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## *The Sources of Addington's Income Tax*

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### ABSTRACT

Addington's Income Tax of 1803 made significant changes to Pitt's Act of 1799 but was introduced at short notice less than a month after resumption of the war with Napoleon in May 1803. This chapter examines the sources of the changes from Pitt's tax made by Addington for which there is no direct record and concludes that the main ones were the Land Tax and Adam Smith's *The Wealth of Nations*.

### INTRODUCTION

WHATEVER THE TRUTH in general of Canning's famous jibe that Pitt is to Addington as London is to Paddington—and it is fair to say that Pitt must have been a hard act for anyone to follow<sup>1</sup>—it cannot be doubted that the importance of their roles were reversed so far as their respective Income Taxes are concerned. This chapter explores Addington's sources for the major differences between his and Pitt's tax. The second section considers the nature of a source of income by reference to Adam Smith's *The Wealth of Nations*; the third section deals with the difference

\* I am grateful to Dr Diane Kraal, Senior Lecturer, Monash University, Australia, for her assistance in recommending material about Adam Smith and Ricardo.

<sup>1</sup> P Ziegler, *Addington: a Life of Henry Addington, first Viscount Sidmouth* (London, Collins, 1965) 220, said of Addington that he 'laboured under three crippling disabilities: that he was not an aristocrat, was not an orator and was not William Pitt'. Ziegler also observed (at 221) 'Addington's failure, therefore, was not so much one of achievement as of personality and of will. He was not a bad Prime Minister but he was bad at behaving like a Prime Minister and at convincing others that he was an effective Prime Minister'. Addington was Prime Minister in 1801–04 and held other important posts including that of Speaker of the House of Commons (1789–1801); Lord Privy Seal (1805, 1806–07 and 1812); Lord President of the Council (1806); Home Secretary (1812–21); and Minister without Portfolio (1822–24). He was created Lord Sidmouth in 1805 but for convenience will be referred to throughout as Addington.

between Pitt's tax on income and Addington's tax on sources of income, comparing the latter with land tax; the fourth section considers deduction of tax from sources of income also by reference to land tax; the fifth section brings together the influences of land tax and Adam Smith on the treatment of interest; and the final section draws conclusions.

Pitt's pioneering<sup>2</sup> but rather unsuccessful income tax of 1799<sup>3</sup> suffered from the defect that it was easy to evade as the tax merely required a return of total income. Only if the General or Commercial Commissioners<sup>4</sup> were dissatisfied with the return could they require income to be specified under four main headings subdivided into a number of Cases. For example, there are no less than 14 Cases concerning land, dealing separately with letting of land and houses each in relation to three types of lease (rack rent only, premium only, and both rent and a premium), using the actual rent and requiring valuations by the Commissioners where there was a premium.<sup>5</sup>

<sup>2</sup> J Ehrman, *The Younger Pitt*, vol 3 (vol 3 is split into two volumes in the paperback edition breaking after p 492), *The Consuming Struggle* (London, Constable, 1996) 262 quotes *The Morning Chronicle*, 3 November 1798, describing the then-rumoured idea of his tax as 'a daring innovation in English finance'.

<sup>3</sup> An Act to repeal the Duties imposed by an Act, made in the last Session of Parliament, for granting an Aid and Contribution for the Prosecution of the War; and to make more effectual Provision for the like Purpose, by granting certain Duties upon Income, in lieu of the said Duties (39 Geo 3 c 13. 1799), with the Schedule as retrospectively substituted by c 22 (the original Schedule is available at <http://books.google.co.uk/books?id=DNs0AAAAIAAJ>); see n 39 below for a summary of the changes to the Schedule. Pitt's original estimate of the yield (at a rate of 10%) on his estimate of the tax base of £102m was £9m–10m, reduced to £7.3m in the summer and then to £6.2m. The final net figure for the first year might have been only £1.671m: Ehrman, n 2 above, 265. For 1800–01 the net yield was some £4.5m, and a gross (of reliefs for small incomes and children) yield for the following year was £5.3m: *ibid* 267. Pitt's tax was abolished by Addington, who had replaced Pitt as Prime Minister (using later terminology) and Chancellor of the Exchequer, in his Budget of April 1802 following the Peace of Amiens on 25 March 1802 (42 Geo 3 c 42).

<sup>4</sup> Commercial Commissioners assessed trading profits. Their use was not a success as they were too far removed from local knowledge: A Farnsworth, *Addington, Author of the Modern Income Tax* (London, Stevens, 1951) 21. The Report by the Commissioners for the Affairs of Taxes of 25 April 1800 (they were able to do this because the first year of the tax ran to 5 April 1799) (The National Archives, Public Record Office (TNA) file PRO 30/8/279) Pt 2 said at 281: 'The total abolition of the Commercial Commissioners (except in London) is most strongly recommended by almost all the Commissioners for the general Purposes of the Acts'. This did not happen.

<sup>5</sup> The main headings of types of income in Pitt's tax were (1) Income of Owners of Lands (comprising Case 1 land occupied by the owner; Case 2 houses occupied by the owner; Case 3 land occupied by tenants at a rack rent; Case 4 land demised to tenants at a fine [premium] and rent (which required taking the rent and adding a further sum in respect of the premium); Case 5 land demised to tenants at a fine only (or with nominal rent) (also requiring a proportion of the premium to be fixed by the Commissioners); Case 6 houses demised to tenants at a rack rent; Case 7 houses demised to tenants at a fine and rent; Case 8 houses demised to tenants at a fine only (or with nominal rent); Case 9 tithes in respect of owners; Case 10 profits or manors, or timber, mines, insurance offices from fire and other profits of uncertain annual amount; Case 11 income of lands occupied by tenants at a rack rent; Case 12 income arising from mines, tithes, woods; Case 13 income from lands demised for a fine with or without rent; Case 14 income of mesne lessors from demises for fines with or without rent); (2) Income arising from Personal Property and from Trades, Professions, Offices, Pensions, Allowances, Stipends,

These Cases were essentially an aide memoire for taxpayers when completing their returns of total income. This power to require a detailed return was apparently rarely exercised.<sup>6</sup> Pitt subsequently wanted to change to a general requirement to make itemised returns but even he could not obtain Parliament's approval.<sup>7</sup>

Addington's 'property tax'<sup>8</sup> of 1803 is sometime portrayed as Pitt's with the addition of deduction of tax at source which made it work in practice.<sup>9</sup>

Employments and Vocations, Annuities, Interest of Money, Rent Charge (Cases 15 and 16); (3) Income arising out of Great Britain (Cases 17 and 18); and (4) Income not falling under any of the foregoing Rules. See text at n 33 for Adam Smith's sources of income. Of these, only category (3) was adopted in Addington's 1803 tax (see n 9 below). Taking the annual value of a lease premium also applied to Addington's tax (Sch A r 4) although if the land was not let at a rack rent an estimate of the annual value had to be made so it is not clear why this was included; it was not repeated in the 1805 Act (45 Geo 3 c 49, 1805).

<sup>6</sup> G Pellew (Dean of Norwich who was married to Addington's daughter Frances), *The Life and Correspondence of the Rt Hon Henry Addington, First Viscount Sidmouth* (London, John Murray, 1847) vol 2, 196, available at <http://books.google.co.uk/books?id=QC46AAAAcAAJ>. Pellew often cites Nicholas Vansittart (later Lord Bexley) who was Addington's Secretary to the Treasury as the source of his information on financial matters. Pitt did introduce a Bill on 4 April 1800 (contained in TNA PRO 30/8/279 Pt 2 and also in HC Parliamentary Papers, Fourth Sess 1799–1800, vol 127, the clause being at 230–31, and discussed by Farnsworth, n 4 above, 26–28) to require itemised returns but this provision met with strong opposition and was never included in the amending Act (39 & 40 Geo 3 c 49) (discussed by Farnsworth, n 4 above, 30); Ehrman, n 2 above, 266, suggests at n 3 that the copy of the Bill in TNA may be the only copy, but it is in Parliamentary Papers (as above).

<sup>7</sup> Ehrman, n 2 above, 266.

<sup>8</sup> An Act for granting to his Majesty, until the sixth Day of May [the reason for May is obscure as the tax year in the Act ran to 5 April] next after the Ratification of a Definitive Treaty of Peace, a Contribution on the Profits arising from Property, Professions, Trades, and Offices (43 Geo 3 c 122, 1803), introduced in his Budget of 13 June 1803 following the resumption of war on 18 May 1803 and passed on 11 August 1803. Note that while Pitt's tax granted 'certain duties upon income' (n 3 above), Addington's was a 'Contribution ... from Property, Professions, Trades, and Offices' (emphasis added). The change of title is significant and did more than differentiate it from Pitt's unpopular tax. Addington is reported as saying in Parliament 'He had no objection to the present tax being called an income tax, except that he thought that the title assigned to it more fully described its nature' (Cobbett's Parliamentary History from the Earliest Period to the Year 1803 (the forerunner of Hansard), available at <http://books.google.co.uk/-books?id=Mpw9AAAAcAAJ>, 13 July 1803, vol 36, col 1667). Hope Jones, *Income Tax in the Napoleonic Wars* (Cambridge, Cambridge University Press, 1939) 20 said that 'The new name did not deceive anyone'. This may have been true but it was not a matter of deception but of proper description. See n 20 below for the titles of the two originally separate Bills leading to Addington's Act. The title of the 1803 Act continued in the 1842 and 1853 Acts (5 & 6 Vict c 35, 1853); the title of the 1842 Act as the Income Tax Act 1842 dates only from the Short Titles Act 1892.

<sup>9</sup> In stark contrast to Pitt's estimates (see n 3 above), Addington's estimate of the yield (at a rate of 5% compared to Pitt's 10%) was £4.7m for a full year and £4.5m for the current year (and this was on the basis of deduction of tax at source on Schedule C income which did not happen because of Pitt's opposition, see n 62 below); the actual yield was £4.6 to £4.8m in the first year: Addington's Private Memoir on Finance (June 1803, Sidmouth archive DHC 152M/C1803 OT29) 14; Ehrman, n 2 above, 680; Parliamentary Register 1802–05, 13 June 1803, 572–73 and 30 April 1804, 683; Cobbett's Parliamentary History, n 8 above, vol 36, col 1597. Farnsworth, n 4 above, 93 sets out a breakdown of Addington's estimate of the amount

The difference is far greater than this. In order to have deduction of tax at source one first needed to have a tax on sources of income. Addington's tax was not an income tax in the sense that Pitt's had been, a tax on total income for which the derivation of the income was irrelevant, but a tax on separate sources of income, similar to the (later) mainland European *impôts réels*<sup>10</sup> but in principle comprehensive.<sup>11</sup> Structurally the starting point was the opposite of Pitt's; it looked not to the receipt of income but to the origin of the payment—to the source (the tree) that produces the income (the fruit).<sup>12</sup> Addington's own description was 'duties upon Property producing Income'.<sup>13</sup> The contemporary Exposition of the Act which is anonymous but must have been written within the Commissioners for the Affairs of Taxes, described the differences:

As the former [Pitt's tax] was imposed on the general account of income derived from all the sources; the present duty is imposed on each source by itself, in the hand of the first possessor, at the same time permitting and authorizing its diffusion through every natural channel in its course to the hand of the ultimate proprietor. The present measure, then, must be considered as a tax on the first produce,

assessed for 1803–04 of £111.5m compared to the actual assessments of £115.3m, the actual figure being higher in all cases except Schedule C (which he had estimated on the basis of deduction of tax at source). The yield with the increased rates of 1s 3d (6.25%) in 1805–06, and 2s (10%) from 1806–07 subsequently increased to £10.2m in 1808, £12.4m in 1810 and £14.5m in 1815: Ehrman, n 2 above, 681. The provisions for taxation at source are usually claimed to be the reason for the success of Addington's tax. Ehrman, n 2 above, 678 makes the point that in judging such claims it needs to be borne in mind that 'a probable majority of those concerned were self-employed (many farmers, small entrepreneurs in trades and manufactures) who continued to pay their taxes in the same manner as before'. Two points may be made in reply. First, deduction at source removed one of Pitt's main problems with traders claiming deductions for interest without anyone paying tax on the receipt (and in some cases without any interest in fact being paid), see n 55 below for the view of the Commissioners for the Affairs of Taxes in their Report, n 4 above. Secondly, both the annual value for Schedule A and deduction of tax from rent and rentcharges affected the taxation of farmers.

<sup>10</sup> Separate taxes on sources of income in which the identity of the recipient was irrelevant. However, the presence of Cases IV and V dealing with foreign income accruing to a resident (where therefore the identity of the recipient is relevant)—the only ones copied from Pitt's tax—is contrary to the concept of an *impôt réel*. Thus, in *Williams v Singer* (1920) 7 TC 387, the fact that the remittance basis had ended for foreign investment income accruing to UK resident trustees for a non-resident life tenant did not result in the trustees being taxed because the income, being foreign income of a non-resident, was not taxable; see Malcolm Gammie 'The Origins of Fiscal Transparency in UK Income Tax' in J Tiley (ed), *Studies in the History of Tax Law* (Oxford, Hart Publishing, 2010) vol 4, 33.

<sup>11</sup> Sir Josiah Stamp said in 1921 that up to 14 years earlier the UK tax had been a tax *in rem* (J Stamp, *The Fundamental Principles of Taxation in the Light of Modern Developments* (London, Macmillan, 1921) 17, available at [www.archive.org/stream/fundamentalprin00stampgoog#page/n8/mode/2up](http://www.archive.org/stream/fundamentalprin00stampgoog#page/n8/mode/2up)). The reference to 14 years earlier is presumably to Finance Act 1907 s 19 introducing earned income relief where total income did not exceed £2,000.

<sup>12</sup> Ehrman, n 2 above, 681–83 categorises Pitt's contribution to Income Tax as the fundamental one and Addington's merely an improvement on it. It is respectfully suggested that this does not do justice to the wholly different structure of the two taxes.

<sup>13</sup> Private Memoir on Finance, n 9 above, 12–13, also quoted by Farnsworth, n 4 above, 42.

gradually subsiding itself into a tax upon the income of the ultimate proprietor; affecting in its immediate object the hand that acquires, but extending by direct motion to the hand which converts the income so acquired.<sup>14</sup>

The famous Schedules A to E, which became a long-lasting feature of the tax, listed the sources of income, without which there could be no tax on the income derived from them, so that, for example a post-cessation trading receipt could not, in the absence of legislation, be taxed because at the time of receipt the trade (the source) no longer existed.<sup>15</sup> Source has been rightly described as 'a more or less coded subtext to income tax and corporation tax statutes'.<sup>16</sup>

The fact that Addington's tax represented a major change in the structure of the tax indicates that the changes were thought about in advance. One of Addington's first acts as Prime Minister (as we would call it today) was to repeal Pitt's tax in his Budget of 5 April 1802 following the Peace of Amiens on 25 March 1802. In the course of doing so he made a statement of some significance:

I think, however, that it [Income Tax] should be reserved for the exigencies and pressures inseparable from a state of war; but at the same time not under the present regulations, although the changes which it might be necessary to make would not be very dissimilar.<sup>17</sup>

This shows that Addington had already considered what changes would need to be made if Income Tax were to be introduced. It also demonstrated that politically there would be no reintroduction of Income Tax unless war was resumed, as indeed occurred on 18 May 1803. Addington had to introduce a second Budget<sup>18</sup> on 13 June 1803 within a month of war being declared. Income Tax was again needed in a hurry and the temptation must have been to re-enact Pitt's tax. That this did not happen confirms Addington's quoted statement that at least the outlines of his tax had been thought about in advance, but, on the other hand, the Bills leading to his Act show a number of significant changes demonstrating that important details had

<sup>14</sup> Anon, *Exposition of the Act for a Contribution on Property, Professions, Trades and Offices* (London, J Gold, 1803) 3.

<sup>15</sup> See, eg, *Carson v Cheyney's Executors* [1959] AC 412; 38 TC 240. The effect was most obvious where the cash basis of accounting was used; on an earnings basis normally receipts would be brought into the final accounts but there could be exceptions such as the forgiveness of a trading debt. The legislation reversing this (in part) is Finance Act 1960 ss 32, 33.

<sup>16</sup> *Memec v IRC* [1996] STC 1336, 1349f per Robert Walker J (who later became Lord Walker of Gestingthorpe).

<sup>17</sup> *The Times*, 6 April 1802, quoted by Farnsworth, n 4 above, 36. Pellew, n 6 above, 195 also states, without giving any source, that 'Mr Addington, on full consideration, resolved to new-model it [Pitt's Income Tax] entirely, and to reproduce it as a property tax' (part quoted by Farnsworth, n 4 above, 41).

<sup>18</sup> He had already introduced one Budget for 1803 in December 1802.

not been worked out in advance. While it was by no means certain that the Peace of Amiens would last, particularly from October 1802,<sup>19</sup> it seems unlikely that work would have continued on an income tax before the outbreak of war. This would be consistent with the Bills being drafted with the new approach but with significant changes made to them during the parliamentary process.

As an example of the changes made while the Bills were going through Parliament, Addington's tax was originally contained in two separate Bills, one relating to income from real property and public offices, therefore including what became Schedules A, B and E; and the other relating to personal property containing what became Schedule D, the equivalent of Schedule C not then existing.<sup>20</sup> After being introduced they were combined into a single Bill.<sup>21</sup> The original Schedule D Bill taxed all interest and annuities under Case III of that Schedule; the first combined Bill moved this charge to a separate Schedule C containing provisions for deduction of tax at source from public revenue interest but was silent on the method of taxing other interest, thus excluding interest altogether from Case III of Schedule D which was left to cover property of an uncertain annual value not charged under Schedule A. The final Bill limited the Schedule C charge to interest on the Funds but, as a result of Pitt's objections,<sup>22</sup> now without taxation at source; deduction of tax from other annual interest was dealt with outside the schedules. These changes to the treatment of interest will be dealt with in more detail below.<sup>23</sup>

<sup>19</sup> France invaded Switzerland in October 1802 and looked like invading Egypt. The United Kingdom never complied with all its obligations under the Treaty of Amiens either; for example, it never evacuated Malta.

<sup>20</sup> There are four Bills in HC Parliamentary Papers. These comprise the two originally separate Bills: Session 1802–03 Bill No 120 of 20 June 1803 (as amended by the committee) entitled 'for granting to His Majesty ... a Contribution on the Profits of certain Descriptions of Property and Offices, therein described', comprising what became Schedules A, B and E (there is an abstract of this Bill in *The Times*, 28 June 1803); and No 126 of 22 June 1803 (as amended by the committee) entitled 'a Contribution on the Profits of certain Descriptions of Personal Property and from Professions, and Trades, therein mentioned', comprising what became Schedule D divided into six cases but also including interest (there is an abstract of this Bill in *The Times*, 12 July 1803). There are two versions of the combined Bill: No 126 of 5 July 1803 (as amended), and No 164 of 22 July 1803 (as amended on second commitment) both entitled 'a Contribution on the profits of certain descriptions of property and from professions, trades, and offices, therein mentioned'. The *Times* refers to the 'Property and Income Tax Bill', for example when reporting its second reading (*The Times*, 22 June 1803), but this is obviously a name to assist readers (Ehrman, n 2 above, 678 may have been misled by this); 'Income Tax' never appears in the title of any of the Bills. Farnsworth, n 4 above, is wrong in saying at 57 that no copies of the two separate Bills survived the fire which destroyed the Houses of Parliament in 1834.

<sup>21</sup> Proposed, *The Times*, 4 July 1803; agreed to, *The Times*, 6 July 1803.

<sup>22</sup> See n 62 below.

<sup>23</sup> Text at n 77 below, and Appendix 2.

It is odd that no record seems to exist<sup>24</sup> detailing Addington's reasons for his significant departures from Pitt's 1799 tax when designing his own in 1803, particularly as he took an interest in the detail of legislation, for example, trying, albeit unsuccessfully, to obtain information about the successful Dutch taxation.<sup>25</sup> We can, however, deduce what are likely to have been their origins. Principal among these are the Land Tax and, it will be argued in this chapter, Adam Smith's *The Wealth of Nations*.<sup>26</sup>

#### WHAT IS A SOURCE?

Before considering the detail of Addington's tax as a tax on sources of income it is necessary to consider the nature of a source of income. It is suggested that the nature of sources of income in Addington's tax was influenced by Adam Smith's *The Wealth of Nations*. This was first published in 1776, the fifth edition had been published in 1789, and he died in 1790. The book was extremely well-known and would therefore have been fresh in the minds of those designing income tax from Pitt's triple assessment of 1798 onwards.<sup>27</sup> Indeed Pitt quotes 'the celebrated author of the Treatise on the Wealth of Nations, Adam Smith' in his 1798 Budget speech leading to the 1799 income tax in support of his £20 million estimate of the rent of land in the United Kingdom.<sup>28</sup> Addington, with his interest in finance, would certainly have been familiar with *The Wealth of Nations* even though he

<sup>24</sup> Unfortunately virtually all the available papers deal with much higher-level questions, such as the balance between taxation and borrowing, that one would expect from a Chancellor of the Exchequer. Addington's papers are in the Devon Record Office in Exeter. Apart from the ones quoted I found nothing of relevance in the archives for 1802 and 1803. I am grateful to Professor Chantal Stebbings for also sharing with me her own researches of the archives. I have also consulted the papers of Nicholas Vansittart (later Lord Bexley), the Secretary to the Treasury in Addington's Cabinet, in the British Library and have not found anything of relevance. There is also nothing of relevance in TNA in the Treasury (T 22/10) or Revenue (IR 31/151, 152) files of this time.

<sup>25</sup> He noted that in spite of high taxation under French occupation ('that the total charge of direct Taxation during the war could not be less than 45 per cent on the Capital of every Inhabitant'), 'the people appear to be still at their ease; industry to prevail, and trade in a considerable degree to have revived since the peace [of Amiens (1802)]'. He continued that 'I have taken considerable pains to acquire accurate information of the extent and nature of the Dutch Taxation, but the Accounts I have obtained have generally been so technical as to be hardly intelligible to a foreigner' (Private Memoir on Finance, n 9 above, 9–10, part also quoted by Farnsworth, n 4 above, 42; this is dated June 1803 and the Budget introducing his tax was on 13 June 1803; the document refers to 'the proposed Bill').

<sup>26</sup> Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (London, W Strachan and T Cadell, 1776). Page numbers are taken from the Penguin Classics version in two volumes, London, Penguin Books, 1999, referred to below as 'Penguin (Books 1–3)' and 'Penguin (Books 4–5)'.

<sup>27</sup> 38 Geo 3 c 16.

<sup>28</sup> Budget speech, 3 December 1798, Parliamentary Register 1796–1802, 104; *The Speeches of the Rt Hon William Pitt in the House of Commons* (London, 1808), vol 2, 438. This was unsurprisingly out of date. For comparison, Addington estimated income from land (excluding

does not seem to have referred to it and his biographies do not mention any connection with its author.<sup>29</sup> Adam Smith categorised the sources of income in this way:<sup>30</sup>

Wages, profit, and rent, are the three original sources of all revenue as well as of all exchangeable value<sup>31</sup> ... All taxes, and all the revenue which is founded upon them, all salaries, pensions, and annuities of every kind, are ultimately derived from some one or other of those three original sources of revenue, and are paid either immediately or mediately from the wages of labour, the profits of stock,<sup>32</sup> or the rent of land.<sup>33</sup> ...

houses) and tithes at £28m; Pitt's figure for tithes was £4m so that Addington estimate on the same basis as Pitt's was £24m (Farnsworth, n 4 above, 14 and 89). The figure actually assessed under Schedule A in 1803–04 was £38.7m (which includes houses (estimated at £6m) and Scotland (estimated at £3.5m), so that the actual figure on the same basis as Pitt's was about £29m: Farnsworth, n 4 above, 89–90, 93.

<sup>29</sup> There is no reference to Adam Smith in Ziegler, n 1 above, or Pellew, n 6 above. But, for example, Adam Smith was cited by Mr W Smith MP in the Parliamentary debate on Addington's Bill on 5 July 1803, Parliamentary Register 1802–05, 713. The story of Adam Smith arriving at Henry Dundas's (the Lord Advocate's) house in London where the company included Pitt, Grenville, Addington and Wilberforce at which Pitt asked Adam Smith to be seated first 'for we are all your scholars' is regarded as possibly apocryphal by Nicholas Philipson, *Adam Smith, An Enlightened Life* (London, Allen Lane, 2010) 268. There is, however, nothing unlikely about that group of people meeting in London.

<sup>30</sup> RL Meek, *Precursors of Adam Smith* (London, Dent, 1973) viii describes Adam Smith's new division of society into landlords, wage-earners and capitalists as 'the really central element in that work [*The Wealth of Nations*]'. The French economists (physiocrats) Quesnay (1694–1774) and Turgot (1727–81) were known personally to Adam Smith from his stay in France in 1764–66, see Andrew Skinner, 'Introduction' in *The Wealth of Nations*, n 26 above, Penguin (Books 4–5) xvi–xvii. Although Turgot listed land, labour, capital and entrepreneurship as four factors of production, and rent, wages and profit as the return from them; the separation of entrepreneurs and employees and therefore profit and wages (sections VI, VII, VIII, LXI, LXV) was his advance on Quesnay: Skinner, *ibid* xxii; and Meek, *ibid* 4, suggests that Turgot was influenced in this respect by Richard Cantillon (1680?–1734), who (unusually) is mentioned by Adam Smith, though not on this point (Penguin (Books 1–3) 170–71). RL Meek, *Turgot on Progress, Sociology and Economics* (Cambridge, Cambridge University Press, 1973) contains a translation of Turgot's *Réflexions sur la Formation et la Distribution des Richesses* [*Reflections on the Formation and the Distribution of Wealth*]. However, there is doubt whether Adam Smith owned the whole of Turgot's *Réflexions* (published in the journal *Éphémérides du Citoyen* in three parts 1769–70): PD Groenewegen, 'Turgot and Adam Smith' (1968) 15 *Scottish Journal of Political Economy* 271, but Skinner in his n 21 cites Meek's information that Adam Smith possessed the first two parts.

<sup>31</sup> Adam Smith's theory was that the price of a commodity depended on the costs of these three items. Later theory, for example that of Ricardo (1772–1823), regarded wages as the only determinant of prices with capital being regarded as primarily an advance payment of wages (see n 67 below). The modern theory is that prices are determined by the utility of the goods produced.

<sup>32</sup> ie capital (other than land) generally, but in the context more specifically relating to trade in the form of fixed capital (machinery) and circulating capital (trading stock), see *The Wealth of Nations*, n 26 above, Book 1 ch 9 ('On the Profits of Stock') Penguin (Books 1–3) 190. The distinction between fixed and circulating capital (*avances primitives* and *avances annuelles*) derives from Quesnay and Turgot. In this context stock does not seem to include capital lent at interest, see text at n 67 below.

<sup>33</sup> *The Wealth of Nations*, n 26 above, Book 1 ch 6 ('Of the Component Parts of the Price of Commodities'), Penguin (Books 1–3) 155–56; repeated in the conclusion of Book I ch 11 (*ibid* 356).



The private revenue of individuals, it has been shown in the first book of this Inquiry, arises, ultimately from three different sources; rent, profit, and wages. Every tax must finally be paid from some one or other of those three different sources of revenue, or from all of them indifferently.<sup>34</sup>

Addington's Schedules follow the principle but not the detail of this categorisation. Whilst it might be tempting to regard Schedules A and B, D, and E respectively as reflecting 'the rent of land, the profits of stock and the wages of labour', with Schedule C as a special case, the fit is far from exact: Schedule D includes both stock (trades) and labour (comprising employments—other than public employments which are within Schedule E—and professions which Adam Smith included within labour).<sup>35</sup> The origin of Schedule D in the second of the separate Bills leading to the tax demonstrates that it merely dealt with the whole of personal property income.<sup>36</sup> The Cases within it are designed to enable different computational rules, rather than reflecting any division based on Adam Smith's sources. But the more significant point is that Addington's sources followed Adam Smith's principle that a source must produce income in its own right. It follows that Adam Smith did not consider interest to be a source of income, and nor did Addington's tax. We shall return to the treatment of interest in section V after looking at the effect of Addington's tax being on sources, and the origin of deduction of tax at source.

#### DIFFERENCE BETWEEN PITT'S TAX ON INCOME AND ADDINGTON'S TAX ON SOURCES: LAND TAX AS THE ORIGIN OF ADDINGTON'S TAX

The Land Tax,<sup>37</sup> which was in force at the time, was the origin of Addington's tax being a tax on property rather than on the receipt of income. Indeed,

<sup>34</sup> *The Wealth of Nations*, n 26 above, Book 5 ch 2 pt 2 ('Of Taxes'), Penguin (Books 4–5) 415.

<sup>35</sup> Schedule D Case II taxed professions (for Adam Smith's inclusion with wages see *The Wealth of Nations*, n 26 above, Book 5 ch 2 pt 2 art III) ('Taxes upon the Wages of Labour'), Penguin (Books 4–5) 461, employments (other than those within Schedule E) and vocations; Schedule E originally taxed 'every publick office or employment of profit and every annuity, pension, or stipend, payable by his Majesty, or out of the publick revenue of Great Britain, except annuities before charged by Schedule C'. Adam Smith said of public offices some of which were sinecures: 'The emoluments of offices are not, like those of trades and professions, regulated by the free competition of the market, and do not, therefore, always bear a just proportion to what the nature of the employment requires. They are, perhaps, in most countries, higher than it requires; the persons who have the administration of government being generally disposed to regard both themselves and their immediate dependents, rather more than enough. The emoluments of offices, therefore, can, in most cases, very well bear to be taxed' (Book 5 ch 2 pt 2 art III, Penguin (Books 4–5) 461. As mentioned in n 40 below profits from public offices were taxable under Land Tax (Land Tax Act 1692 [old style] (and all subsequent Acts) s 3), and Soos, n 49 below, 114 has traced its earlier use back to 1688 in an aid to William and Mary (1 Will & Mar sess 2 c 1).

<sup>36</sup> See n 20 above for the Bills.

<sup>37</sup> Land Tax started in 1692 (4 Will and Mary c 1) but the form of the 1697 Act (9 & 10 Wm 3 c 10) was repeated annually, the last one being that of 1797 (38 Geo 3 c 5), after which the Land Tax Perpetuation Act 1798 (38 Geo 3 c 60) provided that the tax raised by the 1797

Addington's description of his tax was a tax on 'Property producing Income', to which he added 'I propose a Land Tax and a personal Contribution'.<sup>38</sup> That land tax was the origin of his tax being a tax on property will be seen from Table 1.1. Pitt's 1799 Act merely lists types of income from landed property in great detail, treating rent from land separately from rent from houses,<sup>39</sup>

Act 'shall ... continue to be raised, levied and paid yearly to his Majesty, his heirs and successors, from and after the twenty-fifth day of March [the land tax year was not changed by the Calendar Act 1751 (25 Geo 2 c 30)] in every year for ever', a change that Income Tax has still never achieved. The perpetuation of Land Tax was necessary in order to provide for voluntary redemption by the Land Tax Redemption Act 1802 (42 Geo 3 c 116). Despite its name, Land Tax also taxed personal property, at least in theory, see n 40 below. It seems that in practice the contribution from personal property was small: in JV Beckett 'Land Tax or Excise: the Levying of Taxation in Seventeenth- and Eighteenth-century England' (1985) *C English Historical Review* 285, 296 only 7.4% of the yield in 1798 was from personal property. On Land Tax generally, see WR Ward, *The Land Tax in the Eighteenth Century* (Oxford, OUP, 1953). Land Tax continued until it was abolished by Finance Act 1963 s 68 by which time it yielded only £200,000 pa (there had also been provisions for compulsory redemption since 1949). For an interesting history see William Phillips, 'No Flowers, By Request' [1963] *British Tax Review* 285. Ehrman, n 2 above, 678 is wrong in referring to it as 'the now defunct Land Tax'; in 1803 the amount redeemed and purchased was £55,819 (First Report of the Commissioners of Inland Revenue, 1857).

<sup>38</sup> Private Memoir on Finance, n 9 above, 13, as Farnsworth, n 4 above, 42 points out. He may have had Land Tax in mind here only in relation to tax on land as he goes on to describe Schedules A and B and then adds 'The Duties on Pensions and Offices to be likewise at the rate of one Shilling in the pound [5%] ... Dividends in the funds and in Corporation Stocks to be also charged at 1/- in the pound ... Property in trades to be rated by Commercial Commissioners at the like rate of 1/- in the pound on the annual Profits in a similar manner to what was practical under the [ie Pitt's] Income Tax'. In his Budget speech on 13 June 1803 Addington refers to 'the times of William and Anne ... a great and glorious period in the history of this country', as the precedent for taxing land and personal property at the same rate (then 4s in the £ (20%) on most income, and 0.5% on stock in trade) (Cobbett's Parliamentary History of England, n 8 above, 13 June 1803, vol 36, col 1600, quoted by Farnsworth, n 4 above, 43). This is an indirect reference to Land Tax, introduced in 1688 during the reign of William and Mary; it is not clear why Queen Anne was mentioned as the Land Tax was in its final form by 1697, during William III's reign. This is a poor report of the speech as the reporters had earlier inadvertently been excluded from the public gallery and had subsequently made only sparse reports: Farnsworth, n 4 above, 51. However, this reference is not contained in the report in *The Times* or in the Parliamentary Register, although Pellew, n 6 above, 201 refers to it.

<sup>39</sup> Interestingly the substituted Schedule (see n 3 above) to Pitt's Act when compared to the original schedule demonstrates a deliberate move in the direction of taxation of income rather than property or annual value, suggesting that the thought process was not complete when it was originally enacted. (Surprisingly the 9 Cases of the Triple Assessment (38 Geo 3 c 16, 1798) were more consistent in referring to income.) In the 1799 Act in Cases 2, 3, 4, 6, 10, 13, 15 and 16 the change is from annual value to income; Case 3 is typical of this, the original saying 'The annual value of such Lands shall be taken at the full Amount of the Rent reserved', and the substituted version 'The income arising from such lands shall be taken'. Cases 9 and 12 originally contained a charge to tax on the property or, in Case 14 the person (mesne lessors); Case 12 originally said 'Mines, Tythes, Woods, and other hereditaments of uncertain Amount, when occupied by Tenants, to be charged as the same would be charged in the Hands of the Owner, deducting also the Rent payable for the same', and the substituted version was 'The Income arising from Mines, Tythes'. Only Cases 1, 11, 17 and 18 and the unnumbered sweeping-up provision in the original Schedule referred to income (any Cases not listed above merely contain cross-references to other cases or wording that was not changed). By contrast Addington's tax demonstrates a deliberate move in the opposite direction.

while Addington's Schedule A closely follows the wording of the Land Tax Act in describing the landed property itself.<sup>40</sup>

**Table 1.1: Comparison of the treatment of landed property in Pitt's and Addington's Acts with Land Tax**

<i>Pitt's 1799 Act</i>	<i>Land Tax 1697 onwards</i> <sup>a</sup>	<i>Addington's 1803 Act</i>
INCOME arising from Lands, Tenements, and Hereditaments Case 1 land occupied by the owner Case 2 houses occupied by the owner Case 3 land occupied by tenants at a rack rent Case 4 land demised to tenants at a fine [premium] and rent Case 5 land demised to tenants at a fine only (or with nominal rent) Case 6 houses demised to tenants at a rack rent Case 7 houses demised to tenants at a fine and rent Case 8 houses demised to tenants at a fine only (or with nominal rent) Case 9 Tythes in respect of Owners Case 10 Profits of Manors, or of Timber or Woods, usually cut, periodically, and in certain Proportions, Mines, Insurance Offices from Fire, and other Profits of uncertain Annual Amount	That all and every Manors, Messuages Lands and Tenements; And also all Quarries, Mines of Coal, Tin or Lead, Copper, Mundick, <sup>b</sup> Iron and other Mines, Iron Mills, Furnaces and other Iron works, Salt-springs and Salt-works; All Allom-mines <sup>c</sup> and Works; All Parks, Chases, Warrens, Woods, Underwoods, Coppices and all Fishings, Tythes, Tolls, annuities, and all other Yearly Profits and all Hereditaments or what Nature or Kind soever ...	For all Lands, Tenements, Hereditaments, or Heritages, there shall be charged throughout Great Britain ...; and the said Duty shall be construed to extend to all Manors and Messuages, to all Quarries of Stone, Slate, Limestone, or Chalk, Mines of Coal, Tin, Lead, Copper, Mundic, Iron, and other Mines; to all Iron Mills, Furnaces, and other Iron Works, and other Mills and Engines of the like Nature; to all Salt Springs and Salt Works; to all Alum Mines and Alum Works; to all Parks, Chases, Warrens, Forests, Underwoods, and Coppices; to all Water Works, Streams of Water, Canals, Inland Navigations, Docks, and Fishings; to all Tythes, Rents, and Compositions for Tythes, Corn Rents, and other Payments in lieu of Tythes; to all

*(continued)*

<sup>40</sup> Land Tax also described personal property which was taxable under s 2: 'any Estate in ready Monies, or in any Debts whatsoever owing to them ... or having any Estate in Goods, Wares Merchandises or other Chattels or personal Estate whatsoever'. Section 3 charged the profits of all 'publick Offices or Employments of profit', words that were used in Addington's Act: see n 35 above.

Table 1.1: (*Continued*)

<i>Pitt's 1799 Act</i>	<i>Land Tax 1697 onwards</i>	<i>Addington's 1803 Act</i>
Case 11 income of lands occupied by tenants at a rack rent Case 12 income arising from mines, Tythes, woods Case 13 income from lands demised for a fine with or without rent Case 14 income of mesne lessors from demises for fines with or without rent		Rights of Markets and Fairs; to all Ways, Bridges, and Ferries, and all other Profits arising out of Lands or Tenements, and all Hereditaments or Heritages throughout Great Britain, of what Nature or Kind soever they be, belonging to any Person or Persons ...

## Notes:

- a This wording can be traced back at least to 1688 (1 Will and Mar c 20) and is quoted by William Phillips, 'No Flowers, By Request' [1963] *British Tax Review* 44. The references to ironworks, saltsprings, or works, alum mines or works still live on in ITTOIA 2005 s 12 (and CTA 2009 s 39) (see note c below about alum mines); and fishings has become 'rights of fishing'. An earlier First Exposure Draft on Trading Income of Individuals by the Tax Law Rewrite in 1997 had said 'In 1803, the advantages of the original rule were clear. At the end of the 20th century however section 55 [ICTA 1988] is an anachronism—not just its archaic wording but its very existence' (commentary to clause 3.1.3 at para 11 in [www.hmrc.gov.uk/rewrite/exposure/first/ed1.pdf](http://www.hmrc.gov.uk/rewrite/exposure/first/ed1.pdf)), but for some reason it was never changed. Following a recommendation of the 1920 Royal Commission (Cmd 615) para 433, from 1926 these items were transferred from Schedule A and taxed under Case I but without being treated as a trade, which they were not because no purchase of the asset sold was involved, with the result that relief for trading losses was unavailable. They are now treated as a trade.
- b An archaic name for iron persulphide ( $\text{FeS}_2$ ) (archaically known as iron pyrite because it emits sparks (Greek pyr, fire) when struck), or arsenopyrite ( $\text{FeAsS}$ ), either of which is popularly known as 'fool's gold'. I am grateful to Victor Baker for his assistance with this and the following note.
- c Alum is a collection of hydrated double salts all containing aluminium, the commonest of which is potash alum or potassium aluminium sulphate dodecahydrate hydrated ( $\text{K}_2(\text{SO}_4) \cdot \text{Al}_2(\text{SO}_4) \cdot 12\text{H}_2\text{O}$ ). It was used as a dye-fixer for wool and was extracted from shale in North Yorkshire from 1607 (it had earlier been imported from the Papal States which accordingly stopped in Henry VIII's reign). It has not been mined since about 1855 when a synthetic substitute was invented, which makes the continued existence of alum mines in the legislation today (see note a above) even more surprising. Disused alum mines can still be seen in North Yorkshire, for example, the National Trust Loftus Alum Quarries at Boulby Cliffs.

The draftsman of Addington's Act clearly had the Land Tax Act in front of him. The effect of the difference in approach from Pitt's tax is striking: land comprises one source of income for Addington but 14 types of income (with some duplication) for Pitt.<sup>41</sup>

But other domestic income which had been two types of income in Pitt's Act, the only difference between them being whether the amount of income was certain or uncertain, which determined the basis of assessment,<sup>42</sup> became many more sources of income in Addington's Act. Addington divided domestic income into its many constituent sources: trade or manufacture (Schedule D, Case I); professions, employments or vocations (Case II); property of uncertain value not charged under Schedule A (Case III);<sup>43</sup> interest on the Funds (Schedule C); public offices or employments (Schedule E); and annual interest, annuities and other annual payments outside the schedules.<sup>44</sup> This gave Addington more scope for differences in the method of assessment.<sup>45</sup> The only items which are the same in Pitt's and Addington's tax are the charge on foreign income in Cases 17 and 18 of Pitt's Act and Cases IV and V of Schedule D in Addington's Act.<sup>46</sup> Case IV regards the

<sup>41</sup> The 1806 Act (46 Geo 3 c 65, 1806) split up Schedule A into three parts and introduced different bases of assessment, eg manors, average of seven-preceding years; mines, five-year average; quarries, iron works, etc, preceding year; tithes paid in kind to an ecclesiastical person, three-preceding years. See *Coltness Iron Co v Black* (1881) 1 TC 287.

<sup>42</sup> Case 15: 'income from any Trade, Profession, Office, Pension, Allowance, Stipend, Employment, or Vocation being of uncertain Annual Amount' (preceding year (or three-year average) basis), and Case 16: 'income from Offices, Pensions, Stipends, Annuities, Interest of Money, Rent Charge, or other Payments being of certain Annual Amount' (preceding year (or preceding year to 5 February, or to the accounting date) basis). Thus trade, profession and vocation, allowance and (surprisingly) employment are necessarily uncertain in amount, while annuities, interest and rentcharges are necessarily certain, with offices, pensions, stipends capable of falling within either category.

<sup>43</sup> This was extended by the 1805 and 1806 Acts to include public revenue interest not within Schedule C (because it was not 'annuities, dividends or shares of annuities', eg interest on exchequer bills), discounts, short interest; and the 1806 Act adds profits of dealers in cattle and milk where the annual value of the land did not afford a just estimate of the profits, see Anon, *Guide to the Property Act*, 2nd edn (London, Joyce Gold, 1807) 39–40.

<sup>44</sup> See text before n 66 below.

<sup>45</sup> Three-year average (Case I), preceding year (Cases II and III), current year (Schedules C and E). Even different tax rates could be applied (under Schedule B the tax rate was 9d in the pound (3.75%), or 6d (2.5%) in Scotland, rather than the normal 1s (5%)), and deduction of tax at source could be applied to certain sources. Addington had also proposed reliefs for small earned income which Pitt opposed, arguing that all income should be treated equally. Although Addington obtained a majority of 150 to 50 he did not press the point and gave the relief to small incomes of all types (s 193): *The Times*, 14, 15 July 1803; Cobbett's Parliamentary History, n 8 above, 13 July 1803, vol 36, col 1668.

<sup>46</sup> Case IV 'Interest arising from Securities in Ireland, or in the British Plantations in America, or in any other of his Majesty's Dominions out of Great Britain, and foreign Securities' (see n 64 below for the reason for this different treatment of foreign interest); Case V 'Possessions in Ireland, or in the British Plantations in America, or in any other of his Majesty's Dominions out of Great Britain, and foreign Possessions'. The difference between Cases IV and V was that the former taxed remittances of the current year, and the latter remittances of an average of

security as the source in a similar way to Schedule C; the foreign possession is clearly a source in Case V. This reliance on source for foreign income only might be regarded as an anomaly in Pitt's Act. But it might be said that treating the whole of foreign income as two sources is itself an anomaly that was changed only in 2005 in the course of the Tax Law Rewrite.<sup>47</sup> The Income Tax (Trading and Other Income) Act 2005 now deals with foreign income in a similar way to domestic income of the same type. Both taxes also contained a similar sweeping-up clause covering other income.<sup>48</sup>

#### LAND TAX AS THE ORIGIN OF DEDUCTION OF TAX AT SOURCE IN ADDINGTON'S TAX

The change in Addington's tax to being a tax on sources of income made possible deduction of tax at source. This, the most important feature of Addington's Act, is also derived from the land tax. Dr Piroška Soos<sup>49</sup> has noted that five of the provisions of Addington's Act for deduction of tax at source also featured in the Land Tax Act with very similar wording. These related to (1) rent; (2) rentcharges; (3) company dividends; (4) salaries payable by the Exchequer; and (5) salaries paid to a deputy.<sup>50</sup> Addington's Act contained

the three preceding years which was the same basis as Case I. Pitt's tax applied the arising and preceding year (or if not existing, an estimate for the current year) bases to the equivalent of Case IV, and remittances of the current year (to 5 February), or the three preceding years, or to the accounting date at the taxpayer's option, to the equivalent to Case V.

<sup>47</sup> Whether or not this was an anomaly Pitt's wording lasted until 2005 with the courts successfully adapting its interpretation to encompass enormous business changes over this long period: see J Avery Jones, 'Taxing Foreign Income from Pitt to the Tax Law Rewrite: the Decline of the Remittance Basis' in J Tiley (ed), *Studies in the History of Tax Law* (Oxford, Hart Publishing, 2004).

<sup>48</sup> In Pitt's Act: category IV (without any Case number) 'Income not falling under any of the foregoing Rules'; in Addington's Act: 'The Duty to be charged in respect of any annual Profits or Gains not falling under any of the foregoing Rules, and not charged by virtue of any of the other Schedules contained in this Act'. The strange positioning of this in Addington's Act at the end of Schedule D and before Schedule E arises because in the originally separate Bills (see n 20 above) what became Schedule E was originally Schedule B in the real property Bill and for some reason was placed after Schedule D in the combined Bill. The reason cannot be that the Schedules are in order of importance because although Schedule E income was estimated to be lower than Schedule D, so was Schedule C. Even in the original personal property Bill this provision had to exclude income taxed by the Act derived from the real property Bill. The income must be *eiusdem generis* with income in the preceding Cases, see *Attorney-General v Black* (1871) LR 6 Ex 308, 310.

<sup>49</sup> PE Soos, *The Origins of Taxation at Source in England* (Amsterdam, IBFD, 1997) 156. She also notes at 126 a land tax provision in s 135 relating to interest applying only to Scotland entitling a person who owed money at 6% to deduct from his annual rent one-sixth of the 6%.

<sup>50</sup> See (i) 1803 Schedule A II r 2; Land Tax Act (LTA) s 17; (ii) 1803 Schedule A II r 3; LTA s 5; (iii) 1803 s 127; LTA s 57; (iv) 1803 Sch E, Fifth; LTA s 32; (v) 1803 s 186; LTA s 109. These provisions are all set out by Soos, n 49 above, 156–80. She traces the principle of deducting and retaining tax back to the new subsidy of 1671 and to pensions paid out of clerical

three further such provisions which are not found in land tax, relating to interest, annuities and other annual payments,<sup>51</sup> salaries required to be paid to another person, and payments to a deputy or clerk out of salaries.<sup>52</sup> Thus, out of eight provisions for deduction of tax at source in Addington's Act, five were contained in the land tax and the remainder were similar in principle. A great advantage of these provisions of Addington's Act was that the payer could, so long as the payments were made out of taxed income of the same year, deduct and retain the tax on them, thus obtaining tax relief<sup>53</sup> and making them taxed income ('pure income profit') of the recipient on which he could not be assessed as it had already been taxed. In relation to trading income the procedure was modified by a separate requirement that the General Commissioners give a certificate before the deduction at source procedure could be used.<sup>54</sup> This both made it unnecessary for income paid under deduction of tax to be disclosed, and also reduced evasion in relation to claiming a trading deduction for interest, which was a significant problem under Pitt's tax.<sup>55</sup> The advantage of Addington's system over Pitt's can be seen from the example in the Exposition of the Act:

The occupier, charged with the whole duty, deducts from his landlord a portion of the tax, proportionate to his share of the profits. The superior proprietor, the mortgagee, the annuitant, the creditor by personal contract, and any other legitimate participant of the profits, is subject to the like proportionate deduction, without other interference from the powers created by the act.<sup>56</sup>

revenues in the sixteenth and seventeenth centuries, and so Addington's application of deduction of tax at source was far from original. Farnsworth, n 4 above, 44 also quotes the relevant Land Tax provisions. In Parliament Addington claimed taxation at the source which avoided disclosure in relation to land and interest to be the main advantage over Pitt's tax (*The Times*, 6 July 1803; Parliamentary Register 1802–05, 5 July 1803, 710).

<sup>51</sup> 'Annual payments' is an expression also used in land tax, see Table 1.2.

<sup>52</sup> 1803 s 208 (interest, see Table 1.1); Schedule E, Seventh; Schedule E, Eighth.

<sup>53</sup> If the payer's income was 100, the annual payment 10 and the tax rate 10%, the taxpayer paid tax on 100 (= 10) but retained 1 from the annual payment, making the net tax 9. He was still taxed on 100 (there was a prohibition on deduction from income or trading profits of the payer) but the result is the same as if he had paid tax on 90 (= 9). Because the recipient received taxed income no disclosure of the interest by him was necessary.

<sup>54</sup> 1803 s 209. See n 78 below for the derivation of this and the general provisions in the Bills leading up to the Act. This separate provision for interest paid out of trading profits survived until 1853 s 40.

<sup>55</sup> Interest deduction from trading profits was noted by the Report of the Commissioners for the Affairs of Taxes, n 4 above, 299 as one of the causes of 'extensive frauds and evasions' in Pitt's Act for which they recommended registration of debts, quoted by Farnsworth, n 4 above, 20–21. Addington's Private Memoir on Finance, n 9 above, 14 refers to his proposals being 'much less liable to Concealment and Evasion, as no returns of Income will be required except for such as does not arise from visible Property'.

<sup>56</sup> Exposition, n 14 above, 4.

The only assessment is on the farmer; all the others are paid out of taxed income starting with the rent.

Table 1.2 compares the rentcharges provision in the Land Tax Act and Addington's 1803 Act, which are extremely similar in their drafting, and the last column sets out the interest provision in Addington's Act which had no equivalent in Land Tax showing that it is no different in principle.<sup>57</sup>

**Table 1.2: Comparison of provisions of Addington's 1803 Act and Land Tax**

<i>Land Tax 1697 onwards (rentcharges, etc)</i>	<i>Addington's 1803 Tax (rentcharges, etc)</i>	<i>Addington's 1803 Tax (interest)</i>
Section 5. And whereas many of the Manors, Messuages, Lands, Tenements, Tithes, Hereditaments, and Premises in England, Wales and Berwick-upon-Tweed, <sup>a</sup> intended by this Act to be charged with a Pound-rate as aforesaid, stand incumbered with, or are subject or liable to the Payment of several Rent-charges or Annuities, or other Annual Payments issuing out of the same, or to the Payment of divers Fee-farm Rents, Rents-service or other Rents thereupon reserved or charged,...	Schedule A, II, Third—Where any such Dwelling Houses, Lands, Tenements, or Hereditaments, are subject or liable to the Payment of any Rent Charge, Annuity, Fee Farm Rent, Rent Service, Quit Rent, Feu Duty, Teind Duty, <sup>b</sup> or other Rent or annual Payment thereupon reserved or charged, the Landlords, Owners, or Proprietors, by whom any Deductions or Payments shall have been allowed as aforesaid,	Section 208. That upon all Annuities, yearly Interest of Money, or other annual Payments, whether such Payments shall be payable within or out of <i>Great Britain</i> either as a Charge on any Property of the Person or Persons paying the same, or as a Reservation thereout, or as a personal Debt or Obligation by virtue of any Contract, or whether the same shall be received and payable half-yearly, or at any shorter or more distant Periods, there shall be charged for every twenty Shillings of the annual Amount thereof, the Sum of one Shilling, without Deduction, according to and under and subject to the Provisions by which the Duty in Schedule (D.) may be charged; provided, that in every

<sup>57</sup> Bill 142 (see n 20 above) in Schs A and B r 4 (at 17) applies the rentcharges provision to interest by reference; it is only in the final Bill 164 that the interest provision (now limited to annual interest) is set out in full in the wording in Table 1.2. The changes to how interest was taxed are set out in n 78 below.



Table 1.2: (Continued)

<i>Land Tax 1697 onwards (rentcharges, etc)</i>	<i>Addington's 1803 Tax (rentcharges, etc)</i>	<i>Addington's 1803 Tax (interest)</i>
<p>It is therefore declared and enacted by the authority aforesaid, That it shall and may be lawful to and for the Landlords, Owners and Proprietors of such Manors, Messuages, Lands, Tenements, Hereditaments and Premises in England, Wales and Berwick-upon-Tweed, being charged with a Pound-rate as aforesaid, to abate and deduct, and to detain and keep in his, her or their Hands, out of every such Fee-farm Rent, or other Annual Rent or Payment, so much of the said Pound-rate which shall be taxed or assessed upon the said Manors, Messuages, Lands and Premises, as a like Rate for every</p>	<p>and the Landlords, Owners, and Proprietors, being respectively Occupiers, and charged to the said Duties, shall abate and deduct, and detain and keep in their Hands, out of every such Rent Charge, Annuity, Fee Farm Rent, Rent Service, Quit Rent, Feu Duty, Teind Duty, or other Rent or annual Payment aforesaid, so much of the said Duties or Payments on account of the same as a like Rate of one Shilling for every twenty Shillings on such Rent Charge, Annuity, Fee Farm Rent, Rent Service, Quit Kent, Feu Duty, or any Rent or Composition for Tythes, Corn Rent, or other Payment in lieu of Tythes, or any</p>	<p>Case where the same shall be payable by any Person or Persons out of any Profits or Gains charged by virtue of this Act, no Assessment shall be made upon such Annuity, Interest, or other annual Payment, but the whole Duty due in respect of such Profits or Gains shall be charged without regard to such annual Payment, and the Person so liable to make such annual Payment, shall be authorized to deduct out of such annual Payment at the Rate of one Shilling for every twenty Shillings of the Amount thereof, except where the Party to whom the Payment is to be made shall produce a Certificate of Exemption or Abatement, as hereinbefore is mentioned;</p>

(continued)

Table 1.2: (Continued)

<i>Land Tax 1697 onwards (rentcharges, etc)</i>	<i>Addington's 1803 Tax (rentcharges, etc)</i>	<i>Addington's 1803 Tax (interest)</i>
<p>such Fee-farm Rent or any other Annual Rent or Payment respectively shall be a just Proportion amount unto, so as such Fee-farm Rent or other Annual Rent or Payment respectively do amount unto twenty shillings per annum, or more;</p> <p>and all and every Person or Persons who are or shall be any ways entitled to such Rents or Annual Payments, their respective Auditors, Reeves, Receivers, and their Deputy or Deputies, are hereby required to allow such Deductions and Payments, according to such Rates, upon Receipt of the Residue of such Monies as shall be due and payable to them for such Rents or Annual Payments reserved or charged as aforesaid, without any Fee or Charge for such Allowance.</p>	<p>Teind Duty, or other Rent or annual Payment aforesaid respectively, not being less than twenty Shillings <i>per Annum</i>, shall by a just Proportion amount unto;</p> <p>and all and every Person and Persons who are or shall be anyways entitled unto such Rents, Duties, or annual Payments, their Receivers, Deputies, or Agents, are hereby required to allow such Deductions and Payments, according to such Rates, upon the Receipt of the Residue of such Monies as shall be due and payable to them for such Rents, Duties, or annual Payments, without any Fee or Charge for such Allowance; and the Landlord, Owner, Proprietor, and Occupier respectively, being charged as aforesaid, or having allowed such Deductions or Payments, shall be acquitted and discharged of so much Money as the Deductions or Payments shall amount unto, as if the</p>	<p>and the Person or Persons to whom such Payments are to be made, shall allow such Deduction upon the Receipt of the Residue of such Money, and the Person charged to the said Duties shall be acquitted and discharged of so much Money as such Deduction shall amount unto, as if the Amount thereof had actually been paid unto the Person or Persons to whom such Payment shall have been due and payable;<sup>c</sup></p>

Table 1.2: (Continued)

<i>Land Tax 1697 onwards (rentcharges, etc)</i>	<i>Addington's 1803 Tax (rentcharges, etc)</i>	<i>Addington's 1803 Tax (interest)</i>
	same had actually been paid unto such Person or Persons to whom such Rent Charge, Annuity, Fee Farm Rent, Rent Service, Quit Rent, Feu Duty, Teind Duty, or other Rent or annual Payment aforesaid, shall have been due and payable.	and where any Person having allowed such Deductions on account of any such annual Payment as aforesaid, or being liable to allow the same, shall himself be liable to make any such Payment, whether charged upon such first-mentioned annual Payment, or reserved thereout, or payable as a Debt or Obligation by virtue of any Contract as aforesaid, then and in every such Case, and so on upon each successive Payment to be made thereout, there shall be deducted the like Proportion thereof as aforesaid, at the Rate before-mentioned, which Deduction and Deductions shall be allowed in Discharge of so much Money as such Deductions shall respectively amount unto in the same Manner as is provided in respect of the first Deduction; but in every Case where any annual Payment as aforesaid shall, by reason of the same being

(continued)

Table 1.2: (Continued)

<i>Land Tax 1697 onwards (rentcharges, etc)</i>	<i>Addington's 1803 Tax (rentcharges, etc)</i>	<i>Addington's 1803 Tax (interest)</i>
		charged on any Property or Security in <i>Ireland</i> , or in the <i>British</i> Plantations, or in any other of his Majesty's Dominions, or on any foreign Property or foreign Security, or otherwise, be received or receivable without any such Deduction as aforesaid, there shall be charged upon such Interest, Annuity, or other annual Payment as aforesaid, the Duty before mentioned, according to and under and subject to the Provisions, by which the Duty in Schedule (D.) may be charged. <sup>d</sup>

## Notes:

- a Land tax was originally so limited but was extended to Scotland in 1707 on the Union by 6 Anne c 35.
- b A Scots term similar to tithes in England; annexed to the Crown after the Reformation and granted to secular owners called Titulars.
- c In Bill 120 at 19 and Bill 126 at 36–37 (see n 20 for the Bills) refusal to allow deduction was deemed usury. This was not repeated in the combined Bills (or the Act) which provided that the payer was 'acquitted and discharged' for the amount deducted; refusal to allow deduction incurred a penalty. There is an interesting report of *Attorney-General v Page*, *The Times*, 12 July 1811, in which a lender refused the deduction of tax from interest. The borrower stated his case to the Board of Taxes and the lender called in the loan secured on the borrower's farm. The Board prosecuted the lender, pointing out that the maximum penalty was treble the amount of the loan (£7,200) (1806 s 115), but on the lender accepting that he was wrong a verdict was entered for a penalty of £100.
- d These exceptions were expanded in 1805 and 1806, see text at n 82 for the 1806 version.

The considerable similarity of wording between land tax and Addington's Act in relation to rentcharges can be seen, particularly 'abate and deduct, and detain and keep', 'required to allow such deductions', and 'without any Fee or Charge for such Allowance' which demonstrates unquestionably the land tax origins of deduction of tax at source in Addington's Act. Other provisions for deduction of tax at source in land tax and Addington's Act are set out in Appendix 1 to this chapter.

The drafting of the deduction of tax from interest follows the same outline as for rentcharges but in a more modern style; land tax was over 100 years old by then. It should be mentioned that interest on funded<sup>58</sup> government debt ('the Funds') ('annuities,<sup>59</sup> dividends,<sup>60</sup> and shares of annuities ... out of any publick revenue') was taxed separately under Schedule C, with foreigners being exempted until the Income Tax expired in 1816.<sup>61</sup> Addington's original proposal was for deduction of tax at source on funded debt but this was opposed by Pitt;<sup>62</sup> it reverted to his original proposal in

<sup>58</sup> Funded debt implies the existence of a fund which is mortgaged or assigned to pay the debt. Adam Smith, *The Wealth of Nations*, n 26 above, Book 5 ch 3 ('of Public Debts'), Penguin (Books 4–5) 512 explained: 'Sometimes it [the government] has made this assignment or mortgage for a short period of time only, a year, or a few years, for example; and sometimes for perpetuity. In the one case the fund was supposed sufficient to pay, within the limited time, both principal and interest of the money borrowed. In the other it was supposed sufficient to pay the interest only, or a perpetual annuity equivalent to the interest, government being at liberty to redeem at any time this annuity upon paying back the principal sum borrowed'. For example, Pitt had mortgaged the yield of his income tax for a loan of £11m which, on the repeal of the tax, had to be funded by a new loan of £57m charged on the Consolidated Fund. Only funded debt is within Schedule C. By contrast, Adam Smith (at 511) explains unfunded debt: 'It consists partly in a debt which bears, or is supposed to bear, no interest, and which resembles the debts that a private man contracts upon account, and partly in a debt which bears interest, and which resembles what a private man contracts upon his bill or promissory note'. He gives as an example of the latter navy and exchequer bills. Unfunded debt was taxable under Case III of Schedule D; there is an express reference there to exchequer bills from 1805 (see n 78 below).

<sup>59</sup> Funded debt was then irredeemable and the only return was in the form of an annuity (for life, for a fixed term, or perpetual) with no right to repayment of the capital (see Adam Smith, *Lectures on Justice, Police, Revenue and Arms* (1763) (Oxford, Clarendon Press, 1896) 247, available at [https://openlibrary.org/books/OL7197564M/Lectures\\_on\\_justice\\_police\\_revenue\\_and\\_arms](https://openlibrary.org/books/OL7197564M/Lectures_on_justice_police_revenue_and_arms)).

<sup>60</sup> Dowell's *Income Tax Laws*, 7th edn (London, Butterworths, 1913) 217 explains: 'On the creation of the "consols" in 1752, of annuities [see n 59 above] consolidated into one joint stock of annuities, the annuities dealt with were made payable in half-yearly dividends on January 5th and July 5th, hence the word "dividends", meaning these shares of the bank annuities'. This use was probably confusing even at the time. On 6 August 1842 the Solicitor's Office advised against an argument put forward by Rothschilds that they were in receipt of interest and not dividends or annuities on a foreign loan on the basis that 'there is no doubt that the term dividends is applicable to interest and is commonly used to designate it' (TNA IR 99/102 p 30). The expression was still causing problems as late as *Esso Petroleum Co Ltd v Ministry of Defence* [1989] STC 805, in which it was held to be limited to interest on securities and did not include interest on damages payable by the Crown.

<sup>61</sup> Interest on the Funds held by non-resident non-nationals were exempt: 1803 s 71; 1805 s 77; 1806 s 103 Fifth. Adam Smith notes that 'the Dutch, as well as several other nations, having a very considerable share in our public funds' (*The Wealth of Nations*, n 26 above, Book 5 ch 3, Penguin (Books 4–5) 528); see n 25 above for their continued prosperity during French occupation in spite of heavy taxation. Under Pitt's 1799 Act no exemption was necessary because non-resident foreigners were not taxed on British income anyway. This relief for foreigners was fully debated in 1806 but no change was made. It was not continued in the 1842 Act; Pellew, n 6 above, vol 2, 199 explained that by then a foreigner could have withdrawn his capital at a profit, which was not the case in 1803.

<sup>62</sup> Addington had proposed deduction at source for Schedule C (see his Private Memoir on Finance, n 9 above, 13: 'to be deducted at the Bank or Office where the same may be payable'), which was contained in Bill 142 (see n 20 above) but Pitt successfully opposed this as late as 13 July 1803 because the conditions of issue were that the interest would be paid 'without any deduction whatsoever', and so deduction would be a 'violation of the public compact entered

1806.<sup>63</sup> Naturally deduction of tax at source was not a possibility for interest on foreign securities (Case IV of Schedule D).<sup>64</sup> Since deduction at source applied originally only to interest paid out of taxed income it did not apply where this was not the case.<sup>65</sup> Interest will be considered further in the next section.

ADAM SMITH'S *THE WEALTH OF NATIONS* AS THE ORIGIN OF THE  
TREATMENT OF INTEREST IN ADDINGTON'S TAX

Interest is clearly income but it is not a source of income because money does not earn income in itself but has to be paid out of some other income-producing source (unless it is paid out of further borrowing). Significantly, interest was not treated as a source by Adam Smith:<sup>66</sup>

The interest of money is always a derivative revenue, which, if it is not paid from the profit which is made by the use of the money, must be paid from some other

into between the Government and the holders of stock' (*The Times*, 14 July 1803; Parliamentary Register 1802–05, 13 July 1803, 740; Cobbett's Parliamentary History, n 8 above, 13 July 1803, vol 36, col 1666; the date of 5 July 1803 in Pellew, n 6 above, vol 2, 197 appears to be an error). Pitt therefore rested his argument on the condition about deduction rather than taxation itself; indeed he had included income from the Funds in his 1799 Act under annuities and interest of money in Case 16 without mentioning it specifically. Pellew, n 6 above, vol 2, 198–99 quotes a letter to him from Lord Bexley (Nicholas Vansittart): 'Mr Pitt replied, that he certainly did not mean that they should be exempted, but that they should be called upon to pay on their dividends as a part of their income. This, I said, would be felt by the stockholders as much as a direct tax; but he persevered in his opinion'.

<sup>63</sup> Addington was ultimately proved right. When in 1806 Lord Henry Petty, the Chancellor of the Exchequer in Lord Grenville's Ministry of All the Talents, introduced deduction at source the income assessed under Schedule C rose from £11.9m to £22.499m (on which tax at 10% = £2.249m): Farnsworth, n 4 above, 67–68.

<sup>64</sup> See text at n 46 above in relation to foreign income generally. Presumably no distinction between annual and short interest could be made for foreign interest because there was no possibility of investigating its terms (which is the deciding factor, see n 70 below), and so the security was treated as the source. It is interesting that Case V also treated a dividend from a non-resident company differently from one from a resident company. A UK resident company was transparent for tax purposes, but the source of a dividend from a non-resident company was the dividend itself because it would be impossible to apply transparency to a non-resident body. So long as the share in the company ('the tree') remained intact a dividend ('the fruit') from a non-resident company was taxable whatever the underlying source, so that a dividend paid out of a capital gain by a non-resident company was taxable (*IRC v Reid's Trustees* (1949) 30 TC 431) whereas the same paid by a resident company was not (*Centlon Finance Co v Ellwood* [1962] 2 WLR 871). For cases where the 'tree' remained intact, see *Rae v Lazard* (1963) 41 TC 1 (partial liquidation under Maryland law, likened to cutting the tree in two) and *Courtaulds Investments Ltd v Fleming* (1969) 46 TC 111 (Italian share premium reserve, the distribution of which was treated as a return of capital). See J Avery Jones, 'Defining and Taxing Companies 1799 to 1965' in J Tiley (ed), *Studies in the History of Tax Law* (Oxford, Hart Publishing, 2012) vol 5, ch 1, p 1.

<sup>65</sup> Deduction became compulsory by Customs and Inland Revenue Act 1888 s 24(3). See Richard Thomas, Chapter 2, for more details.

<sup>66</sup> Adam Smith was against taxing interest on the grounds that the amount of a person's capital stock was a secret and 'An inquisition into every man's private circumstances, and an

source of revenue, unless perhaps the borrower is a spendthrift, who contracts a second debt in order to pay the interest of the first.<sup>67</sup>

Addington's income tax, unlike Pitt's,<sup>68</sup> followed exactly the same approach as Adam Smith in not treating domestic interest as a source.<sup>69</sup> In this respect Addington followed Adam Smith more closely than he did for the contents of the Schedules. In Addington's tax, annual interest,<sup>70</sup> as well as annuities<sup>71</sup> and other annual payments, were not sources in their own right but were regarded as coming out of the fund of the payer's general income.<sup>72</sup> Addington's 1803 Act was careful not to place these within a schedule, which would have implied that they constituted sources, but instead charged tax

inquisition which, in order to accommodate the tax to them, watched over all the fluctuations of his fortune, would be a source of such continual and endless vexation as no person could support'. And secondly (a typically perspicacious comment although relating to taxation on a source, rather than a residence, basis; under a residence basis the incentive is for the owner, rather than the investment, to move), 'The proprietor of stock is properly a citizen of the world, and is not necessarily attached to any particular country. He would be apt to abandon the country in which he was exposed to a vexatious inquisition, in order to be assessed to a burdensome tax; and would remove his stock to some other country, where he could either carry on his business, or enjoy his fortune more at his ease'. (Both quotations from *The Wealth of Nations*, n 26 above, Book 5 ch 2 pt 2 ('Of Taxes'), Penguin (Books 4–5) 441–42).

<sup>67</sup> *The Wealth of Nations*, n 26 above, Book 1 ch 6, Penguin (Books 1–3) 155. This aspect seems to be original to Adam Smith uninfluenced by Turgot (or, so far as I am aware, anyone else). Turgot had a highly developed section on interest in the last part of *Réflexions* that Adam Smith did not follow in other respects and had probably not seen for the reasons given in n 30 above, of which Schumpeter, *History of Economic Thought* (London, Routledge, 1997) 332 said was 'not only by far the greatest performance in the field of interest theory the eighteenth century produced but it clearly foreshadowed much of the best thought of the last decade of the nineteenth century'. Turgot lists five ways of employing capital: buying a landed estate; investing in agricultural enterprises as a tenant; employing it in industrial or manufacturing enterprises; or in commercial enterprises; or lending it at interest (summarised in his section LXXXIII, in RL Meek, *Turgot on Progress, Sociology and Economics* (Cambridge, Cambridge University Press, 1973) containing a translation of Turgot's *Réflexions sur la Formation et la Distribution des Richesses* [*Reflections on the Formation and the Distribution of Wealth*]). Presumably if Turgot had been listing sources of income he would have included loans at interest. At the time interest was not regarded as important. D Ricardo, *On the Principles of Political Economy and Taxation* (London, John Murray, 1817) writing slightly later regarded labour as the prime determinant of price with capital being to a great extent regarded as an advance payment for labour leaving only a small interest element in addition, see G Stigler, 'Ricardo and the 93% Labor Theory of Value' (1958) 48 *American Economic Review* 357.

<sup>68</sup> Pitt's 1799 Act included interest in his Case 16 along with offices, pensions, stipends, annuities, rentcharge or other payments of a certain annual value, see text at n 42 above. Case 9 of Pitt's 1798 Triple Assessment (38 Geo 3 c 16) was similar.

<sup>69</sup> See n 64 above for the treatment of foreign source interest. Interest on funded government debt taxable under Schedule C is mentioned in the text around n 58 above and will not be dealt with here.

<sup>70</sup> In essence if the liability cannot by its terms continue for a year the interest on it is short interest; otherwise it is annual interest. See Richard Thomas, Chapter 2, for more details.

<sup>71</sup> Note Adam Smith's reference to annuities not being within his three sources in the text at n 33 above.

<sup>72</sup> On the other hand, interest on the Funds and interest on foreign securities do have a source.

on them ‘according to and under and subject to the provisions by which the duty in Schedule D may be charged’,<sup>73</sup> with the 1806 Act specifying this to be under Case III of Schedule D.<sup>74</sup> The charging provision was the section from which the quotation is taken, not Case III.<sup>75</sup> This referential treatment continued until 1853 when all interest, annuities and other annual profits and gains not charged under any of the other schedules was put into Schedule D contrary to Adam Smith’s approach;<sup>76</sup> presumably by then the reason for charging tax on them by reference to, rather than including them in, Case III had been forgotten. They are unlike other sources in that they arise from the payer’s general income, whatever type of income it comprises, rather than a specific income-producing source.

The question is whether this treatment of interest can be attributed to Adam Smith’s influence or whether it is merely that where deduction of tax at source applies there is no need for the income to be within a Schedule because it will never be assessed. In answering this we can therefore concentrate on the situations where deduction at source did not apply, although it should be mentioned that provisions for deduction at source existed from the earliest available Bills leading to the 1803 Act<sup>77</sup> even though the details changed considerably, as summarised in Appendix 2 to this chapter. Where deduction of tax at source does not apply, we must first make a distinction between annual interest and short interest.<sup>78</sup> So far as annual interest is concerned (and annuities and other annual payments) the treatment of

<sup>73</sup> 1803 s 208 set out in Table 1.2, column 3 (this provision was included for the first time in the Bill of 22 July 1803 at 118–19). The quoted words originally applied to cases where deduction of tax did not apply but in the Act they were added to the first part of the general section thus applying to all yearly interest, resulting in the 1803 form of the section set out in Table 1.2. As has been mentioned dividends were not a source either because companies were transparent.

<sup>74</sup> 1806 s 114.

<sup>75</sup> *Attorney-General v London County Council* (1900) 4 TC 265, 295–96 per Lord Macnaghten. See John Tiley’s strong criticisms of the successor section (by then no longer applying to annual interest) ‘The Repeal of Section 52 of the Taxes Act 1970’ [1981] *British Tax Review* 263.

<sup>76</sup> 1853 s 2. It is interesting to note that Anon, *Guide to the Property Act*, 2nd edn (London, J Gold, 1807) 40 lists annuities, yearly interest of money and other annual payments as one of the items under Case III, which is clearly not the case in the statute itself. Presumably it was thought that making the distinction between something which is within Case III and something which is taxed ‘according to and under and subject to the provisions by which the duty in [Case III] may be charged’ was unhelpful to the reader.

<sup>77</sup> See n 20 above for the Bills.

<sup>78</sup> 1803 did not specifically deal with short interest. 1805 s 93 expressly included short interest (see n 70 above) for the first time in Case III of Schedule D, Second: ‘The Profits on all Exchequer Bills, and other Securities bearing Interest payable out of the publick Revenue [these were outside the scope of Schedule C], and on all Discounts, and on all *Interest of Money not being annual Interest*, payable or paid by any Persons whatever, shall be charged according to the preceding Rule in this Case’ (emphasis added).



such income in circumstances not qualifying for deduction of tax at source continued to develop between the 1803, 1805<sup>79</sup> and 1806 Acts. It is better to focus on the last of these on the basis that the 1803 Act was enacted under great pressure following the re-declaration of war and it is not surprising that changes had to be made later.<sup>80</sup> The equivalent to section 208 of the 1803 Act set out in Table 1.2 in the 1806 Act<sup>81</sup> is the exclusive charging section for annual interest whether or not deduction of tax in fact applies. The section lists the cases where deduction does not apply:

but [1] in every Case where any annual Payment as aforesaid shall, by reason of the same being charged on any Property or Security in Ireland, or in the British Plantations, or in any other of His Majesty's Dominions, or on any Foreign Property or Foreign Security, or otherwise, be received or receivable without any such Deduction as aforesaid, and [2] in every Case where any such Payment shall be made from Profits or Gains not charged by this Act, or [3] where any Interest of Money shall not be reserved or charged or payable for the Period of One Year, then and in every such Case there shall be charged upon such Interest Annuity or other annual Payment as aforesaid, the Duty before mentioned, according to and under and subject to the several and respective Provisions by which the Duty in the Third Case of Schedule (D.) may be charged.<sup>82</sup>

Item (1) seems to be a recognition that the law governing the security, then almost certainly real or immovable property, is not likely to accept deduction of tax in accordance with British tax law.<sup>83</sup> In items (1) and (2) the

<sup>79</sup> As mentioned, 1805 put short interest into Case III and also specifically dealt with it in the deduction section (1805 s 192), which additionally dealt with payments not made out of taxable income.

<sup>80</sup> The whole tax was introduced in the extremely short period of just over eight weeks between the Budget on 13 June 1803 and the Act on 11 August 1803, during which two separate Bills were introduced and then combined, so it is not surprising that some of the details needed to be changed in subsequent years.

<sup>81</sup> 1806 s 192.

<sup>82</sup> 1806 s 114 (my addition of the numbers in square brackets). See n 83 below in relation to item (1). The 'according to' phrase was first used in Bill 164 at 118–19 in relation to interest charged on foreign property. It was then applied by the Act to payments to which deduction of tax did apply at the last minute not having been in any of the Bills (see the first paragraph of 1803 s 208 in Table 1.2).

<sup>83</sup> Since deduction of tax was not mandatory it is not clear why this provision was necessary. Failure to deduct would normally mean that the payer did not obtain any tax relief but the 1803 Act (Schedule D Case 1 r 4) contained an exception from the prohibition on the deduction of annual interest in computing profits for 'interest of debts due to foreigners not resident in Great Britain', with the 1806 Act adding 'or in any other of His Majesty's Dominions', which would give relief for interest on a secured debt paid gross to a non-resident foreigner; this was for some reason not repeated in 1842 but had to be reintroduced in 1949 (see Richard Thomas, Chapter 2). Deduction of tax is really only a matter between the parties. When in 1888 it became necessary to deduct tax and pay it to the Revenue if interest was not paid out of taxed income, the Revenue became an interested party. See the obiter remark in *Keiner v Keiner* (1952) 34 TC 346, 348 that the UK resident husband, who it had been held was not entitled

referential treatment applies: the assessment is not under Case III but by reference to it. Item (3) is unnecessary as the deduction section does not apply to short interest anyway as it concerns only ‘yearly interest of money’. Short interest was specifically charged under Case III: ‘all interest of money, not being annual interest’.<sup>84</sup> The reference to it in the deduction section is probably there only to clarify that the section does not apply to it, although the double provision for short interest is confusing. Effectively, apart from short interest, all payments of domestic interest, annuities and other annual payments, and not just those where deduction at source applied, were outside the Schedules in accordance with Adam Smith’s approach. Accordingly, the conclusion is that one can attribute the nature of Addington’s sources to Adam Smith.

### CONCLUSION

Despite the absence of contemporary evidence about the origins of the difference between Addington’s tax and Pitt’s, it is reasonably clear that Land Tax was the origin of Addington’s being a tax on sources rather than on income, and in consequence deduction of tax at source, and that Adam Smith was the origin of the nature of a source of income, as illustrated by Addington’s treatment of domestic annual interest, not that Adam Smith would have approved of taxing interest.<sup>85</sup> The strange feature of Pitt’s tax is that he ignored the contemporary precedent of land tax for both sources and deduction of tax, so it was more that Pitt was out of line than that Addington’s tax was original.

to deduct tax from arrears of maintenance payments to his wife in the United States because the obligation was governed by New Jersey law, might if r 21 (the equivalent of the 1888 Act provision in the 1918 Act) applied have been in the position of having to deduct tax and pay it to the Revenue but still pay his wife gross.

<sup>84</sup> 1806 s 112, Third Case.

<sup>85</sup> See n 66 above. He would have been even more against taxing trades, as in this famous passage: ‘The state of a man’s fortune varies from day to day, and without an inquisition more intolerable than any tax, and renewed at least once every year, can only be guessed at. His assessment, therefore, must in most cases depend upon the good or bad humour of his assessors, and must, therefore, be altogether arbitrary and uncertain’: *The Wealth of Nations*, n 26 above, Book 5 pt II art 4 (‘Taxes which, it is intended, should fall indifferently upon every different Species of Revenue’), Penguin (Books 4–5) 462. Objection to inquisitorial powers was a constant tax theme at the time, see Chantal Stebbings, ‘Consent and Constitutionality in Nineteenth-Century English Taxation’ in J Tiley (ed), *Studies in the History of Tax Law* (Oxford, Hart Publishing, 2009) vol 3, 293.

## APPENDIX 1

Table 1.3: Other provisions for deduction of tax at source in Land Tax and Addington's Act<sup>a</sup>

<i>Land Tax 1697 onwards</i>	<i>Addington's 1803 Tax</i>
<p><i>Deduction of tax by tenants</i></p> <p>Section 17 ... and the several and respective Tenant or Tenants of all Houses, Lands, Tenements, and Hereditaments In England, Wales or Berwick-upon-Tweed which shall be rated by virtue of this Act, are hereby required and authorised to pay such Sum or Sums of Money as shall be rated upon such Houses, Lands, Tenements or Hereditaments, and to deduct out of the Rent so much of the said Rate as, in respect of the said Rents of any such Houses, Lands, Tenements, and Hereditaments, the Landlord should and ought to pay and bear;</p> <p>and the said Landlords, both mediate and immediate, according to their respective Interests, are hereby required to allow such Deductions and Payments, upon Receipt of the Residue of the rents.</p> <p>Section 18 And every Tenant paying the said Assessment or Assessments last mentioned shall be acquitted and discharged of so much Money as the Assessment or Assessments shall amount unto, as if the same had actually been paid unto such Person or Persons to whom his Rent shall have been due and payable ...</p> <p><i>Taxation of companies</i></p> <p>Section 57 [The New River Company, the Thames waterworks, the Marylebone or Hampstead waterworks, or any office</p>	<p>Schedule A II, rule Second—The Occupier or Occupiers of any Lands, Tenements, Hereditaments, or Heritages, being respectively Tenants of the same, and paying the said Duties, shall deduct so much thereof as a Rate of one Shilling for every twenty Shillings of the Rent payable to the Landlord or Landlords for the Time being would, by a just Proportion, amount unto, which Sums shall be deducted out of the first Payments thereafter to be made on account of Rent;</p> <p>all Landlords, both mediate and immediate, their respective Heirs, Executors, Administrators, and Assigns, according to their respective Interests, shall allow such Deductions and Payments upon Receipt of the Residue of the Rents,</p> <p>and the Tenants paying the said Assessments shall be acquitted and discharged of so much Money, as if the same had actually been paid unto the Person or Persons to whom his or their Rent shall have been due and payable: ...</p> <p>Section 127 ... and such Estimate shall be made on the Amount of the annual Profits and Gains of such Corporation, Fraternity, Fellowship,</p>

(continued)

Table 1.3: (Continued)

<i>Land Tax 1697 onwards</i>	<i>Addington's 1803 Tax</i>
<p>for insuring of houses, or in any lights, or the King's Printing House shall pay four shillings in the pound of the full yearly value] and they and all Companies of Merchants in London, and the Bank of England and all Salaries and Pensions (taxable in London) arising and payable or the General Post-office and Excise-office, charged by this Act shall be assessed by the Commissioners nominated and appointed for the said City, or any Two or more of them, for their respective Shares and Interests aforesaid, and the aforesaid joint Stock or Stocks, and for such Salaries and Pensions; and the same shall be paid by the Governors or the respective Treasurers or Receivers of the said River-waters, and Waterworks, and of the said Offices and Stocks respectively, to such Person or Persons as the said Commissioners, or any two or more of them, shall appoint to collect the same, and be deducted at and out of their next Dividend.</p> <p><i>Withholding from public salaries, etc</i></p> <p>Section 32 ... in all Cases where any Pensions, Annuities, Stipends, or other Yearly Payments, or the Fees, Salaries, Wages, or other Allowances or Profits charged by this Act, shall be payable at the Receipt of the Exchequer, or at any other publick Office, or by any of his Majesty's Receivers or Paymasters in England, Wales, or Berwick-upon-Tweed, the Tax or Payment which in pursuance of this Act shall be charged for or in respect of such Annuities, Pensions, Stipends, Fees, Salaries, Wages, Allowances, or Profits,</p>	<p>Company, or Society, before any Dividend shall have been made thereof to any other Person or Persons, or publick Bodies having any Share, Right, or Title, in or to such Profits or Gains; and all such other Person or Persons, and publick Bodies, shall allow out of such Dividends a proportionate Deduction in respect of the Duty so charged;</p> <p>Schedule E, Fifth—In all Cases where any Salaries, Fees, Wages, or other Perquisites, or Profits, or any Annuities, Pensions, or Stipends shall be payable at the Receipt of the Exchequer, or at any publick Office, or by any Officer of his Majesty's Household, or by any of his Majesty's Receivers or Paymasters, or by any Agent or Agents employed in that Behalf, then and in every such Case the Duties chargeable under this Act in respect of such Salaries, Fees, Wages, Perquisites, or Profits, or in respect of such Annuities, Pensions, or Stipends,</p>

(continued)

Table 1.3: (Continued)

<i>Land Tax 1697 onwards</i>	<i>Addington's 1803 Tax</i>
shall and may (in case of Non-payment thereof) be detained and stopped out of the same, or out of any Money which shall be payable upon such Pensions, Annuities, Stipends, Fees, Salaries, Wages, Allowances, or Profits, or for Arrears thereof, and shall be applied to the Satisfaction of the Rates and Duties not being otherwise paid as aforesaid.	shall and may, in case of Non-payment thereof, be detained and stopped out of the same, or out of any Money which shall be payable upon such Salaries, Fees, Wages, Perquisites, or Profits, or upon such Annuities, Pensions, or Stipends, or for the Arrears thereof, whenever the same shall happen, and be applied to the Satisfaction of the Duties on such Offices or Employments, or on such Annuities, Pensions, or Stipends respectively (not being otherwise paid) in the Manner directed by this Act.
<i>Payment to deputy</i>	
Section 109 ... That where any Office or Employment of Profit chargeable by this Act, is or shall be executed by Deputy, such Deputy shall pay such Assessment as shall be charged thereon, and deduct the same out of the Profits of such Office or Employment	Section 186 That where any Office or Employment of Profit chargeable by this Act, is or shall be executed by Deputy, such Deputy shall, in all Cases where he shall receive the Profits thereof, be answerable for and shall pay such Assessment as shall be charged thereon, and deduct the same out of the Profits of such Office or Employment; ...
and in case of Refusal or Non-payment thereof, such Deputy shall be liable to such Distress as by this Act is prescribed against any Person having and enjoying any Office or Employment of Profit, and to all other Remedies and Penalties respectively therein respectively contained.	and in case of Refusal or Non-payment thereof, shall be liable to such Distress as by this Act is prescribed against any Person having the Office or Employment, and to all other Remedies and Penalties respectively herein contained.

Note:

a In addition to the provisions about deduction of tax from rentcharges set out in Table 1.2.

APPENDIX 2: CHANGES TO ADDINGTON'S BILLS  
RELATING TO INTEREST

Both of the originally separate Bills<sup>86</sup> dealt with deduction of tax from 'any interest of money, annuity, or other annual payment ... annually paid' out of what became Schedule A and Schedule D income respectively, subject to obtaining a certificate from the General Commissioners by providing the name and address of the recipient and the amount.<sup>87</sup> In both there was also a procedure for the creditor to apply for a certificate that the interest be paid in full. The Schedule A clause was changed to one deducting tax by reference to the rentcharges clause in the first combined Bill, thus confirming the relationship between the land tax provisions for deduction of tax at source (which included rentcharges) and interest. That Bill also contained two clauses relating to deductions from Schedule D income, one in the description of Schedule D income and the other in a separate clause, both requiring a certificate and the latter expressly stating that no certificate was required for interest paid out of profits from land, public offices or income from the Funds.<sup>88</sup> The duplication was probably an error made while consolidating the two Bills. The Bill also provided that no deduction was allowed under Schedule D Case I for any annual interest, or any annuity, allowance or stipend 'in any other manner than as before directed';<sup>89</sup> presumably in consequence, the clauses in the separate Bills permitting the creditor to obtain a certificate from the General Commissioners requiring payment in full were not repeated as its operation would have meant that there was no deduction from trading profits for annual interest paid in full. In the final Bill not only was the duplication within Schedule D continued,<sup>90</sup> but a further duplication was introduced in the form of a more general provision permitting deduction of tax at source from the slightly differently-worded 'annuities, yearly interest of money or other annual payments' without reference to the type of income out of which they were paid and without needing to obtain a certificate.<sup>91</sup> This is the first use of 'yearly interest'. This clause became section 208, which is set out in Table 1.2. The Act also eliminated the duplication within Schedule D but the section dealing with payments out of Schedule D income subject to obtaining a certificate was retained alongside the general provision (which covered payments out of any type of income without requiring a certificate), which was odd, but the intention

<sup>86</sup> See n 20 above for the Bills.

<sup>87</sup> Bill 120 at 19 and Bill 126, 36–37; from the clause numbering of Bill 120 this clause was added in Committee, but it is not possible to tell from the Bill or the debates whether this was also the case with Bill 126.

<sup>88</sup> Bill 142, 17 (Schedule A r 4) and 45, 107–8 (Schedule D).

<sup>89</sup> Schedule D Case I rr 4, 47.

<sup>90</sup> Bill 164, 48, 119–20.

<sup>91</sup> Bill 164, 118–19.

was reasonably clear—that a deduction from trading profits required a certificate from the Commissioners. Lord Macnaghten described the Schedule D section which became 1803 section 210 as ‘a curious section, and one rather clumsily framed’ in *Attorney-General v London County Council*.<sup>92</sup> The explanation is presumably that what became section 210 was originally in the earlier Bills before what became 1803 section 208 was added in Bill 164 without specifically saying that it was restricted to payments out of non-Schedule D income. Section 210 survived until 1853 section 40 which dispensed with the need for a certificate,<sup>93</sup> but since Acts did not then contain repeals even this is not clear.

Apart from these provisions for deduction at source, the original Schedule D Bill taxed all interest and annuities under Case III of what became that Schedule; the first combined Bill moved this charge to a separate Schedule C containing provisions for deduction of tax at source from public revenue interest but being silent on other interest, thus excluding interest altogether from Case III of Schedule D which was left to cover property of an uncertain annual value not charged under Schedule A;<sup>94</sup> and the final Bill limited the Schedule C charge to annuities, dividends and shares of annuities payable out of the public revenue, that is funded debt, but, as a result of Pitt’s objections,<sup>95</sup> now without deduction of tax at source.<sup>96</sup>

<sup>92</sup> *Attorney-General v London County Council* (1900) 4 TC 265, 296.

<sup>93</sup> *ibid* Lord Macnaghten 296.

<sup>94</sup> Bill 142, 37 (Schedule C) and 47 (Case III of Schedule D). The scope of the charge was later extended, see n 43 above.

<sup>95</sup> See n 62 above.

<sup>96</sup> Bill 164, 40.