Deeny and others v Gooda Walker Ltd (in liq) and others (No 2)
(Inland Revenue Commissioners, third party) and other appeals

[1996] 1 All E.R. 933

HOUSE OF LORDS

LORD GOFF OF CHIEVELEY, LORD BROWNE-WILKINSON, LORD MUSTILL,
LORD NICHOLLS OF BIRKENHEAD AND LORD HOFFMANN
15, 16, 17 JANUARY, 7 MARCH 1996

Damages Underwriting losses Income tax - Underwriting members of Lloyd's recovering damages for losses caused by agent's failure to exercise reasonable skill and care - Whether damages taxable in hands of names Whether damages due to names should be reduced by amount equal to tax on damages – Finance Act 1993, ss 171(2), 184(1).

The plaintiffs (the names), underwriting members of Lloyd's, were awarded damages against their managing agents and members' agents (the defendants) for conducting the names' underwriting business negligently, thereby causing the names' loss. The defendants' negligence consisted principally of failing to arrange adequate reinsurance cover to protect the names against losses. The measure of damages was held to be the amount the names would have received from the reinsurance cover which the defendants ought reasonably to have put in place. The question then arose whether the damages payable by the defendants should be reduced by an amount equal to the tax thereon, on the basis that if appropriate reinsurance cover had been in place the names' receipts would have been greater and they would either have made profits instead of losses or would have had lower losses to carry forward to future years or to set off against other profits, and in either case the additional profits would have been liable to income tax. The names contended that there should be no set-off because the damages were themselves taxable receipts of their underwriting business which would have to be brought into account in computing the profits arising from that business. The judge held that no reduction fell to be made. The Court of Appeal dismissed the defendants' appeal, on the grounds that the source of the right to damages was the negligence of the defendants as the names' agents in conducting the names' underwriting business, and accordingly the damages had arisen from the names' underwriting business and were subject to tax in their hands under Case I of Sch D pursuant to ss 171(2)a and 184(1)b of the Finance Act 1993 as receipts from 'his underwriting business as a member of Lloyd's carried on through an underwriting agent', with the result that no reduction fell to be on made. The defendants appealed, contending that the damages would not be taxable in the names' hands because the source of the cause of action under which the damages had been awarded was the rights and obligations between the names and their agents and not the trade of underwriting carried on by the names. The Commissioners of Inland Revenue were joined as a party in the proceedings.

a Section 171, so far as material, is set out at p 939 a, post
b Section 184, so far as material, is set out at p 939 b, post {*933}

Held

The receipt of damages by Lloyd's names from their managing and members' agents arising out of the agents' negligence in conducting the names' underwriting business constituted a receipt of the names' underwriting business as members of Lloyd's and was taxable in their hands pursuant to ss 171(2) and 184(1) of the 1993 Act, since for tax purposes a name's underwriting business at Lloyd's constituted a single business. Entering into agency agreements with his managing and members' agents was part of a name's underwriting business and the contracts were made in the course of that business. Accordingly, where an agent failed to perform his duties under the agreements or performed them negligently, so that the name realised less money than he would otherwise have done if they had been performed properly, the damages payable by the agent were a receipt of the name's business. The appeal would therefore be dismissed (see p 935 g j to p 936 a f h, p 939 f to j, p 940 j to p 941 b, p 942 e f and p 944 g, post).

British Transport Commission v Gourley [1955] 3 All ER 796 distinguished.

Per Lord Hoffmann. In order that a receipt should arise out of a trade, it need not become payable by virtue of some pre-existing trade relationship. There need have been no previous contractual relationship between the parties at all. Accordingly, it does not matter whether the damages by way of compensation for lost reinsurance recoveries arise from a contractual right against a members' agent or a right in tort against a managing agent or claim in tort against a broker who negligently failed to act according to instructions or a claim for fraud against a stranger who diverted the money to himself. In

each case it arises from a right to be compensated for damage to the trade and the payment therefore arises out of the trade (see p 942 g, p 943 b c g and p 944 f g, post); dictum of Diplock LJ in London and Thames Haven Oil Wharves Ltd v Attwooll (Inspector of Taxes)[1967] 2 All ER 124 at 134 approved.

Notes

For the general principles of assessment of damages, see 12 Halsbury's Laws (4th edn) paras 1134, 1200, and for the reduction of damages by reason of gain to the plaintiff, see ibid para 1196.

For insurance at Lloyd's underwriters, see 25 Halsbury's Laws (4th edn) para 21.

Cases referred to in opinions

British Transport Commission v Gourley [1955] 3 All ER 796,[1956] AC 185,[1956] 2 WLR 41, HL.
Donald Fisher (Ealing) Ltd v Spencer (Inspector of Taxes)[1989] STC 256,(1989) 63 TC 168, CA.
Gliksten (J) & Son Ltd v Green (Inspector of Taxes)[1929] AC 381,[1929] All ER Rep 383, HL; affg [1928] 2 KB 193, CA.
Henderson v Merrett Syndicates Ltd [1994] 3 All ER 506,[1995] 2 AC 145,[1994] 3 WLR 761, HL.
Higgs (Inspector of Taxes) v Olivier [1952] Ch 311, CA.
IRC v Newcastle Breweries Ltd (1927) 12 TC 927,[1927] All ER Rep 287, KBD, CA and HL.
Lewis v Daily Telegraph Ltd [1963] 2 All ER 151,[1964] AC 234,[1963] 2 WLR 1063, HL.
London and Thames Haven Oil Wharves Ltd v Attwooll (Inspector of Taxes)[1967] 2 All ER 124,[1967] Ch 772,[1967] 2 WLR 743, CA; affg [1966] 3 All ER 145, [1967] Ch 772,[1966] 3 WLR 325.
{*934}
Napier and Ettrick (Lord) v R F Kershaw Ltd (14 May 1992, unreported); rvsd in part [1993] 1 Lloyd's Rep 10, CA; affd [1993] 1 All ER 385,[1993] AC 713,[1993] 2 WLR 42, HL.
R v British Columbia Fir and Cedar Lumber Co Ltd [1932] AC 441,[1932] All ER Rep 147, PC.
Society of Lloyd's v Morris [1993] CA Transcript 636.

Appeal

The defendants, Gooda Walker Ltd and 70 others referred to in the writ of summons, appealed from the decision of the Court of Appeal (Simon Brown and Peter Gibson LJJ; Saville LJ dissenting)([1996] STC 39) dated 5 October 1995 dismissing their appeal from the first part of the decision of Potter J ([1995] STC 439) delivered on 11 January 1995 whereby he held (i) that the damages awarded to the plaintiffs, Michael Eunan McLarnon Deeny and 3,062 other Lloyd's names (the names), by Phillips J ((1994) Times, 7 October) in his judgment of 4 October 1994 would be subject to tax in the hands of the names; and (ii) that the damages so recoverable ought not to be reduced by the amount of any tax-saving achieved by them. Pursuant to RSC Ord 15, r 6(2)(b)(ii) and Ord 77, r 8A the Commissioners of Inland Revenue consented to be joined as a party to the proceedings in respect of the first issue. The facts are set out in the opinion of Lord Hoffmann.

Bernard Eder QC, Philip Baker and Simon Bryan (instructed by Elborne Mitchell) for the defendants.

Geoffrey Vos QC, John Walters and David Lord (instructed by Wilde Sapte) for the names.

Ian Glick QC and Launcelot Henderson QC (instructed by the Solicitor of Inland Revenue) for the Revenue.

Their Lordships took time for consideration.

7 March 1996. The following opinions were delivered.

Lord Goff of Chieveley. My Lords, I have had the opportunity of reading in draft the speech of my noble and learned friend Lord Hoffmann; and, on the first and principal ground relied upon him in his speech, viz that the receipt of damages by a name constitutes a receipt of his underwriting business as a member of Lloyd's, I too would dismiss the appeal.

At the conclusion of his speech Lord Hoffmann addressed the question whether a statement by Diplock LJ in London and Thames Haven Oil Wharves Ltd v Attwooll (Inspector of Taxes)[1967] 2 All ER 124 at 134,[1967] Ch 772 at 815 provides an accurate statement of the law. He concluded that it does. However, having regard to the concern expressed on this point by my noble and learned friend Lord Browne-Wilkinson, a concern shared by the remainder of my noble and learned friends on the Appellate Committee, I am content that the appeal should be dismissed only on the first ground considered by Lord Hoffmann

Lord Browne-Wilkinson. My Lords, I agree that the appeal should be dismissed on the first ground relied on by my noble and learned friend Lord Hoffmann: the receipt of damages by a name constitutes a receipt of 'his underwriting business as a member of Lloyd's' within the meaning of ss 171(2) 935and 184(1) of the Finance Act 1993, because the name entered into the contracts with the agents in the course of carrying on that business.

My noble and learned friend Lord Hoffmann further concludes that, whether or not the contracts with the agents formed part of 'his underwriting business', the same result is achieved by applying the statement of law made by Diplock LJ in London and Thames Haven Oil Wharves Ltd v Attwooll (Inspector of Taxes)[1967] 2 All ER 124 at 134,[1967] Ch 772 at 815 which he quotes. Where compensation is received by a trader, two questions arise, viz first, was the receipt of the compensation a receipt of the recipient's business and, second, was such receipt of an income or capital nature? I have no doubt that the test propounded by Diplock LJ correctly determines the answer to the second of those questions, i e whether such compensation falls to be treated as income or capital of the taxpayer's trade. As to the first of those questions, in the ordinary run of cases the receipt of a sum by a trader as compensation for the failure to receive what would have been a receipt of his trade will normally demonstrate that the compensation is itself a receipt of that business. But there may be unusual cases where the test propounded by Diplock LJ might not be appropriate to the correct determination of the question whether the compensation is a receipt of the taxpayer's business. For example, in Higgs (Inspector of Taxes) v Olivier [1952] Ch 311 the Court of Appeal held, rightly or wrongly, that the receipt by an actor of a sum to compensate him for not carrying on part of his trade for a limited period was not a receipt of the actor's trade. It may be that the test propounded by Diplock LJ would have led to a contrary conclusion. Since it is unnecessary to decide the point in order to determine this appeal, I prefer to express no view whether the test propounded by Diplock LJ is in all circumstances determinative of whether or not a receipt of compensation is a receipt of the taxpayer's business.

Lord Mustill. My Lords, I too agree that the appeal should be dismissed, for the reasons given by my noble and learned friend Lord Hoffmann in support of the first ground of his decision.

I would, however, also wish to express my agreement with the observations of my noble and learned friend Lord Browne-Wilkinson concerning London and Thames Haven Oil Wharves Ltd v Attwooll (Inspector of Taxes)[1967] 2 All ER 124,[1967] Ch 772. In my opinion the question whether a particular receipt is a receipt of the taxpayer's trade must always come first. No doubt in practice it will often be so closely linked to the second question whether if it is a receipt of the trade it is in the nature of interest or capital, that an affirmative answer to one will demand an affirmative answer to the other. But this need not always be so, and I too would prefer to decide this appeal on the first ground alone.

Lord Nicholls of Birkenhead. My Lords, I have had the advantage of reading in draft the speeches of my noble and learned friends Lord Browne-Wilkinson, Lord Mustill and Lord Hoffmann. I agree that this appeal should be dismissed on the first of the two grounds relied on by Lord Hoffmann. As to the second ground, I agree with the observations of Lord Browne-Wilkinson and Lord Mustill.

Lord Hoffmann. My Lords, this appeal is the latest episode in the storm of litigation which has blown up in the wake of the huge losses suffered by insurance underwriters at Lloyd's a few years ago. It raises a narrow but important point, namely whether damages awarded to a member of Lloyd's in compensation for 936 losses caused by the negligent conduct of the underwriting on his behalf are a taxable receipt of his underwriting business.

(1) UNDERWRITING AT LLOYD'S

Underwriting members of Lloyd's (names) are individuals who each carry on insurance business. The way in which the business is conducted has a number of special features, including the following.

(a) Members' agents

A name who is not himself an underwriting agent must carry on his business through an underwriting agent, known as a 'members' agent'. This is a statutory requirement: see s 8(2) of the Lloyd's Act 1982. The relationship between the name and his members' agent is governed by a standard form of agency agreement prescribed by a Lloyd's Byelaw and gives the agent wide discretionary powers.

(b) Syndicates and managing agents

For the purposes of writing insurance policies, names join together in syndicates which usually specialise in the underwriting of particular forms of risk. The managing agent of the syndicate will appoint one or more 'active underwriters' who will enter into contracts of the insurance on behalf of all the names,

including sometimes himself. A syndicate is not a legal entity but an aggregate of the names who have joined the syndicate for a given underwriting year. Nor is a syndicate a partnership: each name undertakes to be liable for his several share of the risk but not for the share of any other name.

(c) Sub-agents and combined agents

The name's members' agent may or may not be the same person as the managing agent of one or more of his syndicates. If they are, they will be called combined agents. If not, the name's members' agent will enter into a sub-agency agreement in standard form with the managing agent of the syndicate which the name wishes to join, delegating his discretionary power to carry on the underwriting business on behalf of the name.

(2) THE LITIGATION

In the period 1988 to 1990 there occurred a number of catastrophes (such as the total loss of a North Sea oil rig and a hurricane in the United States) which resulted in very large claims being made against certain syndicates. When the extent of the losses became known on the closure of the three-year Lloyd's accounting period, litigation followed. Large numbers of names sued their members' agents and the managing agents of the loss-making syndicates. They alleged that the losses had been caused by the negligence of the managing agents in the conduct of the underwriting and that the members' agents were contractually liable for that negligence. In Henderson v Merrett Syndicates Ltd [1994] 3 All ER 506,[1995] 2 AC 145 this House decided two questions of principle. The first was that a managing agent owed a duty of care in tort to all members of his syndicate, whether he was acting as combined agent or under a sub-agency agreement. The second was that under the terms of the standard agency agreement, a members' agent was responsible for the negligent conduct of a managing agent to whom, under a sub-agency agreement, he delegated his discretions in carrying on the business of underwriting on behalf of the name. {*937}

The actions with which this appeal is concerned were commenced by names belonging to syndicates managed by Gooda Walker Ltd and an associated company. I shall for convenience call them both 'Gooda Walker.' The defendants were Gooda Walker and the members' agents of those names for whom Gooda Walker were not combined agents. In a judgment dated 4 October 1994 Phillips J ((1994) Times, 7 October) held that Gooda Walker had failed to exercise proper care and skill in the conduct of the underwriting. In consequence, he held that Gooda Walker and the members' agents were liable for such damages as would place the names 'in the same position as if the underwriting carried on on their behalf by each syndicate had been competently performed'. More specifically, he held that the damages should be assessed by computing what each syndicate would have received from the reinsurance cover which Gooda Walker ought reasonably to have had in place, less what such cover would have cost. An assessment of damages on these lines has since been undertaken. In the course of that assessment, however, a further question of principle arose. If appropriate reinsurance cover had been in place, the receipts of the syndicate members would have been greater and they would have made profits instead of losses, or at any rate smaller losses. The additional profits would have been liable to income tax, or if there had still been losses, there would have been less to set off against other profits or carry forward to future years. In either case, the names would have paid more tax. In computing what should be paid to the names to put them in the same position as if the underwriting had been competently performed, should there be a deduction o the extra tax which would have been payable?

In British Transport Commission v Gourley [1955] 3 All ER 796, [1956] AC 185 this House decided that where a sum of damages which is not liable to tax is calculated by reference to income which would have been liable to tax, the computation should be made by reference to the net amount which the plaintiff would have received. The defendants rely on this principle. It is accepted, however, that the principle does not apply if the award of damages is itself a taxable receipt. In this case the names say that the damages constitute taxable receipts of their underwriting businesses which will have to be brought into account in computing the profits arising to them from those businesses. The defendants say that the damages are not receipts of their underwriting businesses at all.

The Commissioners of Inland Revenue, who have a lively interest in this question, have been joined as parties so that they may be bound by the outcome. Not unnaturally, they support the names. Gooda Walker have gone into liquidation and ceased to take an active part in the proceedings. So the dispute is between the names and their members' agents. Potter J ([1995] STC 439) held in favour of the names and the Inland Revenue. His decision was upheld by a majority of the Court of Appeal (Simon Brown and Peter Gibson LJJ)([1996] STC 39). But Saville LJ, who has probably heard more of the Lloyd's litigation than any other judge, dissented.

(3) TAXATION OF LLOYD'S UNDERWRITING PROFITS

The profits of an underwriting business are taxed under Case I of Sch D, which is applied to underwriting members of Lloyd's by s 171(2) of the Finance Act 1993: {*938}

'As respects the profits arising to a member from his underwriting business for any year of assessment (a) the aggregate of those profits shall be chargeable to tax under Case I of Schedule D '

Section 184(1) defines 'underwriting business', in relation to an underwriting member of Lloyd's, as

'his underwriting business as a member of Lloyd's, whether carried on personally or through an underwriting agent, and does not include any other business carried on by him, and in particular, where he is himself an underwriting agent, does not include his business as such an agent '

We are not concerned in this case with what the expression 'does not include.' The relevant words are 'his underwriting business as a member of Lloyd's carried on through an underwriting agent'. So the question is simply whether the damages are a receipt of that business.

My Lords, if it were not for the dissenting judgment of Saville LJ I would have thought that the question admitted only one answer. If a trader sells goods, the price of what he sells is a receipt of his trade. If the buyer has to be sued for the price, the money recovered is a receipt of the trade and the irrecoverable costs are an expense. If the buyer does not accept the goods and the trader recovers damages for non-acceptance (being the difference between the price and the value of the goods left on his hands) the damages are a receipt of the trade. What is true of goods is also true of services. If a trader employs someone to perform services for the purposes of his trade, the money which he realises from the performance of those services is a receipt of the trade. If the employee in breach of his legal duty fails to perform the services, or performs them badly, so that the trader realises less money than he would have done if they had been performed properly, he will be liable in damages and the damages will be a receipt of the trade. In each case the receipt arises out of the trade.

Mr Eder QC who appeared for the defendants did not dispute that if the employment of the members' agent was part of the name's trade, the damages for which he was liable would be a receipt of that trade. His submission was the name's only trade at Lloyd's was writing contracts of insurance as part of one or more syndicates. It was not employing members' agents, still less suing them for compensation. Underwriting business is what is done at 'syndicate level' and gives rise to receipts and expenses which enter into the syndicate accounts. These would not include damages payable by a members' agent for breach of the agency agreement. A name has to employ a members' agent as a condition of being allowed to trade at Lloyd's but the employment does not form part of that trade.

My Lords, I reject this analysis which seems to me entirely artificial. Of course the purpose of the name's business is to write insurance. The premiums, the income of the fund in which they are invested and his reinsurance recoveries will ordinarily be his only receipts. Equally it can be said that the business of a shopkeeper is buying and selling goods. But I think that he would be surprised to be told that employing a shop assistant was not part of the trade, so that wages were not a deductible expense. Apart from the fact that the use of an agent is compulsory, which in the present context seems to me neither here nor there, I can see no difference between the employment of agents to conduct one's underwriting business at Lloyd's and their employment in any other kind of business. {*939}

(4) NAPIER'S CASE

Mr Eder relied principally upon the decision of Saville J in Lord Napier and Ettrick v Kershaw (14 May 1992, unreported) as indeed did Saville LJ in this case in the Court of Appeal. The issue in that case turned on the construction of words in a Lloyd's Premiums Trust Deed similar to the words of s 171(2) of the 1993 Act with which this appeal is concerned. In Napier's case the words were 'all monies whatsoever becoming payable to the Name in connection with the Underwriting' and 'the Underwriting' was defined as 'The underwriting business of the Name at Lloyd's carried on through the agency of the Members' Agent'. In this case the words of s 171(1) are 'profits arising [to a member from his] underwriting business' and 'underwriting business' is defined to mean 'his underwriting business as a member of Lloyd's carried on through a [members'] agent.'

On the other hand, the context in which the words are used is not the same. Section 171(1) identifies receipts for the purpose of computing profits charged to tax. The premiums trust deed identifies receipts for the purpose of requiring them to be held in a trust fund rather than at the free disposal of the name. The purpose of the trust fund is to put a ring fence around the receipts of the name's underwriting business so that they are earmarked to pay the debts of the business. Only the net profits become available to the name, his other creditors or his trustee in bankruptcy. The debts of the business are of course primarily insurance claims but include 'any expenses whatsoever from time to time incurred in

connection with or arising out of the underwriting', including the remuneration of the members' agent and any tax he is liable to pay on his underwriting profits.

The issue in Napier's case was whether damages payable to a name by members' were caught by the trust. Saville J decided that they were not. His reasoning was as follows:
'["Underwriting" means] the underwriting business of the name at Lloyd's carried on by or though the members' agent and not just the underwriting in a more general sense. The money in question is clearly not a receipt of the underwriting business, for the business is one of underwriting at Lloyd's and not one of compensating names for the mistakes allegedly made by their agents in conducting the names' business of underwriting at Lloyd's It is not a profit of the underwriting business for the same reason, nor would it feature in the accounts of the names' syndicate: and it should be remembered that a name is only allowed to conduct underwriting business at Lloyd's through syndicates What, to my mind, the money has to do with is not the names' business of underwriting at all, but the rights and obligations existing between the name and his members and managing agents: and those rights and obligations are not part of the names' business of underwriting at Lloyd's either, but part of the internal arrangements made between these parties as a means of enabling the names' business at Lloyd's to be conducted. That business is business with third parties and not business between the name and his agents. In my judgment, the money is payable in connection with the latter business and not the former business within the meaning of the deed.'

Mr Eder says that this reasoning is of general application, at any rate as demonstrating what was meant by a name's underwriting business at Lloyd's. It applies equally to the computation of his profits for the purposes of income tax.

I do not think that the judge's reasoning was intended to be of general application. If it was, I confess that I would not be able to agree with it. I have 940 difficulty with the contrast drawn in the first sentence between the underwriting carried on through the members' agent and 'the underwriting in a more general sense' and in the last sentence between the business with third parties and the 'business between the name and his agents'. Why is it necessary to suppose that the name is carrying on two businesses? William of Ockham would not have approved. He said 'entia non sunt multiplicanda': an explanation should not postulate more entities than are necessary. We have not been asked to examine the premiums trust deed in detail and it may be that its context gives rise to an absolute necessity to postulate the existence of two businesses. But I find no such necessity in the Finance Act 1993. For most purposes, including income tax, I think that the name is carrying on a single business.

The argument that 'the business is one of underwriting at Lloyd's and not one of compensating names for mistakes' echoes the rhetoric of counsel in a number of cases down the years, arguing that a payment in compensation for lost trading revenue or additional trading expense was not a receipt of the trade. In IRC v Newcastle Breweries Ltd (1925) 12 TC 927,[1927] All ER Rep 287 the payment was statutory compensation for the company's stocks of rum which had been requisitioned by the Admiralty during the war. Mr Latter KC said that it was not a receipt of the trade but compensation for interference with the trade. Rowlatt J (12 TC 927 at 937) said that it was in substance a sale of the company's stock and the fact that it was under compulsion was irrelevant. His decision was affirmed by this House (12 TC 927 at 951 955,[1927] All ER Rep 287 at 291 293). In Green (Inspector of Taxes) v J Gliksten & Son Ltd [1928] 1 KB 475 the payment was insurance money for the company's stock of
timber which had been destroyed in a fire. Sir John Simon KC said the company traded in timber and not in fires. Rowlatt J (at 481) said that the insurance policy had been taken out as part of carrying on the business and the result of the transaction was to convert the company's stock into money in the same way as if it had been sold. His decision was affirmed by this House ([1929] AC 381,[1929] All ER Rep 383). I need not multiply the examples. The fallacy in each case is the same. A trader may have a number of rights in respect of his stock in trade. For example, he may have a right to the price or alternatively a right to damages against a purchaser, a right to compensation under an insurance policy if it is accidentally lost, a right to compensation against the Crown if it is requisitioned, a right to damages against a tortfeasor if it is negligently damaged or destroyed. All these rights, because they are rights to compensation for his stock in trade, arise out of his trade. The fact that the circumstances giving rise to one or more type of receipt may be of rare occurrence does not make it any the less a receipt of the trade.

No case on the construction of one document is authority on the construction of another, even if the words are very similar. Any view which I expressed on the application of the reasoning in Napier's case to the construction of the premiums trust deed would necessarily be obiter. I therefore say only that I cannot accept it as an authority on the construction of s 171(2) of the Finance Act 1993.

Mr Eder says, however, that Napier's case does not stand alone. It was approved by the Court of Appeal in Society of Lloyd's v Morris [1993] CA Transcript 636. The question in Society of Lloyd's v Morris, however, was a different one. It was whether the proceeds of personal stop-loss insurance taken

out by a name were caught by the trust deed. The evidence was that taking out stop-loss insurance was a personal decision for the name which he could, if he wished, arrange outside Lloyd's. It does not fall within the powers and discretions in the conduct of the name's business which the agency agreement vests in the members agent. I think that if, as appears to be th case, personal stop-loss is a 941 contract to indemnify the name against a part of the overall losses arising in a given underwriting year from his underwriting business at Lloyd's, then a payment under such a policy cannot itself be a receipt of the business. It is a payment under a contract independent of the business which depends for its calculation upon the prior computation of all the receipts and expenses of the business. To treat the stop-loss recovery as a receipt of the business would therefore involve a circularity. This appears to have been the view of the Revenue, which until 1973 did not allow the premiums for personal stop-loss policies as expenses of the underwriting business and did not tax the proceeds as receipts. The Finance Act 1973 reversed these rules by special provisions which are now in s 178 of the 1993 Act.

There is of course no reason why a trader should not, as part of his business, take out an insurance policy to compensate him for the profits he may lose or the losses he may suffer in a given event. In that case there is no circularity. The premium will be a business expense, and the payment a business receipt, calculated by reference to the additional profit he would have made or the losses he would not have made if the event had not occurred (see R v British Columbia Fir and Cedar Lumber Co Ltd [1932] AC 441,[1932] All ER Rep 147). But payment under a Lloyd's personal stop-loss policy is not calculated by reference to the profits which would have been made if a given contingency had not occurred. It is simply a payment in respect of the losses which have actually been suffered.

I therefore think that Morris's case was rightly decided on its own facts but that it does not justify the application of the reasoning in Napier outside the facts of the latter case.

(5) ATTWOOLL'S CASE

Thus far I have been considering the question of whether the damages arose to the names from their underwriting businesses as if it was equivalent to asking whether they arose from a contract made in the course of that business. This is the way Mr Eder asked us to approach the matter. I have answered that question in the affirmative because, contrary to his submission, I consider that the agency agreement with the members' agent is a contract made in the course of the name's underwriting business at Lloyd's. Mr Vos QC submits however on behalf of the names that this is applying too narrow a principle. In order that a receipt should arise out of a trade, it need not become payable by virtue of some pre-existing trade relationship. There need have been no previous contractual relationship between the parties at all. In IRC v Newcastle Breweries Ltd (1927) 12 TC 927,[1927] All ER Rep 287, for example, there had been no previous relationship between the Crown and the company. The Admiralty simply descended on the company and requisitioned its rum, thereby coming under a statutory obligation to pay compensation. The same is true of the compensation payable by a tortfeasor for negligently causing damage which deprives the trader of a revenue receipt or causes him to incur a revenue expense. Mr Vos says that these cases show that a legal right to compensation for the loss of a trade receipt gives rise to a payment which by definition arises out of the trade. He relied upon a statement to this effect by Diplock LJ in London and Thames Haven Oil Wharves Ltd v Attwooll (Inspector of Taxes)[1967] 2 All ER 124 at 134,[1967] Ch 772 at 815:

'Where, pursuant to a legal right, a trader receives from another person compensation for the trader's failure to receive a sum of money which, if it had been received, would have been credited to the amount of profits (if any) arising in any year from the trade carried on by him at the time
when the 942 compens tion is so received, the compensation is to be treated for income tax purposes in the same way as that sum of money would have been treated if it had been received instead of the compensation.'

Although Diplock LJ refers to the trader's failure to receive a sum of money which would have been a revenue receipt, his principle must apply equally to compensation for his liability to pay a sum of money which was a revenue expense (see Donald Fisher (Ealing) Ltd v Spencer [1989] STC 256). So Mr Vos says that we need not concern ourselves with whether the employment of the managing agent was a contract made in the course of the name's trade. The managing agent could have been a stranger to the name's business. The fact that the name is entitled to the damages as compensation for what would have been a revenue expense or receipt of the trade is enough to identify the damages as a trade receipt.

Since I have rejected the arguments of Mr Eder on his own preferred formulation of the question, I need not decide whether the Attwooll formula (by which I mean the sentence of Diplock LJ which I have quoted) is applicable to this case or not. But the question has been fully argued and it is right that I should express an opinion on it.

Mr Eder says that it cannot be of general application because there is no special rule in the 1993 Act for compensatory payments. There is only one test for all payments, namely whether they are receipts arising out of the trade. The rule propounded by Diplock LJ might be a useful test for deciding whether a payment which undoubtedly arose out of the trade was capital or income but cannot take the place of the statutory language. The context, says Mr Eder, was a case in which the only question was whether the payment was capital or income: a tortfeasor had negligently damaged the plaintiff's jetty, an asset of their trade, and the compensatory payment in dispute was for their inability to use it while it was being repaired.

I think that Diplock LJ can safely be credited with having known that the duty of the court is to apply the language of the statute and not to add its own glosses or addenda. He described his proposition as one of logic rather than law, by which I think he meant that it did no more than express what was logically entailed by the proposition that a trader was entitled to receive a payment in compensation for what would have been a receipt of his trade. It meant, in his view, that the compensatory payment was likewise a receipt of the trade.

I respectfully think that this is right and that it is consistent with the cases. Of course, like all such reformulations, it restates the question rather than providing an answer. It is still necessary to decide what the compensation was for. Was it for a revenue receipt or expense? Or was it for the partial or total loss of a capital asset employed in the trade? Or was it for something which does not form part of the trade at all? These questions sometimes give rise to very fine distinctions. The fact that damages are computed by reference to income which would have been earned does not mean that they are compensation for the loss of that income. The income which might have been expected to be received may be merely an element in the valuation of a different asset or interest. As Diplock LJ said in Attwooll's case [1967] 2 All ER 124 at 135,[1967] Ch 772 at 816:

'The method by which the compensation has been assessed in the particular case does not identify for what it was paid; it is no more than a factor which may assist in the solution of the problem of identification.' {*943}

It is accepted, for example, that damages for personal injury are compensation for the personal injury, though partly calculated by reference to the income which the injured person would have earned (see British Transport Commission v Gourley [1955] 3 All ER 796,[1956] AC 185). In Lewis v Daily Telegraph Ltd [1963] 2 All ER 151,[1964] AC 234 it was decided that damages awarded to a company for libel are compensation for damage to its reputation, even though calculated in part by reference to the loss of profits which the libel has caused. In both cases, therefore, the damages were not taxable because they were not compensation for a revenue receipt. What both cases show is that the answer to the question of what the damages were for also provides the answer to the question of whether they arose out of the trade.

Neither of these cases, it will be noticed, was concerned with the distinction between capital and income. An individual's physical health and integrity or a company's reputation are only in the loosest sense capital assets of their respective trades. It is true that in many of the cases, the only plausible alternative to the payment being compensation for a revenue trade item was that it was compensation for a capital asset employed in the trade. But this was not always the case. In J Gliksten & Son Ltd v Green (Inspector of Taxes)[1929] AC 381, for example, it was not suggested that the timber was a capital asset. The argument was that having fires was not part of the company's business. It seems to me that the Attwooll proposition is about which compensatory payments can be said to arise from the trade. It identifies them as payments in compensation for what would have been revenue items in the trade. If they are not compensation for such revenue items, the question of what else they are compensation for is irrelevant. So I do not accept Mr Eder's submission that one first asks whether a receipt arises out of the trade and then whether it is capital or income. There is nothing special about compensatio for a capital asset. It is no more than one kind of compensation which does not for income tax purposes arise out of the trade.

I therefore think that Mr Vos's wider argument was right. I do not think it matters whether the damages by way of compensation for lost reinsurance recoveries arose from a contractual right against a members' agent or a right in tort against a managing agent or claim in tort against a broker who negligently failed to act according to instructions or a claim for fraud against a stranger who diverted the money to himself. In each case it arises from a right to be compensated for damage to the trade and the payment therefore arises out of the trade.

I would therefore dismiss the appeal.

Appeal dismissed.