1982 September 18

[PIKIS, J.]

IN THE MATTER OF ARTICLE 146 OF THE CONSTITUTION

CONSTANNE ESTATES LIMITED,

Applicants,

v.

1. THE REPUBLIC OF CYPRUS, THROUGH THE ATTORNEY-GENERAL,
2. THE MINISTER OF FINANCE, THROUGH THE COMMISSIONER OF INCOME TAX,

Respondents.

(*Case No.* 239/79).

Practice—Recourse against income tax assessment—Initial burden of proof rests on the applicant as in any other recourse.

Income tax—Additional assessment—Possible whenever Commissioner of Income Tax bona fide forms the view that the tax payer was undercharged as a result of an earlier assessment—Section 23 *of the Assessment and Collection of Taxes Law.*

Words and phrases—"Rent".

Income tax—Rent—Premium—Lease agreement of ten years' duration —50% of the rent of the ten years period prepaid—Subsequent agreement relieving lessees of their obligations under contract of lease, in consideration of compensation—Unappropriated rents agreed to be surrendered as part of such compensation —Amount received under the lease agreement, in every sense, a payment of rent and its pre-payment a premium—Liable to tax under section 5(1)(*f*) *of the Income Tax Laws,* 1961–1977 *—Where money is received as rent or as premium, nothing that happens subsequently may alter, retrospectively, its character at the time of payment.*

Mrs. Georghallides owned a piece of land at Limassol that she agreed to let to the British authorities under settled terms

for use, after development, as a school for English children. Subsequently the property was conveyed to a family company, the applicants, with Mr. and Mrs. Georghallides as shareholders, apparently in the interests of better financial exploitation, who took up the contract with the British authorities, becoming in that way contracting parties thereto. The agreement provided that the applicants, the lessors, would in consideration of the rent stipulated therein, erect a school to be leased to the British authorities for a period of ten years at a yearly rent of £10,000.– payable in the manner agreed therein. The lessees were given the right to extend the lease for a further period of five years, at their option. A substantial part of the total rent, £50,000.–, was paid to the applicants upon execution of the agreement in 1972. In effect, 50% of the rent for the ten-year period was paid in advance, in consequence of which the yearly obligation of the lessees for rent was limited to £5,000.–

Following negotiations between the lessors and the lessees an agreement was reached, whereby in consideration of compensation agreed therein, the lessors relieved the lessees of their obligations under the contract of lease.

The agreement provided, inter alia, that unappropriated rents, amounting to £37,500.–, be surrendered as part of the compensation payable to the lessors, in addition to an amount of £20,000.–, as well as an amount of £1,000.– for repairs. In this way, unappropriated rents were kept as part of the compensation payable to the applicants.

In the accounts submitted to the income tax authorities by the applicants for the years 1972–1974, only a part of the amount of £50,000.– was credited as income, viz. £12,637.–, whereas the balance, £37,363.–, was treated as a receipt other than income.

On May 24, 1979, the respondent Commissioner acting in exercise of his power vested in him by virtue of section 23(1) of the Assessment and Collection of Taxes Law raised a new assessment by means of which the said amount of £50,000.–, which was received in 1972, was treated as chargeable income. Hence this recourse.

It was the case of the applicants that unappropriated rents lost, in consequence of the above agreement, their character

as rent and merged for all purposes in the compensation agreed, entitling them thereby to treat the amount of £37,363.– as capital reserve.

Held, (1) that the initial burden of proof in a recourse directed against tax decisions, rests on the applicant, as in any other recourse.

(2) That section 23 of the Assessment and Collection of Taxes Law confers power on the Commissioner to raise, subject to the time limitation envisaged by the law, an additional assessment whenever he bona fide forms the view that the tax payer was undercharged as a result of an earlier assessment; that it is open to the Commissioner to conclude thus, either because of a new appreciation of the facts or the implications of the law in their application to the particular facts of the case; and that the decision of the Commissioner cannot be faulted on this score.

(3) That "rent" encompasses income from the lease of property; that the amount of £50,000.– was, in every sense, a payment of rent, whereas its pre–payment a premium probably intended to encourage the landlord to enter into the agreement; that, therefore, the amount was subject to permissible deductions liable to tax in accordance with the provisions of s.5(1)(f) of the Income Tax Laws 1961 to 1977; that nothing that happened subsequently could change the character of the receipt; that where money is received as rent or as premium, nothing that happens subsequently may alter, retrospectively, its character at the time of payment; that any such approach would defeat income tax legislation at its core and it would open the door to the avoidance of tax by the subsequent action of the tax payer; that the basic principle of Income Tax Law is that income is liable to tax when received by the tax payer or upon becoming legally entitled to it; accordingly the recourse should fail.

Application dismissed.

Cases referred to:

Coussoumides v. *Republic* (1963) 3 C.L.R. 1;

Kittides v. *Republic* (1973) 3 C.L.R. 123;

Georghiades v. *Republic* (1982) 3 C.L.R. 659;

Solomonides v. *Republic* (1968) 3 C.L.R. 105;

R. v. *Kensington Income Tax Commissioners* [1913] 3 K.B. 870;
Commercial Structures Ltd. v. *Briggs* [1948] 2 All E.R. 1041;
Cellon Finance Co. Ltd. v. *Ellwood*, 40 T.C. 176;
R. v. *Frangos* (1965) 3 C.L.R. 641;
Fitikkides v. *Republic* (1970) 3 C.L.R. 15.

Recourse.

Recourse against the decision of the respondents whereby the amount of £50,000.- paid to applicants in 1972, was subject to permissible deductions, taxable under the provisions of s.5(1)(f) of the Income Tax Laws, 1961-1977.

P. Anastassiades, for the applicants.

M. Photiou, for the respondents.

Cur. adv. vult.

PIKIS J. read the following judgment. Mrs. Georghallides owned a piece of land at Limassol that she agreed to let to the British authorities under settled terms for use, after development, as a school for English children. Subsequently the property was conveyed to a family company, the applicants, with Mr. and Mrs. Georghallides as shareholders, apparently in the interests of better financial exploitation, who took up the contract with the British authorities, becoming in that way contracting parties thereto. The agreement provided that the applicants, the lessors, would, in consideration of the rent stipulated therein, erect a school to be leased to the respondents for a period of ten years at a yearly rent of £10,000.- payable in the manner agreed therein (see exhibit No. 2). The lessees were given the right to extend the lease for a further period of five years, at their option. A substantial part of the total rent, notably £50,000.-, was paid to the applicants upon execution of the agreement; in effect, 50% of the rent for the ten-year period was paid in advance, in consequence of which the yearly obligation of the lessees for rent was limited to £5,000.-. The inevitable inference is that a large portion of the rent was paid in advance in order to facilitate financially the applicants to build the school envisaged by the agreement.

In the accounts submitted to the income tax authorities by the applicants for the years 1972 - 1974, only a part of the amount of £50,000.- was credited as income, viz. £12,637.-,

whereas the balance, £37,363.-, was treated as a receipt other than income. These accounts were subject to minor qualification accepted as correct, a fact intimated to the auditor of the applicants, namely Mr. Andreas Modinos, by a letter dated 28/4/76 (see exhibit No.4). It is not clear whether this acceptance resulted in a final assessment, but that need not concern us in these proceedings for, it is common ground that when the Commissioner purported to revise this assessment, he acted pursuant to the provisions of s.23(1) of the Assessment and Collection of Taxes Law. In exercise of the powers vested in the Commissioner by the aforesaid section 23, the Commissioner raised an additional assessment on 24.5.79 (see exhibit No.7). The intention of the Commissioner to raise an additional assessment was signified to the applicants on 18.12.78 (see exhibit No.3). The applicants objected to the proposed course albeit without success. By the new assessment the amount of £50,000 subject to legitimate deductions, received in 1972, is treated as chargeable income.

The decision to raise an additional assessment was taken, so it appears, after the submission on 29.5.77 by the applicants, of accounts for the year of assessment 1976, whereupon it transpired that the amount of approximately £37,000.-, originally left out of charge, was treated as reserve capital. Thereupon, it dawned to the Commissioner that his original decision was wrong, whereupon, after receiving advice from the Attorney-General, he proceeded to the raising of the additional assessment.

To comprehend the issues raised in their proper perspective, reference must be made to facts subsequent to 1972, leading to the accounts of 1976, particularly those concerning the fate of the lease and its termination, after the tragic events of 1974. Evidently, the British authorities regarded, after the events of 1974, the location of a British school in the soil of the Republic as dangerous and initiated negotiations for the termination of the lease. The negotiations resulted in an agreement between the parties to the lease, whereby, in consideration of compensation agreed therein, the lessors relieved the lessees of their obligations under the contract of lease (see exhibit No.3). The agreement provided, inter alia, that unappropriated rents, amounting to £37,500.-, be surrendered as part of the compen-

sation payable to the lessors, in addition to an amount of £20,000.-, as well as an amount of £1,000.- for repairs. In this way, unappropriated rents were kept as part of the compensation payable to the applicants. It is the case of the applicants that unappropriated rents lost, in consequence of this agreement, their character as rent and merged for all purposes in the compensation agreed, entitling them thereby to treat the amount of £37,363.- as capital reserve. The respondents, on the other hand, maintain that the aforesaid amount is liable to tax as rent or premium, under the provisions of s.5(1) of the relevant legislation. On the last appearance before the Court, counsel for the Republic made it abundantly clear that their claim to bring the amount in question to charge, rested on the ground that it formed, at the time of its receipt, rent or premium. Therefore, the amount of £50,000.- paid in 1972, was, subject to permissible deductions, taxable under the provisions of s.5(1)(f) of the Income Tax Laws 1961 to 1977, as rent or premium. This decision was challenged, hence the present recourse.

The case was well argued, and numerous aspects of the principles of taxation were touched upon in the course of their address, by learned counsel who represented the parties.

The submission of the applicants may be summarised, hopefully, without doing injustice to the elaborate arguments of counsel, into three parts:-

A) The amount of £50,000.- never represented, in its entirety, an income receipt at the time of its payment, or at any subsequent time; that portion which formed part of unappropriated rents was not, at the time of its receipt, income; it was a receipt other than income. One is led to surmise that in the contention of the applicants, only rents payable for a current year are liable to be brought to charge as taxable income.

B) The surrender in 1974 of unappropriated rents, amounting to approximately £37,500.–, merged for all purposes in the compensation paid to the applicants for the rescision of the lease, entitling them to treat it as a capital receipt.

C) The right of the Commissioner to raise an additional asses-

sment under s.23(1), is disputed in the absence of new facts entitling him to reopen the assessment.

The answer of the respondents may, with like brevity, be summed-up as follows:-

(i) The amount of £50,000.- was, at the time of its payment, an income receipt, received as rent or premium, and so liable to tax. The critical period for identifying the character of the payment is the time of its receipt, and inasmuch as it was an income receipt, it was at all times liable to tax. Nothing that happened subsequently could, conceivably, alter the character of the receipt.

(ii) In any event, even if it were permissible to take into consideration and delve into subsequent events, the fact that the amount of £37,500.- was surrendered as compensation, does not, automatically, classify it as a capital receipt; on the contrary, it should be treated as income for it was a payment meant to compensate the applicants for loss of income.

(iii) The decision of the Commissioner to raise an additional assessment is compatible with, and a proper exercise of his powers under s.23(1), he had every right to proceed as he did, on realisation that the amount of £37,500.- was left out of charge as income.

Conflicting submissions were also made with regard to another matter, the initial burden of proof and on whom it rests. We shall go into this aspect of the case first, and then examine the ambit of the powers vested in the Commissioner by s.23(1). The last issue we shall debate, assuming it was competent for the Commissioner to raise an additional assessment, is the merits of the application revolving round the nature of the receipt of £50,000.-.

INITIAL BURDEN OF PROOF IN RECOURSES DIRECTED AGAINST TAX DECISIONS:

In the contention of the applicants, the taxing authority is burdened all along to justify the act of taxation and that encompasses the initial burden of proof as well. For the

respondents it was argued that the presumption of administrative regularity puts, as in every recourse, the initial burden of proof on the applicants. Reference was made, by counsel for the respective parties, to two decisions, apparently conflicting, those of *George Coussoumides* v. *The Republic* (1963) 3 C.L.R. 1 (a judgment of Triantafyllides, J., as he then was), and *Phtis Kittides* v. *The Republic* (1973) 3 C.L.R. 123 (a judgment of Hadjianastassiou, J.). In the former case, it was pointed out that the initial burden of proof, entailing the making out of a case justifying interference, lay on the applicant in a taxation recourse, as in any other recourse. Tax cases are no exception. In the second case, there is a passage (page 133) which, read in isolation, lends support to the submission of applicants. However, if read in the context of the judgment in its entirety, it does not purport to lay down any exceptional principle with regard to the initial burden of proof in cases of taxation. Hadjianastassiou, J., stressed that the onus to satisfy the Court as to liability to pay tax, is on the taxing authorities, a proposition that echoes the general principle, that an act of taxation must be specifically justified by reference to the statute creating liability to pay tax. It seems to me that the learned Judge was referring to the ultimate burden, after the applicant overcomes the initial hurdle as to the burden of proof. So, I discern no irreconcilability between the two judicial pronouncements. But if there was any, it has been resolved beyond doubt by the recent decision of the Full Bench in *Lilian Georghiades* v. *The Republic* (1982) 3 C.L.R. 659, laying down that tax cases are litigated upon the same principles as any other recourse. Having come this far, I must point out that questions relating to the onus and standard of proof are of limited significance in proceedings of a revisional character, proceedings of a fundamentally inquisitorial nature. Questions relating to the burden and standard of proof, are of especial importance in the adversary system of justice, such as that evolved under the common law, and practised in Cyprus in other spheres of litigation. In an adversary system, the outcome of a case depends to an extent on the strength of the case made out by a party, the task of the Court being pre-eminently of an arbitrational character. So, questions relevant to the onus of proof, are of great consequence. This is not so in proceedings of a revisional character, where the principal aim is to conduct an inquiry with a view to ascertaining the legality of the act

of the administration, with the Court exercising a central role in the conduct of the inquiry. In matters concerning public administration, the Court cannot sit back and let the case be decided on the strength of the case, as presented by the parties. In my judgment, the initial burden of proof rests on the applicant, as in any other recourse, although the issue is one of limited significance for the reasons above given.

THE POWERS OF THE COMMISSIONER UNDER SECTION 23(1) *UNDER THE ASSESSMENT AND COLLECTION OF TAXES LAW:*

On any reading of the wording of s.23(1), the power of the Commissioner to raise an additional assessment, is wide and far reaching. He is entitled to raise an additional assessment, subject to a time limit, whenever he "κρίνει" (that may appropriately be translated in English as "judges" or "forms the view") that the amount of tax levied is less that it ought to have been. The only limitation to the exercise of these powers is a time one; it must be exercised within six years from the year of assessment. On a literal reading, it would appear that the Commissioner is entitled to invoke his powers under s.23(1), whenever he, bona fide, forms the view that the tax levied is insufficient. This construction is also warranted on authority. As Hadjianastassiou, J. observed in *Solomonides* v. *The Republic* (1968) 3 C.L.R. 105, the Commissioner is made, by law, the judge of the need for raising an additional assessment. In the same case, the learned Judge makes extensive reference to the powers vested in the Commissioner by analogous provisions of the English legislation, that is s.41 of the English Income Tax Act, 1952, and the interpretation accorded to them by English courts. However, the analogy should not be carried too far, for the pertinent words are not precisely the same. The crucial word in the English statute is "discovers" which, arguably, makes the powers of the Commissioner less extensive than they are under Cyprus legislation. A series of English cases establish, that the levying of additional taxation is warranted and justified whenever the original assessment is made, either on a mistaken view of the facts or of the law including a mistake as to the effect of the general law. (See *R.* v. *Kensington Income Tax Commissioners* [1913] 3 K.B. 870; *Commercial Structures Ltd.*, v. *Briggs* [1948] 2 All E.R. 1041, and *Cellon Finance Co. Ltd.*, v. *Ellwood*, 40 T.C. 176).

The Supreme Court resolutely dismissed in *R.* v. *Frangos* (1965) 3 C.L.R. 641, the suggestion that the power vested in the Commissioner under s.23(1) is tantamount, in its exercise, to the imposition of taxation retrospectively.

In our judgment s.23 confers power on the Commissioner to raise, subject to the time limitation envisaged by the law, an additional assessment whenever he bona fide forms the view that the tax payer was undercharged as a result of an earlier assessment. It is open to the Commissioner to conclude thus, either because of a new appreciation of the facts or the implications of the law in their application to the particular facts of the case. I am of the view that the decision of the Commissioner cannot be faulted on this score.

THE VALIDITY OF THE ADDITIONAL ASSESSMENT IN VIEW OF THE FACTS OF THE CASE:

Section 5(1)(f) of the Income Tax Laws 1961-1977, makes, inter alia, liable to tax rents as well as premiums arising from property. A large part of the argument of counsel was directed towards establishing what receipts qualify as "rent" and "premium", accompanied by analysis of the nature of the receipt of £50,000.- in this case. Counsel for the applicant made extensive reference to a number of textbooks in support of his submission, that the receipt in this case was one other than rent or premium. (In particular, he referred to *Tiley's Revenue Law, 2nd ed.*, and *E. F. George on Taxation and Property Transactions, 3rd ed*). Counsel for the respondents embarked upon a similar exercise, laying stress in the process on variations in the meaning of rent, depending on the context it is used, and differences between the wording of s.5(1)(f) of our legislation, and that of s.67(1) of the Income Tax and Corporation Taxes Act, 1970, the English Statute rendering rents and other income from land liable to tax.

In *Renos Fitikkides* v. *The Republic* (1970) 3 C.L.R. 15, it was held that the fact that a payment is made in a lump sum, does not seal the nature of the receipt and does not attach to it the imprint of capital. Liability to pay tax depends on the purpose for which the payment is made.

In the work of *Tiley* and *George* supra, it is appropriately

indicated that the word "rent" may import a different meaning to an economist and a different one to a lawyer.

"Rent" is one of those words that has a settled popular meaning, and one need not go far to ascertain what it conveys. It encompasses, on any view of this understanding income from the lease of property. In essence, it tallies with the definition supplied by *Jowitt's Dictionary of English Law*, wherein "rent" is defined as a "periodic payment due by the tenant of land as compensation for the use of the land". It would be time consuming, and in the end unprofitable, to probe further into the matter and refer to particular definitions of the word "rent" approved in various cases. They all include income from the letting of property.

And the pertinent question is, whether the sum of £50,000.– was received as, or represented at the time of its receipt, in 1972, rent. In the contract of lease, the sum of £50,000.– is described as rent, a consideration relevant to our exercise, though not conclusive. The Court is not fettered from this description, its task being to ascertain the true nature of the receipt. On any construction of the agreement, the sum of £50,000.– was paid as compensation for the lease of immovable property for a ten–year period. It was income from the lease of property. In my judgment, it constituted rent. Indeed, I find it difficult to see how this amount could be treated as a receipt of any other kind; and certainly it was not capital. That rent was paid in advance, it does not alter the character of the receipt nor does it render the payment anything other than what it was, notably rent. The pre–payment of rent leaves the character of the receipt unaffected. Evidently, it was paid in advance as an inducement to encourage, on the one hand, the landlord to enter into the contract of lease, and on the other to facilitate him to respond to his obligations undertaken therein. The fact of pre–payment was a kind of premium intended to encourage the landlord to lease his land to the tenant. In my judgment, the amount of £50,000.– was, in every sense, a payment of rent, whereas its pre–payment a premium probably intended to encourage the landlord to enter into the agreement. Therefore, the amount was subject to permissible deductions liable to tax in accordance with the provisions of s.5(1)(f) of the law.

I agree with counsel for the respondents that nothing that happened subsequently could change the character of the receipt. Where money is received as rent or as premium, nothing that happens subsequently may alter, retrospectively, its character at the time of payment. Any such approach would defeat income tax legislation at its core and it would open the door to the avoidance of tax by the subsequent action of the tax payer. The basic principle of Income Tax Law is that income is liable to tax when received by the tax payer or upon becoming legally entitled to it.

Counsel for the applicants laid stress throughout on the fact that eventually the money originally received as rent, viz. unappropriated rents, became compensation in their hands for the termination of the contract, submitting that it lost its income character. Even if those were the relevant facts, the fact that a certain amount was received by way of compensation, would not be conclusive as to its nature, and certainly it would not render it, ipso facto, a payment of a capital nature. In the case of *Georghiades* supra, it was held that payment of compensation for the forfeiture of a right or property, is not in itself conclusive of the nature of the receipt. The enquiry must be carried further and it must be ascertained whether compensation was for the loss of income or capital. In the former case, the liability to tax arises, notwithstanding the fact that receipt was by way of compensation. So, in this case, the compensation paid to the applicants was for the loss of rent, and as such, it would, had a subsequent year been the year of assessment, be equally liable to tax as rent.

The recourse is dismissed. There will be no order as to costs.

Recourse dismissed. No order as to costs.