

1984 July 12

[PIKIS, J.]

IN THE MATTER OF ARTICLE 146 OF THE CONSTITUTION

NINA RAINBOW,

*Applicant,*

v.

THE COMMISSIONER OF INCOME TAX,

*Respondent.*

(Case No. 11/83).

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*Income tax—Assessment—Deductions—Discretion of Commissioner under section 51 of the Assessment and Collection of Taxes Law, 1978 (Law 4/78) to reject a claim for deduction notwithstanding its apparent nature in the absence of reliable audited accounts—Legitimate for Commissioner, in the exercise of such discretion to have regard to the conduct of the taxpayer in its entirety in connection with the discharge of his obligations under the Law.*

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Applicant was running a restaurant-bar business in rented premises at Larnaca. She was not keeping any records of revenue or disbursements and she did not submit audited accounts. Following a submission by her of a statement of assets and liabilities as at 31.12.80 at the instance of the Commissioner, the latter made inquiries about the accuracy of previous statements of income by her and raised the assessment complained of in this recourse. Counsel for the applicant mainly contended that the sub judice decision was liable to be set aside for lack of reasoning in rejecting the claim of applicant for a proper discount of her income for salaries paid to her husband and in making proper allowance for the element of goodwill represented in the sale price of her business.

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*Held*, that section 51 of the Assessment and Collection of Taxes Law, 1978 (Law 4/78) confers power on the Commissioner to reject a claim for deduction notwithstanding its apparent nature in the absence of reliable audited accounts; that in exercising his discretion under s.51 it is legitimate for the Com-

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missioner to have regard to the conduct of the taxpayer, in its entirety, in connection with the discharge of his obligations under the tax law; that a taxpayer who is less than forthcoming in the declaration of his income and fails to keep records to substantiate deductions from his taxable income, can hardly expect the Commissioner to exercise his discretion, under s.51, in his favour; that the burden of substantiating before the Court the legitimacy of deductions from taxable income, lies on the taxpayer; that confronted with the lacuna in the financial affairs of the applicant, the Commissioner carried out whatever inquiries were possible in the circumstances, with a view to ascertaining her true liability to tax; that certainly, it was reasonably open to the Commissioner to arrive at the decision he did, and nothing said in these proceedings persuades this Court otherwise; accordingly the recourse must fail.

*Application dismissed.*

*Per Pikiis, J.:* The payment of income tax constitutes a social duty upon the diligent discharge of which depends the effective functioning of the modern State and realisation of social objectives. Avoidance of tax erodes economic planning and makes for uneven distribution of social burdens contrary to Article 24.1 of the Constitution. Section 51 aims to seal the door to the unmerited avoidance of tax. It is in this spirit it must be read and applied.

Cases referred to:

*Lord Chetwode v. I.R.C.* [1976] 1 All E.R. 641; [1977] 1 All E.R. 638;

*I.R.C. v. Church Commissioners for England* [1974] 3 All E.R. 529; [1976] 2 All E.R. 1037 (H.L.);

*Shiner v. Lindblom* [1960] 3 All E.R. 832;

*Hadji Yiannis v. Republic* (1966) 3 C.L.R. 338;

*Georghiades v. Republic* (1982) 3 C.L.R. 659 at pp. 667-669.

### Recourse.

Recourse against the decision of the respondent to review the income tax assessments raised on applicant for the income years 1975, 1976 and 1977.

*A. Poetis*, for the applicant.

*M. Photiou*, for the respondent.

*Cur. adv. vult.*

PIKIS J. read the following judgment. In the course of investigating the tax affairs of the applicant, the Commissioner inclined to the view she had been undertaxed. To this conclusion he was driven because of the otherwise unaccountable increase in the assets of the applicant emerging on a comparison of capital statements, submitted by applicant in November, 1974 and December 1980, respectively. Invoking his powers under s.23 of the Assessment and Collection of Taxes Law - 4/78, he reviewed the assessments of income tax liability of the applicant for the income years 1975, 1976 and 1977. The decision was communicated to the applicant by a letter dated 26.10.82, disclosing therein his reasons for the review of previous assessments (Appendix C' to the opposition). The recourse is directed against the soundness of this decision, invalid in the contention of the applicant, for over-statement of her gross income, as well as omission on the part of the Commissioner to make proper allowance for deductible expenditure, as well as inclusion in her income of a sum of money not qualifying as income.\*

Applicant was running a restaurant-bar business in rented premises at Larnaca. So far as one may surmise from the history of the dispute recited in the opposition, she hardly kept any records of revenue and disbursements; nor did she submit audited accounts. Her assessment to income tax before revision, was principally based on her statement of her income. In face of this disorderly state of affairs, it was proper on the part of the Commissioner to require the applicant to submit a statement of assets and liabilities as at 31.12.80, in order to discern therefrom her financial position with a view to determining her tax liabilities. Following this disclosure, and the inquiries made by the Income Tax Authorities about the accuracy of previous statements of income made by the applicant, the latter engaged an accountant to advise her on her tax liabilities and negotiate a settlement with the Authorities. Failing a settlement, the Commissioner resolved the matter by the decision under review. At the hearing, following the submission of written addresses on behalf of the parties, the challenge mounted against the decision, was confined to two matters:-

\* For a definition of "income", see, *Lord Chetwode v. IRC* [1977] 1 All E.R. 638 (HL); *Lord Chetwode v. IRC* [1976] 1 All E.R. 641 (CA)—Judgment of Sir John Pennycuik.

- (a) Unjustified refusal of the respondent to discount the income of the applicant by £15,000.-- and not £7,900.-- for salaries allegedly paid to the husband of the applicant, and
- 5 (b) wrongful omission to make proper allowance for the element of goodwill represented in the sale price of her business, evidenced by a written agreement dated 4.2.80 (exhibit 1).

10 It is the case for the applicant that the decision is liable to be set aside for lack of reasoning in rejecting the claim of applicant for a proper discount of her income to reflect the above, and lack of proper inquiry into the validity of her claims.

15 Another claim for wrongful non discount of her taxable income arising from increase of capital accruing from remittances from the United Kingdom, was rightly abandoned in the absence of any supporting evidence. Counsel for the Commissioner supported the decision as well founded. Not only applicant was not wronged but in the final analysis the assessment was actually benevolent for her. In actual fact, it contained an element of

20 concession on the part of the Commissioner. For he could legitimately reject the claim for payment of salaries to her husband, in the absence of any evidence to support it. Equally warranted was, in his submission, the decision of the Commissioner to treat the receipt of £4,700.-- as wholly referable to the

25 sale of furniture, fittings and equipment of the restaurant of the applicant, in the absence of -

- (a) proper identification of the element of goodwill in the sale price, and
- 30 (b) the circumstances surrounding the execution of the agreement, particularly the absence of any right on the part of the applicant to sublet the premises.

35 As a matter of fact, inquiries made by the Commissioner, revealed that under the terms of the lease, whereby she had possession of the premises, she had no right to sublet the premises; subletting, or, more appropriately, the installation of the purchaser in the premises, was made without the authority of the owner who continued to collect rent from the applicant. All that belonged

to her to dispose of, were the furniture and fittings in the premises.

It is settled on authority that the fact-finding body concerned with the determination of the liability to tax of the taxpayer, may receive extrinsic evidence in relation to the nature of a transaction in order to appreciate its true nature and effect (see, *IRC v. Church Commissioners for England* [1976] 2 All E.R. 1037 (H.L.); *IRC v. Church Commissioners for England* [1974] 3 All E.R. 529). On the other hand, it must be said that had the Commissioner been satisfied that the amount of £4,700.-- represented, wholly or in part, the sale of goodwill of a business, it would be right on his part to ignore such receipt for income tax purposes, unless he had reasons to believe that applicant traded in the build up of goodwill and its sale, either in the course of her ordinary business or by adventuring in the matter with a view to profit - See, *Shiner v. Lindblom* [1960] 3 All E.R. 832.

Section 51 of Law 4/78 confers power on the Commissioner to reject a claim for deduction notwithstanding its apparent nature in the absence of reliable audited accounts. The acknowledgment of such discretion to the Commissioner to reject claims for deductions unless properly validated, is justified in the context of the income tax legislation in view of the peculiar knowledge of a taxpayer of his financial affairs and amenity to document them. In fact, unless he documents his affairs, it is next to impossible to ascertain his precise income and, more so, his taxable income. If it was not for this power, a taxpayer might be allowed to shield behind a cloud of uncertainty that is mostly his creation.

The payment of income tax constitutes a social duty upon the diligent discharge of which depends the effective functioning of the modern State and realisation of social objectives. Avoidance of tax erodes economic planning and makes for uneven distribution of social burdens contrary to Article 24.1 of the Constitution. Section 51 aims to seal the door to the unmerited avoidance of tax. It is in this spirit it must be read and applied.

The discretion vested in the Commissioner under s.51 must, like every discretionary power, be reasonably exercised with a

view to promoting the aims of the law. In exercising his discretion, it is legitimate for the Commissioner to have regard to the conduct of the taxpayer, in its entirety, in connection with the discharge of his obligations under the tax law. On a review of  
5 the facts of the case as a whole, one can infer that applicant was less than forthcoming in the declaration of her income. Failure to keep records did not facilitate the ascertainment of her taxable income either. There is substance in the submission of counsel for respondent that reduction of her taxable income for any  
10 amount on account of the payment of salaries to her husband, can rightly be regarded as a concession on his part in the absence of records evidencing such payments. Liability of the applicant to tax, did not arise from her statements but was revealed indirectly on investigation of her assets. Faced with the prospect  
15 of paying tax, the applicant kept raising claims for deductions previously unmentioned. In the light of his investigations the Commissioner could treat the amount of £4,700.--, realised from the sale of her business, as solely referable to furniture equipment and fittings of her business.

20 A taxpayer who is less than forthcoming in the declaration of his income and fails to keep records to substantiate deductions from his taxable income, can hardly expect the Commissioner to exercise his discretion, under s.51, in his favour. And the burden of substantiating before the Court the legitimacy of  
25 deductions from taxable income, lies on the taxpayer - See, *Hadji Yianni v. Republic* (1966) 3 C.L.R. 338. Confronted with the lacuna in the financial affairs of the applicant, the Commissioner carried out whatever inquiries were possible in the circumstances, with a view to ascertaining her true liability to tax.  
30 Certainly, it was reasonably open to the Commissioner to arrive at the decision he did, and nothing said in these proceedings persuades me otherwise - See, *Georghiades v. Republic* (1982) 3 C.L.R. 659, 667-669.

35 The recourse fails. It is dismissed. Let there be no order as to costs.

*Recourse dismissed. No order as to costs.*