The Society's appeal was heard in the House of Lords (Lords Keith of Kinkel, Brightman, Oliver of Aylmerton, Goff of Chieveley and Lowry) on 11, 12, 13, 18, 19, 20 and 21 June 1990 when judgment was reserved. On 25 October 1990 judgment was given unanimously against the Crown, with costs.

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John Gardiner Q.C., *Nicholas Underhill* and *Jonathan Peacock* for the Society.

S.A. Stamler Q.C. and *Alan Moses Q.C.* for the Crown.

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The following cases were cited in argument in addition to the cases referred to in the speeches:—*Ayrshire Employers Mutual Insurance Association Ltd.* v. *Commissioners of Inland Revenue* 27 TC 331; 1946 SC 1; *Fry* v. *Burma Corporation Ltd.* 15 TC 113; [1930] AC 321; *Reid* v. *Reid* (1886) 31 ChD 402; *Lauri* v. *Renad* [1892] 3 Ch 402; *Kingsway Investments (Kent)*

A *Ltd.* v. *Kent County Council* [1971] AC 72; [1970] 1 All ER 70; *Dunkley* v. *Evans & Another* [1981] 1 WLR 1522; [1981] 3 All ER 285; *Potato Marketing Board* v. *Merricks* [1958] 2 QB 316; *Olsen* v. *City of Camberwell*; [1926] VLR 58; *Regina* v. *Secretary of State for Transport* ex parte *Greater London Council* [1986] QB 556; [1985] 3 All ER 300; *Thames Water Authority* v. *Elmbridge Borough Council* [1983] QB 570; *Director of Public Prosecutions* v. B *Hutchinson & Another* [1989] QB 583; [1989] 1 All ER 1060; *Grosvenor Place Estates Ltd.* v. *Roberts* 39 TC 433; [1961] Ch 148; *Vestey & Others* v. *Inland Revenue Commissioners* 54 TC 503; [1980] AC 1148; *Strickland* v. *Hayes* [1896] 1 QB 290; *Dyson* v. *Attorney General* [1912] 1 Ch 158; *Moore* v. *Austin* 59 TC 110; [1985] STC 673; *In re Lang Propeller Ltd.* 11 TC 46; [1927] 1 Ch 120 *Skinner & Another* v. *Cooper & Another* [1979] 1 WLR 666; [1979] 2 All C ER 836.

Lord Keith of Kinkel:—My Lords, I have had the opportunity of consid- D ering in draft the speech to be delivered by my noble and learned friend Lord Oliver of Aylmerton. I agree with it, and would allow the appeal for the reasons he gives.

Lord Brightman:—My Lords, I also have considered in draft the speech to be delivered by my noble and learned friend Lord Oliver of Aylmerton, E and for the reasons given by him would allow the appeal.

Lord Oliver of Aylmerton:—My Lords, the Appellants in this appeal, to whom it may be convenient to refer simply as "the Woolwich," call in question the validity of regulations made pursuant to s 343(1A) of the Income and Corporation Taxes Act 1970, which they claim were *ultra vires*. The F question reduces, in the end, to a short, but by no means simple, question of construction of the relevant statutory provisions, but in order to understand the problem it is necessary to say something of the historical background to the section. This has been conveniently and intelligibly set out in the judgment of Nolan J. in the High Court [1987] STC 654 and to do more than merely to summarise it would be a work of supererogation.

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The collection of income tax from the recipients of annual interest and dividends by means of deduction at source, enshrined at the date of the commencement of these proceedings in ss 52, 53 and 232 of the Act of 1970, is a system which has been established for many years and would, but for the arrangements described below, have applied to investment income from H building societies in the same way as it applied to other investment income. Under this system, income tax at the basic rate is accounted for to the Revenue by the paying institution and the recipient is treated, for tax purposes, as having received a grossed-up amount which, after deduction of tax at the basic rate, is equal to the income actually received by him. If he is a high-rate taxpayer he pays additional tax on that amount. If his total income I is such that he is not liable to pay even basic rate tax, he is entitled to reclaim the tax deducted or the appropriate proportion of it from the Revenue.

Building societies have traditionally provided a safe and simple form of investment for persons of relatively modest means, many of whom are not liable to pay basic rate income tax on the whole of their income, a circum-

stance which would either have given rise to a very large number of small repayment claims or would have resulted in the Revenue retaining more tax than was actually due owing to the failure of investors, either from ignorance of the law or inertia, to make claims for repayment. Accordingly, in the year 1894, the Revenue offered to the building societies two alternative arrangements. "A" and "B," for the discharge of the tax liability of investors in a way which obviated the necessity for claims for repayment. Under arrangement "B," which was the one selected by the Woolwich, the society discharged the liability for income tax payable in the tax year 1894–95 in respect of interest paid to its investors by paying to the Revenue tax at one half of the standard rate on the amount of interest paid and in practice this was, then and thereafter, treated as applying equally to dividends. The purpose of this was to achieve a position of "revenue neutrality," the calculation being that the Revenue would thus receive, as nearly as may be, the same amount in tax as it would have received under the ordinary system of tax deduction if investors qualified to make repayment claims had availed themselves of their right to do so.

The basic features of this arrangement have been repeated in each year since 1895 up to and including the tax year 1985–86, although there have been refinements. In 1925 a distinction was made between investors who were clearly liable for tax at the basic rate, such as corporate investors or commercial undertakings, and individual investors. As regards interest or dividends paid to the former, the societies account for tax at the basic rate, whilst as regards the latter, they accounted for a reduced rate of tax which was arrived at each year on the basis of statistical evidence and was calculated to produce a position of revenue neutrality. An important complication in this procedure, which has given rise to the problem raised by this appeal, is that, no doubt for administrative convenience both to the societies and to the Revenue, the amount payable under each annual arrangement was calculated not by reference to the payments made in the actual fiscal year for which the tax was due but by reference to the payments shown as made or accrued in each society's annual accounts. Originally it was calculated by reference to the accounts of the accounting period ending in the previous year of assessment, but in the year 1940–41 societies were given the right to elect, once and for all for that and all subsequent years, that the calculation should be based on the accounts for each society's accounting year ending in the current year of assessment. The Woolwich, whose accounting years end on 30 September in each year, made that election.

These arrangements, which were entirely voluntary on the part of the societies, were renewed annually and were, up to 1951, entirely extra-statutory. Section 23 of the Finance Act 1951, however, accorded them statutory recognition and from 1970 until the end of the tax years 1985–86 they were regulated by s 343 of the Act of 1970.

Subsection (1) of s 343 provided as follows:

"The Board and any building society may, as respects any year of assessment, enter into arrangements whereby—(a) on such sums as may be determined in accordance with the arrangements the society is liable to account for and pay an amount representing income tax calculated in part at the basic rate and in part at a reduced rate which takes into account the operation of the subsequent provisions of this section; and (b) provision is made for any incidental or consequential matters, and

any such arrangements shall have effect notwithstanding anything in this Act . . . ”

There followed a proviso obliging the Board to secure the position of tax neutrality already referred to. It is unnecessary to set it out here for, as will be seen, the Finance Act 1984 transferred the function of fixing the reduced rate for the purposes of the section from the Board to the Treasury and s 26(3) of that Act contained provisions to the same effect to the terms of which I will refer a little later. Section 343(2) provided for the deduction of dividends and interest paid for the purposes of the society's corporation tax and also regulated the treatment for corporation tax purposes of dividends and interest paid by a society to company investors. The position of investors in and borrowers from a building society are dealt with in subss (3) and (4) which, so far as material, provide as follows:

> “(3) Where any arrangements under this section are in force in the case of any society as respects any year of assessment—(*a*) notwithstanding anything in Part II of this Act, income tax shall not be deducted from any dividends or interest payable in that year in respect of shares in or deposits with or loans to that society, (*b*) subject to subsection (2)(*b*) above no repayment of income tax and, subject to paragraph (i) of the proviso below, no assessment to income tax shall be made in respect of any such dividends or interest on or to the person receiving or entitled to the dividends or interest, (*c*) any amounts paid or credited in respect of any such dividends or interest shall, in computing the total income of an individual entitled thereto, be treated as income for that year received by him after deduction of income tax from a corresponding gross amount . . . provided that—(i) paragraph (*b*) above shall not prevent an assessment in respect of income tax at a rate other than the basic rate; (ii) for the purpose of determining whether any or what amount of tax is, by virtue of paragraph (*c*) above, to be taken into account as having been deducted from a gross amount in the case of an individual whose total income is reduced by any deductions so much only of that gross amount shall be taken into account as is part of his total income as so reduced . . .
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> (4) Where any arrangements under this section are in force in the case of any society as respects any year of assessment then, notwithstanding anything in Part II of this Act, income tax shall not be deducted upon payment to the society of any interest on advances, being interest payable in that year.”

Thus it will be seen that the payment by a society under an arrangement made under this section in any year of assessment has the effect of discharging entirely any liability for individual investors for basic rate tax on dividends or interest received by them in that year of assessment even though, as previously noted, the “amount representing income tax” is in fact calculated not upon the income actually received in that year but upon those sums which have been paid or accrued in the society's accounts for the accounting period ending in that year. So long, of course, as successive arrangements continue to be made on the same basis, amounts paid during the period between the end of the society's accounting year and the beginning of the next year of assessment will be brought into account for the purposes of the computation of the society's liability in that year of assessment. If, however, the arrangement is discontinued—if, for instance, the society declines to enter

into an arrangement for the next year of assessment and elects to deduct and account for tax on dividends and interest actually paid in that year of assessment—there will be what has been referred to as a "gap period" which will never be brought into account. That is, in effect, what has occurred in this case and it is this that has given rise to these proceedings.

Just to complete the picture, under s 343 as it originally stood there are two further matters which ought to be mentioned. Obviously in the case of any building society whose accounting year-end did not coincide with the end of the fiscal year the amounts upon which tax fell to be calculated straddled two financial years in respect of which different rates of tax might be applicable. Thus from the year 1975–76 onwards the practice was to apportion dividends and interest paid on a time basis and to calculate the reduced rate separately for each apportioned part according to the tax rate for the actual year of assessment into which it fell. Secondly, and no doubt for administrative convenience, it was the universal rule that the tax payable by each society under the arrangement was paid on 1 January of the year of assessment to which the arrangement related.

The Finance Act 1984 introduced new arrangements with regard to tax on interest payments on bank deposits and, as already mentioned, transferred to the Treasury the responsibility for fixing the reduced rate in each year for arrangements with buildings societies under s 343. The proviso to subs (1) of that section was repealed and was replaced by s 26(3) of the Act of 1984 which was in the following terms:

> "Whenever they exercise their powers under this section the Treasury shall aim at securing that (assuming for the purposes of this subsection that the amounts payable by building societies under section 343 of the Taxes Act and by deposit-takers under section 27 of this Act are income tax) the total income tax becoming payable to, and not being repayable by, the Crown is (when regard is had to the operation of those sections) as nearly as may be the same in the aggregate as it would have been if those sections had not been enacted."

In his budget statement delivered on 19 March 1985 the Chancellor of the Exchequer indicated that since, on 6 April of that year, the banks were to move over to the composite rate system for the payment of tax on bank interest (which tax, I observe in parenthesis, was accounted for quarterly and calculated on payments made or credited during the quarter) it was now necessary to put the building societies' payments onto a similar footing as from the beginning of the following tax year. For reasons which, I confess, are not entirely clear to me, Parliament determined to effect this, not directly by primary legislation, but by empowering the Board of Inland Revenue, to introduce the new system by regulation. By s 40 of the Finance Act 1985, s 343(1) of the Act of 1970 was amended by adding to the words "in respect of any year of assessment" the words "ending before 6 April 1986," thus terminating, as from that date, the system of annual voluntary arrangements. Two new subsections, numbered respectively (1A) and (1B) were added in the following terms:

> "(1A) The Board may by regulations made by statutory instrument make provision with respect to the year 1986–87 and any subsequent year of assessment requiring building societies, on such sums as may be determined in accordance with the regulations, to account for and pay an amount representing income tax calculated in part at the basic rate

A and in part at the reduced rate determined for the year of assessment concerned under section 26(1)(*a*) of the Finance Act 1984: and any such regulations may contain such incidental and consequential provisions as appear to the Board to be appropriate, including provisions requiring the making of returns.

B (1B) A statutory instrument made in the exercise of the power conferred by subsection (1A) above shall be subject to annulment in pursuance of a resolution of the Commons House of Parliament."

At the same time amendments, to take effect for the year 1986–87 and subsequent years, were made to subss (2) and (3) to substitute reference to C the regulations under subs (1A) for references to arrangements made under subs (1).

So matters stood on 25 October 1985 when the Woolwich entered into arrangements under the amended s 343(1) for the year of assessment 1985–86. Under those arrangements a sum of £138,201,856 became payable D in respect of dividends and interest payable during that year of assessment, such sum being calculated in the usual way on the sums shown as paid or credited in the Woolwich accounts for the financial year ended 30 September 1985. These arrangements, by virtue of s 343(3) had the effect of discharging once and for all any ability of investors for basic rate tax on dividends or interest paid to them by the society during that year of assessment and on 1 E January 1986 the sum was duly paid, thus discharging in full the society's liability to the Revenue under the arrangements.

On 13 March 1986, the Commissioners of Inland Revenue made regulations (the Income Tax (Building Societies) Regulations, 1986 (S.I. 1986 No. 482)), the broad effect of which was, as from 6 April 1986, to impose on the F building societies a compulsory system of collection of tax in respect of dividends and interest paid and to require the tax to be accounted for quarterly and to be calculated in each quarter not, as previously, on the sums shown in the audited accounts ending in the year then current but on the sums actually paid or credited in the quarter concerned. The quarter-days were fixed, presumably as a matter of administrative convenience, as the last days of G February, May, August and November. These regulations were laid before Parliament on 14 March 1986 and came into operation on 6 April 1986.

It can readily be seen that, in the absence of any further taxing provision the effect of a changeover from calculating tax payable, by reference to each H society's annual accounts for the year ending in the current year of assessment (1985–86) to calculation on the actual payments made during the year of assessment (1986–87) would have the result that payments made or credited between the end of the accounting year and 6 April 1986 would never be brought into account for the purposes of calculating the tax payable, for they related to the year 1985–86, the tax liability for which had already been discharged by the arrangements made for that year. On one view of the matter I this is an entirely equitable result because, it is argued, if one goes back through the years, there must have been, when arrangements first came to be made on the basis of the society's annual accounts, an element of double-counting which balances the period falling out of account. Whether that is right or wrong in fact, the Commissioners were clearly of the view that provision was required to prevent sums paid during the gap period from escap-

ing, as they would put it, liability for tax. It was quite evidently with this in mind that they introduced into the Regulations of 1986 transitional provisions designed to bring these sums into account. The question is whether, on their true construction, the provisions of s 343(1A) enable them to do so. A

Turning now to the Regulations of 1986, Regulation 2 contains a number of definitions, the material one for present purposes being "payment" which is defined to include "credit" and "payment quarter" meaning "a period of three months ending with the last day of February, May, August or November." The obligation on a building society to pay tax—that is, the charging provision—is in Regulation 3 which, for relevant purposes, provides as follows: B

> " . . . a building society shall pay to the Board on the relevant payment date for each payment quarter or other period to which regulation 7 applies, in respect of any payments of dividends or interest . . . made after February 1986, a sum made up of the reduced rate amount and the basic rate amount for that payment quarter or period." C

Regulation 7 (which deals with the collection of amounts in respect of income tax payable) incorporates Schedule 20 to the Finance Act 1972 and applies it to building societies with certain modifications. Broadly that Schedule regulates the collection of income tax from companies, imposes a duty to make returns and provides for payment to be due without assessment. As regards the obligation to make returns in the case of a building society, the regulation provides that a return shall be made for D E

> "(*a*) each complete payment quarter within the accounting period beginning with the payment quarter ending 31 May 1986; (*b*) each part of an accounting period being a part which begins after February 1986 and which is not a complete payment quarter." F

Paragraph 5 of Schedule 20 enables a company to set off against its tax liability the tax on payments which it itself has received under deduction of tax. Regulation 7(3)(*e*) applies this only in relation to payments received after February 1986. Regulation 4(1) applies the reduced rate amount to dividends and interest paid (in broad terms) to individuals and Regulation 5 applies the basic rate amount (again in broad terms) to payments made to corporate investors beneficially entitled.

It will be seen, therefore, that Regulation 3 has the effect of charging to tax in 1986–87 payments which in fact were made between 28 February 1986 and 6 April 1986, that is to say, during the year of assessment 1985–86. This forms one branch of the Woolwich's attack on the validity of the Regulations of 1986. The same point, but of greater quantitative importance arises in relation to Regulation 11 which contains transitional provision designed to charge to tax any balance of dividends and interest paid during 1985–86 between the end of a society's accounting year and 28 February 1986. It is headed: "*Transitional payments in 1985–86 taken into account under 1985–86 arrangements*" and provides, so far as material, as follows:

> "(1) This regulation applies with respect to any payment by a building society, after the end of the society's last accounting period which ends in the year 1985–86, but before 1 March 1986—(*a*) made to an investor by way of dividends or interest in respect of an investment; or (*b*) which is a section 53 payment."

A (The reference to a s 53 payment is a reference to payment by building societies of annuities or other annual payments from which tax is to be deducted at source within the meaning of s 53(1)(*a*) of the Act of 1970.)

"(2) Subject to the provisions of these regulations, any such payment shall be treated in all respects as a payment to which these regulations apply and as made in the payment quarter to which the payment dates specified in paragraph (3) below relate.

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(3) The accounting periods concerned, the specified payment dates to which paragraph (2) refers, and the amounts in respect of the sum payable to the Board to which regulation 3 applies which shall be payable on or before those dates, are as follows:

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Accounting period ending	*Payment Date*	*Amount*
In December 1985, January or February 1986	14 March 1987	The whole
In September, October or November 1985	14 March 1987 14 March 1988	One half One half
In June, July or August 1985	14 March 1987 14 March 1988 14 March 1989	One third One third One third
Before June 1985	14 March 1987 14 March 1988 14 March 1989 14 March 1990	One quarter One quarter One quarter One quarter

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(4) Subject to paragraph (5), the sum payable to the Board to which paragraph (3) refers is the sum of the reduced rate amount arrived at by reference to a rate of 25.25 per cent. and the basic rate amount arrived at by reference to a rate of 30 per cent.

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(5) Regulation 7(3) shall apply for the purposes of this regulation with the substitution of the following paragraph for paragraph '(*e*)'—

(*e*) as if, for the purposes of paragraph 5 (set off against company's, income tax payable), the period from the end of the society's last accounting period ending in the year 1985–86 down to the end of February 1986 were an accounting period."

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If these regulations stood alone the effect would, of course, be that sums shown as accrued due in society's accounts for the year ended in the fiscal year 1985–86 but actually paid after the end of the society's accounting year would be brought into account for the purpose of the regulations even though they were already taken into account of for the purposes of the arrangements for that year. That position, however, is catered for by Regulation 12 which underlines the intention behind Regulation 11 and is in the following terms:

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"The above regulations shall not apply to any payment of dividends or interest in respect of an investment or to any section 53 payment to the extent that account was taken of any such payment in computing the

amounts representing income tax payable by a building society under the arrangements as respects the year 1985–86 to which subsection (1) of section 343 applies."

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So far as the Woolwich is concerned the effect of these regulations is to subject it over a period of 24 months to tax on 29 months income, with the result that, on the calculations contained in the evidence, the Revenue receives for the fiscal years 1986–87 and 1987–88 some £76m more than it would otherwise have received in respect of the dividends and interest paid or credited during those years. It is, therefore, perhaps not altogether surprising that on 17 June 1986 the Woolwich commenced proceedings for judicial review seeking a declaration that the Regulations of 1986 were unlawful.

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My Lords, for my part I entertain very little doubt that, as the legislation in fact stood at the date when these regulations were made, the Woolwich was entitled to succeed. Income tax, as has been forcefully pointed out in the course of the argument, is an annual tax which is assessed in respect of a particular year of assessment. Whilst the concept of calculating the amount of tax payable in respect of that year by reference to the income received during another period—for instance, the previous year of assessment—is a familiar one, no precedent exists for charging tax for a particular year on the income of a period of more than a year. Section 343(1A) enables the Revenue only to make provision "with respect to the year 1986–87 and any subsequent assessment" and to require a building society to account for and pay "an amount representing income tax." That cannot, clearly, refer to the society's income tax because the society does not pay income tax. The amount which the society is required to pay can only sensibly "represent" income tax which could otherwise be payable by its depositors and it is to be calculated in part at the basic rate and in part at the reduced rate "determined for the year of assessment concerned under s 26(1)(*a*) of the Finance Act 1984." That section requires the Treasury to determine the rate individually for each year of assessment and with the aim of producing a position of tax neutrality for that year of assessment. The words "such sums as may be determined" cannot, on any ordinary principles of statutory construction, be read as unrelated to the year of assessment with respect to which the regulations of 1986 are made and as unrelated to the income tax which those sums are to represent. On no ordinary analysis could it be read as embracing a power to make provision for the taxation of sums paid or credited in the year 1985–86.

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The subsection did not, however, remain in the form in which it stood at the date when these proceedings were commenced. Section 47(1) of the Finance Act 1986, which received the Royal Assent on 25 July 1986, introduced a deliberately retrospective amendment. It provides:

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"In section 343 of the Taxes Act (Building Societies), subsection (1A) (which was inserted by the Finance Act 1985 and enables the Board to make regulations requiring societies to account for amounts representing income tax on certain sums) shall have effect and be deemed always to have had effect with the insertion after the words 'in accordance with the regulations' of the words '(including sums paid or credited before the beginning of the year but not previously brought into account under subsection (1) above or this subsection)'."

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It is the effect of these additional and retrospective words which forms the real issue on this appeal. In the argument on the application for judicial

review before Nolan J. they played a relatively insignificant part: [1987] STC 654. Nolan J. could see nothing in s 343(1A) which authorised the Commissioners to go back on the arrangements made with the Woolwich for 1985–86 and he treated the provisions of Regulation 11(4), which seek to charge tax at the 1985–86 rates and which the Commissioners now accept are *ultra vires* as a clear indication that the regulations went beyond the power conferred by s 343(1A). On no analysis could Parliament have intended to delegate to civil servants the power to fix the rate of tax payable for a year of assessment. He found himself unable to ascribe any sensible meaning to the words added by s 47 of the Finance Act 1986 save, possibly, to authorise what was probably unnecessary, that is to say, the utilisation of sums paid or credited in a previous year as an artificial measure of the tax payable in the year 1986–87 in the same way as sums shown in a society's accounts had been used under the previous arrangement as the measure of the tax payable in respect of the fiscal year in which the accounting period expired. He accordingly made the declaration sought by the Woolwich.

From this decision the Commissioners appealed to the Court of Appeal which, on 13 April 1989 unanimously reversed the decision of Nolan J. on the short ground that whatever might have been the effect if the section had remained unamended, the words introduced by s 47 of the Act of 1986 fairly and squarely covered the interest paid between 30 September 1985 and 5 April 1986. The pith of the Court's decision lies in the following short passage from the judgment of Sir Nicolas Browne-Wilkinson V.-C. [1989] STC 463, 469[1]:

> "As a matter of ordinary construction, I find the conclusion contended for by counsel for the Crown inescapable. The section 47 words are clear and they cover the present case. Moreover the Regulations have been made and their validity challenged before Parliament had to consider the Finance Bill 1986. It was in those circumstances that Parliament enacted section 47 of the Finance Act 1986 which introduced the section 47 words. In such circumstances, in the absence of any other reason for Parliament to have enacted section 47 so as to deem section 343(1A) always to have included the section 47 words, the inference must be that Parliament intended to put to rest the existing challenge to the validity of the Regulations."

Before your Lordships the Woolwich has argued strenuously that this is altogether too simple an approach. For my part, I confess that I find the conclusion irresistible that Parliament intended by these words to enable the Revenue to take account of and to charge to tax sums which, rightly or wrongly, it regarded as otherwise representing windfalls in the hands of building societies. One has only to look at the circumstances. The Regulations of 1986 had been made and had been objected to. They were made the subject of a direct challenge in legal proceedings, the evidence in support of which clearly adumbrated the arguments advanced before the Judge and the Court of Appeal. The notion that Parliament should go to the trouble of enacting an expressly retrospective amendment in order to provide, unnecessarily, for the use of these sums as a measurement of tax liability—a matter never remotely in issue—is simply fanciful. But that is not, of course, a total answer to the issue raised, for it is said that the question is

(1) Page 607B/D *ante*.

ultimately not one of what, subjectively, Parliament may (or must) have intended to do but whether, by the words which it has used, it has effectively done it. A

I hope that I shall not be thought to be lacking in deference to the lengthy, and in many respects, cogent arguments which have been advanced by Mr. Gardiner on the Woolwich's behalf if I do not set them out here in extenso. They highlighted a number of anomalies, not least of which is that s 343(1) provides in terms that for the year 1985–86 arrangements entered into shall "have effect notwithstanding anything in this Act." To create in relation to sums paid in that year and therefore covered by that arrangement a liability to tax in the following year of assessment must involve to some extent going back on that arrangement. The difficulties are far from unreal but the argument failed on what appears to me to be the salient point, that is to say, the necessity for ascribing some sensible meaning other than that suggested by the Revenue to the words which the legislature has advisedly chosen to use. I confess that I have not found the problems raised as easy of resolution as have the majority of your Lordships and I have been oppressed by what appeared to me and still appears to me to be very real difficulties, not altogether dispelled, for me at any rate, by Mr. Stamler's robust arguments on behalf of the Revenue. I console myself that I am not alone in finding the problem a difficult one. It is rightly said that the application of what is essentially an annual tax on income of a particular year of assessment to a period in excess of a year is without precedent. I see force in the argument that an intention to produce what Nolan J., with his long experience in matters of taxation, described [1987] STC 654, 660d, as "a truly astonishing result" should not be ascribed to Parliament without very clear words. Again, it is not easy to see how, on the footing that sums paid or credited in the gap period are to be brought into account and taxed at the reduced rate in another year of assessment as an addition to the sums paid or credited in that year, the Treasury is to exercise its powers under s 26 of the Act of 1984, for these powers have to be exercised in relation to a particular year of assessment, in this case 1986–87. In exercising its powers the Treasury has to assume that the sums payable by the society are income tax—which can only mean income tax for the year of assessment—and to produce the net result that the total income tax becoming payable to the Crown (again in that year of assessment) is no more than it would have been if s 343 (including subs (1A)) had not been enacted. In the end, however, I have been persuaded that the Court of Appeal was right in its conclusion that no other sensible meaning can be given to what were conveniently referred to as "the s 47 words" than that they were intended to authorise the taxation in the year 1986–87 and the subsequent years of assessment of sums paid or credited in the gap period and not previously brought into account. B C D E F

It is, of course, true that the ultimate test of Parliamentary intention is by reference to the words which Parliament has chosen to use. But here there is no real difficulty in construing Parliament's words. Read in their ordinary natural meaning s 343(1A), as amended, authorises the Revenue to make regulations requiring, in respect of identified years of assessment, payment of an amount representing income tax on any sums paid before the year in question and not previously brought into account. "On" here must I think mean "in respect of" and, indeed, s 343(2) as amended by s 47 of the Act of 1986 says as much. On the face of it, that clearly authorises, for instance, a requirement to pay in the year of assessment 1986–87, a sum in respect of interest in fact paid before the commencement of that year. One then asks,

A what, as a matter of construction, prevents the Revenue from requiring such payment in addition to payment of sums in respect of interest paid during that year of assessment? The suggested inhibition against such cumulative taxation lies not in the words which Parliament has chosen to use but in certain well-established presumptions or principles—a presumption against double taxation, a presumption that income tax, being an annual tax is payable B only on the income of a particular year and so on. But these are only presumptions. They are clearly rebuttable if sufficiently clear express words are used. But they can also be rebutted, as it seems to me, by circumstances surrounding the enactment of the particular legislation which lead to an inevitable inference that Parliament intended, in using the words that it did, that these presumptions or principles should not apply. I am bound to say C that I think it unfortunate that the Revenue, through Parliament, should have chosen by secondary rather than primary legislation to take what was, on ordinary principles, the very unusual course of seeking to tax more than one year's income in a single year of assessment, but s 47 of the Finance Act 1986 is, on any analysis, a very unusual provision and I have, in the end, found myself irresistibly driven to the conclusion that this was what D Parliament intended should occur. It may be—I do not know—that the legislature did not appreciate fully that the effect of the arrangements made in 1985 was to discharge all liability for tax on interest paid in the year of assessment 1985–86, including tax on interest paid after the end of a society's accounting year, and that, accordingly, to tax those sums again in a subsequent year was, in a sense, to tax them twice. But even making that assump- E tion it amounts to no more than saying that the legislature should not have intended to do that which it plainly set out to do. I would, for my part, therefore, reject the Woolwich's principal argument.

That is not, however, the end of the matter for an alternative argument is advanced. This arises out of the Revenue's concession—clearly rightly F made—that Regulation 11(4) is *ultra vires*. What is said here is that this has the effect of invalidating Regulation 11 in toto. On the other side, it is argued that the only effect of invalidating Regulation 11(4) is that it is notionally deleted from the Regulations of 1986, so that there is simply no specification of a rate of tax applicable. It would follow that the appropriate rate is simply G that which s 343(1A) prescribes, that is to say, the rate for the year of assessment into which the sums are brought. That argument found favour with the Court of Appeal which held Regulation 11 to be valid save to the extent that para (4) purported to fix a rate of tax. Before your Lordships, Mr. Underhill has submitted that this case cannot be approached on such a simple "blue-pencil" basis. Clearly "severance," to use the convenient and conversational H expression, by a process of simple deletion is practicable here without altering the grammatical sense of what is left. But Mr. Underhill has submitted—and, in my judgment, rightly submitted—that this does not provide the complete answer. One has to ask also the question whether the deletion of that which is in excess of the power so alters the substance of what is left that the provision in question is in reality a substantially different provision from I that which it was before deletion. If it is, it cannot be assumed that the legislator would have enacted it in its altered form and the whole must be declared bad. Your Lordships have been referred to a number of authorities, but I do not think the principles, at any rate as they apply to this case, are seriously in doubt. The matter is in essence one of reading and construing the provision in question and if, on a fair reading, the provision shorn of the offensive part is, in substance and effect, a different provision from that

which the legislator, on his own showing, intended to enact, then, for my part, I do not see how any of it can stand.

Turning to the Regulations of 1986, the essential scheme adopted is to begin with a charging provision (Regulation 3) which, in terms, does not apply to payments made prior to 1 March 1986. Those are brought into charge by Regulation 11, but they are brought in a very particular way, that is to say, by subjecting them to Regulation 3, deeming them under that regulation to be paid at times when they were not in fact paid, and then avoiding, by Regulation 11(4), the taxation consequences which would otherwise have flowed from this scheme, that is to say, that they would be taxed for the rates appropriate for the periods in which they are deemed to have been paid. If one follows the regulations through and relates Regulation 11 back to Regulation 3 it becomes immediately apparent how vitally important Regulation 11(4) was to the scheme which the draftsman adopted. The starting assumption was, quite clearly, that the intention of s 343(1A) was that sums paid prior to the specified years of assessment but not previously brought into account would be charged to tax at the rate appropriate for the year of assessment in which they were actually paid or credited. There is nothing in subs (1A) which justifies this, but it was clearly assumed to be so. This is borne out by the fact that in respect of the period from 1 March 1986 to 5 April 1986 tax has in fact been levied at the 1985–86 rate, a course of action which the Revenue now admits and asserts was a mistake. Similarly, Regulation 11(5) is all of a piece with this scheme for it authorises the set-off against the sums to be paid in respect of tax on payments made by the society during the gap period of the tax deducted from those payments made to the society in the same period which have been paid under deduction of tax. Whether this provision was strictly authorised by the power in s 343(1A) to make regulations "with respect to the year 1986–87" may be open to doubt, but the intention was clearly to levy tax, albeit payable in a subsequent year, in exactly the same way as if it had become payable for the year of assessment 1985–86.

In considering the Regulations of 1986 it may be convenient, by way of shorthand, to refer to "interest" as including also dividends. If we go first to Regulation 3 we see that what the building society is required to pay is a sum "in respect of payments of interest made after February 1986." Nothing else is charged by this regulation and it is the only charging provision. The payment is to be made on the payment date for each payment quarter to which Regulation 7 applies and it is a sum made up of the reduced rate and basic rate amount for that payment quarter. The payment quarters have been defined already by Regulation 2 to which I have already referred and those to which Regulation 7 applies are, by Regulation 7(3)(*e*) "each complete payment quarter . . . beginning with the payment quarter ending 31 May 1986." So far, therefore, there is nothing which charges tax in respect of payments of interest made in the year 1985–86 except insofar as those payments were made after February 1986. Regulation 11 then seeks to bring them into charge. Paragraph (1) defines the payments to which the regulation relates and the charging provision is in para (2). This has a dual purpose. First, notwithstanding that Regulation 3 applies only to post-February 1986 payments, it subjects the para (1) payments to that regulation. If that stood alone it would be self-contradictory, so the second part of the paragraph deems them to have been paid, not when they were in fact paid, but at dates after February 1986. This is done by treating them "in all respects" as if made in the payment quarters which are set out in para (3)—that is to say, in

A the case of the Woolwich, as if they were made as to one half in the payment quarter ending on 28 February 1987 and as to the other half in that ending on 28 February 1988. If then we relate that back to Regulation 3 we find that the sums which the building society is obliged to pay are to be calculated at the reduced and basic rates applicable for the years of assessment in which those payment quarters fall. No other rate of tax is prescribed. But this B would contradict the basic assumption upon which the Regulations of 1986 have been framed, namely that the applicable rate for the sum should be the rate for the year of assessment in which they were actually paid, i.e. 1985–86. Thus para (4) is introduced to correct this.

It thus becomes apparent that the one thing the draftsman did not C intend was that the sums artificially deemed to be paid in the specified payment quarters in 1987 and 1988 in order to bring them into charge under Regulation 3, should be taxed at the rate applicable for those years of assessment. Yet, if para (4) is deleted, as the Revenue concede that it must be, that is exactly what Regulation 11 now achieves. It seems to me, accordingly, that it is beyond argument that Regulation 11 without para (4) is in substance D quite different from the regulation which the draftsman actually produced and intended. Whether such a result is one which is strictly authorised by s 343(1A) may be open to doubt for it seems extremely unlikely that Parliament can have intended to confer upon the Revenue a discretion to tax the sums paid during the gap period at differential rates according to the adventitious dates upon which, during 1985–86, individual societies had cho- E sen to close their financial years. But this is in any event immaterial, for the one thing that is perfectly clear is that this was not the result that the Revenue intended or contemplated.

Mr. Stamler had really no answer to this save to suggest that a combi- F nation of Regulation 3 and Regulation 11(2) produced, by a process of reasoning that I confess that I was unable to follow, the result that the sums deemed to be paid in 1987 and 1988 fell to be taxed according to the rates fixed for the year of assessment 1986–87. That might be possible for the payments falling to be made on 14 March 1987 but I find it quite impossible to ascribe that result to the regulation in relation to the remaining payment G dates referred to in para (3) and it quite clearly does not accord with the intention to which the Revenue and its draftsman intended to give effect. The Court of Appeal were prepared to treat the remainder of Regulation 11 as unaffected by the deletion of para (4) because, it was said, s 343(1A) itself contained the formula for fixing the rate of tax which could apply in the absence of para (4) and which, they surmised, the draftsman would have H been prepared to allow to operate had he appreciated the invalidity of the paragraph. I cannot agree that this is a correct approach. The draftsman's hypothetical intention is by no means obvious. If, as Mr. Stamler submitted, the whole purpose of the transitional provision was to compel societies to disgorge to the Revenue tax which, in fixing their interest rates, they notionally and indirectly deducted from payments to investors in the gap period, I there can be no logic at all in subjecting those payments to rates of tax which bear no relation to, and indeed might well exceed, the tax notionally deducted. That becomes even clearer when one considers that Regulation 11(1) applies not only to payments of interest and dividends but to payments of annuities to which s 53 of the Act of 1970 applies and where tax would have been deducted at source by the society. It cannot rationally have been intended that the society should come under an obligation to account to the

Revenue for tax at a higher rate than that which obtained at the time when the tax was deducted. What form the regulation might have taken if the invalidity of para (4) had been appreciated is a matter of pure speculation.

Nor does the matter stop simply with Regulation 11. The same erroneous assumption which produced para (4) of that regulation appears in a slightly different form also in Regulation 3. That this is so is demonstrated by the fact that the Revenue, as it is now admitted mistakenly, applied the tax rates for the year 1985–86 to payments made in the period from the end of February 1986 to 6 April 1986. It is suggested that this can be rectified simply by a refund of the excess amount of tax demanded. The matter is not, however, as simple as that. It has to be remembered that what s 343(1A) authorises—and this is all that it authorises—is the making of regulations requiring societies to pay, on the sums determined, an amount calculated in part at the basic rate and in part at the reduced rate "determined for the year of assessment concerned" under s 26(1)(*a*) of the Act of 1984. "The year of assessment concerned," as a result of the opening words of the section can only be the year 1986–87 or some subsequent year. Regulation 3, however, requires payment on the relevant payment date for each payment quarter of "a sum made up of the reduced rate amount and the basic rate amount for that payment quarter or period." As already mentioned, the regulation applies expressly to payments made after February 1986 and therefore covers, as the first payment quarter, the period 1 March 1986 to 6 April 1986 (falling in the year of assessment 1985–86) and the period 7 April 1986 to 31 May 1986 (falling in the year of assessment 1986–87). These payments therefore fall between two stools. There is no single "reduced rate amount" or "basic rate amount" for that quarter. That is the first difficulty. Regulation 7, it is true, contemplates (in para (3)(*a*)) a period which is not a complete payment quarter and may be said to enable the references to *the* basic rate amount and the reduced rate amount to be read plurally as referring to the amounts applicable to the separate periods of the quarter in question according to whether they fall within the year 1985–86 or the year 1986–87. But that could only have the result of making the amounts "for" the period 1 March 1986 to 6 April 1986 the amounts determined for the year 1985–86. Thus the regulation is manifestly *ultra vires* to this extent because the section under which it is made does not authorise the application of any rate other than that "for the year of assessment concerned" and that, as already explained, has to be either the year 1986–87 or some subsequent year. Again, this is not a defect which can be cured by deletion. The whole regulation would have to be re-written and it is entirely a matter of speculation what form the re-writing would take if the draftsman had appreciated the error into which he was falling.

Whether it is open to the Commissioners now to lay before Parliament new regulations containing different transitional provisions is not a matter which it is necessary to consider nor, indeed, would it be appropriate to do so. If they can and do, then the exercise upon which the, Woolwich is engaged may seem a singularly sterile one. Nevertheless, although I am very sensible of the manifest inconvenience which this will involve, it is, I, think, clear on analysis that the admitted invalidity of Regulation 11(4) infects the whole of that regulation and I see no alternative to declaring it to be wholly void and ineffective. It follows that, whilst dismissing the appeal as regards the power to make regulations having the effect of imposing tax on sums paid during the gap period, I would allow the appeal as regards the invalidity of Regulation 11 and of Regulation 3 so far as it relates to the period after February and before 6 April 1986.

A **Lord Goff of Chieveley**:—My Lords, I have had the advantage of reading in draft the speech of my noble and learned friend, Lord Oliver of Aylmerton. I agree with him that the Woolwich's principal, argument, that the regulations were unlawful in so far as they purported to require building societies to pay an amount representing income tax in respect of sums paid or credited before 6 April 1986, must fail. On this point, I do not wish to add B anything to what has been said in the speech of my noble and learned friend.

I turn to the Woolwich's second argument, which arises from the Revenue's concession that Regulation 11(4) is *ultra vires*. This is that, because that paragraph cannot be severed from the remainder of Regulation 11, no other part of that regulation can be saved.

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Since my noble and learned friend has so fully analysed the Regulations, in terms with which I am very substantially in agreement, I am relieved from the burden of setting out the terms of the Regulations in extenso or of indulging in a complete analysis of them. I can proceed straight to Regulation 11, which is described as a transitional provision, being con- D cerned with certain payments made after the end of the society's last accounting period which ends in the year 1985–86, but before 1 March 1986. It is therefore concerned with payments made in the so-called "gap period," but not with those made after 28 February and before 6 April 1986, since those are dealt with directly by Regulation 3. Paragraph (2) of Regulation 11 provides that:

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> "Subject to the provisions of these Regulations, any such payment shall be treated in all respects as a payment to which these Regulations apply and as made in the payment quarter to which the payment dates specified in paragraph (3) below relate."

F So far as the Woolwich is concerned, para (3) has the effect that payments made by it during the specific period are thereby treated as paid in part on 14 March 1987, and in part on 14 March 1988. Paragraph (4) specifies the applicable reduced rate amount and basic rate amount which together produce the sum payable to the Revenue by the building societies in respect of the relevant payments. The trouble with para (4) is that the basic G rate amount so specified is plainly based on the basic rate of tax applicable in 1985–86 (30 per cent.), whereas s 343(1A) of the Act provides that the relevant rates shall be those for the year of assessment into which the omitted sums are brought—which, however, cannot be before 1986–87, when the basic rate was 29 per cent.

H I wish to add that, in my opinion, Regulation 3 reveals that (as one would expect) a similar mistake was made in so far as the regulation refers to payments made after February 1986 and before 6 April 1986. Under the regulation, the sum payable by the building society to the Board on the relevant payment date for each payment quarter is to be made up of the reduced rate I amount and the basic rate amount "for that payment quarter or period." Those words must be read, in my opinion, as referring to the reduced rate and basic rate applicable in the year of assessment in which the relevant payment quarter or period falls. It follows that, consistently with Regulation 11(4), the applicable rates for that part of the first payment quarter which fell before 6 April 1986 were the rates for 1985–86; and so to this extent Regulation 3 is also *ultra vires*.

Reverting to Regulation 11, the contention of the Revenue has been that, in these circumstances, the problem can be solved if the Court simply excises para (4). However, as my noble and learned friend has pointed out, the problem cannot be solved as easily as that, for the simple reason that para (4) forms an integral part of Regulation 11. Paragraph (2), which is the central paragraph, has been drafted on the assumption that para (4) will specify the relevant reduced rate amount and basic rate amount; and if para (4) is simply excised, this will leave para (2) providing, unqualified, that the payments shall be treated *in all respects* as made in the relevant payment quarters specified in para (3), which would lead to the basic rate amount being arrived at not by reference to a rate of 30 per cent., but in part by reference to the basic rate for 1986–87, and in part to that for 1987–88. In any event, the Revenue's contention does not deal with the problem that, for the reasons I have explained, Regulation 3 is also in part *ultra vires*.

Now it is true that, so far as severance is concerned, the Court no longer has to proceed on the basis of what has been called the blue pencil test, under which the Court can only sever the good from the bad where the bad can be excised by a simple deletion of words from the instrument in question. It is now open to the Court, taking advantage of the remedy of a declaration, to declare that the instrument in question shall not take effect in so far as the maker of the instrument has acted beyond his powers, even though verbal severance of the offending provision is not on the old blue pencil approach: see *Director of Public Prosecutions* v. *Hutchinson*[1], [1990] 3 WLR 196, 199–220, *per* Lord Bridge of Harwich. But the Court must nevertheless be satisfied that, in so proceeding, it is effecting no damage to the substantial purpose and effect of the instrument.

However, as I see it, the problem in the present case is that the mistake made by the Revenue in Regulations 3 and 11(4) cannot be cured, either by the simple excision of particular words (as proposed, by the Revenue with regard to Regulation 11(4)), or by a declaration. In the case of Regulation 11, this is because what is left after the excision of Regulation 11(4) has the effect of providing for rates of tax different from those intended by the Revenue. What is required in these circumstances is not merely the excision of Regulation 11(4), but the introduction of a new provision in its place. The same applies, in my opinion, to Regulation 3, for there too a new provision is required in relation to payments made after February 1986 and before 6 April 1986.

The Court of Appeal considered that, in relation to Regulation 11, the invalidity of Regulation 11(4) did not leave a complete blank as to the applicable rate, because s 343(1A) provided that the omitted interest should be brought into account at the rate fixed for the year of assessment under which it has to be brought in. But the difficulty with Regulation 11 is that, once para (4) is removed, para (2) is left free to operate in unqualified terms and specifies the payment quarters in which the relevant payments are treated in all respects as made; and plainly the Revenue did not intended para (2) to operate to fix the reduced rate amount and basic rate amount applicable in relation to such payments. So far as Regulation 3 is concerned, if it is declared *ultra vires* so far as it relates to payments made after February 1986 and before 6 April 1986, then there is no provision which identifies the year

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(1) [1990] 2 AC 783

A of assessment under which such payments have to be brought in. In truth, what is required in relation to the offending parts of both Regulation 11 and Regulation 3 is not merely that they should be quashed or declared ineffective in so far as they are *ultra vires*, but that fresh provision should be made for the appropriate rates of tax in place of those which were unlawfully specified. It is however, in my opinion, no part of the Court's function to legis-
B late in this way. It is for the Revenue, if it is still able to do so, to amend both regulations to bring them in accordance with its statutory powers.

For these reasons I would, like my noble and learned friend, Lord Oliver of Aylmerton, allow the appeal as regards the invalidity of Regulation 11, and also allow the appeal as regards the invalidity of Regulation 3 in so far
C as it relates to the period after February and before 6 April 1986.

Lord Lowry:—My Lords, in this appeal I have concluded that neither in its original form nor as amended by s 47(1) of the Finance Act 1986 did s 343(1A) of the Income and Corporation Taxes Act 1970 authorise the collection of additional tax from the Woolwich (amounting to £69m) which was
D referable to the period from 1 October 1985 to 5 April 1986. For convenience I shall call it "the gap period", but without accepting the implication which might thereby gain credence that this appellation signifies a gap in the rightful revenues of the Crown, as the Respondents would contend.

E I gratefully adopt the description which Nolan J. has given of the historical background and the scheme of taxation [1987] STC 654, 655–658, and also the summary contained in the speech of my noble and learned friend, Lord Oliver of Aylmerton, which I have had the advantage of reading in draft. Therefore I can go straight to the main question.

F Not surprisingly, there is much in my noble and learned friend's reasoning which I happily accept, including his cogently expressed opinion that s 343(1A), as first enacted, did not, with regard to the gap period, authorise what the Regulations purported to achieve. It is only when I come to consider the s 47(1) amendment that I feel obliged to adopt a different view. I cannot, however, take a short cut by starting there, because I think it is
G important for me to consider the meaning first of s 343(1), then of the original s 343(1A) and finally of s 343(1A) as amended. Although these provisions are found in my noble and learned friend's speech, it will be convenient to set them out again, together with s 26 of the Finance Act 1984 and s 47(1) of the Act of 1986. Section 343(3) is, of course, also important but I can refer to the text of my noble and learned friend's speech.

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Here are subss 343(1) and (1A) as they had effect at the time the Regulations were made on 13 March 1986 to come into operation on 6 April 1986:

"343(1) The Board and any building society may, as respects any
I year of assessment ending before 6th April 1986, enter into arrangements whereby—(a) on such sums as may be determined in accordance with the arrangements the society is liable to account for and pay an amount representing income tax calculated in part at the basic rate and in part at a reduced rate ... and (b) provision is made for any incidental or consequential matters, and any such arrangements shall have effect notwithstanding anything in this Act: ...

(1A) The Board may by regulations made by statutory instrument make provision with respect to the year 1986–87 and any subsequent year of assessment requiring building societies, on such sums as may be determined in accordance with the regulations, to account for and pay an amount representing income tax calculated in part at the basic rate and in part at the reduced rate determined for the year of assessment concerned under section 26(1)(a) of the Finance Act 1984; and any such regulations may contain such incidental and consequential provisions as appear to the Board to be appropriate, including provisions requiring the making of returns."

To begin with, s 343(1) had ended with a proviso:

"Provided that in exercising their powers of entering into arrangements under this section, the Board shall at all times aim at securing that (if the amount so payable by the society under the arrangements is regarded as income tax for the year of assessment) the total income tax becoming payable to, and not becoming repayable by, the Crown is, when regard is had to the operation of the subsequent provisions of this section, as nearly, as may be the same in the aggregate as it would have been if those powers had never been exercised."

This was repealed on the enactment of s 26 of the Finance Act 1984 ("section 26"), which applied to arrangements under s 343(1) for the year of assessment 1985–86 and continued to apply to the year 1986–87 and subsequent years. So far as material, it provides:

"26(1) In the year 1984–85 and in every subsequent year of assessment the Treasury shall by order made by statutory instrument determine, a rate which shall, for the following year of assessment, be—(*a*) the reduced rate for the purposes of section 343 of the Taxes Act (building societies); and (*b*) the composite rate for the purposes of section 27 of this Act. (2) The order made under subsection (1) above in each year of assessment shall—(*a*) be made before 31st December in that year; and (*b*) be based only on information relating to periods before the end of the year of assessment in which the order is made. (3) Whenever they exercise their powers under this section the Treasury shall aim at securing that (assuming for the purposes of this subsection that the amounts payable by building societies under section 343 of the Taxes Act and by deposit-takers under section 27 of this Act are income tax) the total income tax becoming payable to, and not being repayable by, the Crown is (when regard is had to the operation of those sections) as nearly as may be the same in the aggregate as it would have been if those sections had not been enacted. (4) In relation to the exercise of their powers under this section at any time before the year 1988–89, the Treasury may regard subsection (3) above as directed only to amounts payable by building societies under section 343 and to the operation of that section. (5) In section 343(1) of the Taxes Act, the proviso and in paragraph (*a*) the words from 'which takes' to 'this section' shall cease to have effect from 6th April 1985 . . ."

Section 47(1) of the Finance Act 1986 ("section 47(1)") was enacted in July 1986 and provided:

A "47(1) In section 343 of the Taxes Act (building societies), subsection (1A) (which was inserted by the Finance Act 1985 and enables the Board to make regulations requiring societies to account for amounts representing income tax on certain sums) shall have effect *and be deemed always to have had effect* with the insertion after the words 'in accordance with the regulations' of the words '(including sums paid or credited before the beginning of the year but not previously brought into B account under subsection (1) above or this subsection)'."

(I have emphasised the words which gave the amendment retrospective effect.)

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Accordingly, subss 343(1) and (1A) must be read for all purposes as follows:

"343(1) The Board and any building society may, as respects any year of assessment ending before 6th April 1986, enter into arrange- D ments whereby—(*a*) on such sums as may be determined in accordance with the arrangements the society is liable to account for and pay an amount representing income tax calculated in part at the basic rate and in part at a reduced rate: and (*b*) provision is made for any incidental or consequential matters, and any such arrangements shall have effect notwithstanding anything in this Act: . . . E

(1A) The Board may by regulations made by statutory instrument make provision with respect to the year 1986–87 and any subsequent year of assessment requiring building societies, on such sums as may be determined in accordance with the regulations (including sums paid or F credited before the beginning of the year but not previously brought into account under subsection (1) above or this subsection), to account for and pay an amount representing income tax calculated in part at the basic rate and in part at the reduced rate determined for the year of assessment concerned under s 26(1)(*a*) of the Finance Act 1984; and any such regulations may contain such incidental and consequential provi- G sions as appear to the Board to be appropriate, including provisions requiring the making of returns."

I shall call the amendment introduced by s 47(1) "the section 47 amendment".

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I have been impressed by and grateful for the cogent and often persuasive arguments of counsel on either side, but I remain unimpressed by talk of injustice and inequity on the one hand and by references to lost interest and the gap period on the other. Nor am I affected by ingenious examples of the strange financial results which could conceivably arise from the adoption of one construction or the other. If something unforseen were to happen, it might be dealt with by enactment or regulation, but in reality such figures as your Lordships have seen tend to show a fairly steady investors' income from year to year. But, subject always to interpreting the words of s 343(1A), the Woolwich is entitled to say that it would be surprising and *prima facie* contrary to accepted tax principles for the amount representing the investors' income tax for the years of assessment 1986–87 and 1987–88 to be based on

the income of two-and-a-half years. As Sir Nicolas Browne-Wilkinson V.-C. said in the Court of Appeal [1989] STC 463, 470([1]):

> "As to counsel for Woolwich's second submission, *there is no doubt* that in relation to the charging of income to income tax it is fundamental that in any one tax year the income brought into tax must be the income of a period of one year only. Tax payable in any one tax year may be measured by the income of some other year; but in all cases the income brought into tax is the income of one year and no more."

The words I have emphasised show that the Vice-Chancellor was expressing a general view about income tax, which of course must be subject to the meaning of the relevant provisions in this case, to which I now turn.

Section 343(1) allows the Board and a building society *as respect any year of assessment* ending before 6 April 1986 to enter into arrangements whereby on such sums as may be determined in accordance with the arrangements the society is liable to account for and pay an amount representing income tax calculated in part at the basic rate and in part at a reduced rate: "as respects any year of assessment" refers to the year of assessment of the society's investors (in the instant case the fiscal year 6 April 1985 to 5 April 1986), the period of *charge* and all payments and credits of dividends and interest by the society to investors during that period would, but for the arrangements, be charged by deducting the tax before payment. The phrase "on such sums as may be determined" means "by reference to such sums as may be determined"; in the instant case this is by reference to the sums paid or credited to investors during the society's accounting year 1 October 1984 to 30 September 1985 (this choice of arrangement having been made by the Woolwich in 1940–41). The building society then becomes liable to account for and pay to the Revenue an amount representing the investors' income tax for the year of assessment 1985–86. The "reduced rate" of income tax was calculated under the arrangements, when the proviso was part of s 343(1), in order to achieve what has been called revenue neutrality, as described by my noble and learned friend, Lord Oliver. My explanation is illustrated by the arrangements (which were put in evidence) entered into by the Board with building societies for the year of assessment 1985–86. The arrangements (giving here only the words needed to illustrate the point) provide:

> "1. Charge to income tax at composite rates
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> By virtue of section 343 . . . the society shall be liable to account for and pay an amount representing income tax calculated at the rate of 25.25 per cent. for 1984–85 and 25.25 per cent. for 1985–86 '—(the rates by chance coincided but could have differed)—' . . . *on the total of the following sums*: (a) the sum of the dividends and interest . . . payable *in the basis period* by the society to its investors . . .
>
> 2. Charge to income tax at basic rates
>
> The society shall also be liable to account for and pay an amount representing income tax calculated at the basic rates for 1984–85 and 1985–86 *on the total of the following sums*: (a) The sum of the dividends and interest payable in the basis period by the society to its investors . . .

([1]) Page 607G/H *ante*.

A 3. Determination of basis period

(1) Subject to the provisions of this paragraph the basis period shall be determined as follows: (a) If an account is made up for a period of one year to a date in the year of assessment 1985–86 and is the only account made up to a date in that year of assessment, that period shall B be the basis period. (b) In any other case the Board of Inland Revenue shall decide what period of 12 months ending in the year of assessment 1985–86 shall be the basis period. (2) If during the year of assessment 1985–86 the society ceases or unites with another society to which paragraph (3) below applies, the basis period shall be that period ending on the rate of cessation or union and commencing on 6 April 1985 . . . " C (Emphasis added)

The words I have emphasised above show *on* what sums it was determined that the building society was liable to account for and pay an amount representing income tax. Those sums were payable to investors in the basis period, that is, the accounting year of the society ending during the year of D assessment.

The word "on" in s 343(1) and in the arrangements made thereunder is very important. It is a neutral word and, like many words in the English language, including statutory language, takes its colour, like a chameleon, from its surroundings or, more literally, its meaning from its context. The society's E accounting year, called "the basis period" in the arrangements (a familiar concept in relation to the income tax liability of a taxpayer), is the measurement period and the amount representing the investors' income tax in respect of the fiscal year 1985–86 which the building society is liable to account for and pay is measured by reference to the sums payable to the investors in the basis period (in the case of the Woolwich 1 October 1984 to 30 September F 1985). In the context of s 343(1) "on" means "by reference to" and not "charged on" or "in respect of". That this must be so is obvious when one recalls that part of the basis period (1 October 1984 to 5 April 1985) lies outside the year of assessment and is not part of a chargeable period for the purposes of 1985–86 income tax. Mr. Gardiner, for the Woolwich, referred your Lordships to ss 108 and 109 for the use of the phrase "in respect of" G and to ss 115(1), 116(1), 117(2), 118(1), 119 and 120(1) of the Act of 1970 as exemplifying the use of "on" meaning "by reference to" and also cited *Duckering* (*Inspector of Taxes*) v. *Gollan*(1) [1964] 1 WLR 414. I need only refer to the Case Stated 415–418 and to s 132 of the Income Tax Act 1952 for further examples of "on" used in this sense.

H The grammatical structure of s 343(1) should be noted. The building society is liable to do something, namely "account for and pay". The object of those verbs is "an amount representing income tax", and the verbs are modified by the adverbial phrase "on such sums as may be determined", which is not an adjectival phrase qualifying "income tax". This is confirmed both by the position of the phrase in the subsection and by the wording of I paras 1 and 2 of the arguments which I have mentioned above.

Section 343(1A) closely follows s 343(1) in its wording. The difference is that regulations are to take the place of arrangements and, that the regula-

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(1) 42 TC 333.

tions, once made, will require building societies to pay. But the difference ends there. The regulations are to make provision *with respect to* (s 343(1) said "as respects") a year of assessment, starting with 1986–87. The building societies' obligation will be *to account for and pay an amount representing income tax* (that is the investors' income tax) *calculated in part at the basic rate* (so far the words emphasised are the same as in s 343(1)) and in part at the reduced rate determined for the year of assessment concerned under s 26(1)(a) of the Finance Act 1984. (The difference in wording here, which does not alter the effect, is due to s 26 having been enacted before s 343(1A), whereas, apart from repealing the proviso, it was necessary to amend s 343(1) when s 26 was introduced.)

And they were to pay that amount *on such sums as may be determined under the regulations* (instead of in accordance with the arrangements).

Your Lordships do not know whether the responsible Government department had the 1986 Regulations in draft or even in mind when s 343(1A) was enacted. We do know, however, that on 19 March 1985 the Chancellor of the Exchequer had indicated that, since the banks were to change their system of payment of tax on bank interest on 6 April 1985, the building societies would be put on a similar footing from 6 April 1986.

The scheme of taxation in s 343(1A), apart from the fact that it would no longer be an optional alternative to the conventional way of taxing payments to investors, was just the same as that of s 343(1). It dealt with the investors' tax liability in respect of one fiscal year and obliged the building societies to pay an amount "representing income tax", that is, the investors' income tax for (in the first place) 1986–87. The duty of the Treasury under s 26(1) and (3) to determine a reduced rate and achieve revenue neutrality is to be exactly the same as it was with respect to the year 1985–86. And "on such sums" still means "by reference to such sums". This rather wearisome analysis makes it easy to see why Mr. Stamler, for the Revenue would not admit, even with regard to s 343(1), that the word "on" in the phrase "on such sums as may be determined" meant "by reference to," because one can see that it already has the same meaning in s 343(1A). I scarcely need to point out that tax is "charged on" all sums paid or credited to investors in the relevant year of assessment. Those sums are readily ascertainable; they do not need to be "determined" either "in accordance with the arrangements" or "in accordance with the regulations".

After the enactment of s 343(1) three events occurred:

(1) the regulations were made and laid and came into operation on 6 April 1986; (2) the Woolwich commenced proceedings for judicial review; and (3) section 47 was enacted.

I shall assume that the object of introducing the s 47 amendment was either to make it clear that s 343(1A) was a valid statutory authority for the making of the impugned regulations or to convert that provision into a valid statutory authority. It seems highly probable, in so far as it is relevant at all, that one of these explanations is the right one. The ambivalence of any diagnosis is consistent with the Revenue's presentation of their case. Before Nolan J. they seem to have relied on s 343(1A) and to have introduced the s 47 amendment as a make-weight, but in the Court of Appeal the emphasis seems to have been on the effect of the amendment, while before your

A Lordships the Revenue advanced both arguments with equal vigour. Mr. Gardiner, while conceding that it would be *ex abundanti cautela*, suggested that the purpose of the s 47 amendment was to make it clear that the Regulations of 1986 could require building societies to pay amounts by reference to sums which had been paid or credited before 6 April of the relevant year of assessment. It clearly has that *effect*, in my opinion, assuming that B such an effect was ever needed, and therefore I am inclined to infer that the amendment had a different *purpose* from that attributed to it by Mr. Gardiner. For the Revenue, Mr. Stamler, when arguing that s 343(1A) as enacted already authorised the Regulations of 1986 in their entirety (except Regulation 11(4)), said that the s 47 amendment was on that basis unnecessary. I shall come back to this point, but I take leave of it for the moment by C saying that "the purpose of legislation" is not the same thing as "the intention of Parliament", which may be gathered only from the actual words of the statute.

Before examining the amendment I will briefly consider one or two things which the Regulations of 1986 *could* have done consistently with s D 343(1A) as drafted, and, indeed, with the arrangements under s 343(1). They could have continued the existing scheme by requiring building societies to account for and pay an amount representing income tax by reference to the society's accounting year (in the case of the Woolwich, 1 October 1985 to 30 September 1986). Or they could have designated a year commencing on 1 March 1986 and ending on 28 February 1987. Or they could have made the E basis period coterminous with the year of assessments, in which case the sums *by reference to which* the amounts were to be paid would have precisely coincided with the sums on which tax was chargeable. The Regulations could have provided for an annual payment on 1 January, as before, or for a different system such as quarterly payment on specified days, as they actually did. The true cause of complaint is not the Board's choice of the gap period F but the combination of the gap period with the relevant years of assessment, which results in a basis period of excessive length.

Let me now consider what the s 47 amendment did. I shall set it out again:

G "(including sums paid or credited before the beginning of the year but not previously brought into account under subsection (1) above or this subsection)."

It is, of course, necessary to incorporate the new words into the syntax of the existing subsection and to keep in mind, as I have already said, that H s 343(1A), of which the amendment is now a part, is modelled on, and now refers to, s 343(1).

Accordingly, as the legislature now tells us, "such sums as may be determined in accordance with the Regulations" include "sums paid or credited I before the beginning of the year but not previously brought into account under subsection (1) above or this subsection". So the s 47 amendment simply defines more specifically (I do not say it extends) the expression "such sums as may be determined in accordance with the Regulations". It achieves *absolutely nothing else*. (I emphasise these words because I believe they provide the key to the problem.) The consequence is that s 343(1A) *as amended* continues to authorise precisely the same regulations as it authorised in its

original form, namely, regulations requiring building societies to account for and pay an amount representing income tax (that is, representing investors' income tax in respect of the relevant year of assessment) and to pay that amount by reference to such sums (now more exactly defined) as may be determined in accordance with the regulations. The Treasury's duty to determine the reduced rate and to aim at revenue neutrality, as required by s 26, is unchanged. In fact nothing has changed.

With all respect to those who may take a different view, I do not consider that s 343(2) as amended by s 47(2) of the Finance Act 1986 places any difficulty in the way of construing the word "on" as "by reference to" in s 343(1A) or s 343(1A) as amended. The original s 343(2), which is concerned with a building society's corporation tax, refers to "dividends or interest payable *in respect of* shares in, or deposits with or loans to, the society", and para (*a*) of the subsection speaks of "the amount accounted for and paid by the society *in respect thereof* as representing income tax," meaning "in respect of any such dividends or interest". Dividends and interest *are* paid in respect of shares etc. and in para (*a*) the amount accounted for and paid by the society as representing income tax *is* paid *in respect of* the actual dividends and interest paid to investors in the society's accounting period, but it is also paid *on* (or by reference to) "such sums as may be determined in accordance with the arrangements" under s 343(1).

Section 343(2) was the subject of two amendments by s 40(4) of the Finance Act 1985 and s 47(2) of the Finance Act 1986 to have effect for 1986–87 and subsequent years and, as amended, provides as follows:

> "(2) For any year of assessment to which regulations under subsection (1A) above apply, dividends or interest payable in respect of shares in, or deposits with or loans to, a building society shall be dealt with for the purposes of corporation tax as follows: (*a*) in computing for any accounting period ending in the year of assessment the income of the society from the trade carried on by it there shall be allowed as a deduction the actual amount paid or credited in the accounting period of any such dividends or interest, together with any amount accounted for and paid by the society in respect thereof as representing income tax, (*b*) in computing the income of a company which is paid or credited in the year of assessment with any such dividends or interest in respect of which the society is required to account for and pay an amount in accordance with the regulations, the company shall be treated as having received an amount which, after deduction of income tax, is equal to the amount paid or credited, and shall be entitled to a set off or repayment of income tax accordingly, (*c*) no part of any such dividends or interest paid or credited in the year of assessment shall be treated as a distribution of the society or as franked investment income of any company resident in the United Kingdom."

Nothing arises before para (*b*). It is concerned with computing the income of a company "which is paid or credited *in the year of assessment*" (for present purposes not before 1986–87) "with any such dividends or interest" (that is, such dividends or interest as are mentioned in line 2 of para (2)). The words introduced by s 47(2) are "in respect of which the society is required to account for and pay an amount in accordance with the regulations". They describe further the dividends or interest referred to. There is a close parallel with my analysis of para (2)(*a*): the dividends and interest are

A paid to the company *in the year of assessment* and in respect of those dividends and that interest the building society is required to account for and pay an amount in accordance with the regulations; by looking again at s 343(1A) it can be seen that the amount is to be paid "on such sums as may be determined in accordance with the regulations", by looking again at s 343(1A) it can be seen that the amount is to be paid "on such sums as may B be determined in accordance with the regulations", but I can see absolutely no indication that the dividends or interest *in respect of which* that amount is to be paid under s 343(1A) are or can be dividends or interest paid to the company in 1985–86.

In my judgment the only possible means of escape from this conclusion C is (1) to assume or pretend that "on" in the phrase "on such sums as may be determined" in ss 343(1) and 343(1A) means and has always meant "charged on" (because the s 47 amendment did not change the meaning of "on") and (2) to say, as the Revenue did, that "brought into account" in the amendment means "brought into account for the purpose of paying tax thereon". As to the first point, I refer to my earlier observations. As to the second, the D words "not previously brought into account under subs (1) above" are significant. From an income tax point of view, the "arrangements" and s 343(3) have ensured that the sums paid or credited to investors in the whole of the year of assessment 1985–86, including the sums paid or credited in the gap period, have already been "brought into account" in the Revenue's sense of the word, but the sums paid or credited in the gap period have not been E "brought into account" in the way envisaged by arrangements made under s 343(1). In this respect s 343(1A) has the same effect as s 343(1) and continues to have that effect after amendment.

The Revenue's case depends, in my view, on three fallacies. These are:

F (1) The theory that the deductions made by the building societies during the gap period from the dividends and interest which they paid to their investors represent money for which the building societies ought to account to the Revenue. This view explains the inclusion of the gap period by the Regulations of 1986 together with the relevant fiscal years and, when advanced in argument, is calculated to predispose a court to accept the G Revenue's interpretation.

(2) The confusion of the probable purpose of introducing the amendment with the intention of Parliament as it is to be gathered from the words used in the Act.

H (3) The acceptance of the proposition that, if the words of the s 47 amendment clearly *refer to* the sums paid or credited in the gap period, they also have the *effect* contended for by the Revenue, I shall deal with these points in turn.

I (1) As respects the year of assessment 1985–86, the Board and the Woolwich entered into arrangements whereby the entire liability of the investors for income tax (except for tax at the higher rate) was discharged, and the Woolwich was also discharged when on 1 January 1986 it paid to the Board an amount representing that income tax. Thereafter no income tax or money representing income tax was due in respect of the fiscal year 1985–86. The Woolwich does not pay income tax in its own right but has a personal

liability for corporation tax with which this case is not concerned. Under proper regulations the investors' income tax liability for the year 1986–87 and subsequent years of assessment ought to be disposed of on similar principles, using either the year of assessment itself or some other 12-month period as the basis period. If a cessation or merger occurs, special rules will apply, as also happened under the former arrangements. The legitimate and declared object of the old arrangements and the new regulations was and is to collect each year from the building societies an amount representing the investors' income tax *for that year*. When the Woolwich and other building societies changed their basis period in 1940–41 from the accounting year which ended before the year of assessment to the accounting year which ended during the year of assessment, there was a gap period, but this did not give rise to legislation to fill the gap. Thus to disregard the 1940 gap was correct in principle. The Regulations of 1986 introduced a current year basis of assessment in place of what had been in part a previous year basis. The Revenue's proposition amounts to a spurious charge of unjust enrichment against the building societies and overlooks the point that both s 343(1) and s 343(1A) are not directed to the tax liability of building societies in their own right but are concerned with the liability of building societies (as an alternative to conventional tax accounting) to pay to the Revenue in respect of each single year of assessment an amount representing the *investors'* income tax *for that year*.

(2) Assuming (in all probability rightly) that the purpose of the s 47 amendment was to validate the Regulations of 1986 by retrospectively enlarging the authority to make them, it does not follow that the amendment achieved that purpose. One fallacy is to infer that purpose must be equated with legislative intention as expressed in the words used in the enactment. Another fallacy is to conclude that, because no other sensible purpose of the amendment can be found, therefore the purpose contended for by the Respondents not only *existed* (which can be readily enough inferred) but *has been achieved* (which calls for an examination of the enacting words in their context). If the purpose of an enactment, including an amending enactment, can be found and if the words of the statute are on one possible construction apt to achieve the purpose, but not on another construction, then the Court should prefer the construction which achieves the purpose, but, if no reasonable construction of the words used can lead the Court to conclude that the purpose has been achieved, the intention of Parliament as elicited from the words of the statute prevails and the purpose, however obvious, is defeated. There is no room for a purposive construction if the words to be construed will not bear the interpretation sought to be put upon them and it must always be borne in mind that the art of statutory interpretation can be applied only when the provision to be interpreted is ambiguous. I refer to *Maxwell on Interpretation of Statutes*, 12th ed. (1969), pp. 1–2, and 28–29 and also to *Bennion, Statutory Interpretation* (1984), p. 237 where the matter is put succinctly:

> "The distinction between the purpose or object of an enactment and the legislative intention governing it is that the former relates to the mischief to which the enactment is directed and its remedy, while the latter relates to the legal meaning of the enactment."

(3) The unacceptability of this proposition is obvious.

I turn now to the judgments delivered in the Courts below.

A The judgment of Nolan J. is worthy of careful study and, I suggest to your Lordships, of considerable respect as well. After describing the effect produced by the Regulations of 1986 as a truly astonishing result, the Judge added [1987] STC 654, 660([1]):

> "Parliament is omnipotent, and if it enacted that income tax for any year should be paid on the income to two years or the income of twenty years, then that would be the end of the matter; but in none of the Finance Acts of this or of the last century has it ever sought to levy a year's income tax upon the income of more than a year. If it wished to do so one would expect the clearest terms to be employed. The suggestion that it has implicitly authorised the Revenue to achieve such a result by way of delegated legislation is one which defies acceptance."

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He then said, at pp. 660–661([2]):

> "By claiming further tax (albeit from the taxpayer rather than directly from its members) upon the dividends and interest received by the members during that period" (i.e. the gap period) "the Revenue are, as it seems to me, going back on that arrangement. I can see nothing in section 343(1A) which authorises them to do so."

D

Having adverted to the preceding year basis of assessment, he continued, at pp. 661–662([3]):

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> "The income thus taxed is none the less in law the income of the year of assessment, albeit artificially measured in this way. As Lord Donovan said in *Duckering (Inspector of Taxes)* v. *Gollan*([4]) [1965] 1 WLR 680, 689 . . . 'My Lords, it is a truism which the Appellant does not dispute that United Kingdom income tax for any year of assessment for which the tax is granted by Parliament is a levy upon the income of that year. It is not a levy upon the income of a preceding year, nor does it become so by virtue of the fact that this latter income may be used to measure the amount of tax payable.'
>
> Precisely the same principle applies, of course, when the income used as a measure is income of a period ending in the current year of assessment rather than in a preceding year of assessment. That sometimes happens in the case of income charged under Case VI of Schedule D (see section 125 of the Income and Corporation Taxes Act 1970) which it will be noted expressly incorporates the requirement that the period whose income is used as a measure must not exceed 12 months.
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> One result of the system of using as the unit of measurement the income of a period which has ended before or during the year of assessment concerned is that when that system ceases to operate it leaves a gap. It leaves a period running from the end of the last unit of measurement until the end of the last year of assessment for which the system is in operation. The actual income of that gap will not be used as a measure of liability unless the legislation contains special provisions avoiding that result. Various provisions to that effect are set out in the Act of 1970: see, for example, section 118 dealing with trades and professions. It is not necessary for me to set out these provisions in detail. Their gen-

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([1]) Page 597E/F–G *ante*. ([2]) Page 598C *ante*. ([3]) Pages 598G/599E *ante*.
([4]) 42 TC 333, at page 349.

eral purpose is to prevent artificial exploitation of the gap. In every case they do this by providing for the inclusion in the measure of liability of income which would otherwise drop out. Equally in every case—and this is the point—for each fresh period whose income is brought into the measure another period of equal length is left out, so that in all cases the assessment for the year remains an assessment upon not more than 12 months' income. The inevitable corollary is that a gap remains. It is just a different gap of the same length. The only way in which it could be avoided would be by loading more than 12 months' income into the measure of liability for a year of assessment, and that is anathema."

The Judge reviewed the arguments and found himself unpersuaded by the arguments for the Revenue. He then turned to s 47(1), saying at p. 662(1):

> "The reason why it figures late in my judgment (as it did in the argument of counsel for the Crown) is because of the difficulty I find in seeing what effect it has, or was intended to have."

Having quoted the subsection he concluded his judgment as follows, at pp. 662–663(2):

> "If this was intended to mean that the Revenue were authorised to use dividends and interest paid before 6 April 1986 as a measure of liability in 1986–87 following the same pattern as in previous years it would be intelligible, though I would have thought it unnecessary. Counsel for the Crown contends, however, although without basing his case upon section 47(1), that it goes further than that and confirms the validity of the tax imposed by regulations 3 and 11 on dividends and interest paid before 6 April 1986. This I cannot accept. Section 47(1) still leaves the power conferred by section 343(1A) as a power exercisable only with respect to 1986–87 and subsequent years. It does not purport to legitimise the tax sought to be imposed by regulation 11 at the 1985–86 rates. It does not purport to withdraw the protection of section 343(3)(b) from the taxpayer's members for that year. If section 47(1) has misfired, or has been based upon an erroneous view of the law, it would not be the first piece of fiscal legislation to do so.
>
> The case for the taxpayer was also supported by a comparison with the treatment accorded to bank interest by section 27 of the Finance Act 1985, and by helpful illustrations in figures of the effects which regulations 3 and 11 would produce. Upon these points too I accept the validity of the arguments put forward by counsel for the taxpayer; but it would do nothing to improve an already over long judgment if I set out in full. It is enough to say that for the reasons given I consider the regulation to be *ultra vires* in so far as they purport to levy tax upon dividends and interest paid by building societies in 1985–86."

My Lords, I derive comfort, if little satisfaction, from those words of a Judge who is thoroughly experienced in tax matters: "If s 47(1) has misfired, or has been based upon an erroneous view of the law, it would not be the first piece of fiscal legislation to do so." I think that that is what has happened here and I feel that what might otherwise be an improbable conclusion on my part is fortified by the presence of the admittedly *ultra vires* Regulation 11(4), by the Revenue's admission (or assertion) during the hear-

(1) Page 600B *ante*. (2) Page 600D/E–H/I *ante*.

A ing of this appeal that they were wrong to charge 1985–86 rates of reduced tax in relation to the period 1 March to 5 April 1986 and by the fact that the Revenue's primary case before Nolan J. involved the contention that the original s 343(1A) was itself effective to authorise the impugned portions of the Regulations. Against that background, it would not be at all surprising if s 47(1) had missed its mark.

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My Lords, I now come to the judgment of Sir Nicolas Browne-Wilkinson V.-C. [1989] STC 463 with which the other members of the Court of Appeal concurred and which I take up at p. 469. The Vice-Chancellor's first observation was that the case for the Revenue before Nolan J. was fundamentally different from that presented to the Court of Appeal because, C having earlier relied "to a very minor extent" on s 47, they now contended "that Woolwich is *not accountable for the tax payable by the investors* and that the whole case turns on the s 47 words which . . . retrospectively validate the regulations." (Emphasis added.) He then said that Crown counsel's argument was very straightforward, to the effect that the omitted interest(1):

D "falls fairly and squarely within the express terms of the section 47 words, i.e., the omitted interest consists of 'sums paid or credited before the beginning of the year but not previously brought into account under section 343(1) or (1A)'. It follows, says counsel for the Crown, that the regulations cannot be *ultra vires* in requiring payments to be made in respect of the omitted interest."

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The Vice-Chancellor expresses a tentative conclusion, at pp. 469–470(2):

"As a matter of ordinary construction, I find the conclusion contended for by counsel for the Crown inescapable. The section 47 words are clear and they cover the present case. Moreover the regulations had F been made and their validity challenged before Parliament had to consider the Finance Bill 1986. It was in those circumstances that Parliament enacted section 47 of the Finance Act 1986 which introduced the section 47 words. In such circumstances, in the absence of any other reason for Parliament to have enacted section 47 so as to deem section 343(1A) always to have included the section 47 words, the inference G must be that Parliament intended to put to rest the existing challenge to the validity of the regulations.

What, then, is the contrary argument? Counsel for Woolwich relied on the cumulative effect of three submissions to persuade us that the section 47 words should not be given their apparent meaning: first, that section 47 was retrospective in its effect and should be narrowly con- H strued; second, that the effect of regulation 11 was to charge to tax in one year the income of a period of more than one year and this was an impossible concept under our tax law—it was anathema; third, that the Crown's argument, if right, involves an element of double taxation against which the Court should always lean. I will deal with these submissions in turn."

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In fairness to Mr. Gardiner, who has appeared for the Woolwich at every stage of these proceedings, it should be acknowledged that in your Lordships' House he did not at all concede that the s 47 words, *according to*

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(1) Page 606I *ante*. (2) Page 607B/C–E/F *ante*.

their apparent meaning, authorised the regulations complained of. What he said here, rightly in my opinion, was that, although those words clearly *referred to* the sums paid or credited in the gap period, they did not authorise the exaction of tax, or an amount representing tax, on those sums *as well as* on the sums paid or credited in the relevant years of assessment, namely, 1986–87 and 1987–88.

The next passage in the Vice-Chancellor's judgment, at p. 470, is crucial[1]:

> "It was principally the anathema argument that led the Judge to the conclusion that regulation 11 was *ultra vires.* But he was proceeding on the basis, urged before him by the Revenue, that Woolwich was accounting for the tax payable by its investors. In this court the Revenue changed its stance and submitted that the liability of Woolwich under section 343 is not a liability to account for the income tax payable by its investors but a liability *sui generis*, i.e. a liability to make a composition payment 'representing', and calculated by reference to, what would otherwise have been the net tax liabilities of the investors as a body as opposed to accounting for each investor's tax deducted by Woolwich. Therefore, argues the Revenue, the anathema argument has little, if any, relevance to the present case.
>
> In my judgment the revised Revenue stance is correct. Under section 343(3) interest is payable to investors without deduction of tax and the investor is not liable to basic rate tax on such interest. Therefore the building society in making the lump sum payment is not accounting to the Revenue for the tax liability of anybody. Nor is the lump sum payable by the society calculated by reference to what would, apart from section 343(3), have been the tax liability of each individual investor. The lump sum is a sum calculated on a statistical basis seeking to reflect the net 'take' for the Revenue from all investors in all building societies. The nature of the payment to be made by the building society is a composition payment calculated by reference to the aggregate net tax liability of all investors but is not a payment of income tax as such."

Here the Court of Appeal accepted the Revenue's contention that the liability *under section 343* was not a liability to account for the income tax payable by its investors but a liability *sui generis*. I need not repeat every word of the sentence which I have just quoted above. The anathema, it will be recalled, is the ideal of computing a year's tax liability by reference to a period of more than one year, and the Court has accepted the Revenue's submission—that the anathema argument has no relevance *because* the amount to be paid is not income tax but merely represents income tax. Therefore, said the Vice-Chancellor, the building society in making the lump sum payment is not accounting to the Revenue for the tax liability of anybody. He then aptly summarised the effect of s 26(3), but disregarded the fact that inextricable from the anathema argument is the point that the Treasury simply cannot achieve revenue neutrality by determining a reduced rate of tax if the area of the "net take" measures two-and-a-half years when the periods with respect to which provision is made by the Regulations of 1986 add up to two years. Indeed, to put it this way is a concession to the Revenue because under s 26(1) and (3) the Treasury must look to the year of assess-

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[1] Pages 607I/608D *ante*.

A ment 1986–87 while tax at the basic rate and the reduced rate is collected on the immediately preceding six months but payment thereof is spread over two years. The fact that what has to be paid is an amount representing income tax and not the tax itself is quite irrelevant.

B The Vice-Chancellor continues on the same tack, at p. 471[1]:

"For these reasons the arrangements affecting the lump sum liability of building societies are a unique form of statutory impost to which ordinary principles of tax law do not necessarily apply. Since the composition payment is designed to put the Revenue in the position it would have been in had interest been payable under deduction of tax, there is C nothing inherently contrary to principle in bringing into the computation of such composition payment sums which would normally have suffered deduction of tax (if there had been no arrangement) and which, due to the change in the system introduced by the 1985 Act, would otherwise have dropped out of account. Given the special nature of the lump sum payment, to my mind the anathema argument has little D force."

This statement, with great respect, completely disregards the wording of s 343(1) and (1A) and the arrangements made in the past and even the general drift of the Regulations of 1986, so far as they are not impugned. It E would be strange if ordinary principles of tax law did not apply, when one considers that the purpose of s 343 was not to abandon those principles but, with the help of s 26, to find a practical way of applying them.

After discussing the arguments on double taxation the Vice-Chancellor F concluded the main part of his judgment, at p. 471[2]:

"For these reasons I do not find any compelling reason to depart from the plain meaning of the section 47 words. Even if the factors relied on by Woolwich had more substance, it would still be necessary to give the section 47 words *some* effect: they cannot have been specifically inserted for no reason at all. Counsel for Woolwich suggested that they G were inserted *ex abundanti cautela* to make it clear that there was no objection to the regulation providing that liability should be measured by reference to interest paid before the commencement of the tax year 1986–87. But, in my judgment, this does not fully explain the introduction of the section 47 words. Section 47 is directed to a case in which two requirements are satisfied, *viz*, first, that the interest had been paid H or credited before the beginning of the year and, second, that such interest had not previously been brought into account. No suggestion has been put forward for the presence in section 47 of words referring to monies not previously brought into account save that relied on by the Revenue, i.e. that the words were included to authorise the taxing, in the years 1986–87 and thereafter, of monies not previously brought into I account under the old arrangements.

I am therefore satisfied that the Regulations of 1986 are not *ultra vires* apart from regulation 11(4) which the Revenue accepts is invalid."

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(1) Page 608G–H/I *ante*. (2) Page 609E/H *ante*.

I again have to make the point that it is not only the plain *meaning* of the s 47 words but their *effect* which has to be considered. The rest of the passage quoted is, I hope, adequately covered by what I have said already. A

And now, my Lords, before I finish, I wish to pull together some loose ends and then to comment on the way in which the Revenue put their case to your Lordships. B

Like my noble and learned friend, I am impressed by the argument that an intention (using that word in its proper sense) to produce what Nolan J. described as a truly astonishing result should not be ascribed to Parliament without very clear words. As Mr. Gardiner put it, Regulation 3, shorn of its transitional feature, exhausts the power conferred by s 343(1A) by charging the entire dividends and interest for the year of assessment 1986–87 and the s 47 amendment does not increase or expand the liability to charge. He also submitted that an amount paid by the Woolwich in respect of the gap period dividends and interest discharged no liability of the investors and could not be called an amount representing their income tax of any year of assessment. C D

Another approach for the Woolwich is to ask, "Does s 343(1A) in its original form or as amended authorise the Board to adopt a different principle from that allowed by s 343(1)?" On the analysis which I have made, I suggest that the answer must be "No". It would, moreover, be strange if the Board has been given the power to decide what sums should be charged to tax, as distinct from being used as the measure of the investors' tax. In this connection Regulation 11(2) is an interesting artificial provision: E

> "Subject to the provisions of these Regulations, any such payment shall be treated in all respects as a payment to which these Regulations apply and as made in the payment quarter to which the payment dates specified in paragraph (3) below relate." F

Against the background that no precedent exists for charging tax for a particular year on the income of a period of more than a year, both s 343(1A) and s 26 are directed towards one year of assessment, in the present instance 1986–87. What has to be paid is an amount representing income tax and that can only be the tax chargeable against the investors with respect to 1986–87. Having come this length, I would adopt what my noble and learned friend, Lord Oliver, has said about s 26([1]): G

> "In exercising its powers the Treasury has to assume that the sums payable by the society are income tax—which can only mean income tax for the year of assessment—and to produce the net result that the total income tax becoming payable to the Crown (again in that year of assessment) is no more than it would have been if s 343 (including subsection (1A)) had not been enacted." H

I

Finally I come to the Revenue's presentation of their case which, thanks to the ability of Mr. Stamler, lacked nothing in thoroughness, ingenuity or force. For the first time he will be unable to answer back. So I must be careful with my comments.

([1]) Page 620F/G–G/H *ante*.

A (1) Mr. Stamler would not concede that "on" meant "by reference to" in s 343(1) or s 343(1A). I formed the view that the position he took up was necessary to his case but untenable.

(2) He ruthlessly disregarded s 26 in the interpretation of s 343(1A). Again he had to do so.

B

(3) He described the Woolwich as an accounting party in respect of its gap period deductions, but both the investors and the Woolwich have fully accounted for the investors' 1985–86 income tax. The fact that the Woolwich has made deductions from the gap period payments does not oblige it to pay

C the deductions to the Revenue because, while the Woolwich has to account for and pay all deductions made in 1986–87, it cannot credibly be argued that the gap period deductions represent investors' income tax of either 1985–86 or 1986–87. The forbidden choice of 1985–86 rates by the Board in Regulation 11(4) illustrates by accident the Revenue's vulnerability.

D (4) Mr. Stamler said, "Admittedly, you cannot tax the investors again in respect of the gap period, but you *can* tax the Woolwich." He made the point that the Woolwich paid no tax in respect of the gap period (except, presumably, such corporation tax as was due). With respect, that means nothing unless it can be correctly equated with failing to pay an amount representing income tax of the depositors, a point I have covered already.

E

(5) It seems to me that the Revenue's argument on these lines depends not on the meaning of s 343(1A) but on the supposed absurdity of the Woolwich's getting away with non-payment of tax (which was not lawfully due).

F

(6) Mr. Stamler argued that there was no reason for symmetry between the period in respect of which the investors' liability for income tax has been discharged and the period in respect of which the liability of the Woolwich to account for an amount representing income tax has to be discharged. He also said that the concept of measurement was irrelevant to the situation of the

G Woolwich and that for "an amount *representing* income tax" in s 343(1A) (and presumably also in s 343(1)) one might as well substitute "an amount *instead of* income tax". These propositions, with respect, are further examples of the complete abandonment of ss 343(1A) and 26 in favour of saying, "The Woolwich made deductions in the gap period and must pay them to us."

H

The only authority I will mention is *Partington* v. *Attorney General* (1869) L.R. H.L. 100 in which Lord Cairns said, at p. 122:

> "If the person sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax,
>
> I
>
> cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be. In other words, if there be admissible, in any statute, what is called an equitable construction, certainly such a construction is not admissible in a taxing statute, where you can simply adhere to the words of the statute."

My Lords, I have not seen in the Revenue's printed case or heard in argument any reasoned statement which shows how s 343(1A) or s 47(1) achieves the result contended for by the Revenue. Accordingly, I would allow this appeal.

Appeal allowed, with costs.

[Solicitors:—Solicitor of Inland Revenue; Messrs. Clifford Chance.]

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