

Colonial Life Insurance Company (Trinidad)  
Limited

*Appellant*

*v.*

The Board of Inland Revenue of Trinidad  
and Tobago

*Respondent*

FROM

THE COURT OF APPEAL OF  
TRINIDAD AND TOBAGO

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JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE  
OF THE PRIVY COUNCIL, DELIVERED THE  
1st JULY 1991  
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*Present at the hearing:-*

LORD KEITH OF KINKEL  
LORD BRANDON OF OAKBROOK  
LORD TEMPLEMAN  
LORD OLIVER OF AYLMEYTON  
SIR ROBERT MEGARRY

*[Delivered by Lord Oliver of Aylmerton]*

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This appeal from the Court of Appeal of Trinidad and Tobago (*des Iles*, *McMillan* and *Davis J.J.A.*), although involving a consideration of some lengthy and somewhat ill-drafted documents, raises what is, in the end, a very short point, that is to say whether income received by the appellant company ("*Colonial Life*") during the year 1971 from the investment of moneys paid to it as the consideration for the provision of pensions for employees of a number of contributing companies is exempt from corporation tax as "profits of approved annuity business" pursuant to the provisions of paragraphs 3(4) of the Fourth Schedule of the Corporation Tax Act of Trinidad and Tobago.

In December 1977, *Colonial Life* was assessed to tax in respect of (*inter alia*) the income concerned. On 29th December 1978 it appealed against the assessment to the Tax Appeal Board which, on 9th November 1984, allowed the appeal and referred the assessment back to the respondent, the Board of Inland Revenue, for reassessment on the basis that the income concerned was exempt from tax. At the request of the respondent a case was stated for the opinion of the Court of Appeal and on 28th July 1989 that court allowed the

appeal with costs and confirmed the assessment. From that decision Colonial Life now appeals to their Lordships' Board.

In the year to which the assessment relates the relevant legislation was contained in Part II of the Finance Act 1966, as amended, but it was subsequently published separately in the Corporation Tax Act (Ch. 75:02) and since, both in the Tax Appeal Board and in the Court of Appeal, the arguments were addressed by reference to the provisions of that Act, it will be convenient if their Lordships adopt the same course. Corporation tax is imposed by section 3 of the Act upon the annual profits of "any company" but special provision is made (in section 14) for (*inter alios*) insurance companies (including life insurance companies) to which there are applied the provisions of the Fourth Schedule. The rate of tax payable under section 3 is specified in the First Schedule which prescribes a rate of 45% except in the case of profits of the long-term insurance business of an assurance company not transferred to the shareholders' account, where the rate is 15%. Paragraphs 2 and 3 of the Fourth Schedule contain provisions for various aspects of the business of assurance companies carrying on "long-term insurance business" to be treated as separate classes of business and for the deduction of expenses (regulated by paragraph 3) to be calculated separately in the computation of the profits arising from each class. "Long-term insurance business" is defined (in paragraph 5) as meaning (*inter alia*) "general annuity business" and "approved annuity business". The critical provision for the purposes of this appeal is that contained in paragraph 3(4) of the Fourth Schedule which provides that "the profits of approved annuity business shall not be chargeable to tax except to the extent that such profits are distributed to shareholders".

The Act itself contains no definition of "approved annuity business" but paragraph 5(2) applies the First Schedule of the Insurance Act 1966 where the expression is defined as including "any annuity business undertaken for the purpose of establishing and conducting a deferred annuity or approved fund or scheme under section 16 and an approved deferred annuity plan under sections 16A to 16E of the Income Tax Ordinance". It is unnecessary for present purposes to refer to those sections of the Income Tax Ordinance (which do not refer to an approved plan which is not a deferred annuity plan) because the respondent concedes that the definition is merely an inclusive one and that if (which is disputed) the income with which this appeal is concerned can properly be described as a profit arising from "annuity business" that annuity business is in fact "approved annuity business".

The aspect of Colonial Life's business which has given rise to this appeal is that which is described, perhaps rather ineptly, as "deposit administration business", an expression which, as will be seen, embraces the receipt of moneys from the trustees of approved pension schemes as the consideration for the provision by Colonial Life of the pension and other benefits prescribed by the schemes. Broadly the respondent's contention, which succeeded in the Court of Appeal, was and is that Colonial Life was in fact carrying on two severable businesses, that is to say, a business of receiving and managing deposits, which was not annuity business at all and from which the profit in question arose, and a separate business of providing annuities whose connection with the deposit business was simply that it was provided for in the same contract and was paid for out of the deposited funds.

In order to appreciate the basis for this submission, it is necessary to consider, at least in outline, the pattern of the pension schemes which underlie the deposit administration business. It is agreed that these are represented by the specimen scheme referred to both by the Tax Appeal Board and by the Court of Appeal, namely that relating to the Orange Grove National Company Limited. The company pension scheme takes the familiar form of a Trust Deed and Rules approved by the Inland Revenue. In the particular case the Trustee was the Bank of Nova Scotia Trust Company Ltd. and the Deed recites that by agreement between the company and the trustees the pensions provided by the Rules have been secured by means of a Deposit Administration Contract. Clause 2 establishes a Staff Pension Fund Plan and incorporates the Rules which are contained in the Schedule, and clause 3 provides for the payment by the company to the trustees of the contributions payable or to be deducted under the Rules. Clause 3(ii) imposes on the trustees the obligation of providing the benefits of the scheme but at the same time empowers them to delegate that responsibility. It is in the following terms:-

"The Trustees shall out of the Fund pay or provide for the payment of all such benefits to Members or to their designated beneficiaries as shall be payable in accordance with the Rules, provided that the Trustees shall be deemed to have provided such benefits by entering into a Deposit Administration Contract or any other contract under which the benefits required by the Rules are provided."

The only other provision of the Deed which requires mention is the Investment Clause (clause 9) which confers an absolute unrestricted power of investment but also includes expressly a power to invest in Deposit Administration Contracts.

The Rules also follow a familiar pattern, providing for employees of the company to become members of the

scheme, for contributions by members and by the company to be paid to the trustees, and for pensions to be payable on retirement at the rate of one sixtieth of average annual salary over the past five years of employment multiplied by the appropriate number of years of pensionable service. There are provisions for early retirement, for lump sum payments on death before retirement and for deferred pensions for employees leaving the company's service before retirement.

As already mentioned, the Trust Deed recites that the trustees have already exercised their power to delegate by entering into a Deposit Administration Contract and it is upon the terms of that Contract that the argument for the respondent relies. It is dated 24th January 1972, is made between Colonial Life (referred to in the Contract as "the Company") and the trustees, and takes the rather curious form of a short single-page agreement whose detailed provisions are contained in a separate annex. By its terms Colonial Life agrees as follows:-

" TO ADMINISTER A DEPOSIT ADMINISTRATION FUND for the benefit of certain Employees of the ORANGE GROVE NATIONAL COMPANY LIMITED (Hereinafter called the Employer)

Who are included under this Deposit Administration Contract (hereinafter called the Contract) and who continue to be included hereunder until retirement date or prior death, and to pay to the person or persons entitled the Pensions and other Benefits to be determined in accordance with the Provisions hereof.

The effective date of this Contract shall be the 1st day of March, 1970.

This Contract is issued in consideration of the payment of Deposits by the said Trustees to the Company as provided for in the Provision 4 hereof.

The provisions appearing on the subsequent pages hereof form part of this Contract as fully as if recited at length over the signatures hereto affixed."

The Provisions commence with a number of definitions of which the following are material for present purposes:-

"1.1 'Plan' shall mean the Pension Plan for the Employees of Orange Grove National Company Limited, as constituted by the Trust Deed and Rules dated the 2nd day of December, 1970, together with those amendments thereto that are both delivered to and accepted by the Company. ...

- 1.3 'Member' shall mean any employee who upon fulfilling the eligibility requirements of the Plan, becomes a Member of the Plan.
- 1.4 'Registered Member' shall mean any person who is a member or former Member of the Plan for whom or for whose beneficiary the Company is directed by the trustees to purchase Benefits under this Contract in accordance with the terms of the Plan.
- 1.5 'Pension' except where specifically otherwise provided, shall mean an annual amount payable in monthly instalments in advance, to which a Registered Member or his beneficiary is entitled under this Contract.
- 1.6 'Deposits' shall mean any amounts of money which shall be paid to the Company by the Trustees from time to time under this Contract.
- 1.7 'Fund' shall mean the fund established in accordance with Provisions 4 and 5 wherein Deposits are invested with the general funds of the Company."

Clause 2.2 provides that pensions as determined by the Plan may not be provided for a registered member except through the provisions of the Contract. Provision 3 sets out the administrative responsibilities of the trustees and the company respectively. In summary, the company is to keep an account of the Fund and furnish an annual statement of the balance up to the last day of February of the previous year of "Deposits" made during the year, interest allocated to the fund, "deductions made to purchase Pensions and to meet Administration Charges", and any other financial transactions affecting the fund; it is to prepare and print Members' Rule Books and literature for distribution to members; it is to keep records of prospective accrued benefits and contributions, to deliver to the trustees an annual statement for each member showing his prospective retirement and accrued death benefits, to provide when necessary an estimate of any additional deposit required to fund benefits, to maintain a record of beneficiaries, to calculate death, retirement or termination of service benefits of members, to provide a quinquennial actuarial report and valuation and to submit to the Internal Revenue Department such material as may be required.

The following provisions are important and must be recited verbatim:-

"PROVISION 4 - DEPOSITS.

- 4.1 Subject to the provisions of Provision 8 hereof the Trustees shall make and the Company shall accept Deposits to the Fund required for the

funding of the Pensions and other Benefits payable under the Plan being the contributions to be made by the Employer and the Members under the Rules."

"PROVISION 5 - THE FUND

5.1 The Company shall establish a Fund wherein the balance at any time shall be the excess of the amounts credited to the Fund in accordance with this Provision over the amounts charged by the Company.

5.2 Credits to the Fund shall consist of:-

- (a) The Deposits referred to in Provision 4.1.
- (b) Interest shall be credited on the 31st day of December in each year and shall be calculated on the minimum monthly balance during each month. The rate of interest to be credited shall during the first five (5) years of the Fund be not less than 6½% per annum and during the next ten (10) years shall not be less than 5% and thereafter shall be at such rate as the Company shall from time to time determine.

5.3 Charges against the Fund shall consist of:-

- (a) Purchase payments in accordance with Provision 7.1 for the purchase of Benefits.
- (b) The Administration Charges which the Company shall be entitled to make for administering the Fund as set out in the Schedule to this Contract. Such charges shall include all fees for Actuarial services performed by or on behalf of the Company.
- (c) Expenses incurred by the Company in connection with the printing of Members' Rules Books and other printing expenses incidental thereto."

Their Lordships note in parenthesis that the reference in 5.3(a) to provision 7.1 is clearly a misprint for provision 6.1.

"PROVISION 6 - RETIREMENT BENEFIT PURCHASES

6.1 (a) Normal Retirement Benefit - At the direction of the Trustees the Company shall, by a deduction of the required purchase payment from the Fund, purchase the immediate normal retirement Benefit or any deferred annuity on termination of service with respect to any Member who qualified for such Benefit or annuity as determined by the Trustees in accordance with the Plan. ..."

Provision 7 relates to payment of the benefits and contains little of significance for present purposes save that provision 7.3 refers to the making of "annuity pension or other payments" and provision 7.4 provides that the liability of the company with respect to any member shall be determined "on the basis of the Deposits actually received by the Company on such Member's behalf in accordance with the terms of this Contract". Provision 8.1 provides for the contingency of suspension or discontinuance of deposits, in which event the Contract continues with respect to any balance remaining in the Fund until the Fund is exhausted. Finally provision 8.2 enables the trustees, on discontinuing deposits, to direct the company to transfer 95% of the accumulated balance of the Fund to another depository or to the trustees but subject to a right of retention for a period of ten years during which, if required, the company will be liable to provide benefits due under the Plan to the extent to which the accumulated balance is able to meet them.

An analysis of the true nature of these provisions discloses at once the inappropriateness of some of the terms used. For instance it is clear that the term "deposit" is not used in the conventional sense of the deposit with a banker where the depositor is entitled to withdraw sums deposited, either with or without notice, and to receive interest in the meantime. There are, it is true, provisions such as 8.2 which enable the trustees to achieve a return of the unapplied balance of the Fund if it is decided to terminate the arrangement for the future, but the essence of the transaction is that the pension contributions are paid over to Colonial Life outright as the consideration for providing to members of the pension plan with the appropriate annuities. Similarly, although the word "purchase" is used in provision 6, the Contract does not in fact contemplate a purchase in any normally accepted sense of the word, for Colonial Life cannot utilise its own moneys to purchase from itself.

Realistically, the Trust Deed and the Rules and the Deposit Administration Contract have to be read together as a single scheme. Under the Trust Deed the trustees assume the obligation of providing the pension benefits prescribed by the Rules and that obligation is discharged by Colonial Life in consideration of the receipt, as part of its funds, of the employers' and employees' contributions. The Fund established under provision 5 and consisting of the contributions and guaranteed interest is necessary accounting machinery not only for Colonial Life's own internal purposes but also to enable it to provide the trustees with the necessary valuations for it to be determined whether additional deposits may be required and to ascertain the extent of Colonial Life's liability in the event of the scheme being discontinued. It does not, however, represent a trust fund in which either the trustees or

the members of the scheme can claim any proprietary interest. In essence, the Contract is simply one for the purchase by the trustees from Colonial Life of annuity benefits for the members and for the provision by Colonial Life of all the administrative services required for implementing the pension scheme.

The way in which the income received by Colonial Life from deposits under the Contract was dealt with in the relevant year was as follows. The global investment income earned during the year was apportioned amongst classes of business in the ratio of the average of the opening and closing balances of the various funds attributable to those classes. The Deposit Administration Contract scheme represented a ratio of 22.090% of the global assets to which was attributed net income of \$893,540, from which there fell to be provided a sum of \$681,315 guaranteed interest and a sum of \$71,024 as the scheme's proportionate share of expenses of earning the income. There thus remained a balance of \$141,201 representing the profit for the year on the Deposit Administration business and it was upon this sum that the corporation tax which is the subject matter of this appeal was assessed. It is not in dispute that the sum in question was never distributed to the shareholders of Colonial Life but was retained as part of the Fund and in fact was utilised in fulfilment of Colonial Life's obligations under the Contract in subsequent years.

The salient facts as found by the Tax Appeal Board were as follows:-

- "(1) The pension plan under which benefits were to be provided was one that had been approved by the Board of Inland Revenue under the Ordinance;
- (2) Under the deed, the trustees were empowered to contract out the duty of providing pensions under a deposit administration contract and had in fact so done;
- (3) The members of the plan were included in the deposit administration contract and the appellant was responsible for providing pensions directly to them;
- (4) The benefits due under the pension plan were a charge on the Fund;
- (5) Under the deposit administration contract, the appellant was more than a mere depository for the management of investments, as it was also obligated to provide pension benefits."

The fourth finding was strictly inaccurate, in that what is charged on the Fund is in fact the capital value at retirement of the benefits due, but this is immaterial. Upon these findings the Board concluded:-

"In the light of the above, we hold that the earnings of the appellant under the deposit administration contract are profits from the carrying on of approved annuity business, and that pursuant to section 3(4) of the Schedule are exempt from corporation tax to the extent that they have not been distributed to shareholders."

In the Court of Appeal the leading judgment was delivered by des Iles J.A. It was his view, with which the other two members of the Court concurred, that what was of essential importance was the purpose for which the profits of the Deposit Administration business might be applied. He accepted that if the Contract provided for the immediate purchase of deferred annuities upon receipt of the contributions, the profits might then have been exempt from tax, but held that because the profits over and above the guaranteed rate of interest were available to Colonial Life as part of its general funds they were not profits of annuity business and so were taxable even though not distributed to shareholders. The ratio of the decision is contained in the following passage from his judgment:-

"In my view, even though both operations are contained in the Contract, they nevertheless remain separate and distinct transactions and whilst the respondent is obligated to provide the Trustees with the 'total of the contributions payable or to be deducted in accordance with the Rules', the monies from which the respondent pays these contributions belong entirely to the respondent, albeit derived from the Deposit Administration business, and not part of the Approved Annuity business, and was thus available as part of the respondent's general funds to do with as it pleased ... I would hold that the transaction of business under the Contract was in the nature of commercial trading and not limited to the purchase of annuities."

There is clearly some confusion here which is perhaps understandable having regard to the unusual way in which the relevant documents have been drafted. The phrase "the total of the contributions payable or to be deducted in accordance with the Rules" comes from the Trust Deed, not the Deposit Administration Contract, and refers to the employers' and employees' contributions payable by the employer to the trustees. What Colonial Life was obliged to provide was not the contributions but the pension annuities provided for in the Rules. Nor does the respondent now seek to uphold the court's reasoning that because profits earned from investment of contributions over and above the guaranteed interest payments are available to Colonial Life as part of its general funds they cannot constitute profits exempt from tax under paragraph 3(4) of the Fourth Schedule. That paragraph is concerned only with the business from which the profits arise and not with their disposition in the

hands of the recipient so long as they are not distributed to shareholders. Nevertheless the respondent submits that the Court of Appeal's decision that the Contract constituted two separate transactions, only one of which was "approved annuity business", ought to be upheld. What is said is that the true analysis of the Contract is that up to the point at which, in relation to each retiring employee, Colonial Life receives the instructions of the trustees to "purchase" the appropriate pension annuity, by debiting the Fund with the market value of such annuity at that time, it is engaged simply in the carrying on of a business of taking deposits on behalf of the trustees just as if the contribution had been deposited with the bank or other deposit-taking company. On this analysis, the approved annuity business did not commence until the effecting of the notional "purchase" of each separate annuity and constituted a separate and independent business.

Their Lordships find themselves unable to accept this as a realistic view of the true nature of the Contract. The Contract is a single agreement for the carrying out by Colonial Life on behalf of the trustees of their obligations under the Trust Deed to provide pension annuities for the members of the scheme in accordance with the Rules, and the fact that it contains accounting provisions for the establishment of a separate Fund to cover such provision and for maintaining the actuarial solvency of the Fund so established cannot alter the essential nature of the Contract as one for the provision of annuities. The sole purpose of the Fund is to provide annuities and it is, in their Lordships' opinion, impossible to regard the profits and losses generated or sustained from it, whether they take the form of a surplus or deficit of investment income, surplus of administration fees over costs or an excess of the "purchase" price of annuities over the actual cost of provision, as other than profits of "annuity business". The Trust Deed having provided expressly for the benefits to be secured by a Deposit Administration Contract and the Pension Plan thus constituted having been approved by the Inland Revenue there can, as is conceded, be no room for argument that the business is other than "approved annuity business".

Their Lordships accordingly allow the appeal and restore the decision of the Tax Appeal Board. The respondent must pay the appellant's costs before the Tax Appeal Board, the Court of Appeal and their Lordships' Board.