 1 W.L.R. 667; 103 S.J. 451; [1959] 2 All E.R. 270; 227 L.T. Jo. 262; (C.A.) [1960] Ch. 27; [1959] 3 W.L.R. 739; 103 S.J. 898; [1959] 3 All E.R. 590; 228 L.T. Jo. 240; (H.L.) [1961] A.C. 352; [1960] 3 W.L.R. 255; 104 S.J. 563; [1960] 2 All E.R. 763; 230 L.T. Jo. 38.

CASE

Stated under the Income Tax Act, 1952, Section 64, by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the High Court of Justice.

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 24th February, 1958, E. C. Abbott (hereinafter called "the Appellant") appealed against an assessment for the year 1955–56 made upon him under Schedule E of the Income Tax Act, 1952, in respect of emoluments from his employment. The question for our decision was whether the Appellant was assessable for the year 1955–56 in respect of an option granted to him by his employing company to subscribe for shares, such option having been exercised in the year 1955–56, or whether he was not so assessable (as he contended) but was assessable in the previous year, in which the option was purchased by him.

2. The following facts were proved or admitted:

(*a*) The Appellant was at all material times the secretary of a company, E. S. & A. Robinson, Ltd. (hereinafter called "the company") which carried on business as wholesale stationers.

(*b*) At the annual general meeting of the company held on 28th June, 1954, the following resolution was passed:

> "That 250,000 of the 290,319 Unclassified Shares of £1 each in the capital of the Company be and they are hereby classified as Ordinary Shares and that the Directors be and they are hereby authorised to grant options over such 250,000 Ordinary Shares or any of them to Executives of the Company or its subsidiaries (including Managing and other Directors who may for the time being hold office in the management of the business of the Company or any of its subsidiary companies for the time being) at such times and generally on such terms and subject to such conditions as they think proper."

(*c*) Pursuant to this resolution the directors at a board meeting held on 6th October, 1954, considered the terms under which options were to be granted. The following is a copy of the relevant minute of that board meeting:

> "Share Options
>
> The Secretary produced a list of Executives of the Company and its Subsidiaries whom the Managing Directors had nominated as grantees of Share Options showing against the name of each individual the number of shares over which his Option would extend. It was noted that the total number of shares affected was 243,000 and that the middle price ruling on the Bristol Stock Exchange today was 68/6d. per share.
>
> It was resolved that pursuant to the Resolution of the Company passed at the Annual General Meeting held on 28th June, 1954, Options in accordance with the said list to subscribe for Ordinary Shares of the Company at 68/6d. per share be and they are hereby granted upon the terms and subject to the conditions set out in a letter to be addressed to each grantee, a copy of such letter having been produced to the Meeting approved and signed by the chairman for the purpose of identification.
>
> The Secretary was instructed to despatch today to each grantee letters in the said form."

(*d*) A copy of the letter referred to setting out the terms of the option is hereto attached, marked "A"(1). The salient conditions were that the executive was granted, at the price of £1 for every 100 shares involved, an option to purchase a specified number of shares at the price of 68*s.* 6*d.* per share, such an option to be exercisable at any time within ten years from the date of the grant of the option. The option was expressed to be not transferable and was to expire upon the death or retirement of the employee prior to the ten years. If the employee desired to purchase the option he was required to send in a form of application which accompanied the letter (together with his cheque for the amount specified being the price of the option), whereupon an option certificate would be issued to him.

(1) Not included in the present print.

(*e*) Option certificates were not in fact issued until 6th May, 1955, by which time the company had obtained, in response to its application on 4th March, 1955, the consent of H.M. Treasury to the issue of shares in response to the exercise of options; and by letter dated 9th May, 1955, option holders were so advised. A copy of this letter is attached hereto, marked "B"(1).

(*f*) The Appellant was included as one of the selected list of executives above referred to in respect of 2,000 shares in the company and on 7th October, 1954, he sent in an application to the company to purchase an option in respect of such 2,000 shares on the terms of the letter above referred to, forwarding with such application his cheque for £20, which was duly cashed by the company. A copy of such application is hereto attached, marked "C"(1). Owing to the circumstances hereinbefore mentioned he was not given a certificate until 6th May, 1955, but the certificate, a copy of which is hereto attached, marked "D"(1), states on its face that the option was granted on 6th October, 1954. There was endorsed on such certificate the terms and conditions applicable to the option, and a copy of such terms and conditions is hereto attached, marked "E"(1). As previously stated, the option was expressed to be not transferable and to expire on the holder's death or retirement or on the tenth anniversary of the date of the grant of the option.

(*g*) Under the terms of the option any number of shares up to the number of 2,000 could be applied for by the Appellant, and on 28th March, 1956, the price of the company's shares having then risen to 82*s*., the Appellant applied to the company for 250 ordinary shares at the option price of 68*s*. 6*d*. per share, sending with such application the sum of £856 5*s*. A copy of such application by him is hereto attached, marked "F"(1). The Appellant was duly allotted the 250 shares.

(*h*) The Appellant was assessed to tax under Schedule E for the year 1955–56 in the sum of £7,086 which included the sum of £166 in respect of the share transaction, such sum of £166 being made up as follows:

	£ *s*.	£ *s*.
250 shares taken up on 28th March, 1956, when the middle market price was 82*s*.		1,025 0
Deduct: (1) option price 68*s*. 6*d*.	856 5	
(2) cost of option at £1 per 100 shares ...	2 10	858 15
		£166 0

As will be evident, such assessment charged the Appellant to tax under Schedule E for the year 1955–56 in respect of the benefit, received by him by virtue of his employment, of being able to purchase shares worth 82*s*. at a cost of 68*s*. 6*d*. (plus a proportionate part of the price of the option). Tax under Schedule E being in respect of the current year's emoluments, such charge was appropriate to tax a benefit arising in the year 6th April, 1955, to 5th April, 1956.

3. It was contended on behalf of the Appellant:

(*a*) that the contract of option vested a right of property in the Appellant forthwith;

(*b*) that such right represented money's worth and was inherently capable of realisation;

(*c*) that such right was, to the extent of any excess in value over the price paid therefor, an emolument of the Appellant's employment assessable under Schedule E in the year of assessment 1954–55 and not otherwise;

(1) Not included in the present print.

(*d*) that the shares issued to the Appellant in the year 1956 were issued in virtue only of the right of property acquired by the Appellant in the previous year of assessment; and

(*e*) that any excess in value of the shares when issued over the price paid therefor represented an appreciation in the value of an item of property owned by the Appellant and was not an emolument of his employment.

4. It was contended on behalf of H.M. Inspector of Taxes:

(*a*) that when the shares were issued to the Appellant there arose or accrued to him a profit from his employment assessable to tax for the year 1955–56;

(*b*) that the said profit so assessable amounted to £166, computed as set out in paragraph 2(*h*) above; and

(*c*) that the appeal should therefore be dismissed and the assessment confirmed.

5. We, the Commissioners who heard the appeal, took time to consider our decision and gave it in writing on 9th April, 1958, as follows:

We consider that the present case is indistinguishable from that of *Forbes's Executors* v. *Commissioners of Inland Revenue*, 38 T.C. 12, and that the decision of the Court of Session in that case is binding upon us. In the present case the Appellant paid a small sum for his option whereas Mr. Forbes was given his option, but we do not consider that difference material: in each case it was common ground that a benefit accrued to the Appellant as part of his remuneration, and in each case the rights granted were personal to the Appellant. It was suggested on behalf of the Appellant that the decision in *Forbes's* case may have turned on some peculiarity of Scots law, but we can find no support for such a suggestion in the judgment of the Court of Session and we consider that case decisive of the present one. We accordingly hold that the appeal fails, and we leave the figures to be agreed in accordance with our decision.

Figures having subsequently been agreed in accordance with our decision, we confirmed the assessment on 22nd May, 1958.

6. In making suggestions in the usual course on the draft Case, the solicitors to the Appellant stated (in effect) that the suggestion mentioned in our decision above that the decision in *Forbes's Executors*(1) "may have turned on some peculiarity of Scots law" did not represent one of the Appellant's contentions, and we agree that this is so. The suggestion arose incidentally during the course of argument and was present in our minds when considering our decision.

7. The Appellant 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 High Court pursuant to the Income Tax Act, 1952, Section 64, which Case we have stated and do sign accordingly.

8. The question for the decision of the Court is whether, upon the facts proved or admitted, our decision was correct in law.

B. Todd-Jones
R. A. Furtado
} Commissioners for the Special Purposes of the Income Tax Acts.

Turnstile House,
94–99, High Holborn,
London, W.C.1.
14th October, 1958.

(1) 38 T.C. 12.

The case came before Roxburgh, J., in the Chancery Division on 17th, 18th and 19th March, 1959, when judgment was given against the Crown, with costs.

Mr. F. Heyworth Talbot, Q.C., and Mr. Desmond Miller appeared as Counsel for the taxpayer, and Mr. Roy Borneman, Q.C., and Mr. Alan Orr for the Crown.

Roxburgh, J.—At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 24th February, 1958, E. C. Abbott (hereinafter called "the Appellant") appealed against an assessment for the year 1955–56 made upon him under Schedule E of the Income Tax Act, 1952, in respect of emoluments from his employment.

> "The question",

say the Special Commissioners in the Case Stated,

> "for our decision was whether the Appellant was assessable for the year 1955–56 in respect of an option granted to him by his employing company to subscribe for shares, such option having been exercised in the year 1955–56, or whether he was not so assessable (as he contended) but was assessable in the previous year, in which the option was purchased by him."

Rule 1 of the Rules applicable to Schedule E provides that

> "Tax under Schedule E shall be annually charged on every person having or exercising an office or employment of profit mentioned in Schedule E . . . in respect of all salaries, fees, wages, perquisites or profits whatsoever therefrom for the year of assessment."

after making certain possible deductions. It will be observed that the question is not whether the emolument in question does or does not fall within that Rule as an emolument taxable under Schedule E, because the Appellant has throughout this case conceded that it is so taxable. Mr. Heyworth Talbot, as indeed he was bound to do, conceded it at once, but he did advance the view that it was a perquisite and that it came within the Schedule on that ground. Mr. Borneman has assured me that he does not attach any importance to that question because it is within the Schedule. He may be right or he may be wrong in that view, but as he has not contended that it is not a perquisite—he asked me not to say that he conceded it and I have chosen my words carefully—naturally enough I see no reason why I should explain why I think Mr. Heyworth Talbot was right in describing it as a perquisite. In my judgment the emolument was a perquisite, and no contention has been advanced before me to the contrary.

I should like to deal at once with an argument—not his only argument, but one of his principal arguments—which has been consistently advanced by Mr. Borneman. He says that once the item—and I am now going to call it a perquisite because I have decided that it is a perquisite—is in the box all considerations as to its quality are exhausted, and that one does not look any further into whence it was derived or why it was paid. If I may say so, that proposition seems to me to be contrary to logic, jurisprudence and the whole trend of authority. I will deal first of all with logic. You do not deprive persons of all symbols of identity by putting them into a box. When Noah put the animals into his box he did not deprive them of both species and gender. That is the logic of the thing. From the point of view of jurisprudence, the question is not whether they are in the box but when they got into the box, to adopt Counsel's metaphor. In other words, were they perquisites from the employment for the year of assessment? There would be no question at all for me to consider if it were true that once the perquisite got into the box all considerations as to its quality are exhausted and that one does not have to

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look any further into whence it was derived or why it was paid. Thirdly, the process which Counsel so surprisingly disclaims is precisely that process which every other Judge who has had to deal with this question has adopted. I need say no more, I think, about that proposition, but all the same there are some very difficult points in this case.

Paragraph 2 of the Case reads:

> "The following facts were proved or admitted: (*a*) The Appellant was at all material times the secretary of a company, E. S. & A. Robinson, Ltd. (hereinafter called 'the company') which carried on business as wholesale stationers."

Annexed to the Case is a copy of a letter dated 6th October, 1954, which I am about to read, and I regret to say that it is not a true copy. If this action had been a Chancery action I should, of course, have ordered the copy to be forthwith amended or a true copy substituted, but so narrow is the Judge's jurisdiction in Income Tax cases that I am not convinced that I myself have any power to amend it, and I certainly do not intend to send it back to the Commissioners to amend. This is because Counsel fortunately are able to agree not only that it is not a true copy but also how it ought to be amended, and although this is an unusual method of dealing with such a difficulty it presents no real obstacle. Therefore I have first of all to state that it was agreed between Counsel that this is not a true copy in two respects: firstly that whereas, on the face of it, it is not addressed to anybody, it is in fact addressed to the Appellant; secondly that the second paragraph ought to be amended by the insertion of certain figures into two blank spaces. I now propose to read it as thus agreed to be amended:

> "Dear Mr. Abbott, Ordinary Share Options. The Directors consider that it would be to the benefit of the Company if certain Executives of the Company and of its subsidiary companies . . . were afforded an opportunity of obtaining an interest in, or increasing an existing interest in, the capital of the Company. Accordingly, arrangements have been made under which Options to subscribe up to a total of 250,000 Ordinary Shares of £1 each of the Company at the middle price ruling on the Bristol Stock Exchange on the date of the grant of an Option, may be granted to such Directors and Executives as are from time to time nominated by the Managing Directors. The Options will be exercisable at any time within ten years from the date of grant."

That statement is not accurate because it is subsequently qualified, as will appear.

In passing I want to make a reference to a case decided by Wrottesley, J., *Ede* v. *Wilson*, 26 T.C. 381. In that case the headnote reads:

> "The directors of company A, as a reward for past services and a stimulus to future efforts, decided to allow the Respondents, who held managerial offices in a subsidiary company B, to subscribe for certain shares in company A at their par value, which was considerably less than their current market value, on giving a verbal undertaking that they would not sell such shares without the permission of the directors of company A so long as they remained in the employ of company B. The Respondents took advantage of the privilege and gave the required undertaking, and they were assessed to Income Tax under Schedule E on the difference between the par value of the shares so taken up and allotted to them and their market value at the time of the allotment. On appeal they contended that they were not employed by, and rendered no services to, company A; that they were debarred from realising profits on these shares by the verbal undertaking they had given; that they had received no income by the transaction, and that the profit (if any) should be assessed only when realised. The General Commissioners were of opinion that no profit could reasonably arise from the transaction owing to the tie, and discharged the assessments. *Held*, that the Commissioners had come to a wrong conclusion and that the privilege granted to the Respondents represented money's worth and was assessable to Income Tax as a profit of their respective offices in company B, but that the cases must go back,"

—and this is what I am at the moment referring to—

> " . . . in order that the Commissioners might decide the proper amounts of the

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> assessments having regard to the restriction under which the Respondents accepted the allotments."

At the end of the judgment, at page 389, there was this exchange:

> "Mr. Hills.—It will go back just to find the amount in accordance with your Lordship's judgment. Wrottesley, J.—It may be very different in the hands of different persons. Mr. Talbot.—It may be possible to agree it, of course, before we come to the Commissioners."

I may say that, if that is the method by which most of these awkward types of questions regarding valuation have been resolved, that does not absolve the Court from considering the principles upon which valuations ought to be made if the parties do not agree a figure. There is no doubt at all what Wrottesley, J., meant when he said(1):

> "It may be very different in the hands of different persons. . . . To a well-to-do person with capital of his own already it may be worth the stock exchange value; to another man it may not."

If that is good law, I do not know how many of the 250,000 ordinary shares were in fact issued under this letter and it is no business of mine to ask, but there may be some interesting and protracted valuations if they are conducted on the lines indicated by Wrottesley, J. It would be wrong for me to say, because it has got nothing to do with the present case, whether I think those lines are right or wrong, but it is rather difficult, when such a strange thing crops up, to pass it by without comment.

The letter of 6th October, 1954, continues:

> "On the nomination of the Managing Directors"

—and there were more than one, so that is not a mistake—

> "the Directors have therefore decided to grant you, at the price of £1 for every 100 shares involved, an Option to subscribe for 2,000 Ordinary Shares at 68/6d. per share. Kindly complete the enclosed application form and send it to the Secretary by return, together with your cheque for £20 being the price of the Option. In due course you will receive a Certificate specifying the number of Ordinary Shares of the Company in respect of which the Option has been granted, the price payable for the shares, and other terms governing the contract of Option."

I am glad to say, as will shortly appear, that I have been absolved from the difficulties which might arise in relation to that sentence. The letter then says:

> "You will note that the Option is not transferable and to the extent not previously exercised will expire upon your death or retirement, upon your Service with the Company and/or its subsidiaries ending, or on the tenth anniversary of the date of grant of the Option, whichever first occurs. Upon an exercise of the Option, the allotment of Ordinary Shares will be made, subject however to—(*a*) the prior receipt by the Company's Secretary of a form of application duly signed by the Option Holder stating the number of shares (which, it should be noted"

—and this is a matter which I shall have to consider in my judgment as being of some importance—

> "need not be all the shares in respect of which the Option was granted) to be taken up and accompanied by payment in full of the price payable for the Shares; (Forms of application may be obtained from the Secretary)".

As the secretary is the person concerned in this case, no doubt he had the forms without applying to himself for them.

> "(*b*) the consent of H.M. Treasury or such other authority as may under regulations or enactments for the time being in force, be necessary. Allotments will not be made between the date of declaration of a dividend or other distribution on the Ordinary Share Capital of the Company and the date of payment of that dividend or other distribution. In the event of any change in the issued capital of the Company taking effect while any Option is outstanding (otherwise than by reason of the exercise of

(1) 26 T.C. 381, at p. 389.

> Options), such Option (including the number of shares affected and the price payable for the shares) will be appropriately modified by the Directors."

Fortunately I do not have to construe that sentence either.

> "The Directors whose decision in all matters relating to this scheme shall be final and binding, may at any time discontinue the grant of Options or amend any of the above provisions in any way they think fit,"

—I have read that because of the importance of these words:

> "but they may not cancel or (subject to the preceding paragraph) modify the terms of Options already granted."

I may say that the language of this letter—and in this respect I am not differentiating it from the language of many Judges who have pronounced judgments upon the nature of options—indicated the common confusion about the nature of options. English law has, I think, what may be—and this is going to become important presently—a somewhat unique view of options. Options are, of course, contractual rights. That has never been in doubt. A contract of option is a contract recognised by the common law, and breach of it gives rise, as it always did give rise, to an action for damages. Options, however, have been treated somewhat differently since the fusion of law and equity, in theory if not entirely in practice, because of the Chancery tendency which is notable everywhere in equity law to treat contractual rights created on the payment of valuable consideration as being in the sphere of property rather than in the sphere of contract. I shall have something more to say about that when I talk about a certain Scottish case[1]. A layman does not talk about an option contract. He talks about the granting of an option, which immediately introduces by implication an equity conception of an option.

Paragraph 2 (*f*) of the Case reads:

> "The Appellant was included as one of the selected list of executives above referred to in respect of 2,000 shares in the company and on 7th October, 1954, he sent in an application to the company to purchase an option in respect of such 2,000 shares"

—and you will notice that the very phrase "purchase an option" indicates the equity view of it as property rather than the common law view of it as paying a consideration for a contractual right—

> "on the terms of the letter above referred to, forwarding with such application his cheque for £20, which was duly cashed by the company. A copy of such application is hereto attached, marked 'C'."

The application, which is addressed to the secretary of the company—in fact himself—reads as follows:

> "Dear Sir, I desire to purchase an Option upon the terms set out in the Company's Letter of the 6th Oct. 1954 to subscribe for up to 2,000 Ordinary Shares in the Company and enclose my cheque in the Company's favour for £20 being payment at the rate of £1 for every 100 of such Ordinary Shares to which the Option is to apply. Dated this 7th day of Oct. 1954."

That date was, of course, in the year of assessment 1954–55 and not in the year of assessment 1955–56. I record that because that is the whole point of this case.

Owing to circumstances which are mentioned in the Case, and which are in fact as follows, the company had obtained, in response to an application on 4th March, 1955, the consent of Her Majesty's Treasury to the issue of shares in response to the exercise of options, and by a letter dated 9th May, 1955, the option holders were so advised. In consequence of those circumstances, as I say, the Appellant did not receive an option certificate until 6th May, 1955.

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(1) Forbes's Executors *v.* Commissioners of Inland Revenue, 38 T.C. 12.

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The certificate, which I will read, states on the face of it that the option was granted on 6th October, 1954. That is too much equity and too little common law. Not even in a court of equity could the option be deemed to be property until the consideration had been paid, because equity does not treat as creating property rights a contract for no consideration, and there was no deed of grant, nor would there be. As there was no deed of grant and as there was on 6th October, 1954, no contract for a valuable consideration, there could not therefore have been in law a grant of the option upon 6th October, 1954. On the other hand, a somewhat serious question might have arisen as to whether there became a binding contract on 7th October, 1954. I need not go into that, but it arose because of certain ambiguous phrases in the letter. Fortunately, however, as I have said, I do not have to decide that question, which would itself involve looking at about 20 or 30 cases in the Chancery Division, because it was agreed before me by Counsel that a binding agreement was concluded in the manner I have indicated by the letter of offer and the letter of acceptance of 7th October, 1954. Therefore I am going to substitute, instead of the date stated on the certificate, the agreed date of 7th October, 1954. I think I should read the terms of the certificate as it is quite short:

> "This is to Certify that Edward Cranfield Abbott of 4, Harley Place, Clifton Down, Bristol 8, in consideration of the payment by him to the Company of the sum of £20 was granted on the sixth day of October 1954,"

—I have already dealt with that—

> "an Option upon the terms and subject to the conditions set out on the back hereof, to subscribe at 68/6 per share for 2,000 Ordinary Shares of £1 each in the capital of the Company."

Endorsed on the back of the option certificate—it has some relevance to one of the matters that I hope to refer to in my judgment—is this:

> "The within mentioned Edward Cranfield Abbott having exercised his Option on the twenty eighth day of March 1956 in respect of two hundred and fifty shares this certificate now covers an Option of one thousand seven hundred and fifty shares only."

There is no doubt about the exercise of that option, that is to say, the exercise as to the 250 shares. The Case does not state, and it is wholly irrelevant for me to know, whether he has since further exercised the option, and if so to what extent. As, however, I have to deal with that matter in the concluding part of my judgment, if I mis-state the actual position today that will be because the actual position to-day is not before me and there is no need for me to know what the actual position is. It may be that I shall take some alternatives which may not in fact now exist. I do not think I need read the terms and conditions applicable to the options as endorsed on the certificate because there is no material variation for any purpose with which this case is concerned. They are there but they do not appear to me to involve any material variations.

Sub-paragraphs (*g*) and (*h*) of paragraph 2 of the Case read:

> "(*g*) . . . on 28th March, 1956, the price of the company's shares having then risen to 82*s*., the Appellant applied to the company for 250 ordinary shares at the option price of 68*s*. 6*d*. per share, sending with such application the sum of £856 5*s*. . . . The Appellant was duly allotted the 250 shares. (*h*) The Appellant was assessed to tax under Schedule E for the year 1955–56 in the sum of £7,086 which included the sum of £166 in respect of the share transaction"

—and, of course, it is only that figure which is relevant to the present case—

> "such sum of £166 being made up as follows:
>
> | | £ | *s*. |
> |---|---|---|
> | 250 shares taken up on 28th March, 1956, when the middle market price was 82*s*. ... ... | 1,025 | 0 |

	£ s.	
Deduct: (1) option price 68*s.* 6*d.*	856 5	
(2) cost of option at £1 per 100 shares ...	2 10	858 15
		£166 5s."

If I may interpose there, in my view of the case it is not really necessary for me to decide the validity of that method of dealing with the cost of the option, but I propose to make a few observations upon it at the conclusion of my judgment which will, of course, be *dicta*, but this subject-matter is already so impregnated with *dicta* that I shall perhaps not add much flame to the fire by adding any more.

Paragraphs 3 and 4 of the Case read:

> "3. It was contended on behalf of the Appellant: (*a*) that the contract of option vested a right of property in the Appellant forthwith".

I take it that that means this was a *chose in action*. If it did not mean that, that is what I think it should have meant, at any rate.

> "(*b*) that such right represented money's worth and was inherently capable of realisation; (*c*) that such right was, to the extent of any excess in value over the price paid therefor, an emolument of the Appellant's employment assessable under Schedule E in the year of assessment 1954–55 and not otherwise".

That particular contention was narrowed down by Mr. Heyworth Talbot to the contention that it was a perquisite, and it is a view which I have accepted.

> "(*d*) that the shares issued to the Appellant in the year 1956 were issued in virtue only of the right of property acquired by the Appellant in the previous year of assessment; and (*e*) that any excess in value of the shares when issued over the price paid therefor represented an appreciation in the value of an item of property owned by the Appellant and was not an emolument of his employment. 4. It was contented on behalf of H.M. Inspector of Taxes: (*a*) that when the shares were issued"

—I suppose that means "and not before"—

> "to the Appellant there arose or accrued to him a profit from his employment assessable to tax for the year 1955–56; (*b*) that the said profit so assessable amounted to £166, computed as set out in paragraph 2 (*h*) above"

—and I have already read that—

> "and (*c*) that the appeal should therefore be dismissed and the assessment confirmed."

In paragraph 5 of the Case appears the finding of the Commissioners, of which I think I need only read about five or six lines.

> "We consider that the present case is indistinguishable from that of *Forbes's Executors* v. *Commissioners of Inland Revenue*, 38 T.C. 12, and that the decision of the Court of Session in that case is binding upon us. In the present case the Appellant paid a small sum for his option"

—and may I say at once that the size of the sum cannot be the criterion of the law; the law must be the same, and I shall come back to that point, whether the sum was £20 or £20,000—

> "whereas Mr. Forbes was given his option, but we do not consider that difference material".

I need not read any more because it is perfectly plain that the Special Commissioners arrived at their conclusion on that ground and on that ground alone. They considered that they were bound by a case which was indistinguishable because the distinction alleged did not, in their opinion, amount to a material difference. Therefore I do not think anyone can say, at any rate as regards this case, that I am bound by the finding of the Commissioners, and no one has in fact said so.

Rule 1 of the Rules applicable to Schedule E groups together for the purpose of taxation a number of transactions or happenings which are, in my

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judgment, essentially different in character. Of course, Parliament can do that or anything else that it likes and can say that transactions essentially different in character are to be taxed under a particular Schedule, but I dissent from the view, unless Parliament has said so in express terms, that that process amalgamates essentially different transactions for all purposes. I do not think it overrules or overrides the general law, except in so far as is necessary to give effect to the provisions for taxation embodied in the Act. That, I think, is the fundamental ground upon which I have already rejected, and still reject, Mr. Borneman's argument. Admittedly these perquisites are in the box, admittedly salaries are in the box, but that does not mean that salaries and perquisites have essentially the same characteristics, any more than if you put Jack and Jill in the box they would become of one sex together. I think it is necessary to remember, upon any sensible view, that salaries are a revenue item but that transactions in relation to shares are generally not a revenue item. They are sometimes a revenue item, but generally I should have thought they were not. I believe that that distinction has been and ought to be preserved in dealing with perquisites.

It is, in my view, very necessary to consider—and I thereby reject again the argument that has been put to me—what was the character of this perquisite. Was it primarily a revenue item or was it primarily a purchase on favourable terms of a capital asset, or a right to purchase on favourable terms a capital asset? I think that distinction will reconcile the authority at present existing on this point, with the exception of the Scottish case(1) about which I shall have quite a lot to say. There are of course cases other than the Scottish case to which I have been referred, and I have not ignored them in what I have just said. Undoubtedly Mr. Borneman's argument rested mainly, although not entirely, upon three passages in the case of *Bridges* v. *Bearsley*, 37 T.C. 289. My note of Mr. Borneman's main submission, apart from that submission which I have already dealt with, can be summarised as follows: while contending, I think, that the proper appreciation of the contract in the particular case was, at any rate, important, he also contended that those two cases to which I have just referred made it necessary to isolate the option contract from the subsequent application for and allotment of shares, and that when this process had been carried out the benefit of the option contract was not a perquisite because it could not be turned to pecuniary account. He preferred to make use for this purpose of an extract from the speech of Lord Halsbury, L.C., in *Tennant* v. *Smith*, 3 T.C. 158, at page 164. I do not suggest that there is any distinction between the passage which he cited from that speech and the passage which is very commonly cited from the speech of Lord Watson, at page 167, but if there be any distinction—and I am not saying that there is—I shall be in fashion if I prefer, as I do prefer, the extract from the speech of Lord Watson, which is as follows, and which can readily be made without appreciation of the facts of that particular case:

> "Is it then a perquisite or a profit of his office? I do not think it comes within the category of profits, because that word in its ordinary acceptation appears to me to denote something acquired which the acquirer becomes possessed of, and can dispose of to his advantage, in other words money, or that which can be turned to pecuniary account."

In this case the taxpayer paid money, he did not receive it, but the question is: did he acquire something which could be turned to pecuniary account? Now Mr. Borneman submitted—and I may say that this submission is, I think, the actual basis of the judgment of the Scottish Court—that the option contract

(1) Forbes's Executors *v.* Commissioners of Inland Revenue, 38 T.C. 12.

merely—and I stress the word merely—gave the Appellant a right to exercise the option, and that as it was not transferable it was of no value. I propose, before commenting on that submission, to read the headnote and some passages in the *Bearsley* case. The headnote reads, at page 289(1):

> "The Respondents were at the material times respectively managing director and a director of a limited company which they had served for many years in those and other capacities. They had greatly helped in building up the business and in running it when it had become established. Most of the shares in the company were held in trust, under the will of the former principal shareholder (who died in 1936), for his widow during her life and thereafter for his two sons in equal shares absolutely. The Respondents wished to have a fairly substantial holding in the company. They had been under the impression that the former principal shareholder would bequeath them shares by his will, but he had not done so. In due course they approached the sons about the matter and in 1945 the sons entered into covenants"

—and this is important—

> "under which the Respondents, in consideration of their continuing their engagements with the company for four years, were each to receive 8,000 of the shares within three months of the death of the widow. These shares were transferred to the Respondents in July, 1953. On appeal to the Special Commissioners against assessments to Income Tax under Schedule E made on them for 1953–54 in sums which included the value of the shares at the date of transfer, the Respondents contended that the transfers were pure acts of bounty and in no sense rewards for past or future services; and that the stipulations that the covenants were in consideration of continued services were conventional"

—whatever that might mean—

> "and inserted simply to give the Respondents a procedural right to sue on the documents effectively. Alternatively, it was contended"

—and this is the important part of the case—

> "that, if the value of the shares transferred was income assessable under Schedule E, such income either arose on the execution of the deeds or should be spread over the four years 1945–46 to 1948–49. The Special Commissioners found that the transfers and covenants were not remuneration for the Respondents' services in their current offices and held that neither the value of the shares nor the value of the covenants represented income assessable under Schedule E. *Held* (Jenkins, L.J., dissenting),"

—and it is extremely important in this case to follow its vicissitudes—

> "that the shares were not profits from the Respondents' current offices because they were not remuneration for services in those offices but testimonials (which under the covenants might not have accrued until after retirement) for what they had done, including what they had done before holding those offices."

I think I am right in saying that Danckwerts, J.'s judgment was in favour of the Crown. It was reversed on appeal but still, for this purpose, it is not at all irrelevant to read what Danckwerts, J., said at a time when his decision, unless reversed, would have stood. He said this, at page 306(1):

> "Two alternative contentions were put forward on behalf of the Respondents. The first of these was that, if the transaction fell within the terms of Schedule E, the income of the Respondents was the value of the rights acquired in December, 1945, by the Respondents under the deeds of covenant; this would mean that those values would have to be estimated in December, 1945, and the assessment on them now, or at the material date of the assessments under appeal, would be out of time. Evidence was tendered that it was possible for a valuer to make an estimate of some sort as to the values in question. The Commissioners treated the estimates as being such an uncertain matter that they could not amount to money's worth and, therefore, they were not a possible part of the Respondents' income."

Pausing there, again to digress, I can see what great difficulties regarding valuation would have occurred, not merely regarding questions of fact but also regarding questions of principle, but I do not think it could be arguable that a piece of property could not be turned to pecuniary account, not because

(1) 37 T.C.

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it was not capable of being sold at a profit but because the Commissioners could not value it. I cannot see how the question as to whether it amounts to money or money's worth could possibly depend upon whether the Commissioners could or could not think of means of valuing it. I am putting that in in case I forget it, because I am very anxious to make it plain that I do think that very difficult questions of valuation will arise if my judgment stands without being reversed anywhere else. However, it has not been submitted to me that a valuation cannot be made. That would be a submission which, if it had been made, I should have considerably feared, but it has not been made.

Danckwerts, J., went on(1):

> "I do not think that this is the correct answer, but I do not think that the contention can succeed. Mr. Mustoe, in support of this contention, relied upon *Tait* v. *Smith*, 35 T.C. 79, as well as *Weight* v. *Salmon*(2). But I do not think that those cases have any application on the facts of the present case."

There is a clear example of a Judge not adopting the submission which Mr. Borneman made to me and which I dealt with at the beginning of my judgment. He says:

> "If the conclusion is correct that the transfers of the shares were profits of the Respondents' offices and remuneration for the services to be performed by them,"

—and I stress those words "were profits of the Respondents' offices", about which there is no doubt, and those words "and remuneration for the services to be performed by them", as those two propositions are a condition precedent of that which Danckwerts, J., is about to say, and that in my view discloses the kernel of the problem—

> "they were paid for those services when the shares were transferred to them (though the shares were not immediately realised) and assessable accordingly."

Although Danckwerts, J.'s judgment was reversed, it was not reversed, as far as I can see, on that point.

I now come to Jenkins, L.J.'s judgment in the Court of Appeal. He was in a minority and therefore what he says on this topic may, in one sense, be *obiter dictum*, but I should be both disrespectful and unrealistic if I lightly disposed of what he said on that ground. On the contrary, I am happy to be able to say that I agree with him completely, bearing in mind one of the premises upon which Danckwerts, J.'s statement of the law was founded and which recurs in Jenkins, L.J.'s statement of what he thinks would have been the position if his judgment had been the judgment of the majority. He says, at pages 316–7(3):

> "As to the alternative contention to the effect that the proper subject of assessment consisted of the value of the rights acquired by the Appellants under the deeds of covenant in December, 1945, which constituted income of the Appellants for the financial year 1945–46: on the footing that the Appellants fail in their main contention the position was that by the deeds of covenant the Hornby brothers covenanted that, in consideration of the Appellants continuing their respective engagements with the company for four years from the date of the deeds, the Hornby brothers would transfer to them on the death of Mrs. Hornby the specified number of shares in the company by way of remuneration for the services rendered by them to the company during that period. The time at which the Appellants were to receive this additional remuneration for their services to the company for this further period was thus fixed by the terms of the bargain as the death of Mrs. Hornby, or to be strictly accurate the expiration of three months from her death. In fact the Appellants duly completed their four years' further service in Mrs. Hornby's lifetime, and the shares were transferred to them shortly before her death, although the Hornby brothers would have been entitled to withhold such transfer until three months after the happening of that event. I see no reason for treating the stipulated remuneration,"

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(1) 37 T.C. 289, at p. 306. (2) 19 T.C. 174. (3) 37 T.C.

—and I stress those words "the stipulated remuneration"—

> "that is, the shares, as received or receivable . . .".

Just pausing there, Mr. Borneman did not like my use of the word "received". I think he was right and I ought to have said "received or receivable". In other words, I agree *in toto* with this passage in Jenkins, L.J.'s judgment in which he says(1):

> "I see no reason for treating the stipulated remuneration, that is, the shares, as received or receivable on any earlier date than that on which the shares were actually transferred, which, as I have said, was in fact earlier than the date on which the Hornby brothers were obliged under the deeds of covenant to transfer the shares to the Appellants. In *Weight* v. *Salmon*(2) the benefit held to constitute remuneration consisted of an immediate right to subscribe at par for shares worth in the market substantially more than par. In *Tait* v. *Smith*, 35 T.C. 79, it was held that the taxpayer was wrongly assessed for the year 1949–50 in respect of the surrender value of an endowment policy on his life which under the terms of his service he had become entitled to have immediately transferred to him in 1946. I do not think that either of these cases, on which Mr. Mustoe relied, supports his contention that in the present case the taxable profit consisted of the value of the rights conferred by the deeds of covenant at the date of those deeds and not of the value of the shares at the date when they were transferred."

I think I am right in saying that Morris, L.J., did not deal with this point, but Sellers, L.J., at page 327(3), says:

> "It is not, in my view, in harmony with the tax provisions that if the transactions fell within the terms of Schedule E the income was the value of the rights acquired by the Appellants when the deeds were entered into. I agree with the learned Judge when he says".

—and then he makes a citation from the very passage which I have read from the judgment of Danckwerts, J.

The argument which Mr. Heyworth Talbot presented to me involves, as is obvious from the contentions which I have read from the Case, the proposition that a contractual right to receive payments in future, which is a *chose in action*, can, as it were, be capitalised at the date of the deed and be taxed as a perquisite. If you try to apply that theory to an ordinary contract of service you come to a complete standstill as regards common sense. That is the difficulty, in my view, of the argument which Mr. Heyworth Talbot presented to this Court. You could look at a contract of service in the same way that he looks at this option contract. I am not now talking about additional remuneration but about a straight service contract, a contract by an employer to employ the taxpayer for ten years certain at a fixed salary of £1,000 a year. In jurisprudence that is a *chose in action* and it is obviously one which can be turned to pecuniary account, although only by the most appalling imprudence, of course. However, that does not seem to me to be a jurisprudential consideration. Some money could be raised by an equitable mortgage of such a contract—that is without doubt—and therefore one would reach the logical conclusion that in future salaries ought not to be taxed when they are receivable but when the contract to pay them is entered into. For my own part, as I have just said, that is the way I thought the case for the Crown would be presented and to which I have given a great deal of personal attention, because that would obviously be wrong. I think that problem has undoubtedly been in the minds of other Judges before me. I am not conceited enough to think that I, for the first time, have thought of it, and it explains a great deal that is not otherwise explicable.

Starting with salaries, I do not think that the Crown or the taxpayer has ever yet suggested that they should be dealt with in the manner in which Mr. Heyworth Talbot has asked me to deal with this option contract. At any rate, no case has been cited to me and I should not think that one exists.

(1) 37 T.C. 289, at p. 317. (2) 19 T.C. 174. (3) 37 T.C.

(Roxburgh, J.)

You do not deal with salaries as being the benefit of a *chose in action* which can be turned to pecuniary account. You deal with them as sums of money received *de anno in annum* and taxed in the year in which they are received or receivable. I emphasise those words "received or receivable" because I would have thought that proposition could not be disputed or argued. That was the problem which, in a modified form, confronted Jenkins, L.J., because he, and also Danckwerts, J., quite clearly took the view that in the *Bearsley* case (1) the shares were additional remuneration. They both used words to that effect, which I have already cited, and of course you could not possibly have a method of dealing with additional remuneration which was different from the method of dealing with the ordinary remuneration of the particular individual under his service contract. Therefore, in my view, the three *Bearsley dicta* are, if I may say so with respect, plainly right.

Now, in what respects does the *Bearsley* case differ from the present case? First of all, although I think this is not the most important distinction but nevertheless a real one, it is not an option case at all. Secondly, in my judgment it is distinguishable because it relates to a payment under a contract of service and not to a payment which comes as a result of service, which is quite a different matter. Most important of all, to my mind, and here I differ completely from the Special Commissioners, it was not in the present case a reward for services at all, but a thing that was bought. The price paid is immaterial. It was bought, whether £20 or £20,000 was paid for it, and therefore it could not have been extra remuneration for services. However, that is exactly what Jenkins, L.J., thought in the *Bearsley* case. If it had been taxable at all—and we know, in fact, that it was decided that it was not—as what would it have been taxable?

Is it possible to say that this case differs in principle from the *Bearsley* case? For reasons which I shall give I think it helps the Crown more than the Scottish case(2). In my judgment it is not as though all the cases are on the *Bearsley* side of the line. You have got to reconcile a number of cases, most of which are referred to in what I have read, by some principle, and I think there is a principle which quite plainly corresponds with the normal business sense of the community. That principle is that salaries, whether original or additional, fees derived in the course of one's employment, and wages are quite plainly revenue items and are therefore not to be capitalised and taxed on the capitalisation basis. On the other hand, however, option contracts bought for a valuable consideration are clearly, in the ordinary sense of the word, capital transactions. I do not think that anyone would suggest that a self-employed shareholder was taxable under Schedule D for profits which he might derive from having allotted to him as a shareholder a certain number of shares at a price well below the market value which he sold on the Stock Exchange at the market value. It is a well-known and frequent transaction in these days, and I believe—and it certainly has not been contended to the contrary before me—that the profit on such a transaction is not taxable, under Schedule D at any rate, because it is not an income item. Nor is it a revenue item. It is a capital profit. Of course, Schedule E cannot be dealt with in that way because it includes something which is not in Schedule D, namely perquisites. However, as I have already said, I do not think that a perquisite is to be treated as changing its whole nature and character merely because it is brought into the box in an omnibus provision dealing with salaries and wages. In my judgment, the next thing that the Court has to do if the thing is a perquisite—and I have held that it is—is to see what is the nature of the animal, to adopt a

(1) 37 T.C. 289. (2) Forbes's Executors *v.* Commissioners of Inland Revenue, 38 T.C. 12.

phrase which Counsel used himself, and I think he is quite right there. The only thing which I think he is wrong about is that he says it has got to do it with blinkers on. I do not agree with that view. You have to look at the nature of the animal by applying the ordinary principles of English law—and I emphasise at the moment the word "English". Looking at this transaction it may be that I shall be entitled to say—but I have not reached that point yet—that it is the sort of transaction which ought to be capitalised and taxed on the basis of a *chose in action* and not on the basis of a salary. If that is not so it seems to me that Mr. Heyworth Talbot's argument would necessarily fail, and it is only because I have come to the conclusion that it is so that I have not called upon him to reply. If, of course, in another Court my distinction is held to be invalid, all points would be open to Mr. Heyworth Talbot, because I should certainly have called on him to reply if this point had been put before me by Counsel for the Crown—but it was not—and if I had not been convinced that if it had been put before me I should not have accepted it.

The distinction, in my view, is this: is this additional salary, or is it a perquisite and something which is not income in any sense, except that it has been derived by virtue of the taxpayer's employment with the company? If it is that then, in my view, it gets out of the category of the *Bearsley*(1) line of cases and gets into another category.

Before I go further with that matter I want to deal at considerable length with the case of *Forbes's Executors*(2). It is important in this Scottish case to realise what the document was upon which the question was raised. I will read from the Case and not from the headnote because one very important feature of the contract is not mentioned in the headnote. Paragraph II (vii) of the Case reads:

> "On 18th September, 1944, a new minute of agreement was agreed and executed between Watt Torrance, Ltd., of the first part, Watt Torrance Woolwich, Ltd., of the second part and Mr. Forbes of the third part. The eleventh clause of this agreement"

—and that is what does not appear in the headnote—

> "provided that: 'So long as Mr. Forbes remains the Managing Director of the Company [i.e., Watt Torrance, Ltd.] and of the Woolwich Company he shall have the right to apply for and to be allotted shares of any denomination up to the number of Ten thousand in either or each of the companies on payment in cash of the nominal or par value of the shares applied for'."

Now, what have we in *Forbes's* case? We have an option for the first time, but I do not think that is the decisive factor. However, we have the eleventh clause of the service contract, and that, in my view, is the decisive factor. We also have a factor which, if not decisive, is important, namely that the employee did not have to pay anything for this option. He had to render services under his service contract. It seems to me that this Scottish case is plainly a case of additional remuneration and that it falls into the group to which Jenkins, L.J., referred(3). For my own part, if this case of *Forbes's Executors* had come before me in an English Court I have little doubt that I should have reached the same conclusion as the Scottish Court reached, but I should not have reached that conclusion upon the same grounds as the Scottish Court's grounds. If I had done it at all I should have done it upon the grounds which I have already stated, that we are here concerned with additional remuneration and that it is impossible to treat additional remuneration on a different basis from what I might call the primary or principal remuneration—if it is in truth remuneration—whether additional or otherwise.

(1) 37 T.C. 289. (2) 38 T.C. 12. (3) *See* Bridges *v.* Bearsley, 37 T.C. 289.

(Roxburgh, J.)

That being so, I must state what I understand to be my relation to a Scottish case. In stating this I am quite certain that the Scottish Courts would be very anxious not to take a different view, because no one would be more angry than they would be if I told them how to construe a Scottish contract in the Scottish Courts. I want to say at once that in my view they have not done anything of the kind and have, in fact, deliberately disclaimed any such intention. I will read the passage when I read the judgments. It has been put to me that there is some sort of principle for construing contracts which can be built up out of these two authorities, and to that view I cannot assent. If any such thing had been contended I should at once have said that it could not weigh with me. May I explain why I say that. Of course the Income Tax Acts apply, with certain immaterial modifications, to both England and Scotland, and I have always recognised, and hope I shall always recognise, that I ought if possible to follow, if only as a matter of comity, the decision of a Scottish Court on the construction of the Income Tax Acts. Any contrary view would result in sending every case to the House of Lords where alone the question is open, because these principles that I am stating do not, I believe, apply to the House of Lords. However, I have always understood that not only are Scottish decisions not binding in England but that they are not followed, even as a matter of comity, where there is a possibility that Scottish law may differ from English law. In an Income Tax case there is a very special reason why that should be so. Under the general law, Scottish law is a question of fact, odd though that has always seemed to me to be, and it is the duty of the Commissioners and not the duty of the Judge to find facts. Therefore, if the Court, under an Income Tax appeal, had to be informed as to what the Scottish law was, the case would have to be remitted to the Commissioners if they did not find it, and I cannot imagine anything more absurd than remitting a case to the Special Commissioners in order to find as a fact what Scottish law is. Surely, however, the answer is this, that I do not take judicial notice of Scottish law because it is not my duty to apply it, except to the undoubtedly limited extent that they may have expressed a view on the construction of something in the Income Tax Acts. I am very anxious to say that because I am quite certain that what troubled the Lord President (Clyde) was the difficulty which I have already indicated. He did not adopt the way out that I have suggested, and he may ultimately tell me that that is not a good way out. He may suggest another, and may say: "This is the way out", but I am pretty certain that he was not blind to the real difficulty of this case. As I say, I do not take judicial notice of Scottish law, and I am certainly not bound to assume that it is the same as English law. Indeed, there is something in a very relevant passage which I am going to read which makes me think that it probably is different, although I am not holding as a fact that it is. Lord Russell, at the very heart of the case, says this, at pages 20–1(1):

> "*Prima facie*, therefore, it would seem that the obligation of the companies to allot shares to Mr. Forbes was dependent on the existence of a condition and was not enforceable until the condition was purified, viz., the delivery of cash representing the par value of the shares."

The word "purified", of course, is a word which is not in the English legal vocabulary. It is not a term of art in England but it obviously is a term of art in Scotland—obviously, I say, from that paragraph. Lord Russell has explained its meaning, but it seems to me to envisage some doctrine which, as far as I know, is quite alien to English law. Therefore I absolutely decline to assume that in approaching this contract it makes no difference that the Court which approached it was a Scottish Court and not an English Court.

(1) 38 T.C.

(Roxburgh, J.)

As I have already said, I should have decided this case in the same way that they did, but most certainly I should not have done so on the grounds stated by the Lord President. I need only stress once more that I am not for one moment suggesting that those grounds were not valid in Scottish law. I expect they were valid, and there is no reason to doubt it at all, but I doubt their validity in English law and I am entitled to do that. The *ratio decidendi* of that case was, in my view, a conclusion reached upon the construction of the contract, and the Lord President makes that as plain as could possibly be done at page 18(1). He says:

> "It may be that some forms of option could involve a pecuniary benefit from the moment that they are granted, but the option in this case in my opinion did not. For the option itself could not be turned to pecuniary account."

That shows perfectly plainly that the Lord President was not intending to lay down any general principle of construction applicable either to England or Scotland, but merely to construe the contract with which he was concerned. However, I cannot leave it there because there are certain propositions in his judgment which I should find very difficult to accept as an English Judge, and they are propositions of law. Whereas they may be excellent propositions of Scottish law, I am not satisfied that they are propositions of English law at all. He says, at page 17:

> "In my opinion the right which Mr. Forbes obtained on signing the agreement in 1944 was a right merely to apply for the shares: it gave him no right in or to any shares, for this could only emerge when he exercised his right and when he delivered to the company the par value of the shares he demanded."

I certainly assume that that is a proper statement of Scottish law but I cannot accept it as a proper statement of English law, which of course has been very much influenced, as I have taken pains to mention, by the reaction of the principles of equity upon the common law. It is true that it gave him no right in or to any shares—I am speaking now of the contract which the Scottish Court was construing—but according to English law it certainly did give him a right to some shares. That is indisputable. In England the right may be contingent or conditional, but it is none the less a right. The right in the Scottish case was plainly contingent or conditional. I think the right word would be conditional, but it was none the less a right. In Scottish law, apparently, that is not so because the right could only emerge when exercised. That is not so in English law; the right emerges from the contract giving the right, however many conditions there may be precedent to the obligation upon the other party to perform the contract. I feel bound to say that, because otherwise people will try to apply what is a proposition of Scottish law to the construction of English contracts.

Nor can I readily follow, for reasons which will appear later, why the non-transferability of that contract deprived the perquisite of all pecuniary value. Somewhat similar observations may perhaps be made as regards Lord Carmont's judgment(2). Sitting in an English Court I should have regarded the option contract as a complete conditional contract—by "complete" I mean complete as a contract but containing conditions. I could not have construed it, as Lord Carmont appears to have done, as containing a continuing offer which did not give any rights until the continuing offer was accepted by the employee, not by accepting the contract but by exercising the option. It will be seen that he does do that and I need not read the whole of his speech. However, sitting here I should have construed it as a contract for value to allot shares upon application and payment for the shares. That is a very common transaction.

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(1) 38 T.C. (2) *Ibid.*, at p. 19.

(Roxburgh, J.)

Then there is the passage in Lord Russell's speech(1) to which I have already referred and which so clearly seems to reflect some Scottish doctrine. Sitting as an English Judge, I could not accept it as a proposition of English law. My view of the benefit of this option contract is that it is not to be assimilated to and is not additional remuneration. It is a *chose in action* which the employee was enabled to purchase, because of his employment, on beneficial terms, and that is why it is a perquisite. None the less, it is not in my view in any sense remuneration for his services. I have not heard before of any employee having to pay for his own remuneration, and that is why I think this £20 is so important. It is not the amount, it is the effect. Who has ever heard before of an employee paying for his own remuneration, whether it is additional or anything else? In fact, that feature is absent from every case which has hitherto been decided on this topic. After all, it might have been a dead loss, the opposite of additional remuneration. The figure here was £20 and the shares went up. What they have got to now I do not know, but at least we know that they did go up to 82*s*. Therefore, of course, it did enable a profit to be made. However, the shares might have conceivably gone down until the company went into liquidation, and then the £20 which had been spent, so far from being additional remuneration, would have been a dead loss. Nor can you say that it was only £20. It might have been £20,000 and exactly the same principle would apply. It cannot possibly be treated as additional remuneration, as far as I can see. In my view it was a perquisite and it was a perquisite which could be turned to pecuniary account.

Now, how could it have been turned to pecuniary account? It would have been necessary to exercise the option by applying and paying for shares at some time within the period permitted by the option contract. That was in fact done, and I cannot regard the doing of acts expressly or impliedly required by the option contract itself in order to exercise the option in any other light than as turning the benefit of the *chose in action* to pecuniary account. Moreover, the pecuniary profit could easily have been obtained and could hereafter be obtained as long as the option is still subsisting, without transferring the *chose in action* in this manner. The company's employee, in this case Mr. Abbott, having made an application for a number of shares and having paid for them at the rate of 68*s*. 6*d*. per share, could, before any shares had been allotted to him, have sold those shares to a purchaser at a higher price. We know that a higher price was in fact available, because these happen to be shares which are marketable and the price went up to at least 82*s*. If the company had said, "Oh no, no, no—we refuse to allot direct to your purchaser"—I doubt whether they could have said it, but supposing that they had said it—that is not the end of the matter. That is a very common situation and it happens quite often, especially in private companies. The effect would then be that the vendor, the employee, would have to take the shares up as trustee for the purchaser and, subject to getting any consents to transfer, if any, that might be necessary—I have no evidence before me upon that—he would immediately transfer the shares to the purchaser. If the company for some reason refused to register the transfer the only result would be that the vendor would continue indefinitely to be trustee for the purchaser unless and until the company was willing to register the transfer accountable to the purchase and entitled to be indemnified by the purchaser under the general law of trusts. I do not know whether Scottish law is different in that respect. It may well be. If so, I can quite understand why the Lord President arrived at the conclusion that the *chose in action* could not be turned to pecuniary account. However, if the law in Scotland is the same as the law in England—and I say

(1) 38 T.C., at p. 20.

it may well not be because the law of trusts is not always the same in Scotland—then all I can say is that perhaps no one suggested this method to the Lord President. I put it to Counsel, and I put it deliberately, in case there was a flaw in it. No one, however, has suggested any flaw; and to my mind there is no flaw, as far as I know.

It would therefore have been possible for Mr. Abbott to realise it if he had wanted to. I dare say he did not, but that is not the point. The point is whether it could be realised, not whether it was realised. If Mr. Abbott had gone into Bristol Stock Exchange he could have realised a profit on these shares without the slightest difficulty very soon after the option. It is not necessary that the profit should be capable of realisation within the year of assessment. If it were, this case on its facts might present some difficulty because of the necessity of obtaining Treasury consent. Putting that aside, however, he could, immediately after the acceptance by him of the contract, have put in an application form and he would have been in a position to carry out the transaction I have indicated the next day. The only bar, if any, to that transaction, as I see it, was the necessity for the company to obtain Treasury consent.

I may say in passing that I think it must follow that if the *chose in action* was a perquisite received in the tax year 1954–55, and as it consisted of the benefit of the contract to have allotments of shares on certain terms, the shares when allotted could not be taxed in another year as a new or different perquisite or profit. At any rate no such contention has been put before me. Any other view of the proper method of dealing with the option contract would have curious results. The price paid—although, in fact, it was only £20, it might have been £20,000—was for an option to acquire from time to time during a period of years not more than 2,000 shares. Why is the price apportionable, as the Case suggests? This question is not material because of what I have held, but, on the other footing, why would it be apportionable, as the Case suggests? There might never be another exercise. I am, of course, only aware of the facts in the Case. It is possible that it has been further exercised, but there might never be a further exercise, in which case that would presumably be because it is not worth exercising. In other words, the price is not above 68*s.* 6*d.* If that be so, why should not the whole price, whatever it be—£20 or £20,000—be set against the realised profits? On the other hand, it may be exercisable again two, three or more times, in which case it might be that the cost price would have to be apportioned. However, the true position which would have to be known in order to make a proper apportionment could not be known until the option was fully exercised or had expired. As I say, that comment on apportionment is the *obiter dictum* which I promised, because in my view the Special Commissioners were wrong and the benefit of the option contract was a perquisite which fell to be taxed in the financial year 1954–55.

It does not fall to me on this appeal to indicate whether it can be taxed, owing to difficulties of valuation, and, if so, upon what principle it ought to be valued. Those are matters which will only arise if and when some assessment is raised in respect of the year 1954–55. Accordingly I allow the appeal and, as far as I know, with costs.

Mr. Desmond Miller.—That would be suggested, my Lord.

Mr. Roy Borneman.—And it would not be opposed.

Roxburgh, J.—Is there any question of adjusting the assessment?

Mr. Borneman.—I think your Lordship should remit the Case to the Commissioners to adjust the assessment in accordance with your Lordship's judgment.

Roxburgh, J.—I will do that but I am afraid you may have to pay the costs.

Mr. Borneman.—Certainly. We have already said so.

The Crown having appealed against the above decision, the case came before the Court of Appeal (Lord Evershed, M.R., and Sellers and Harman, L.JJ.) on 2nd, 5th and 6th October, 1959, when judgment was given unanimously in favour of the Crown, with costs.

Mr. Roy Borneman, Q.C., and Mr. Alan Orr appeared as Counsel for the Crown, and Mr. F. Heyworth Talbot, Q.C., and Mr. Desmond Miller for the taxpayer.

Lord Evershed, M.R.—This appeal is concerned with the question whether the Respondent in this Court, Mr. Abbott, is in respect of the tax year 1955–56 liable for a certain sum under Schedule E of the Income Tax Act, 1952. As may happen in these cases, Mr. Abbott was the Appellant named in the Case Stated; he is now the Respondent, and for avoiding confusion I shall refer to him as "Mr. Abbott" or "the taxpayer", and to the other party as "the Crown".

For the year of assessment in question, the relevant statutory provisions are contained in the Income Tax Act, 1952. Section 156 of that Act imposed (under the heading "Schedule E") a charge for tax in respect of every employment of profit and made applicable thereto the provisions of the Ninth Schedule to the Act. So far as relevant that Schedule provides:

> "Tax under Schedule E shall be annually charged on every person having . . . an . . . employment of profit mentioned in Schedule E . . . in respect of all salaries, fees, wages, perquisites or profits whatsoever therefrom for the year of assessment",

after making the deduction indicated.

In the course of the argument both in this Court and below the subject-matter alleged to be taxable for the year I have named in Mr. Abbott's case has been called a perquisite, and I will, as Roxburgh, J., did, use that convenient description. But in order that a "perquisite therefrom", that is from the employment, for the year of assessment should be taxable it must have also an additional quality. That quality has been stated in the House of Lords by both Lord Halsbury, L.C., and Lord Watson in *Tennant* v. *Smith*, 3 T.C. 158. Lord Halsbury, at page 164, said in reference to the corresponding tax provision:

> "I come to the conclusion that the Act refers to money payments made to the person who receives them, though, of course, I do not deny that if substantial things of money value were capable of being turned into money they might for that purpose represent money's worth and be therefore taxable."

Lord Watson's language was not much different, and as it has been perhaps more often cited I will read it. It is as follows(1):

> "that word"

—that is, profits—

> "in its ordinary acceptation appears to me to denote something acquired which the acquirer becomes possessed of, and can dispose of to his advantage, in other words money, or that which can be turned to pecuniary account."

I can therefore restate the problem in this case as follows. It is whether during the year I have mentioned, 1955–56, Mr. Abbott was rightly charged in his assessment in respect of what was for that year said to be a perquisite arising from his employment, being something which was capable of being

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(1) 3 T.C., at p. 167.

turned to pecuniary account. As will presently appear, the advantage which he reaped in that year, or at any rate put himself in a position to reap, had its origin 18 months further back, and a great deal of the argument, very rightly, has turned on this: assuming there was here a perquisite, whether that perquisite arose to Mr. Abbott not in the year for which he has been assessed but 18 months earlier when he acquired a right from which sprang the later advantage. That sufficiently perhaps introduces the necessary recital of facts.

Mr. Abbott is—at least, I assume he still is; he certainly at all material times was and had been for some time—the secretary of a public company in Bristol associated with the name of Robinson. In the year 1954 the directors of that company came to the conclusion that it would be to the advantage of the company, and I dare say of those they employed in responsible positions, if they gave to those persons I have just described certain options to take up shares. There were available not less than 250,000 unissued shares in the company, and the scheme was that Mr. Abbott and other responsible officers should get options to take up at any time during the next ten years, provided they remained in the service of the company, a certain number of those unissued shares which for the purpose were created ordinary shares. The number of shares any individual servant was entitled to have depended, I gather, upon his status in the company, but in Mr. Abbott's case the number of shares to which he was to be entitled, if he wished to take them up, was 2,000.

Now I have used, and incorrectly used, the word "gave" when I earlier described the directors' scheme. In actual fact the option offered to Mr. Abbott was offered for a pecuniary consideration, namely £20, and we were informed, and indeed it appears from the papers in the Case, that that figure represented £1 per 100 shares; and the corresponding sums paid, I assume, by other officers of the company were similarly calculated. If it were necessary to reach any precise conclusion upon the matter it might be relevant to consider at some length the actual documents which came into existence and to arrive at a conclusion when the contract of option exactly was made, in what documents its terms were contained, and what is its date. The argument in this case has relieved me of any necessity of that kind. The relevant date for the purpose of the option contract may be taken as being 7th October, 1954. Owing to the necessity of obtaining Treasury sanction, there was delay before a certificate certifying that Mr. Abbott had this option could be given to him, but 7th October I take as the date because that was the date of the form which Mr. Abbott signed accepting the suggestion of taking up this option contained in the company's letter of the previous day, and which he accompanied by sending £20 to the company. The letter of 6th October contained at some length the terms of the option, but for convenience I will refer to the terms and conditions as they appear on the back of the certificate when it was later issued—later for reasons which I have already indicated. There were certain other qualifications beyond the one I am going to read, but for present purposes they can be ignored. The important condition or conditions are contained in the first clause in the terms:

> "The Option is not transferable and to the extent not previously exercised will expire upon the holder's death or retirement, upon his service with the Company and/or its subsidiaries ending, or on the tenth anniversary of the date of grant of the Option, whichever first occurs."

Mr. Abbott, as I have said, took advantage of what the company had suggested. He paid £20 to the company, and from 7th October he became entitled to take up 2,000 of the unissued shares in Robinson's at any time within the period indicated in clause 1 endorsed on the certificate, and to do so at the market price at which those shares stood on 7th October, 1954, which was 68*s.* 6*d.* Mr. Abbott did not immediately take up any shares, but in the month

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of March, 1956, the shares having risen on the Bristol stock exchange to the market price of 82*s.*, or 13*s.* 6*d.* above what I will call the option price, Mr. Abbott took advantage of his rights. He filled in an application form in respect of 250 out of his 2,000 shares, and he accompanied that application form by his cheque for £856 5*s.*, which is 68*s.* 6*d.* multiplied by 250, and he had issued to him 250 of these shares worth then, as I have indicated, 82*s.* per share. It is that event which has brought down upon him the charge of the Inland Revenue, for it has been their case that, when Mr. Abbott exercised that contractual right under the option and when as a consequence he obtained for £856 5*s.* a number of shares which were worth £1,025, he then and in respect of that year got from his employment a perquisite—as that word is expanded by Lord Halsbury, L.C., and Lord Watson[1]—a perquisite worth the difference between £856 5*s.* and £1,025, with a slight further deduction which was rightly or wrongly permitted in respect of a proportionate amount of the option price of £20. Put in simple terms, he was for his Income Tax liability for that year charged in respect of £166 as being the monetary value of the perquisite which was said, and is said, he in that year obtained. Relating my original statement of the question to the facts, is the Crown's claim to tax Mr. Abbott under Schedule E in the sum of £166, arrived at as I have indicated, justifiable or not justifiable in accordance with the relevant language of the Income Tax Act, 1952?

The facts of the case are of course fully narrated in the Case Stated, but I have thought it convenient and useful to make a short summary of them as a foundation to what immediately follows; for it seems to me right that I should at this stage briefly state what I conceive to be the nature of the rights in the eye of the law and their source both in October, 1954, when Mr. Abbott got his option, and in March, 1956, when he applied for and obtained his 250 shares. The option was a right founded in contract and, as Roxburgh, J., observed, of a proprietary nature: it was a right which Mr. Abbott obtained no doubt because he was the secretary of the company. Subject to the conditions which were attached to its exercise, he became thereafter as a matter of right entitled within the limit of time stipulated to apply for any number up to 2,000 of this block of unissued shares, and to pay for them the price of 68*s.* 6*d.* at which they stood when the option came into existence. It is quite true that the option was expressed to be non-assignable, though there was no limitation on what dealings Mr. Abbott might make with any shares which he acquired by virtue of the option. But though it was non-assignable it was said, and said with some force, that none the less the option when it was granted and immediately it was granted was capable of being turned to money account. What, if anything, Mr. Abbott might have obtained in any dealings that he entered into is a matter on which there is no evidence and might be purely speculative. I should assume, although again there is no evidence about it, that the grant of these options had an attraction to those to whom they were granted on the footing that there was at any rate a fair prospect that the shares in the Robinson company would appreciate in the future. As a matter of common sense it was not likely that Mr. Abbott would pay £20 unless he had at any rate some hope that thereafter he would reap some reward. The legal rights in the option were not transferable. He could not transfer the right to apply to anybody else. But as has been pointed out in the argument, and what is plain enough, Mr. Abbott might have been able to find someone who was prepared to pay to Mr. Abbott some monetary consideration on the terms that Mr. Abbott would thenceforth wholly or in part exercise the option as the third person required and when he required. To that

(1) *See* Tennant *v.* Smith, 3 T.C. 158, at pp. 164 and 167.

extent therefore, as I have indicated, it must be said that the option, if it had any inherent value, was capable of being turned to money account.

I have already said that the grant of the option to Mr. Abbott no doubt depended upon the fact that he was, and was a reward for the fact that he was, secretary of the company; and so Mr. Heyworth Talbot has throughout conceded that the grant of this option did constitute a perquisite of Mr. Abbott's office; and if, but of course only if, the option was of a value when it was granted greater than the price Mr. Abbott paid, greater than £20, and if, as I am assuming, it could have been turned to money account one way or other for a sum in excess of £20, then as Mr. Talbot concedes the perquisite would have had the necessary quality to make it then assessable under Schedule E for Income Tax. But it was Mr. Heyworth Talbot's argument on that footing that no subsequent appreciation in the value of the option or of any rights that could be acquired by its exercise could thereafter constitute some other taxable subject-matter.

That brings me to the second question: what was the nature of the rights Mr. Abbott obtained in March, 1956, and whence were they derived? The former question is not, I think, difficult to answer. He obtained for £856 5*s.* the issue of shares worth £1,025. That advantage, that valuable asset, Mr. Abbott was able to obtain because he had by virtue of the contract of option a right to get it so long as he complied with the conditions and paid the 68*s.* 6*d.* per share. The company was bound to issue those shares notwithstanding that their then present value was in excess of the price Mr. Abbott paid. Whence then did that benefit or advantage arise? I have already said that *prima facie*, as it seems to me, it arose because Mr. Abbott had an already existing contractual right to get it; but no doubt it is equally true to say, looking further back, that that contractual right was related to the origin in 1954 of its grant, namely to the circumstance that Mr. Abbott was then and still remained secretary of the company. That I conceive to be the nature of the rights which on those two dates Mr. Abbott obtained.

Now, if Mr. Heyworth Talbot's submission is correct, then the perquisite once and for all was obtained by Mr. Abbott in October, 1954. Anything that happened later is irrelevant for tax considerations. On the other side, the argument of the Crown has been that the option, particularly having regard to its non-transferability, was something not capable of being called a perquisite, or at least not a perquisite within the meaning of Schedule E, in October, 1954; it was something incomplete and imperfect. But, say the Crown, when the option, and to the extent to which the option, 18 months later, was exercised, then, and then for the first time, Mr. Abbott did get in truth a perquisite which can and should be related to his employment as secretary, and it is on that footing that liability for the year 1955–56 was alleged.

The case on the face of it would appear not very difficult; the point may at least be simply stated; but quite properly we have had our attention drawn to certain cases, to the third of which, a Scottish case(1), I shall have to refer at greater length because in the view I take that case ought to be decisive in this Court. But we were first of all referred to *Weight* v. *Salmon*, 19 T.C. 174. I shall indeed refer to it very briefly because it serves rather as illustration of the kind of point that arises than as any direct authority in the present case. The substance of the matter was this, that a certain company at an appropriate directors' meeting of each year, feeling a debt to those who managed its affairs, resolved that certain of its officers if they liked to apply should then be entitled to have

(1) Forbes's Executors *v.* Commissioners of Inland Revenue, 38 T.C. 12.

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allotted to them at par a certain number of shares in the company. The officers in many cases took advantage of that suggestion, applied for shares, had them allotted to them and obtained in the event shares which were worth at the date of allotment considerably more than par value. It was there held that the officers did then get a perquisite, namely the excess in value of the shares which they got attributable to and arising from their office, and were taxable accordingly. I observe that in that case there is no grant of any precedent right. The offer is made, it is accepted, it all occurs within the scope of a short period and certainly within a single tax year.

A little more important, but again, as I think, not conclusive in the present case, is *Bridges* v. *Bearsley*, 37 T.C. 289. The facts of that case were somewhat unusual. The respondent Bearsley and another gentleman (for there were two cases tried at the same time) had been for many years directors of a certain company, the control of which belonged to a Mr. Hornby. When Mr. Hornby died he left his controlling shares in trust for his widow for life and thereafter to his two sons. There was no gift to either Mr. Bearsley or his colleague of shares nor any grant to them of an opportunity of acquiring them. Mr. Bearsley and his colleague obviously took the view that if they were going to continue to serve this company they wanted, at any rate, some proper security in the way of further shareholding, and the end of it all was that in December, 1945, the two Hornby sons entered into deeds of covenant with Mr. Bearsley and his colleague. The arrangement as recorded in the deeds—and it was somewhat loosely framed—was that if Mr. Bearsley and his colleague continued to serve the company for another four years, then at a short interval after the death of Mrs. Hornby the two Hornby sons would transfer free of any consideration to Mr. Bearsley and his colleague certain shares. Time passed, because Mrs. Hornby lived to a considerable age; and eventually, before in fact she died, and to that extent in advance of any covenanted obligation, the two Messrs. Hornby did transfer to Mr. Bearsley and his colleague the requisite shares. A charge was made against both Mr. Bearsley and his colleague on the footing that the value of the shares which they had got for nothing should be taxed as perquisites of their offices as directors for the year when they received them. It was claimed, among other things, on their behalf that that was the wrong approach, that you should look to the date of the covenant, and if they were chargeable at all Mr. Bearsley and his colleague should be charged at that date, for it was from that covenant that sprang the later transfers.

I have dealt a little at length with the facts because much reliance has been placed upon the way in which Danckwerts, J., at first instance and Jenkins and Sellers, L.JJ., in this Court dealt with the point I have last mentioned. It was Danckwerts, J.'s view that these gentlemen were taxable under Schedule E for the year in which the transfers were made and in respect of the value of the shares. As regards the suggested alternative basis of taxation, namely that they should be charged, if at all, at the date when the covenants were entered into, he, Danckwerts, J., as I understand his judgment, at pages 305–6, said in effect: "No, the covenants were really a promise that if they served four more years at £*x*, then at the end of that period and as additional remuneration for the next period they would get this added benefit"; as though, to take a simple example, you are employed at £1,000 a year for four years and £6,000 for the fifth year. This Court by a majority, Jenkins, L.J., dissenting, decided that Mr. Bearsley and his colleague were not taxable at all, on the ground that you could not really relate these gift shares to the contract of service: in truth it was nothing other than generous bounty on the part of the two Hornby sons, and as such

not liable to Income Tax assessment. But Jenkins, L.J., at pages 316–7(1), affirmed the view which Danckwerts, J., had taken in regard to the alternative suggested assessment, namely an assessment at the time of and on the basis of the value then existing, if any, of the deeds of covenant in December, 1945. In other words, he followed Danckwerts, J., in thinking that the deeds constituted merely a promise of future additional remuneration and you could not treat the covenants themselves as a distinct item, a separate perquisite capable of being turned to pecuniary account and taxable as such for the year 1945–46. Sellers, L.J., dealt with it more briefly by the phrase(2):

> "It is not, in my view, in harmony with the tax provisions that if the transactions fell within the terms of Schedule E the income was the value of the rights acquired by the Appellants when the deeds were entered into",

and he too expresses concurrence with Danckwerts, J. The third member of the Court, Morris, L.J., was silent upon this point.

Now that case, upon those facts, is plainly different in many ways from the present. This is admittedly not a case merely of bounty. The option is, as I have indicated, a contractual proprietary right which was obtained in 1954. It was not a mere promise of future remuneration, as were the deeds in *Bearsley's* case(3) in 1945. But the idea of future additional remuneration is one that emerges in Roxburgh, J.'s judgment in the present case when he deals with the third and most important of the three cases, namely the Scottish case of *Forbes's Executors* v. *Commissioners of Inland Revenue*, 38 T.C. 12. I have already indicated that my view is that we should in this Court follow the decision in *Forbes's* case, and Mr. Heyworth Talbot conceded clearly in his argument before us that on its essential facts this case is not distinguishable from *Forbes's* case. That being so, I shall not deal at too great length with the facts in *Forbes's* case. It is sufficient to say that, as in the present case, there was first granted an option and then at a later date the option was exercised. As in this case, the question arose, was the grantee of the option liable to be charged in respect of a previous year for the value of the shares which Mr. Forbes had got when he had exercised the option? The option again is in essential respects similar to that in the present case. It was limited in time, it was subject to Mr. Forbes continuing as a director of the named companies, it was non-transferable. One other distinction may be made, a distinction to which Roxburgh, J., I think, attached importance, but to which, if I may say so, rightly, Mr. Heyworth Talbot did not himself attach significance. In the present case Mr. Abbott paid £20 for his option. In the case of *Forbes*, Mr. Forbes paid nothing. There is perhaps just this further point to be made, though for present purposes I conceive it to be irrelevant: in Mr. Abbott's case there was no sort of limitation or restriction on what he, Mr. Abbott, might choose to do with any shares he took out. It was, I assume, contemplated that if, as has happened, they increased in value he might wish to realise the profit. There was no restriction in terms in *Forbes's* case, but as the general purpose of the transaction was in order to enable Mr. Forbes to acquire a share control, it was obviously not in fact contemplated that he, Mr. Forbes would sell, or would at any rate sell to any appreciable extent. But, as I have said, in considering the rights and the legal consequences I cannot think that that matter is relevant, and it has not been suggested in argument that it is.

Those being the essential facts, indistinguishable, as I think and have said, from those in the present case, what was the conclusion of the Scottish Court? The conclusion was twofold. The Court of Session held that because of the restrictions on dealing with the option, its non-transferability and so forth,

(1) 37 T.C. (2) *Ibid.*, at p. 327. (3) 37 T.C. 289.

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the option, when granted to Forbes, did not fall within the scope of Schedule E because it had not the necessary quality expressed in the passages from Lord Halsbury, L.C.'s speech and Lord Watson's speech(1) that it could be turned to pecuniary account. Having arrived at that conclusion, the opinion of the Lord President (Clyde) proceeded, at page 18(2), as follows:

> "From this it would follow that it is only in 1946, when Mr. Forbes applied for allotment, paid the par value and received shares which he could have sold at a profit in the market, that tax under the Rules becomes exigible."

He then deals with a suggestion that it was at the date of the option that the legal right had vested in Mr. Forbes in respect of which, if at all, he was liable to assessment.

> "The argument for the Appellants was that in 1944 a legally enforceable right had vested in Mr. Forbes when he signed the agreement, which he could have converted into cash forthwith by securing an allotment of shares which he could sell in the market".

As to that he says there are two fallacies.

> "In the first place, the right which Mr. Forbes got under the agreement was not a right to shares which sounded in money but a mere right to apply for shares which he never exercised in that year and which in itself had no market value at all. But in the second place the right which he obtained under the agreement was not an unconditional one. He could not effectively exercise it unless he complied with its conditions, one of which was the payment to the companies of the par value of the shares applied for. These two considerations appear to me to point necessarily to the year 1946 when the right was effectively exercised as the year in which the profit accrued."

I need not, I think, read further passages, except perhaps to refer briefly to an earlier part of the Lord President's opinion, where he says, among other things, at page 17:

> "Moreover—and this appears to me to be fatal to the Appellants' contention—there was no pecuniary value in the mere right which he got by virtue of the agreement. For it was not a right to any shares and could not be disposed of or sold by him."

The opinions of Lord Carmont and Lord Russell were to the same effect. I read only a passage, at page 21, from Lord Russell. He states the appellants' contention and says:

> "In my opinion, whatever may be the rights vested in the holder of an option in the abstract, it is essential to have regard to the nature and the quality of the right created in Mr. Forbes's favour in 1944. As previously stated, that right was personal and unassignable and was qualified by the condition that he must tender cash in payment, while still remaining managing director, before being in a position to enforce compliance by the companies with their conditional obligation to allot. It appears to me that the latter contingency coupled with the personal and unassignable nature of the right prevents it from being something which could be 'turned to pecuniary account'"

—words which appear in quotes and which are, of course, taken from Lord Watson's formula—

> "unless and until the right was exercised and the condition purified."

It follows therefore that in *Forbes* the Court of Session decided two things. They first decided that an option having the essential characteristics of Mr. Abbott's option had not itself the necessary quality at the date of its grant to make it a perquisite within Schedule E liable to tax. They went on to hold, and from the language of the Lord President (Clyde) it may be said that they held as a consequence, that the option-holder was liable to be charged for the profit, the gain, the advantage he got when he turned to account, as he did, this option by getting by its exercise something worth a good deal more than he paid.

The basis of that reasoning has been severely and, if I may say so, by no means ineffectively impugned both in the Court below and in this Court. It

(1) Tennant *v.* Smith, 3 T.C. 158, at pp. 164 and 167. (2) 38 T.C.

is said that the Scottish Judges took altogether too narrow a view of the nature of the rights which the option gave to Mr. Forbes. More particularly it is said that the Judges omitted to notice the fact—obvious enough, as Mr. Heyworth Talbot said—that the holder of such an option could turn it to account, not by assigning the option itself, which he could not do, but by covenanting for a money consideration that he would exercise the option in a particular way and at a particular time as the covenantee required, and that had that fact been present to the Judges' minds they might well have concluded differently on the first point, and if so the second point would have fallen down. Mr. Heyworth Talbot has obtained for us copies of the report of the case in the Session Cases(1), and the argument of the appellants before the Inner House certainly does not make it plain that the point was taken by the appellants that, in the way I have indicated, Mr. Forbes could have turned to money account his option, albeit it was non-transferable. But for my part I think it difficult to say that the terms of the report of the argument are such as to exclude that argument, nor do I think really in the end of all it greatly matters. Apart from that form of transaction it is quite plain—and I cannot think that the Lords of Session could have failed to observe it—that the option-holder could have sold the shares before and not after he had exercised the option. But the fact is that the Inner House in the clearest terms have decided that an option in terms in all material respects identical with Mr. Abbott's option cannot be, at the date of its grant, brought into charge under Schedule E.

As I have already said, I am conscious, having attended to the arguments, of the difficulties which seem to me to present themselves upon that view of it. With the emphasis laid, as the Scottish Judges laid it, on the point of non-transferability, one may ask what would be the right answer if an option of this kind were granted which was transferable. Mr. Borneman, not unnaturally, was unwilling to commit himself to what would happen if such a case arose for consideration. But if the truth is that an option which was assignable would attract tax at the date of its grant, assuming that it had a bonus value which was calculable, then it would seem to follow as the night the day that the Crown could not afterwards seek to tax the benefit or the further gain which was achieved by the exercise of the option, and you would get a somewhat strange anomaly between cases where the option was expressed to be assignable and where the option was expressed to be non-assignable. Other somewhat similar cases might arise. Supposing, for example, a man acquires an option of this kind at a price in the market, being if you like a servant of the company but acquiring it in the ordinary course of commercial dealing. Nobody could then suggest, of course, that he was taxable at all either in respect of any value of the option when he bought it, or still less—at any rate as things now are—in respect of any capital gain which he got on the exercise of it wholly or partly thereafter; and, as Mr. Heyworth Talbot pointed out, what in its essence is the difference? Here Mr. Abbott got for £20 a right, and he later exercised that right and obtained a valuable asset. The answer, right or wrong, of course, is that in Mr. Abbott's case he only got the right because, being one of the valued servants of the company, the directors resolved that he should have it, and he would not otherwise have got it. But that still leaves unanswered the problem that if in truth it could be turned to pecuniary account and if so turned it was worth more than £20, then you should assess him in respect of the perquisite. If it was not at that time turnable to pecuniary account at more than £20, then that is the end of it, because thereafter it is merely a matter of capital gain.

(1) 1958 S.C. 177.

(Lord Evershed, M.R.)

My difficulties, I confess, do not end there, for I am troubled, with all possible respect to the Scottish Judges, by the line of reasoning which seems inherent in the passage I have read from the Lord President's opinion(1), that because the option when granted could not be turned to money account and for that reason is not taxable, therefore

> "it would follow that it is only in 1946, when Mr. Forbes applied for allotment . . . that tax under the Rules becomes exigible."

With all respect, I am not, I confess, satisfied of the logic of that statement. It may be—and I so put it because the Scottish Court has so held—that when Mr. Abbott got his advantage in 1956 it ought to be treated as attributable to something granted to him *qua* servant and therefore treated as a perquisite. But I find difficulty in thinking that the liability arises because the option when granted could not be turned then to pecuniary account. I also ask myself the question upon the footing of the Crown's case, what is it for which Mr. Abbott is being taxed? According to the Case Stated, there is included in his assessment the sum of £166 in respect of the share transaction, such sum being made up as follows: 250 shares taken up on 28th March when the actual market price was 82*s.*, £1,025: deduct option price, so much: net £166. The alleged perquisite, therefore, appears *ex facie* to be a share transaction entered into in March, 1956. The perquisite, in other words, is the gain represented by the fact that Mr. Abbott then got for £859 shares worth £1,025 and gained the balance of £166. I have said, and it is no doubt true to say, that Mr. Abbott's advantage which he got in 1956 was attributable, in a fair sense of words, to the fact that, having been a faithful servant, he had in October, 1954, been given an option contract which entitled him to do what he did, and to get the advantage he got in 1956. But I find nowhere in any contract or elsewhere any provision that, as a perquisite for that year, Mr. Abbott was entitled to get £166 or the difference between the value of any specified number of shares at their then market price of 82*s.* and the option price of 68*s.* 6*d.* Those are my doubts, and if my doubts are well founded they reinforce, at any rate, the view that what Mr. Abbott got in 1956 was a valuable piece of property, which he got because then he had, and had had for 18 months, an absolute contractual right to get it—qualified no doubt to the extent that he had still to be a servant of the company in order to enjoy it, but still attributable to a legal right granted to him 18 months earlier.

I have mentioned these doubts because I have thought that if this matter were to go further it might be of some assistance if I were to state them. I have also mentioned them because it is now right, I think, that I should say something about the judgment of the learned Judge, Roxburgh, J. The learned Judge in the end came to the conclusion that Mr. Abbott was not taxable in respect of the year 1955-56 for this sum of £166. He came to that conclusion, as I follow it, because, and largely because, Mr. Abbott had paid £20 for the option contract. After referring to Lord Russell's opinion(2) and saying that he cannot accept as a proposition in English law what Lord Russell formulated, he said(3):

> "My view of the benefit of this option contract is that it is not to be assimilated to and is not additional remuneration. It is a *chose in action* which the employee was enabled to purchase, because of his employment, on beneficial terms, and that is why it is a perquisite. None the less, it is not in my view in any sense remuneration for his services. I have not heard before of any employee having to pay for his own remuneration, and that is why I think this £20 is so important. It is not the amount, it is the effect. Who has ever heard before of an employee paying for his own remuneration, whether it is additional or anything else? In fact, that feature is absent from every case which has hitherto been decided on this topic. After all, it might have been a dead

(1) 38 T.C. 12, at p. 18. (2) *Ibid.*, at p. 20. (3) *See* page 100 *ante*.

(Lord Evershed, M.R.)

> loss, the opposite of additional remuneration. The figure here was £20 and the shares went up. What they have got to now I do not know, but at least we know that they did go up to 82*s*. Therefore, of course, it did enable a profit to be made. However, the shares might have conceivably gone down until the company went into liquidation, and then the £20 which had been spent, so far from being additional remuneration, would have been a dead loss. Nor can you say that it was only £20. It might have been £20,000 and exactly the same principle would apply. It cannot possibly be treated as additional remuneration, as far as I can see. In my view it was a perquisite and it was a perquisite which could be turned to pecuniary account."

What that, if I have followed it correctly, led to was this, that the learned Judge thought that when the option was granted (and in this he followed Mr. Heyworth Talbot's argument) then there was a perquisite granted to Mr. Abbott, but seeing that he had paid £20 for it and that there was no evidence that it was worth more and had never been turned to account for anything more at that date, it had therefore attracted no tax, and that was then the end of it. So far as what later occurred, the benefit of the shares, that, said Roxburgh, J., cannot be regarded as additional remuneration, as Danckwerts, J., and Jenkins, L.J., thought in *Bridges* v. *Bearsley*(1), because Mr. Abbott paid £20 for what he got, or for the source of what he got, and as Roxburgh, J., said, he might have paid £20,000 for it. At any rate, having paid for it, it cannot be treated as additional remuneration. The consequence, or one particular consequence, was that in the learned Judge's opinion the *Forbes* case(2) was rightly decided but on the wrong grounds, or at any rate on grounds which he as an English Judge could not accept. He, Roxburgh, J., took the view that Forbes or his executors were liable to the tax they were charged because in his case, he having paid nothing for the option, it was a matter purely of additional, albeit postponed, remuneration, as was suggested in the *Bearsley* case. He said he would have so decided *Forbes* himself had the matter come before him in England. But he felt that the grounds upon which the Lord President, Lord Carmont and Lord Russell decided it, though they might well be good grounds in Scots law, were not sustainable in English law.

As to that I am bound to say, with all respect to Roxburgh, J., that I cannot agree that the *Forbes* case could be supported on the ground that the shares when issued were additional remuneration comparable to the additional remuneration suggested to have been promised and granted in, for example, the *Bearsley* case. I am unable to agree with that. I think that what Mr. Forbes got was not additional remuneration which had been promised but something which he became entitled to get as a result of a valid and effective right, namely the option. But I am also, with all respect, unable to agree with Roxburgh, J., that the learned Judges in Scotland applied propositions of Scots law which have no application in England and which, therefore, leave us to decide this case without regard to the *Forbes* decision. I cannot see that there are any propositions of Scots law which form the basis of the decision and which are distinct from anything which we have to apply here. The question before the Scottish Court is the same as the question before us: was the sum of money for which Mr. Forbes was charged, and for which here Mr. Abbott is charged, representing the value of what he got, was that a perquisite within the meaning of the Schedule E provision; and as a prelude to that question, was the option granted to Forbes, as the option granted to Abbott, a perquisite liable to be charged within the meaning of the Schedule E provision? The Scottish Court purported to answer this latter question by applying the test which had been laid down in the House of Lords by Lord Halsbury, L.C., and Lord Watson(3). There was nothing esoteric in the bargains made. They were straightforward

(1) 37 T.C. 289. (2) 38 T.C. 12. (3) *See* Tennant *v.* Smith, 3 T.C. 158, at pp. 164 and 167.

(Lord Evershed, M.R.)

commercial bargains. That being their nature, it seems to me incontrovertible that what the Scottish Court decided was that an option in all relevant respects the same as Mr. Abbott's option cannot be turned to pecuniary account at the date of its grant, and therefore, whether or not it might otherwise be a perquisite, cannot be taxed at that date and in respect of that year, the year of its grant, under Schedule E. They further decided, whether consequentially or not, that when the rights given were exercised and brought, so to speak, to fruition, or to the extent that they were exercised and brought to fruition, then and in that year there did arise a perquisite which was capable of being turned to pecuniary account in the year when the exercise was made.

Those two things the Scottish Court has I think plainly decided. I ask myself, therefore, having expressed such doubts as I have, with all respect to the learned Judges in Scotland, ought this Court now to answer those two questions in a precisely opposite sense? It is of course quite true that we in this Court are not bound to follow the decisions of the Court of Session, but the Income Tax Acts apply indifferently both north and south of the Border, and if we were to decide those questions in a sense diametrically opposite to the sense which appealed to the Scottish Judges we should lay down a law for England in respect of this not unimportant matter which was completely opposite to the law which was being applied on exactly the same statutory provisions north of the Border. I cannot think that that is right. In a case of a revenue Statute of this kind I think it is the duty of this Court, unless there are compelling reasons to the contrary, to say, expressing such doubts as we feel we ought to do, that we should follow the Scottish decision.

I said a little earlier that Mr. Heyworth Talbot put forward an argument that we could treat the case as having been decided *per incuriam* mainly, if not entirely, on the ground that it was never brought to the attention of the Scottish Judges that, after all, this option, if it was worth anything, could have been turned to pecuniary account by the simple device of the option-holder's saying to whoever was interested: "For a consideration of £*x* I will exercise this option as and when you require and on your behalf". But I have not been satisfied that we could or should properly dissent and depart from the Scottish decision on that ground.

It comes therefore in the end to this, I think, that we ought to treat the Scottish case as governing our decision, and taking that view and disagreeing, with all respect, with Roxburgh, J.'s view that the Scottish decision depended upon some special peculiarities of Scots law, I would allow the appeal.

Sellers, L.J.—I agree, for the reasons which my Lord has just given, that the case of *Forbes's Executors* v. *Commissioners of Inland Revenue*(1) ought to be held by us to be decisive of the point raised before us in this present case. The question there for decision, in the words of Lord Russell in the course of his judgment(2), was

> "whether that perquisite accrued to and was acquired by Mr. Forbes at the date of the agreement, viz., September, 1944, or whether it accrued to and was acquired by him only when—and not before—he exercised his right and received an allotment of the shares in 1946."

The issue in that case seems to me to be indistinguishable from the issue in this case and the relevant and material facts likewise have no different effect. Secondly, with respect to Roxburgh, J., it seems to me that it is not shown that there is any difference in the law which the Inner House of the Court of Session invoked to decide that case from the law of our own country. Thirdly, the case

(1) 38 T.C. 12. (2) *Ibid.*, at p. 20.

was argued on all the points which were taken here and it would appear were all in the mind of the Court.

In those circumstances, I feel that we ought to accept that decision and follow it; and I may say that I do so with more satisfaction, perhaps, than my Lord because I take a more favourable view of the decision at which that Court arrived and do not share, at any rate not with the same emphasis, many of the doubts which my Lord has expressed. I do not wish to speak with finality because I apprehend that, having regard to the impact of the *Forbes's Executors* case(1) upon our decision, we discouraged Mr. Heyworth Talbot from pursuing the whole of his argument, but as far as it had gone I have not been persuaded that the judgments in that case were wrong. Indeed, as at present advised, agreeing with the judgments as a whole, I might particularly say I should have been prepared to follow the way in which the matter is put by Lord Russell, 38 T.C., at page 20 in the bottom paragraph and going on to the middle of page 21. If the option was never exercised it seems axiomatic that there would be no profit and no accrued benefit. The contractual right given by the company—and it was by the company to the servant, Mr. Abbott, in this case—could not be transferred, and the view I should be inclined to take of the case, which I think is in harmony with the *Forbes's Executors* case, is that that merely set up the machinery for creating a benefit—that was its intention—which benefit ultimately accrued. It is an ingenious device to avoid the incidence of taxation. In my view it does not achieve it, or at any rate it is doubtful whether it has achieved it. On the date of the option there was no money payment which was a gain. The £20 paid by the taxpayer was an expenditure. A notional use of the option or a use unintended and undesired by the company, the donor, unrealised and unvalued, does not seem to me to have the quality required by the accepted standard set by Lord Halsbury, L.C., and Lord Watson, already quoted by my Lord(2), to make it a taxable perquisite, if indeed it was a perquisite at all at that date.

Not only have we the authority of *Forbes's Executors* v. *Commissioners of Inland Revenue*, but the observations in this Court of Jenkins, L.J., agreeing with Danckwerts, J., as I did myself(3), I think, have been rightly assessed in the *Forbes* case by the Lord President when he says(4):

> "The observations to which I have referred confirm the conclusion to which I have come in the present case",

or in the words of Lord Russell(5):

> "Those opinions are clearly adverse to the Appellants' submission in this case".

It may be said in the particular circumstances that they were *obiter dicta*, but, in effect, I think they support the point on behalf of the Crown in their argument in this case.

For those reasons, and without going into the matter in greater detail, I agree that this appeal should be allowed on the basis of the decision in *Forbes's Executors* v. *Commissioners of Inland Revenue*.

Harman, L.J.—I agree in the result which my brothers have announced. I confess to sharing the doubt expressed with such circumspection, if I may say so, by the Master of the Rolls. The Lords of Session decided *Forbes's* case, as I see it, on a construction they put upon the option document there existing. No doubt that option, like the option in the instant case, was hedged about by a number of conditions; but I cannot see that the number of the conditions

(1) 38 T.C. 12. (2) *See* Tennant v. Smith, 3 T.C. 158 at pp. 164 and 167.
(3) *See* Bridges v. Bearsley, 37 T.C. 289. (4) 38 T.C. 12, at p. 19. (5) *Ibid.*, at p. 22.

(Harman, L.J.)

alters the nature of the right, nor understand why some options appear to their Lordships to come within Lord Watson's formula and others not. They all seem to me to be rights of property more or less valuable according as the conditions are more or less onerous. The Crown's contention here and the decision of the Lords of Session ignore altogether the option and treat the case as being in line with *Weight* v. *Salmon*, 19 T.C. 174, already mentioned by my Lord, where there was no antecedent agreement at all: see the observations of Lord Atkin at page 193. I find this hard to accept. On the other hand, I cannot justify to my mind Roxburgh, J.'s suggestion that the Lords of Session decided *Forbes's* case(1) on some unknown principle peculiar to Scottish jurisprudence. That Court, as I see it, construed a document of option indistinguishable from that in the instant case, and therefore for reasons of policy it would not be right that this Court should express a diametrically opposite view.

Mr. Roy Borneman.—Would your Lordship allow the appeal with costs?

Lord Evershed, M.R.—Have you anything to say about costs, Mr. Heyworth Talbot?

Mr. F. Heyworth Talbot.—I do not think any occasion for remission arises at this stage, my Lord, no, because Roxburgh, J., had allowed the appeal from the Commissioners. So your Lordships' decision just restores the decision of the Commissioners.

Lord Evershed, M.R.—Yes. Then do we order you to pay the costs here and before Roxburgh, J.?

Mr. Heyworth Talbot.—I think that follows, yes. I do not think there is any dispute about that.

Lord Evershed, M.R.—Sometimes I know there is some sort of concession made, but here the ordinary consequence follows?

Mr. Heyworth Talbot.—Yes. The appeal allowed with costs here and below, I think, meets the requirements of the case.

Lord Evershed, M.R.—Yes.

Mr. Heyworth Talbot.—Then I imagine your Lordships will not be surprised that I have been instructed to ask for leave to appeal to the House of Lords. I imagine that in the circumstances of the case you would not wish me to support the application with any argument?

Lord Evershed, M.R.—I imagine the Crown take the usual line?

Mr. Borneman.—My Lord, yes.

Lord Evershed, M.R.—I confess for my part I hope indeed that it will go there and that the House will tell us what the right answer is.

Sellers, L.J.—I agree with that, if I may say so.

Harman, L.J.—I agree.

Sellers, L.J.—May I raise one question? Ought not something to be allowed in the actual quantum for the costs of realisation? That is a matter that might be considered, I think, though it does not really arise here.

Mr. Heyworth Talbot.—The costs of realisation?

Sellers, L.J.—On the £166.

Lord Evershed, M.R.—Did you not have to pay a contract and Stamp Duty or something?

Sellers, L.J.—Supposing the difference is 13*s.* or whatever it is, you would not get that until you got your cheque from the stockbroker, would you?

(1) 38 T.C. 12.

Mr. Heyworth Talbot.—Yes, I see. I think that would be agreed; I do not think there would be any dispute about it.

Sellers, L.J.—I am not so sure that it would. Sometimes it might be a few pounds.

Lord Evershed, M.R.—You might think of that in case it is of any help. You might think that the Crown is or is not damaging its case by allowing you £2 10*s*.

Mr. Borneman.—Your Lordship will recollect that when I opened I said it had been done, but I could see many grounds upon which it should not have been done.

Mr. Heyworth Talbot.—I do not think my learned friend and I are likely to come to any acute controversy on these particular matters. Then I take it that the application for leave is granted?

Lord Evershed, M.R.—Yes, with enthusiasm, I might almost say.

The taxpayer having appealed against the above decision, the case came before the House of Lords (Viscount Simonds and Lords Reid, Radcliffe, Keith of Avonholm and Denning) on 2nd and 3rd May, 1960, when judgment was reserved. On 21st June, 1960, judgment was given against the Crown, with costs (Lord Keith of Avonholm and Lord Denning dissenting).

Mr. F. Heyworth Talbot, Q.C., Mr. R. O. Wilberforce, Q.C., and Mr. Desmond Miller appeared as Counsel for the taxpayer, and Mr. Roy Borneman, Q.C., Mr. Alan Orr and Mr. A. J. Mackenzie Stuart for the Crown.

Viscount Simonds.—My Lords, this appeal relates to an assessment to Income Tax under Schedule E of the Income Tax Act, 1952, made upon the Appellant for the year of assessment 1955–56 in respect of the emoluments of his office as secretary of E. S. & A. Robinson, Ltd., which I will call "the company". The Court of Appeal decided the case against him in deference to a decision of the Court of Session—*Forbes's Testamentary Trustees* v. *Commissioners of Inland Revenue*(1), 1958 S.C. 177. Your Lordships will find it necessary to review that case.

The facts are not in dispute. At the annual general meeting of the company held on 28th June, 1954, it was resolved that 250,000 of 290,319 unclassified shares of £1 each in the capital of the company be classified as ordinary shares, and that the directors be authorised to grant options over such shares, or any of them, to executives of the company or its subsidiaries at such times and generally on such terms and subject to such conditions as they should think proper.

Pursuant to this resolution, the directors of the company, at a board meeting held on 6th October, 1954, resolved that options, upon the terms contained in a draft letter then produced, to subscribe for ordinary shares in the company at 68*s*. 6*d*. per share (being the middle price ruling on the Bristol Stock Exchange on that day) be granted to the executives. The Appellant accordingly, as secretary of the company, sent to each of the executives, including himself, a letter, of which the salient conditions were that he was granted at the price of £1 for every 100 shares an option to purchase a specified number of shares at the price of 68*s*. 6*d*. per share, such option to be exercisable at any time within ten years from the date of the grant of the option. The option was

(1) Forbes's Executors *v*. Commissioners of Inland Revenue, 38 T.C. 12.

(Viscount Simonds)

expressed to be non-transferable, and was to expire upon the death or retirement of the executive (or employee, as I will call him) before the expiration of the ten years. If the employee desired to purchase the option he was required to send in a form of application (which accompanied the letter) together with his cheque for the price of the option, whereupon an option certificate would be issued to him. The Appellant, being included in the list as entitled to a grant of an option in respect of 2,000 shares, applied accordingly on 7th October, 1954, for such option, enclosing his cheque for £20 which was duly cashed. Some delay occurred in the issue of option certificates and he was not given his until 6th May, 1955, but it bore on its face the statement that the option was granted on 6th October, 1954. It was endorsed with the conditions as to the non-transferability and expiry to which I have referred. On 28th March, 1956, the price of the company's shares having then risen to 82*s.*, the Appellant exercised *pro tanto* his option by applying to the company for the issue to him of 250 shares at the price of 68*s.* 6*d.* per share, and sent with his application his cheque for £856 5*s.* The shares were duly issued to him. He was subsequently assessed to Income Tax under Schedule E for the year 1955–56 in, *inter alia*, the sum of £166, which was made up as follows:

	£ *s.*	£ *s.*
250 shares taken up on 28th March, 1956, when the middle market price was 82*s.*		1,025 0
Deduct: (1) Option price 68*s.* 6*d.*	856 5	
(2) Cost of option at £1 per 100 shares ...	2 10	
		858 15
		£166 5

The Special Commissioners upheld the assessment, considering the case indistinguishable from *Forbes's* case(1) to which I have referred. Roxburgh, J., if I understand his judgment, thought it possible to distinguish that case, and upon Case Stated allowed the present Appellant's appeal. The Court of Appeal, as I have already said, decided in favour of the Crown.

My Lords, once more your Lordships have to consider the words of Rule 1 of the Rules applicable to Schedule E contained in the Ninth Schedule to the Income Tax Act, 1952, which is as follows:

> "Tax under Schedule E shall be annually charged on every person having or exercising an office or employment of profit mentioned in Schedule E . . . in respect of all salaries, fees, wages, perquisites or profits whatsoever therefrom for the year of assessment . . .".

Summarily, the question is: Was the difference between (*a*) the market price on 28th March, 1956—£1,025—and (*b*) the option price—£856 5*s.*—plus a proportionate part of the cost of option, £2 10*s.*—a "perquisite or profit therefrom", that is, from the office of secretary held by him, for the year of assessment?

The curious feature of this case is that the Crown appear to reach the conclusion that the sum of £166 was assessable for the year 1955–56 by first denying that the grant of the option was itself a perquisite or profit of the year 1954–55, and this is, I think, the aspect of the case that must first be examined. For it would not, as I understand the argument of learned Counsel for the Crown, be contended that, if the grant of the option was itself a perquisite or profit arising from the office, the subsequent exercise of it would be another perquisite or profit.

(1) 38 T.C. 12.

(Viscount Simonds)

My Lords, I cannot entertain any doubt that, when the company granted the option to the Appellant, he acquired something of potential value. I do not think that it matters whether it falls into the category of proprietary or contractual right or into some dim twilight that divides those juristic conceptions. We are concerned with a taxing Statute whose language is to be reconciled with the law of England and Scotland alike, and the chosen words "perquisites or profits whatsoever" are as wide and general as they well could be. I can concede no relevant limitation of their meaning except in the oft cited words of Lord Watson in *Tennant* v. *Smith*(1), [1892] A.C. 150, at page 159, that they

> "denote something acquired which the acquirer becomes possessed of and can dispose of to his advantage—in other words, money—or that which can be turned to pecuniary account."

How, then, can it be said that an option to take up shares at a certain price is not a valuable, or at least a potentially valuable, right? Its genesis is in the desire of the company to give a benefit to its employees, and at the same time, no doubt, to enhance their interest in its prosperity. It is something which the employee thinks it worth his while to pay for: not a large sum, truly, but £20 deserves a second thought. And it is something which can assuredly be turned to pecuniary account.

This was challenged because the option was itself not transferable, but this objection is without substance. There was no bar, express or implied, to a sale of the shares as soon as the option was exercised, and there could be no difficulty in the grantee arranging with a third party that he would exercise the option and transfer the shares to him. It was further challenged on the ground (to quote the language of Sellers, L.J., in the Court of Appeal(2)) that

> "A notional use of the option or a use unintended and undesired by the company, the donor, unrealised and unvalued,"

does not have the quality required by the accepted standard set by Lord Halsbury and Lord Watson in *Tennant* v. *Smith* to make it a taxable perquisite, if, indeed, it was a perquisite at all at that date.

With great respect to the learned Lord Justice and to counsel, who put it in the forefront of his argument, I find great difficulty in giving any weight at all to this consideration. It is mere guesswork what use of the option was intended or desired. I would not myself assume that the company intended that the grantee of an option should for ever, or for a day longer than he wished, hold the shares that he took up, or that he should not at once, if he wished, reap the benefit of a rise in price. But, guess right or wrong, there is nothing to prevent him doing so: that is his legal right and, if he could so deal with the shares when acquired, nothing could prevent him so using his option by arrangement with a third party as to secure for himself a similar advantage. Two other adjectives were used by the Lord Justice, "unrealised" and "unvalued". But the fact that there was no realisation in the sense of actual turning into money is irrelevant. The test is whether it is something which is by its nature capable of being turned into money. Nor is it relevant that it is "unvalued". I have little doubt that, if the Revenue authorities had addressed their minds to the proper question, they could have ascertained whether it had any, and what, value. But again I must say that it is really irrelevant whether a value could be ascribed to it or not. If it had no ascertainable value, then it was a perquisite of no value—a conclusion difficult to reach since £20 was paid for it. In my opinion, the Crown cannot succeed in this essential aspect of the case unless it is established as a general proposition that an option to acquire shares at a fixed price in such circumstances as those of the present case is not a perquisite of office.

(1) 3 T.C. 158, at p. 167. (2) *See* page 113 *ante*.

(Viscount Simonds)

It must be shown that, even if at the date of the option being granted the market price is higher than the option price, the option is not a perquisite which falls within the Schedule. This appears to me an impossible proposition. What distinguishes such a right from that commonly given to a shareholder in a commercial company, when upon an issue of shares he is given, in the form of a provisional allotment letter, the right to take up new shares at a certain price? He can exercise his right and take up the shares, or he can sell his right to do so, or he can do neither and let the offer go by default. But from the moment he has the letter he has a right of more or less value according to the circumstances. So, too, the grantee of such an option as that which we are considering has a right which is of its nature valuable and can be turned to pecuniary account. He has something at once assessable to tax.

My Lords, as I have said, the argument for the Crown appeared to demand for its success that the grantee of the option did not acquire a perquisite at the date of the grant. There could not be one perquisite at the date of the grant and a second perquisite when the shares were taken up. Therefore, the Crown's case, in my opinion, fails at the initial step. But there are other grave difficulties in the way of its success. The taxable perquisite must be something arising "therefrom", that is, from the office, in the year of assessment. I do not want to embark on the notoriously difficult problem as to the year to which, for the purpose of tax, a payment should be ascribed if it is not expressly ascribed to any particular year. But I do not find it easy to say that the increased difference between the option price and the market price in 1956 or, it might be, in 1964, in any sense arises from the office. It will be due to numerous factors which have no relation to the office of the employee, or to his employment in it. The contrast is plain between the realised value, as it has been called, of the option when the shares are taken up (though the realisation falls short of money in hand) and the value of the option when it is granted. For the latter is nothing else than the reward for services rendered or, it may be, an incentive to future services. Unlike the realised value it owes nothing to the adventitious prosperity of the company in later years. On this ground also I should reject the claim of the Crown.

My Lords, as I have said, the Court of Appeal were constrained to decide this case in favour of the Crown in deference to the decision of the Court of Session in *Forbes*(1). I agree that the two cases are not in any material respect distinguishable, and I think that they took the proper course in following it. The single fact upon which Roxburgh, J., appeared to rely, that in that case, unlike this, the grant of the option was gratuitous, cannot in my opinion affect the issue. The reasoning by which the learned Judges in *Forbes* supported the conclusion to which they came is that which formed the basis of the argument for the Crown on this appeal, and I have already dealt with it. It treats the option as a thing of no value until it has been exercised and places an importance, in my opinion unjustified, on the non-transferability of the option. But, as I have pointed out, though that feature may reduce the value of the option, it cannot alter its character so that it is no longer something which can of its nature be turned to pecuniary account. Nor, even if it be the fact, can I accept the view clearly entertained by the Court of Session that, if in the year of grant the option had no value, it therefore became a taxable perquisite when in later years it was exercised. It was, in my opinion, a perquisite at the date of grant and, if it had no value, there was nothing to tax, and that is the end of the matter.

(1) 38 T.C. 12.

(Viscount Simonds)

Reference was also made to *Weight* v. *Salmon*, 19 T.C. 174. This case does not assist the Crown. The taxpayer, Salmon, was a managing director of a limited company at a fixed salary. In addition, the directors in each year gave him the privilege of applying for certain unissued shares of the company at their par value, which was less than the market value. He accordingly applied for shares and they were issued to him. He was assessed to tax on the difference between the par and market values, and the assessment was upheld in the High Court and the Court of Appeal. The taxpayer appealed to this House and his appeal was dismissed. Lord Atkin, with whom the other learned Lords agreed, pointed out that, while the board had expressed their willingness to entertain an application for shares, nobody was bound and no right was given, and no profit was received of any kind by the appellant until the application had been accepted and the shares in question had been allotted to him. It is by no means a decision that, if the company had vested in him a right to have the shares allotted to him instead of allotting them forthwith, that right would not have been a taxable perquisite or profit.

The facts in *Tait* v. *Smith*, 35 T.C. 79, are somewhat obscure, but the decision of Wynn-Parry, J., in that case appears, if anything, to be favourable to the Appellant.

In *Bridges* v. *Bearsley*, 37 T.C. 289, there are to be found observations of Danckwerts, J., and Jenkins, L.J., which support the contention of the Crown. But the substantial issue in that case was whether shares which had been issued to the taxpayer were or were not profits of his office. The question whether the profit lay in the right to acquire shares or in the shares when acquired was a subsidiary issue which in the event did not arise. If, as I think they probably were, the relevant facts of that case were indistinguishable from those of the present case, I must with respect decline to follow them.

Upon a consideration of the whole case I am of opinion that this appeal should be allowed with costs here and below.

Lord Reid.—My Lords, in 1954 the company of which the Appellant is secretary offered to its executives options to buy a number of its unissued shares at 68*s.* 6*d.*, which was then the market price. The options were not transferable and were to endure for ten years if the purchaser remained so long in the company's service. The price of the option was £1 per 100 shares, and in October, 1954, the Appellant acquired an option on 2,000 shares for which he paid £20. The market price rose and in March, 1956, when the price was 82*s.*, the Appellant exercised his option to the extent of 250 shares and acquired them at 68*s.* 6*d.*, If he had immediately sold those shares he would have made a profit of £166, and he has been assessed in this sum under Schedule E in the year 1955–56. Rule 1 of the Rules applicable to Schedule E provides that

> "Tax under Schedule E shall be annually charged on every person having or exercising an office or employment of profit mentioned in Schedule E, or to whom any annuity, pension or stipend chargeable under that Schedule is payable, in respect of all salaries, fees, wages, perquisites or profits whatsoever therefrom for the year of assessment, after deducting the amount of duties or other sums payable or chargeable on the same by virtue of any Act of Parliament, where the same have been really and bona fide paid and borne by the party to be charged."

The parties agree that the Appellant received something which comes within the words "perquisites or profits whatsoever". The question in this case is what it was. The Appellant says that the option was the perquisite, and he admits that he was liable to be assessed for the year 1954–55 in respect of the value of the option when it was granted, minus the price he paid for it. He maintains that the subsequent appreciation of its value is not taxable. On the

(Lord Reid)

other hand, the Crown maintain that he received no perquisite in 1954, the perquisite being the shares which were allotted to him when he exercised his option: if that is right, the shares when allotted were worth £166 more than he paid for them and he has been properly assessed.

The first observation which I would make is that, on the Crown's view, the granting of the option in 1954 might result in ten different perquisites being received by the Appellant in ten different years if he chose to exercise his option piecemeal. He was entitled to do this and in fact in 1955–56 he only exercised it to the extent of 250 out of 2,000 shares, and the company retained no control over the times at which, or the extent to which, he might exercise the option. If he did not exercise the last of his option until 1964–65 he would then, in the Crown's view, be receiving a perquisite taxable in that year in consequence of an irrevocable act of grace of the company ten years earlier. If in 1965 he held 2,000 shares which he had acquired in ten different parcels under his option, he would have made precisely the same profit on each share—the difference between 68*s.* 6*d.*, the price under the option, and the then market price. But he would have been taxed very differently in respect of each parcel, the tax depending on the market price at the date when he had acquired it, for it is not suggested that further appreciation after shares have been allotted can be taxed. Moreover, let me suppose that the option had been exactly the same except that it was to last for ten years whether the Appellant remained in the service of the company or not. It could hardly be that that change so completely altered the nature of the option as to change the basis of taxation and make the granting of the option, and not the issue of the shares, the perquisite. If, then, it was exercised years after the servant had retired, what would the position be: would the issue of shares then be the perquisite, and for what year of assessment would it be a perquisite? There would be no assessment under Schedule E for the year in which the shares were issued because the servant had retired. I realise that one ought not to be surprised at anything that happens under the Income Tax Acts, but nevertheless all this does seem a little strange.

Both parties rely on *Tennant* v. *Smith*(1) [1892] A.C. 150, and in particular on the familiar passage in the speech of Lord Watson:

> "Is it, then, a perquisite or a profit of his office? I do not think it comes within the category of profits, because that word, in its ordinary acceptation, appears to me to denote something acquired which the acquirer becomes possessed of and can dispose of to his advantage—in other words, money—or that which can be turned to pecuniary account."

I agree that the question is whether this option was a right of a kind which could be turned to pecuniary account. I do not use these words as a definition, but it is undesirable to invent a new phrase if an old one of high authority fits this case, and the parties agree that it does. But the test must be the nature of the right and not whether this particular option could readily have been turned to pecuniary account in October, 1954. Whether this option could then have been turned to pecuniary account is a question of fact, and there is no finding about it. It is true that the option was not transferable, but there are other ways of turning such a right to pecuniary account than assigning it or calling for immediate performance of the obligation to allot the shares. Even taking this particular option, I find nothing to indicate that there would have been much difficulty in finding someone who would have paid a substantial sum for an undertaking by the Appellant to apply for the shares when supplied with the purchase money and called upon to exercise the option, and thereupon to transfer the shares. It is not an unreasonable inference from the whole circumstances

(1) 3 T.C. 158, at p. 167.

(Lord Reid)

that both the Appellant and his employers must have thought the option worth a good deal more than £20, and others may have thought the same. No doubt a person who wished to acquire an option on the shares would pay less for an undertaking such as I have indicated than he would pay for an assignable option because of the risks involved, but that only goes to valuation of the right which the Appellant acquired. And if it is asked, why buy such an undertaking instead of buying shares on the market, the answer is that people often do prefer buying options to buying shares. I am not prepared to assume, in the absence of a finding, that this option could not have been turned to pecuniary account when it was granted. But if there is any doubt about that, let me assume that the option had been to acquire shares at 10*s.* below the then market price. I cannot doubt that that could have been turned to immediate pecuniary account, and surely it could not be said that an option to buy at 58*s.* 6*d.* is itself a perquisite, but an option to buy at 68*s.* 6*d.* is not. And that was not argued.

The argument for the Crown was not based on any special difficulty in turning the particular option to pecuniary account. It was based on the nature of the right: it was said that a right of option does not have the necessary qualities to make it a perquisite. I must confess that I do not understand that. If in fact this type of option is a kind of right which can be turned to pecuniary account, what more is necessary to make it a perquisite? I have not been able to find any clear answer to that question in the authorities cited or from the argument in this case. It appears to me that if a right can be turned to pecuniary account, that in itself is enough to make it a perquisite. Then it was said that, if the Appellant had attempted in any way to raise money on his option before he exercised it, he would have been acting contrary to the tenor of his agreement with his employers. It was not argued that he would have been acting in breach of his contract with them—plainly he would not—nor was it said that there was any "gentleman's agreement" that he should not do this, or even that he would have incurred his employers' displeasure if he had done it. There is no finding to that effect. I am willing to assume that it would not be irrelevant to show that a servant could only exercise his full legal rights at the risk of impairing good relations with his employers, but I do not stop to consider what the position would then be. In this case it was not suggested that his employers would have thought it in any way improper if the Appellant had sold shares immediately they were allotted to him, and I cannot assume that they would have had any objection to his raising money on his option before he exercised it.

Then there appears to me to be another difficulty in the way of the Crown. Rule 1 of Schedule E taxes a person exercising an office or employment of profit

> "in respect of all salaries, fees, wages, perquisites or profits whatsoever therefrom for the year of assessment".

It does not say salaries or perquisites received during the year of assessment. It may be difficult to relate a perquisite strictly to a particular year. But if a reward is given in the form of an option and the option is itself the perquisite, it would generally be sufficiently related to the year in which it is given to be properly regarded as a perquisite for that year. If, on the other hand, the option is not the perquisite—if there is no perquisite until the option is exercised and shares are issued, it may be many years later—in what sense would the shares be a perquisite for the year when they were issued? There would be no relation whatever between the service during that year and the giving of the option many years earlier, or the exercise of the option during the later year. I do not wish to express any concluded opinion on this point, but it does seem to lend support to the conclusion which I have reached on other grounds.

(Lord Reid)

In the present case the Court of Appeal, though not bound to do so, very properly followed the decision of the Court of Session in *Forbes's Trustees*(1), 1958 S.C. 177. I say very properly because it is undesirable that there should be conflicting decisions on revenue matters in Scotland and England. So I must now examine the reasons for that decision. In that case Mr. Forbes, having been appointed manager, was granted by his company an option in 1938, which was repeated in a further agreement in 1944. This option was in all essentials similar to the option in the present case. The only distinction I need note is that the option in the 1944 agreement was to purchase a large number of shares at par, though the market price was then above par; and it was argued that the option gave Mr. Forbes an immediately enforceable right to the shares and that that right could have been converted immediately into cash. Mr. Forbes exercised his option in 1946, and he was assessed under Schedule E, as in this case, on the difference between the value of the shares when they were allotted to him and the price which he paid for them. This assessment was upheld by the First Division. The Lord President's grounds of judgment appear from two passages which I shall quote from his opinion—at page 183(2):

> "In my opinion, the right which Mr. Forbes obtained on signing the agreement in 1944 was a right merely to apply for the shares; it gave him no right in or to any shares, for this could only emerge when he exercised his right and when he delivered to the company the par value of the shares he demanded. Moreover—and this appears to me to be fatal to the appellants' contention—there was no pecuniary value in the mere right which he got by virtue of the agreement. For it was not a right to any shares and it could not be disposed of nor sold by him. . . . For the option itself could not be turned to pecuniary account."

And on the next page(3):

> "The argument for the appellants was that in 1944 a legally enforceable right had vested in Mr. Forbes when he signed the agreement, which he could have converted into cash forthwith by securing an allotment of shares which he could sell in the market. Accordingly, it is said, his benefit should be assessed for tax as a benefit accruing in the year 1944. But this argument appears to me to involve two fallacies. In the first place, the right which Mr. Forbes got under the agreement was not a right to shares which sounded in money, but a mere right to apply for shares, which he never exercised that year and which in itself had no market value at all. But, in the second place, the right which he obtained under the agreement was not an unconditional one. He could not effectively exercise it unless he complied with its conditions, one of which was the payment to the companies of the par value of the shares applied for. These two considerations appear to me to point necessarily to the year 1946, when the right was effectively exercised, as the year in which the profit accrued."

The Lord President also derived some assistance from *Weight* v. *Salmon*, 19 T.C. 174, and *Bridges* v. *Bearsley*, 37 T.C. 289.

The essence of the first passage which I have quoted appears to be that because the option could not be sold or assigned, therefore it could not be turned to pecuniary account. I have already given my reasons for not accepting that. The argument that a right could be turned to pecuniary account by raising money on it without assigning it does not appear to have been put forward, no doubt because the argument that it could be turned to pecuniary account by exercising it and taking up shares worth more than the option price may have seemed even stronger. That argument is dealt with in the second passage which I have quoted.

In the second passage the Lord President finds two fallacies in the argument for the taxpayer, but I am afraid I have been unable to see the force of his objections. If you get a share it is capable of being turned to pecuniary account because you can immediately sell it. There is generally no difficulty about that,

(1) 38 T.C. 12. (2) *Ibid.*, at pp. 17-18. (3) *Ibid.*, at p. 18.

and if there is any difficulty there are other ways of raising money on it though you have to remain on the register. Similarly, if you get an option to buy shares below the market price, it seems to me that the option is capable of being turned to pecuniary account by exercising it, acquiring the shares, and immediately selling them. It is true that that involves an extra step, but why should that matter? I can see no difficulty, unless it be in financing the transaction. But if the whole operation will yield a substantial profit I would not assume that that would be difficult. The second fallacy appears to be a variant on the first. If the condition is one with which the taxpayer can easily and immediately comply, it does not, in my opinion, form an obstacle to turning the option to pecuniary account. If the condition is one which cannot immediately be complied with, that may make a difference. In *Bridges* v. *Bearsley*(1) the taxpayer still had to earn his perquisite by a further four years' service, and it may well be that in such a case an agreement to confer a future benefit gives no immediate perquisite. The case of *Weight* v. *Salmon*(2) seems to me to be entirely different. There the servant had no enforceable right at all until he got his shares. He got his shares because the company chose to give him something then, to give him a perquisite when the shares were issued. But, in this case, the Appellant getting his shares did not flow from any voluntary act of the company when the shares were issued. It flowed from the company's voluntary act in the previous year, when they gave him an option by which they were thereafter bound. It would, I think, require some peculiar circumstances to make a mere expectation capable of being turned to pecuniary account.

Lord Carmont regarded the option as an open offer. I would not dispute about words. But if it can be regarded as an offer, it was an offer which the company had no power to withdraw and which conferred a valuable contractual right on Mr. Forbes. Lord Carmont then dealt with the restrictions and conditions to which the option was subject, and pointed out their material bearing on the value of the option and the difficulty there would be in valuing it. I agree with those observations. But if I am right, that the question whether a particular option is in itself a perquisite does not depend on these factors but rather on whether rights of that class are perquisites and capable of being turned to pecuniary account, then I do not think that these observations necessarily lead to his conclusion.

Lord Russell clearly stated his grounds of judgment in the following passage(3):

> "In my opinion, whatever may be the rights vested in the holder of an option in the abstract, it is essential to have regard to the nature and the quality of the right created in Mr. Forbes's favour in 1944. As previously stated, that right was personal and unassignable and was qualified by the condition that he must tender cash in payment, while still remaining managing director, before being in a position to enforce compliance by the companies with their conditional obligation to allot. It appears to me that the latter contingency, coupled with the personal and unassignable nature of the right, prevents it from being something which could be 'turned to pecuniary account' . . .".

I think that I have already dealt with the reasons which he gives, but I can sum up my view by saying that conditions and restrictions attached to, or inherent in, an option may affect its value, but are only relevant on the question whether the option is a perquisite if they would in law or in practice effectively prevent the holder of the option from doing anything when he gets it which would turn it to pecuniary account. I am therefore of opinion that *Forbes's Trustees* was wrongly decided and should be over-ruled, and that this appeal should be allowed.

(1) 37 T.C. 289. (2) 19 T.C. 174. (3) 1957 S.C. 177, at p. 187; 38 T.C. 12, at p.21.

Lord Radcliffe (read by Lord Reid).—My Lords, on 28th March, 1956, the Appellant applied for and received from E. S. & A. Robinson, Ltd., 250 of its ordinary shares. He paid the company £856 5*s.* for them, a subscription at the rate of 68*s.* 6*d.* per share, although the current market price was then 82*s.* per share. He was enabled to obtain this advantage because in October, 1954, he and other officials and employees of the company had been offered by it options to take up stated amounts of ordinary shares at the market price then ruling, 68*s.* 6*d.* per share, and he had thus acquired at the cost of £20, which he then paid for an option on 2,000 shares, the right to make this call at the date which he selected.

The Crown claim that he is assessable under Schedule E for 1955–56 on the difference between what he paid and the value of what he got, on the ground that this calculated amount is a profit or perquisite from his office. I do not think that he is. Oddly enough, however, the argument that took place before us was concentrated almost exclusively on a different point: whether he was assessable under the same Schedule on the value of the option itself in the year when he acquired it (1954–55), the Crown maintaining with much persuasive force that he was not; the Appellant conceding that he was, provided always that it could be shown that a monetary value could fairly be placed on the option at the date of its acquisition.

It is a natural enough assumption for the tax gatherer that if a transaction does not attract tax in one year it must in another. I do not myself, however, regard that as a good general principle upon which to found the construction of the Income Tax code. Considering that, at any rate since the decision of this House in *Tennant* v. *Smith*(1) [1892] A.C. 150, it has been necessary to put a somewhat restricted meaning upon the words "all salaries, fees, wages, perquisites or profits whatsoever" which now appear in the Ninth Schedule of the Income Tax Act, 1952, I should not be surprised to find that neither an option to take up shares at a price, more particularly perhaps if the option is made non-assignable, nor the advantage obtained later from exercising the option, comes within the range of those words. On the whole, however, I do not think that that is the situation, because in my opinion the Appellant is right in saying that what taxable receipt there is lies in the acquisition of the option and that, if it had a monetary value when received, it is that value that represents the profit or perquisite of the office.

The difficulty in dealing with this point lies wholly in relating words used by several members of the House in *Tennant* v. *Smith*, apparently of general import, to circumstances that they were not dealing with. The benefit of a right of occupation of part of bank premises which the occupier could only enjoy for the service of the bank is not very like the benefit of an option to take up freely transferable shares at a fixed price. The basis of the Crown's claim in *Tennant* v. *Smith* was really to tax the bank manager on expenditure which he was saved, not on any money that he got, or could get, while tax on the full annual value of the premises was taken from the bank itself. It was not, however, the view of the House that profits or perquisites, to be taxable, could consist only of money paid. It was accepted that they could include objects or things of value received, payments in kind, so long as they were

> "capable of being turned into money" [Lord Halsbury, L.C.], . . . "money—or that which can be turned to pecuniary account" [Lord Watson], . . "money payment or payments convertible into money" [Lord Macnaghten], . . . "That which could be converted into money" [Lord Hannen].

I think that it has been generally assumed that this decision does impose a limitation upon the taxability of benefits in kind which are of a personal nature,

(1) 3 T.C. 158.

in that it is not enough to say that they have a value to which there can be assigned a monetary equivalent. If they are by their nature incapable of being turned into money by the recipient they are not taxable, even though they are in any ordinary sense of the word of value to him. It is obvious that this conception raises many attendant uncertainties which are not, so far as I know, cleared up except where some particular class of benefit in kind has offended the eye of the Legislature and has been dealt with by special legislation. Must the inconvertibility arise from the nature of the thing itself, or can it be imposed merely by contractual stipulation? Does it matter that the circumstances are such that conversion into money is a practical, though not a theoretical, impossibility; or, on the other hand, that conversion, though forbidden, is the most probable assumption?

I do not think that the decision of this case can go very far, if any distance, to clear up such points as these. I think that the Crown are right in saying that a line has to be drawn somewhere between convertible and non-convertible benefits and that somehow we have to put a general meaning on the not very precise language used in *Tennant* v. *Smith*(1). What I do not think, however, is that a non-assignable option to take up freely assignable shares lies on that side of the line which contains the untaxable benefits in kind. The option, when paid for, was thereafter a contractual right, enforceable against the company at any time during the next ten years so long as the holder paid the stipulated price and remained in its service. That right is, in my opinion, analogous for this purpose to any other benefit in the form of land, objects of value, or legal rights. It was not incapable of being turned into money or of being turned to pecuniary account within the meaning of these phrases in *Tennant* v. *Smith* merely because the option itself was not assignable. What the option did was to enable the holder, at any time at his choice, to obtain shares from the company which would themselves be pieces of property or property rights of value, freely convertible into money. Being in that position he could also, at any time at his choice, sell or raise money on his right to call for the shares, even though he could not put anyone he dealt with actually into his own position as option holder against the company. I think that the conferring of a right of this kind as an incident of service is a profit or perquisite which is taxable as such in the year of receipt, so long as the right itself can fairly be given a monetary value; and it is no more relevant for this purpose whether the option is exercised or not in that year than it would be if the advantage received were in the form of some tangible form of commercial property.

The claim to tax the advantage obtained in the year 1955–56 is not claimed by the Crown if the right view is that the option itself was taxable in 1954–55. Even if there were no taxable subject in the earlier years, I should regard the 1955–56 claim as failing on its own terms. The advantage which arose by the exercise of the option, say £166, was not a perquisite or profit from the office during the year of assessment: it was an advantage which accrued to the Appellant as the holder of a legal right which he had obtained in an earlier year, and which he exercised as option holder against the company. The quantum of the benefit, which is the alleged taxable receipt, is not in such circumstances the profit of the service: it is the profit of his exploitation of a valuable right. Of course, in this case the year of acquiring the option was only the year immediately preceding the year in which, *pro tanto*, it was exercised. But supposing that he holds the option for, say, nine years before exercise? The current market value of the company's shares may have changed out of all recognition in that time, through retention of profits, expansion of business, changes in the nature of the

(1) 3 T.C. 158.

(Lord Radcliffe)

business, even changes in the market conditions or the current rate of interest or yield. I think that it would be quite wrong to tax whatever advantages the option holder may obtain through the judicious exercise of his option rights in this way as if they were profits or perquisites from his office arising in the year when he calls the shares.

I agree that the appeal must be allowed. As to previous authorities, I am of opinion that, for the reasons I have given, *Forbes's Trustees* v. *Commissioners of Inland Revenue*(1), [1958] S.C. 177, was decided in error. I do not regard either the decision of, or any observations in, *Bridges* v. *Bearsley*, 37 T.C. 289, as being of any significance to the point we have to decide.

Lord Keith of Avonholm.—My Lords, this case may be presented so as to raise some interesting and possibly fine legal points. I think it does. But I have come to the view that these arise by considering certain aspects of the case in isolation, and that this is not the proper approach to the question at issue. The object of the option under consideration was to afford certain selected executives of the company and of its subsidiary companies

> "an opportunity of obtaining an interest in, or increasing an existing interest in, the capital of the Company",

as stated in the company's letter of 6th October, 1954. There is nothing novel in such an idea and, as the authorities show, the issue of shares to employees of a company may, in certain cases, attract tax under Schedule E as being a perquisite or profit from the employment. The simplest case would be a free bonus issue or transfer of fully paid shares, unless this could be related, as in *Bridges* v. *Bearsley*, 37 T.C. 289, to some cause other than remuneration for service in the company.

The specialty in the present case is that the matter started with the grant of an option to subscribe at 68*s.* 6*d.* a share for 2,000 ordinary shares of £1 each in the capital of the company. For this the Appellant paid the sum of £20, a somewhat illusory price of rather less than two pence halfpenny per share on the number of shares over which the option extended. The option was subject to certain terms and conditions. Among others it was not transferable and, so long as the Appellant was in the company's service, it would last for ten years. As Lord Carmont pointed out in *Forbes's Trustees* v. *Commissioners of Inland Revenue*, 1958 S.C. 177; 38 T.C. 12, in my opinion correctly, such an option is no more than a standing personal offer. An offer open for ten years is certainly something unusual, but in Scots law, if expressed in writing, it could not be challenged and would not be revocable. In English law it may be that some element of consideration is required to prevent such an offer being withdrawn, and this may be the reason for the offer in the present case taking the form of an option for which a nominal payment was made. In my opinion, no element of consideration should make any difference, in applying a taxing Statute common to the two countries, to the determination of the nature and effect of the right granted.

The argument for the Appellant is that though the option is not transferable, it left it open to him to turn it to account by agreeing with some third party, in return for a payment, to exercise the option and to transfer the shares, or some part of them, obtained as a result of that exercise to the third party. Clearly the same could be done in the case of a simple revocable offer of shares made on the same terms and conditions. But, in my opinion, the argument introduces a quite irrelevant consideration. Whatever happens, the Appellant has got to apply for shares before any benefit or transferable right emerges. Whatever

(1) 38 T.C. 12.

(Lord Keith of Avonholm)

value the option has comes only from its exercise, and on its exercise the benefit offered to him arises. The option is an offer, to be accepted or not as and when the Appellant pleases, but until it is accepted the transaction is not complete, nor has any profit been realised. The company has no concern with third parties, before the Appellant gets his shares. When he gets his shares it will be seen what profit he has got from his acceptance of the company's offer. Even if he has made some advance arrangement with a third party, it is what he has got from the company in shares that, in my opinion, determines the profit to which he is taxable under Schedule E.

It is conceivable, though I should think unusual, that a company should offer its employees shares, in the form of bonus shares fully paid or for payment on favourable terms, which offer was freely transferable or renounceable in favour of third parties before allotment. That would merely emphasise the favourable nature of the offer, and would in no way impinge on the principles to which I have referred. No one can be put on the share register of a company without his consent. If an employee failed to take up the shares offered or to renounce them in favour of a third party, he could not, in my opinion, be said by virtue of the mere offer to have obtained a profit from his employment. If he renounces his shares in favour of a third party he has accepted, or taken advantage of, an offer made to him by his employer, and by selling his rights he has in effect secured a benefit equivalent to what he would have received if he had applied for the shares to be registered in his own name. I assume always that the renunciation would be for a genuine and not for a fictious price. The result, in my opinion, assuming it could be regarded as a profit of the employment, would be in no way different in principle from that of *Weight* v. *Salmon*, 19 T.C. 174. Though that case was presented as a case of a privilege given to the servant of applying for shares, it is clear from Lord Atkin's speech in this House, concurred in by all their other Lordships, that it was only upon the application being granted by the issue of shares that a profit was regarded as having been received by the servant. Nor is it material, in my opinion, that the offer of shares is at a price which, if accepted, will show an immediate profit, as where the market value of the shares is higher than the offer price. Until accepted, or otherwise dealt with in accordance with the terms of the offer, the offer cannot, for the reason I have given, be regarded as securing for the servant a profit from his employment. It follows, also, that the same option offered to a number of employees at the same time may have different results in the case of individual employees, if it is, as here, a continuing option, according to the respective dates when it is accepted. That follows from the nature and terms of the offer and the action that the particular servant takes upon it. The result is entirely consistent with a general rule of Income Tax law that there can be no profit until it is realised, or can be quantified. I find it unnecessary to speculate on the precise scope or effect of the references by Lord Halsbury and Lord Watson in *Tennant* v. *Smith*[1], [1892] A.C. 150, to a benefit received by an employee from his employer capable of being "turned to pecuniary account" in order that it should be assessable to Income Tax. Their application must be considered in relation to the kind of benefit received in specific cases. They were made in a context which does not make their scope easily definable. They cannot be confined to tangible or corporeal benefits, otherwise a share in a company would not come within their scope. The *dicta* are not, however, in my opinion, of any help to the Appellant, because the normal and, I think, in a case like this, the only way of turning an option, or offer, to pecuniary account is by exercising or accepting it.

(1) 3 T.C. 158.

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If it is exercised, as it was here, the benefit then accrues and, if capable of being valued in terms of money, is assessable to tax.

Under Schedule E no difficulty arises in the matter of relating a profit to a particular fiscal year. Under Rule 1 of the Ninth Schedule it is the year of assessment in which the profit is received that determines the rate of tax. It is common ground here that there has been a profit of the employment, and the only question is whether that profit is to be extracted from the grant of the option *per se* or from the exercise of the option. On either view it is impossible to relate the profit to any year other than the year of receipt. The benefit, however it is estimated, was no doubt given in respect of past services, and possibly in the expectation of future services, but further than that it is impossible to say. The situation, as I see it, is shortly summarised by Sellers, L.J., in words which I would adopt(1).

> "If the option was never exercised" [he says] "it seems axiomatic that there would be no profit and no accrued benefit. The contractual right given by the company—and it was by the company to the servant, Mr. Abbott, in this case—could not be transferred, and the view I should be inclined to take of the case, which I think is in harmony with the *Forbes's Executors* case, is that that merely set up the machinery for creating a benefit—that was its intention—which benefit ultimately accrued."

I would only add that a transferable option, if transferred, might produce corresponding results, for the reasons which I have endeavoured to explain, though it is unnecessary so to decide for the purposes of this appeal.

I would dismiss the appeal.

Lord Denning.—My Lords, when I asked Mr. Heyworth Talbot in the course of the argument whether there was any special virtue in the sum of £20 which Mr. Abbott paid for this option, he said there was no particular merit in it. If the sum had been one shilling or one penny, the result would be the same. It was a nominal sum, he said, which was paid so as to provide consideration for the contract and make it legally enforceable. But it soon appeared that it was essential to his argument that there should be some consideration given for the option, even if it was only, as Sir George Jessel once suggested, a tomtit or a canary. For Mr. Heyworth Talbot acknowledged that, if no consideration had been given, then, unless the option were granted under seal, it would have been unenforceable at law: with the result that the case would have been governed by *Weight* v. *Salmon*, 19 T.C. 174. Now, in *Weight* v. *Salmon*, as your Lordships will recall, the directors of a company passed a resolution that each of the three managing directors

> "be permitted to make application for and to take up at par one thousand 'A' ordinary shares in the capital of the Company."

The managing directors, in pursuance of that resolution, acquired for £1 apiece shares which were worth £3 or £4 each in the market. It was held by this House that, when the directors received those shares, and not before, they received profits in the nature of money's worth as remuneration for their services. The shares, when received, were "profits" on which they were taxable under Schedule E. That case shows decisively that the expectation of receiving a benefit, no matter how well founded, is not itself a perquisite or profit. It must be reduced into possession. A bird in the hand is taxable, but a bird in the bush is not. So here, if nothing had been paid for the option, the letters that passed would have been nothing more than a standing offer by the company to allot shares to Mr. Abbott at 68*s.* 6*d.* a share. That offer could have been withdrawn by the company, at any time before acceptance, with impunity. The offer itself would not be a perquisite or profit, for it conferred only the expectation of profit, not any profit itself. But when it was accepted, and shares worth 82*s.* apiece were

(1) *See* page 113 *ante*.

(Lord Denning)

allotted to Mr. Abbott for 68*s.* 6*d.*, he would then receive "profits" which would be taxable in his hands. No difficulty would arise about the year of assessment. The profits would accrue to him in the year they were received.

My Lords, I ask myself, what is the difference, for tax purposes, between the case I have just put, where nothing is paid for the option, and the case we have before us, where a nominal sum is paid? The difference is that in the one case he has only an expectation of profit: whereas in the other he has a right to make profits in the future, if the opportunity arises. But in either case, until the option is exercised, he has not the profits themselves. And as I read the Act, it is not the expectation to make profits, nor the right to make profits, which is taxable, but only the profits themselves; just as it is not the expectation to salary, nor the right to salary, which is taxable, but only the salary itself. A bird in the bush is not taxable, even if you have the right to get it in the future, if it is still there. You must have it in hand before you can be taxed on it. And when you come to consider what "profits" the servant receives from his employment by virtue of the option, surely it makes no difference whether he pays a nominal sum or not. In either case the employer grants him the option as a reward or return for his services, and the profits he makes out of it are the same save for this: if he paid nothing, it is all profit; if he paid a peppercorn, it is all profit less the value of a pepper berry; if he paid 1*s.*, less 1*s.*; if he paid £20, less £20.

There is, moreover, a very compelling reason why no distinction should be drawn according to whether a nominal sum is paid or not: for it would mean that "profits" in the Income Tax Acts would have a different meaning in Scotland from what it has in England. In Scotland, as your Lordships well know, it is unnecessary to have consideration to support a promise. The option would be legally binding in Scotland, even though nothing was paid for it, whereas it would not be binding in England unless some nominal sum was paid for it. It would not be right, I suggest, for the tax payable to depend on the technical requirements of English law as to consideration. The Income Tax Acts apply to England and Scotland alike, and there is the highest authority for saying that they must, if possible, be so interpreted as to make the incidence of taxation the same in both countries. See *Commissioners for Special Purposes of the Income Tax* v. *John Frederick Pemsel*(1), [1891] A.C. 531, at page 548 by Lord Halsbury, L.C., and at page 557 by Lord Watson; *Commissioners for General Purposes of Income Tax for City of London* v. *Gibbs and Others*(2), [1942] A.C. 402, at page 414 by Viscount Simon, L.C., at page 419 by Lord Macmillan and at page 430 by Lord Wright.

My Lords, the point which I am now making can be tested by taking an illustration which is suggested by what Lord Atkin said in *Weight* v. *Salmon*(3). Suppose that a colliery company made an offer to supply a director, who was in the coal trade, with 1,000 tons of coal at a price which was one-third of the market price of the day. No profit of any kind would be made by the director until he gave an order for coal. But as and when he ordered the coal and got it, he would receive a profit in the nature of money's worth. It would be assessed, said Lord Atkin, at the difference between the price he could get for it and the price he had actually paid. Now, take the same illustration but suppose that, instead of the company making an offer to the director, a clause was inserted in his service agreement giving him the right of obtaining coal at a price which was one-third of the market price of the day. Surely his profit would be just the same as before: it would arise as and when he ordered the coal and got it, and it would be assessed

(1) 3 T.C. 53, at pp. 71 and 76. (2) 24 T.C. 221, at pp. 243-244, 247 and 254.
(3) 19 T.C. 174, at pp. 193-194.

(Lord Denning)

at the difference between the price he could get for it and the price he actually paid. It would not be assessed differently simply because in the one case he made the profit as a result of a standing offer and in the other he made it under a service agreement. It will be noticed that, just as Lord Atkin's illustration corresponded very closely in substance to the facts in *Weight* v. *Salmon*,(1) so my illustration of a service agreement corresponds very closely in substance to the facts in *Forbes's Trustees* v. *Commissioners of Inland Revenue*(2), 1958 S.C. 177: and it leads me to the conclusion that that case was correctly decided. And it is indistinguishable from the present case, as everyone agrees.

But Mr. Heyworth Talbot took a further point. He likened the grant of this option to the gift of a physical thing such as a diamond, or a *chose in action* such as an issue of shares, to a servant as a reward for his services. The value of it has to be assessed, he said, for tax purposes at the time of the grant, and it is immaterial that its value should rise or fall afterwards. But I would point out those are all interests in property and they are very different from purely personal rights such as this option. Take the issue of shares on which Mr. Heyworth Talbot so much relied. It is clearly an interest in property. Baron Parke said that

> "the shareholder acquires, on being registered, a vested interest of a permanent character, in all the profits . . . of the Company, and when registered, may be deemed a purchaser in possession of such interest",

[see *The Birkenhead, Lancashire, and Cheshire Junction Railway Co.* v. *Pilcher*, (1850) 5 Ex. 114, at page 125]—and shares are now, by Statute, personal estate (see Section 73 of the Companies Act, 1948). So also with any other right which is by its nature assignable, such as a bill of exchange or a "rights" issue of shares. It is in the nature of an interest in property. It can be valued at the time it is given to the servant and assessed accordingly. But a purely personal right stands on a very different footing. The right of a servant to his salary or wage is a purely personal right. So is his right to a bonus or commission. Suppose that a company in a service agreement agrees to pay the servant a bonus of 10 per cent. of the net profits whenever the net profits overtop £10,000. The servant, before he gets the bonus, may be able to turn it to pecuniary account in just the same way as it is suggested that he can turn this option to pecuniary account: for he might get someone to pay him something for it, by means of the simple expedient of undertaking to hand the bonus over to him when he gets it. But nevertheless he is only taxable on the bonus when he receives it. And if this be so, what is the difference, I ask, between giving a servant a right to a share of the profits when profits rise, and giving him a right to take up new shares when shares rise? For, after all, shares rise with profits. I can see no difference in principle at all.

There remains to consider *Tennant* v. *Smith*(3), [1892] A.C. 150. That case showed that a right or privilege which cannot be turned to pecuniary account is not taxable at all. It does not prove the converse. It does not prove that a right or privilege which can be turned to pecuniary account is taxable. In any case, I doubt myself whether this option could be turned to pecuniary account, at any rate at the moment when it was given. There was no evidence that it could be done. The option, as I have said, was purely a personal right: Mr. Abbott could not sell it. But it was suggested that he could agree with a third person that he would exercise it for his benefit on his request, and in return the third person would give him money. I should have thought it very difficult to get a third person to do this. There is, so far as I know, no market in options which are purely personal to the holder. But even if the option could be turned to pecuniary account in such a devious way, I do not think it should be regarded

(1) 19 T.C. 174. (2) 38 T.C. 12. (3) 3 T.C. 158.

as taxable. It was, as I have said, only a right to make profits in the future, if the opportunity arose. It was not itself a perquisite or profit.

My Lords, in all the cases hitherto when a servant has been granted by his employer a purely personal right to receive in the future a benefit during his service, the Judges have with one accord held that he receives the "perquisite" or "profit" when the thing is actually transferred to him and not before. So said Danckwerts, J., in *Bridges* v. *Bearsley*(1), [1957] 1 W.L.R. 59 at pages 68–9, and both Jenkins and Sellers, L.JJ., agreed with him on this point, see [1957] 1 W.L.R. 674 at pages 689 and 703(2). So said all the Judges in *Forbes's Trustees* v. *Commissioners of Inland Revenue*(3), [1958] S.C. 177. And I must say that I agree with them. It is the same point as I have insisted on throughout. Tax is not payable on the right in the future to receive "salaries, fees, wages, perquisites or profits", but only on those things when received.

I would therefore dismiss this appeal.

Questions put:

That the Order appealed from be reversed and the judgment of Roxburgh, J., restored.

The Contents have it.

That the Respondent do pay to the Appellant his costs here and in the Court of Appeal.

The Contents have it.

[Solicitors:—Allen & Overy; Solicitor of Inland Revenue.]

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(1) 37 T.C. 289, at p. 306. (2) *Ibid.*, at pp. 316-317 and 327-328. (3) 38 T.C. 12.