IN THE MATTER OF ARTICLE 146 OF THE CONSTITUTION

ARIS CHRISTODOULOU,

Applicant,

and

THE REPUBLIC OF CYPRUS, THROUGH THE COMMISSIONER OF INCOME TAX,

Respondent.

(*Cases Nos.* 71/69 *and* 72/69).

Income tax—Assessable income—Scholarship—"Υποτροφία"*—Gains or profits from employment taxable under section* 5(1)(*b*) *of the Income Tax Laws,* 1961 *to* 1969*—Employee on scholarship under a scholarship agreement with employers—Payment by his employers for his maintenance and tuition at the university not liable to tax under said section* 5(1)(*b*)*—Such payments also exempt from tax as being "income arising from a scholarship"* ("Υποτροφία")*—Section* 8(*d*) *of the Income Tax Laws* (supra).

Words and Phrases—Scholarship—"'Υποτροφία" *in section* 8(*d*) *of the Income Tax Laws* 1961 *to* 1969.

Cases referred to:

Owen v. *Pook* (*Inspector of Taxes*) [1969] 2 All E.R. 1; (H.L.);

Hochstrasser (*Inspector of Taxes*) v. *Mayes* [1959] 3 All E.R. 817; (H.L.);

Coussoumides v. *The Republic* (1966) 3 C.L.R. 1;

Bridges v. *Hewitt, Bridges* v. *Bearsley* [1957] 2 All E.R. 281 at p. 301 per Morris, L.J.

The facts as well as the relevant statutory provisions are set out in the judgment of the Court annulling the assessments challenged by this recourse made by the Applicant under Article 146 of the Constitution.

Recourse.

Recourse against the validity of the decision of the

Respondent in respect of Applicant's taxable income for the years of assessment 1966 and 1967, respectively.

Chr. Demetriades, for the Applicant.

G. Tornaritis, for the Respondent.

Cur. adv. vult.

The following judgment* was delivered by:-

LOIZOU, J.: By these two recourses the Applicant challenges the validity of the decision of the Respondent, the Commissioner of Income Tax, in respect of his taxable income for the years of assessment 1966 and 1967 respectively. Both recourses relate to the same facts and by consent of the parties they were heard together.

The facts are not disputed and may be summarized as follows:

The Applicant is an employee of Lanitis Farm Ltd. On the 19th September, 1965, he entered into an agreement with his employers the terms of which are set out in the letter dated 24th September, 1965 (*exhibit* 1); by the said agreement the employers granted to the Applicant a scholarship for further studies in the university "Davis" of California in the United States of America. The scholarship was for a period of 18 months. Under the terms of the agreement the Applicant would, during the period of his absence, continue to receive the benefits from his employment on the basis of his then salary plus such further sum as would make the total sum received by him during the first year of his studies $ 3,400 and during the last six months $ 1,700 which sums represented the total cost necessary for his maintenance and tuition; the employers further undertook to pay for Applicant's air-fare to and from the United States of America. On his part, the Applicant undertook upon completion of his studies to work for the company for a period of five years at such salary as is normally paid by the company from time to time. There was provision in the agreement whereby the company reserved the right to discontinue payment and recall the Applicant, if he did not make satisfactory progress in his studies and also that failure on his part to resume his work with the company after the completion of his studies or to complete the five years' service, would render him liable to refund all expenses paid by the

* For final decision on appeal see (1971) 2 J.S.C. 141 to be reported in due course in (1970) 3 C.L.R.

company in connection with his studies, or such part thereof as would be proportionate to the unexpired period of such service, as the case might be.

It is common ground that the cost of attending the university had risen from $ 3,400 to $ 3,850 per annum (*exhibit* 2 refers) and that the employers paid the whole of such cost. Further it is not disputed that during the period of his studies the Applicant was a full-time student of the said university devoting all his time to his studies and had ceased rendering his services to his employers.

In computing Applicant's income for the years 1966 and 1967 the Respondent treated a part of the sum paid by his employers under the scholarship agreement equal to his salary prior to the period of his studies, as taxable income. He based his decision, as he clearly states in his letter of the 13th January, 1969, (*exhibit* 3) which he wrote in answer to Applicant's objection, on information received from Applicant's employers. Such information is contained in the letter dated 23rd October, 1968 (*exhibit* 4) addressed by Applicant's employers to the Respondent in which they make a distinction between that part of the expenditure incurred by them in connection with Applicant's studies, which was equal to the salary of the Applicant, and which they treat as such, and the additional expenditure in excess of such sum.

The grounds upon which Respondent based his decision are set out in paragraphs (a) and (b) of his letter *exhibit* 3 which read as follows:

«(α) Αἱ φορολογίαι σας ἐβασίσθησαν ἐπὶ τῆς δηλώσεως τοῦ ἐργοδότου σας καὶ ὡς ἐκ τούτου οὐδεμία μείωσις τούτων εἶναι δυνατή.

(β) Ἔχω ἐξετάσει ἐπισταμένως τὰς ὑφ' ὑμῶν γενομένας παραστάσεις, ἔχω δὲ ἀποφασίσει ὅτι τὸ ὑπὸ τοῦ ἐργοδότου σας καταβληθὲν ποσὸν ἀποτελεῖ φορολογητέας ἀποδοχὰς ἐν τῇ ἐννοίᾳ τοῦ ἄρθρου 5(β) τοῦ Περὶ Φορολογίας τοῦ Εἰσοδήματος Νόμου ἀρ. 58 τοῦ 1961 ὡς ἐτροποποιήθη ὑπὸ τῶν Νόμων 4/63 καὶ 21/66.»

The grounds of law upon which the Application is based are: (a) that the whole amount paid by the employers is in fact and/or in law a payment made for a full-time scholarship and is, therefore, exempted from taxation by virtue of section

8(d) of Law 58/61; and (b) that the said amount cannot be considered as taxable income within the meaning of section 5(1)(b) of Law 58/61.

Respondent in his Opposition contends that the assessments complained of were properly and lawfully made under section 5(1)(b) as the disputed sums were part and parcel of Applicant's emoluments and as such income derived from the Republic, and, therefore, taxable.

It was submitted on behalf of the Applicant that the payments in question are not taxable income under the provisions of section 5(1)(b) of Law 58/61 because they were not made for services rendered by the tax-payer as an employee and, therefore, were not "gains or profits from any office or employment" as required by the section. In any case, learned counsel submitted the disputed payments were exempt from the tax by virtue of the provisions of section 8(d) of the Law. In support of his case he referred to a number of authorities with some of which I shall be dealing presently.

Learned counsel for the Respondent, on the other hand, submitted that "this case falls under section 5(1)(b) of Law 58/61 i.e. that the Applicant was receiving gains or profits from an employment whilst serving abroad". He further submitted that the Applicant was under a contract of employment and under the provisions of that contract he was sent to the United States to take a course, and that the salary was paid to him for future services. With regard to section 8(d) learned counsel expressed the view that the status of the Applicant was that of an employee trainee and not that of a person receiving a. scholarship; and this in view of the condition in the agreement whereby Applicant was bound to work for his employers for a number of years after the completion of his studies. Learned counsel did not cite any authority in support of his argument.

It is convenient, at this stage, to set out the relevant statutory provisions, as they stood at the material time, to which reference has already been made:

> "5-(1). Tax shall, subject to the provisions of this Law, be payable at the rate or rates specified hereafter for each year of assessment upon the income of any person accruing in, derived from, or received in the Republic in respect of –

(a) .....

(b) gains or profits from any office or employment, irrespective of whether the person employed is serving in Cyprus or elsewhere, including the estimated annual value of any quarters or board or residence or of any other allowance granted in respect of employment whether in money or otherwise;"

8. There shall be exempt from the tax –

.....

.....

(d) the income arising from a scholarship, exhibition, bursary or any other similar educational endowment held by a person receiving full-time instruction at a university, college, school or other recognized educational establishment;"

I propose to deal with section 5(1) first. As there is corresponding statutory provision in England (vide Schedule E of the Income Tax Act 1952) it is helpful to look at some of the English authorities on the point.

In *Owen* v. *Pook* (*Inspector of Taxes*), a House of Lords case reported in [1969] 2 All E.R. p. 1, it was held that travelling expenses reimbursed to a medical practitioner, who had to work at two places 15 miles apart, by his employers were not emoluments, in the sense that they were not income or profit received by him and, therefore, were not chargeable.

A case more to the point and which is cited with approval in the *Pook* case is that of *Hochstrasser* (*Inspector of Taxes*) v. *Mayes*. This also is a case which was eventually decided by the House of Lords and it is reported in [1959] 3 All E.R. p. 817. In this case the tax-payer, Mayes, was an employee of Imperial Chemical Industries. Under his service agreement he was bound to serve anywhere in the United Kingdom of Great Britain and Northern Ireland and his employers were at liberty to have him transferred anywhere within those limits. In order, however, to assist married male members of its staff to buy suitably located houses for occupation by themselves and their families in the event of their being transferred from one part of the country to another as a result of their employment, I.C.I. operated a housing scheme under which it

provided interest-free loans for the purchase of houses and guaranteed the employee against a loss through depreciation in the value of the house. Under the terms of the agreement signed by each employee taking advantage of the scheme, he was required, if he wished to sell or let the house on being transferred to a new place of employment in the company's service, to offer to sell the house first to the company. If the company accepted it, the employee received the current market value ascertained by valuation and if the company declined he was free to sell the house; and in either case he received from the company the amount by which the price fell short of his expenditure on the house. The tax-payer in this case took advantage of the housing scheme and signed the relative agreement. He was later transferred by the company to a new district, and he thereupon offered his house for sale to the company under the agreement. The company declined the offer, and he sold the house with the consent of the company. He suffered a loss on the sale and the company paid him £350, being the amount for which the company admitted liability. The Crown claimed income tax under Schedule E in respect of that sum of £350. It was held that the £350 was not liable to tax under Schedule E because the Crown failed to show that it was a payment for services (and consequently, that it was a profit from the employee's office or employment), there being nothing in the housing agreement to suggest that such was the nature of the payment except the relationship of the parties, which was not sufficient to justify such a conclusion.

Viscount Simonds in the course of his speech to the House cited a passage from the judgment of Upjohn, J., before whom the matter first went, which in his Lordship's opinion appeared to sum up the law in a manner which could not be improved on. The following is the passage cited:

> " In my judgment, the authorities show this, that it is a question to be answered in the light of the particular facts of every case whether or not a particular payment is or is not a profit arising from the employment. Disregarding entirely contracts for full consideration in money or money's worth and personal presents, in my judgment not every payment made to an employee is necessarily made to him as a profit arising from his employment. Indeed, in my judgment, the authorities show that, to be a profit arising from the employment, the payment must be made in reference to the service the employee renders by virtue

of his office, and it must be something in the nature of a reward for services past, present or future".

Lord Radcliffe in the same case said (at p. 823):

" The test to be applied is the same for all. It is contained in the statutory requirement that the payment, if it is to be the subject of assessment, must arise 'from' the office or employment. In the past several explanations have been offered by Judges of eminence as to the significance of the word 'from' in this context. It has been said that the payment must have been made to the employee 'as such'. It has been said that it must have been made to him 'in his capacity of employee'. It has been said that it is assessable if paid 'by way of remuneration for his services' and said further that this is what is meant by payment to him 'as such'. These are all glosses and they are all of value as illustrating the idea which is expressed by the words of the statute. But it is, perhaps, worth observing that they do not displace those words. For my part, I think that their meaning is adequately conveyed by saying that, while it is not sufficient to render a payment assessable that an employee would not have received it unless he had been an employee, it is assessable if it has been paid to him in return for acting as or being an employee".

To substantially the same effect is the dictum of Morris, L.J., in *Bridges* v. *Hewitt, Bridges* v. *Bearsley* [1957[2 All E.R. p. 281 at p. 301 where he said:

"..... the fact that someone who receives a benefit is the holder of an office does not by itself prove that what he received was a profit from the office. That has to be decided by considering on the evidence whether what was received was received as remuneration for the services rendered in the office".

The above passage was adopted by Upjohn, J., as the true test in deciding whether a certain payment was within the scope of Schedule E in his judgment in the *Hochstrasser* case.

Lastly I must refer to the case of *Coussoumides* v. *The Republic* (1966) 3 C.L.R. 1; although the facts of that case were different the issue turned on the application of section 5(1)(b) of Cap. 323 which was substantially the same as the

corresponding section of Law 58 of 1961 and a great number of useful authorities, which I need not repeat here, on the principles applicable, were reviewed.

The first question then that falls for consideration in the present case is the nature of the payments made to the Applicant by his employers and, more particularly, whether the payments in question come within the scope of section 5(1)(b) of the Law, or, in other words, whether the employment was the *causa causans* of the disputed payments. Perhaps the question might be posed even more simply, in the words of the section, thus: were the disputed payments received by the Applicant gains or profits from his employment? In the light of the authorities I am clearly of opinion that the answer must be in the negative; to my mind it is obvious that such payments were made in connection with his studies under the scholarship agreement and not by way of remuneration or reward for his services, even though the fact of his employment may have been the *causa sine qua non* of the scholarship agreement.

In spite of the conclusion that I have reached, which disposes of these cases, I think that I should deal briefly with the second point i.e. whether the disputed payments are exempted from income tax by virtue of the provisions of section 8(d); in other words whether such payments amount to "income arising from a scholarship" or to quote from the original Greek text "εἰσόδημα πηγάζον ἐξ ὑποτροφίας".

The meaning of the word "ὑποτροφία" as set out in three Greek dictionaries that I have looked up ('Επιτροπῆς Φιλολόγων, Πρωΐας καὶ Δημητράκου) is "ἡ ὑπὸ τρίτου καταβαλλομένη δαπάνη πρὸς συντήρησιν καὶ ἐκπαίδευσιν σπουδαστοῦ". Having regard to the circumstances of this case I am of the opinion that the disputed payments were made for the maintenance and studies of the Applicant in the university "Davis" in the United States of America and consequently such payments come within section 8(d) and are exempt from the tax.

For all the above reasons both recourses succeed. In the result the decisions of the Respondent challenged by the recourses are hereby declared *null* and *void.* The Respondent to pay Applicant's costs which I assess at £20.

Sub judice decisions annulled;
order for costs as above.