1951 *Present:* **Basnayake J.**

CHELLAPPAH, Appellant, *and* COMMISSIONER OF INCOME TAX, Respondent

S. C. 1,260—M. C. Colombo, 5,317/A

Income Tax Ordinance—Omission of income from return—Making false statement or entry in return—Prosecution under section 87 (1)—" Wilfully with intent to evade tax "—Meaning of words " wilfully " and " evade "—Excess Profits Duty Ordinance, No. 38 of 1941, s. 12 (5).

In a prosecution under section 87 (1) of the Income Tax Ordinance—

(i) the burden is on the Crown to prove that the accused " wilfully with intent to evade tax " committed any one of the acts specified in the section.

(ii) the word " wilfully " should be construed as meaning deliberately or purposely with the evil intent of committing the act or acts enumerated in the section.

(iii) the word " evade " must be understood not in the innocuous sense of avoid tax by taking advantage of the statute, but in the sense of unlawfully escape or avoid by fraud, misrepresentation or underhand contrivance.

(iv) the omission from a return of any income does not constitute an offence unless it is done deliberately and with evil intention of defeating unlawfully the object of the statute by knowingly presenting a false picture of the income of the person making the return by omitting therefrom material which the taxpayer knows should properly be there. An omission based on a mistaken view of the law or facts is not punishable.

(v) the fact that a statement or entry is false does not attract punishment unless the object of the false statement or entry was to defeat the purpose of the statute, to deny to the revenue its legitimate dues.

(vi) proceedings under section 87 of the Income Tax Ordinance cannot be regarded in the same way as a proceeding to recover tax under the Excess Profits Duty Ordinance. The admissions made by a person in proceedings for the recovery of tax cannot by themselves afford proof of a charge under section 87.

Held further, (*a*) that where a building contractor passed over certain of his contracts to another person who gave him a share of the profits for supervising the contracts, such payment should be reckoned as remuneration for services rendered and not as profits from his business as building contractor.

(*b*) that a person could not be punished under section 87 (1) of the Income Tax Ordinance for omitting in his return certain sums which he claimed as secret commissions paid by him. The fact that he submitted to pay tax on these sums did not by itself bring him within the ambit of the penal provision.

APPEAL from a judgment of the Magistrate's Court, Colombo.

H. V. Perera, K.C., with *S. Nadesan* and *N. Nadarasa*, for the appellant.

J. A. P. Cherubim, Crown Counsel, with *E. H. C. Jayetileke*, Crown Counsel, for the Attorney-General.

Cur. adv. vult.

April 18, 1951. BASNAYAKE J.—

The appellant, John Chellappah, has been convicted on nine charges in respect of offences under the Excess Profits Duty Ordinance, No. 38 of 1941. Section 12 (5) of that Ordinance incorporates therein Chapter XV of the Income Tax Ordinance, which prescribes offences and penalties. The penal provision that arises for consideration in the instant case is section 87 of the Income Tax Ordinance. That section, omitting paragraphs (*e*), (*f*) and (*g*) of sub-section (1), and sub-section (2), which are not material to this case, reads as follows:—

" 87. (1) Any person who wilfully with intent to evade or to assist any other person to evade tax—

(*a*) omits from a return made under this Ordinance any income which should be included; or

(*b*) makes any false statement or entry in any return made under this Ordinance; or

(*c*) makes a false statement in connection with a claim for a deduction or allowance under Chapter V or Chapter VI; or

(*d*) signs any statement or return furnished under this Ordinance without reasonable grounds for believing the same to be true;

shall be guilty of an offence, and shall for each such offence be liable on summary trial and conviction by a Magistrate to a fine not exceeding the total of five thousand rupees and treble the amount of tax for which he, or as the case may be the other person so assisted, is liable under this Ordinance for the year of assessment in respect of or during which the offence was committed, or to imprisonment of either description for any term not exceeding six months, or to both such fine and imprisonment."

To succeed in a prosecution under this section the Crown must prove that the appellant " wilfully with intent to evade tax " committed any one of the acts specified therein [1]. In order to understand the scope of the section it is necessary to ascertain the meaning of the words " wilfully " and " evade ".

The dictionary [2] gives the following meanings of the word " wilfully ": " with free exercise of the will; voluntarily; intentionally; in law, designedly, as opposed to inadvertently; in a penal statute, purposely, with evil intent; maliciously ". In commenting on this word in the case of *In re Young and Harston* [3], Bowen L.J. observes:

" Wilful is a word of familiar use in every branch of law, and although in some branches of law it may have a special meaning, it generally, as used in courts of law, implies nothing blameable, but merely that the person of whose action or default the expression is used is a free agent, and that what has been done arises from the spontaneous action of his will. It amounts to nothing more than this, that he knows what he is doing, and intends to do what he is doing, and is a free agent."

[1] *Piyasena v. Vaz, (1945) 47 N. L. R. 1.* [2] *New Standard Dictionary.*
[3] *31 Ch. D. 174.*

In the case of *R. v. Badger* [1], it was held that a surveyor was not guilty of " wilfully " receiving a higher fee than he was entitled to, when acting under an honest mistake.

It will be seen from the above that ordinarily the word " wilfully " means deliberately or purposely without reference to *bona fides* but that in penal statutes it is used in a sense denoting deliberately or purposely and with an evil intention. Section 87 is a highly penal provision. The word should therefore be construed as meaning deliberately or purposely with the evil intent of committing the act or acts enumerated in the section.

The word " evade " has several meanings according to the dictionary [2]. It means: " to avoid by artifice; elude or get away from by craft or force; save oneself from, as an impending evil; to escape; get away." It is also used in the sense of " defeat the intention of the law while complying with its letter ", and, especially in income tax law, of avoiding the incidence of tax by a judicious and skilful use of the various provisions of the statute, especially those dealing with exemptions and such other benefits allowed therein. Certain enterprising text-book writers have even gone to the extent of writing treatises under such titles as " Tax Evasion " and " How to Evade Income Tax ". The words " evasion " and " evade " are in those contexts used in the sense of lawful avoidance. It will be helpful to refer to some of the judicial dicta on the meaning of the expression. In *Simms & others v. Registrar of Probates* [3], Lord Hobhouse observes:

> " Everybody agrees that the word is capable of being used in two senses: one which suggests underhand dealing, and another which means nothing more than the intentional avoidance of something disagreeable."

In the case of *Bullivant & others v. Attorney-General for Victoria* [4] Lord Lindley observes:

> " The word ' evade ' is ambiguous. There are various ways of evading a statute."

and proceeds to illustrate what he has in mind thus:

> " As I have said, there are two ways of construing the word ' evade ': one is, that a person may go to a solicitor and ask him how to keep out of an Act of Parliament—how to do something which does not bring him within the scope of it. That is evading in one sense, but there is nothing illegal in it. The other is, when he goes to his solicitor and says, ' Tell me how to escape from the consequences of the Act of Parliament, although I am brought within it.' That is an act of quite a different character."

It being quite a legitimate thing to avoid tax by taking advantage of the provisions of the Income Tax or Excess Profits Duty Ordinance, the word " evade " must be understood in section 87, which penalises the acts enumerated therein, not in the innocuous sense of avoid tax by

[1] *L. J. M. C. 81 at 90.*
[2] *New Sandard Dictionary.*
[3] *(1900) A. C. 323.*
[4] *(1901) A. C. 196 at 207.*

taking advantage of the statute, but in the sense of unlawfully escape or avoid by fraud, misrepresentation or underhand contrivance. To construe the expression in the sense of avoidance of tax would be to deny the taxpayer of the legitimate benefits of the statute. It is also a rule of construction of statutes that where there are two meanings each equally satisfying the language of the statute and great harshness is produced by one of them and not by the other, the legislature is taken to have intended to use the word in the sense in which the great harshness is avoided and in the sense which least offends our sense of justice [1].

Bearing in mind the meaning I have given to each of the expressions " wilfully " and " evade ", I shall examine the material paragraphs of the section.

Paragraph (*a*) penalises the omission from a return of any income which should be included therein. The mere omission of any income from the return does not constitute the offence. The omission may be due to an oversight or it may even be deliberate but not wilfully with intent to evade tax. A taxpayer is entitled to construe the taxing statute and make his return in accordance with his understanding of it. An omission based on a mistaken view of the law or facts does not attract punishment. The taxing authorities are not bound by the taxpayer's views of the law or by his methods of accounting. They are free to reject his interpretation and assess him on what they think is the correct basis. If the taxpayer is dissatisfied he may appeal. To attract punishment the omission must be done deliberately and with the evil intention of defeating unlawfully the object of the statute by knowingly presenting a false picture of the income of the person making the return by omitting therefrom material which the taxpayer knows should properly be there.

Similarly, for the purposes of paragraphs (*b*) and (*c*), the mere fact that a statement or entry is false in fact does not bring the person making it within the ambit of the provision. In the first place the statement or entry must in fact be false for if it is not there is no offence. The false statement or entry must be deliberately made with the knowledge that it is false and with the evil intention of thereby misleading the taxing officer. The object of the false statement or entry should be to defeat the purpose of the statute, to deny to the revenue its legitimate dues. A statement or entry which is in fact false if made inadvertently or honestly or in the belief that it is true does not attract punishment even if the taxpayer stood to gain by the statement or entry if it passed undetected.

In applying the highly penal provisions of the Income Tax Ordinance, the Crown should not lose sight of the fact that our taxing statute though still not so complex as the law of England, is complex enough to baffle the average taxpayer who finds himself unable to complete the return unaided. May of them have to seek the aid of their legal advisers or income tax advisers or their accountants, by whom they are guided. A taxpayer who seeks a professional adviser's aid as a matter of

[1] *Simms & others v. Registrar of Probates, 1900 A. C. 323 at 335.*

course adopts the view his adviser takes of the tax law and his earnings. If the taxpayer is himself not an accountant he is also largely in the hands of his book-keeper who decides the proper head under which entries relating to his income and expenditure should be made. A psychological factor which cannot be ignored in such a situation is that the taxpayer rarely imposes his will on his adviser. In the instant case too it must be remembered that the appellant, though he was himself conversant with book-keeping, engaged an approved accountant to prepare his income tax accounts. His business activities were varied. They ranged over a wide field—from textiles to fruit drinks and building contracts.

The appellant commenced business as a building contractor about 1937. After the company of Terrazzo Tile Works, Ltd., of which he became managing director, was formed, he transferred a section of his business to it, on condition that the company was not to compete with him in his business as a building contractor. When the war came with its programme of urgent constructional works the appellant was able to obtain a large share of it. He executed some himself and took the profits. Others he passed over to the Terrazzo Tile Works, Ltd. The company gave him one-third share of the profits for supervising the contracts. The Commissioner of Income Tax claims that the income he derived by supervising the contracts is profits from his business as a building contractor (hereinafter referred to as the contract business). With that view I am unable to agree. The payment though made by way of a share of the profits was made for the appellant's services as a superviser. The amount paid shows that his technical skill was highly valued by the company. The fact that the payment for supervision was related to the profits does not alter its nature. The payments made by the Terrazzo Tile Works, Ltd., are in my view remuneration for services rendered and are not profits from the appellant's contract business.

The first set of charges, viz., 1, 2, and 3, relates to the accounting period January to December, 1942. The appellant has disclosed in his return for that period a sum of Rs. 44,992 as the profits of his contract business, but the Commissioner asserts that the amount is much more. His figure is Rs. 131,000. It appears from the evidence that the appellant has in fact omitted two items, one of Rs. 3,500 and the other of Rs. 102, which properly fall within the profits of his contract business. He says that this omission is due to a clerical error on the part of his book-keeper. The mere omission of those two items from the return as I have stated above does not prove the charge. Omitting them from the return is the same as not including them. But the appellant cannot be said to have omitted them wilfully unless it can be shown that having made up his mind not to include them he did not include them. If he did not think about them at all or if they did not occur to him, then his omission is not wilful [1]. There is no evidence to establish that their omission was wilful and with intent to evade duty. The sum of Rs. 3,500 is only one item of a total payment of Rs. 78,500, while the sum of

[1] *In re Mayor of London and Tubbs' Contract, (1894) 2 Ch. 524.*

Rs. 102 was a late payment for a disputed item. The other amounts that go to make the total amount of profits according to the Commissioner are—

(*a*)	Rs. 6,459
(*b*)	5,000
(*c*)	11,064
(*d*)	20,118
(*e*)	1,473
(*f*)	3,750
(*g*)	6,000
(*h*)	13,870

The prosecution offers no evidence in support of the charge in respect of items (*d*), (*e*), (*f*), and (*g*). Item (*a*) represents one-third share of the profits of a military contract paid to the appellant by the Terrazzo Tile Works, Ltd., for supervising the contract. Item (*b*) relates to a sum paid to an architect named S. H. Peiris who was engaged by the appellant for ten months for supervising St. Thomas' Hospital Contract No. D. C. R. E. 7. Item (*c*) is an amount appropriated by the appellant against stores supplied through him by the Royal Engineers' Stores in respect of a contract passed over to another. Item (*h*) represents a sum of money handed to the appellant by various British officers to be transmitted to destinations named by them. They were secret commissions obtained by them, and they did not therefore use the normal channels for transmitting the money. The appellant explains how the amount came into his books. He says this sum was in cash in his safe. One Saturday afternoon he had to make some cash payments and he utilised it and replaced the same by drawing from his account. The learned Magistrate has acquitted the appellant in respect of this item in charge 2.

In addition to these amounts the Commissioner has arbitrarily included 20 per cent. of their total. There being no foundation for that claim it cannot be entertained in a prosecution under section 87. The prosecution offers no evidence to establish that in fact items (*a*), (*b*), (*c*), and (*h*) are profits of the contract business of the appellant. There is no reason to reject the appellant's explanation of these items. S. H. Peiris denies the receipt of money. But he is contradicted by the cheque P. 32 for Rs. 3,000 in his favour, and the document D. 10 given by the appellant to enable him to obtain supplies of petrol. Peiris's evidence does not impress me. In fact it is extremely unsatisfactory. Though he is an architect he has joint bank accounts with more than one contractor and his conduct does not seem to be above board. Tudawe, the other witness who has been called by the prosecution, does not explain why he has taken no action to recover the large sums which he claims are due to him from the appellant. His conduct adds considerable weight to the appellant's claim that item (*c*) was retained against materials issued to him. Charges 1, 2, and 3 must therefore fail as the prosecution has not proved the necessary ingredients of those charges.

I shall now proceed to charges 4, 5, and 6. They relate to the accounting period January to December, 1943. The appellant disclosed the profits

from his contract business at Rs. 10,554. The Commissioner claims that they are more. According to his computation they should be Rs. 51,000. He arrives at that figure by adding the following items and increasing the total by 20 per cent.

(*a*)	Rs. 10,140
(*b*)	1,442
(*c*)	2,229
(*d*)	917
(*e*)	933
(*f*)	1,171
(*g*)	6,500
(*h*)	551
(*i*)	10,094

Item (*c*) has been withdrawn by the Commissioner as it has nothing to do with the appellant's contract business. There is no evidence as respects item (*g*). Items (*a*) and (*b*) represent the appellant's share of the profits for supervising contracts passed on to the Terrazzo Tile Works, Ltd. Items (*d*), (*e*), (*f*), (*h*), and (*i*) represent final payments made on contracts D. C. R. E. 68, 82, 319, 36, and 91. The appellant says that the amounts shown against those items were paid out in secret commissions to military officials who were instrumental in giving him the contracts and form no part of the profits on those contracts. The commissions were as a rule paid out of the final payments. Document P 39 seems to support the explanation of the appellant:—

D. C. R. E. 68	*D. C. R. E. 82*	*D. C. R. E. 319*	*D. C. R. E. 36*	*D. C. R. E. 91*
16,500	6,000	15,200	11,290	48,000
6,380	2,620	1,171·25	4,880	24,000
1,880	933·19		551·25	18,475
917·43				10,094·30

The prosecution relies on the bare omission of these items from the computation of the appellant's profits. That is not sufficient to establish an offence under the section. It must prove that the appellant actually received these profits in his contract business and wilfully with intent to evade tax omitted to disclose them. The paying of secret commissions is not unknown and the Assessor admits in his evidence that large claims are made by taxpayers who carry on certain classes of business in respect of sums paid as commissions. He gives the instance of ship chandlers. In practice he says as a matter of indulgence a certain percentage of such a claim is allowed. That being the case, in the absence of evidence to establish that the sums in question were in fact not paid as commissions the appellant cannot be punished under section 87 (1). The fact that he has submitted to pay tax on these sums by itself does not bring him within the ambit of the penal provision. The appellant is therefore entitled to be acquitted on these charges as well.

Lastly I come to charges 7, 8, and 9. They relate to the accounting period January to December, 1944. The appellant is charged with making a false statement to the effect that he incurred a loss of Rs. 21,132

in respect of his business. This loss was incurred in respect of a contract known as the Kandy contract. The statement of account of this contract P 45A is as follows:—

Dr.	Rs. c.	*Cr.*	Rs. c.
To Amt pd for labour sub-contractors as per statement ..	45,157 47	By Amt recd from Chief Engineer : 19.7.44 ..	22,500 0
Amt pd for labour as per check-roll	11,765 92	12.8.44 ..	35,880 0
Amt pd for small odd jobs ..	1,375 0	19.9.44 ..	39,420 0
Amt pd for Timber to different suppliers as per statement ..	64,438 70	Amt recd for extra works ..	1,713 21
Amt pd for Hinges and Iron materials	7,081 6	Amt due as at 31.12.44 on closing a/cs from Chief Engineer and recovered in August, 1945 ..	15,716 20
Amt paid for Cadjans, Bricks, and Sand	4,684 12	LOSS incurred on Contract ..	21,132 86
Salaries to Clerks, Overseers and Supervisors	1,860 0		
	136,362 27		136,362 27

The prosecution has offered no evidence to prove that the statement respecting the loss is false. In fact the Commissioner admits that there was a loss on the Kandy contract but he puts the figure at Rs. 10,000. The onus is on the prosecution and not the appellant and in the absence of proof of the ingredients of the offence the charge must fail.

I shall now discuss the allegation respecting the omission of the three items of Rs. 788, Rs. 11,643, and Rs. 13,370 in P 17c from the appellant's return. They represent payments received on account of the Victoria Park Vehicles Shed Contract (D. C. R. E. 527), the Madampitiya Contract (D. C. R. E. 565) and the Boralesgomuwa Contract (D. C. R. E. 594). The Victoria Park Vehicles Shed Contract was given over to Tudawe by the appellant who was to get 10 per cent. of the amount of the contract. The sum of Rs. 788 was according to the appellant appropriated against monies due from Tudawe for materials supplied. The Madampitiya contract was a contract passed on to the Terrazzo Tile Works, Ltd., Tudawe being the sub-contractor. The sum of Rs. 11,643 was retained against monies due from Tudawe for stores and materials supplied to him. The payment on account of the Boralesgomuwa contract of which also Tudawe was the sub-contractor, is claimed by the appellant against monies due from Tudawe for materials supplied.

The prosecution offers no evidence to prove the charge beyond showing that the payments were made by the Command Paymaster. That fact alone is insufficient to establish the charge and the appellant is entitled to an acquittal. As stated by me earlier, I am not prepared to act on Tudawe's evidence, for it appears to be unsatisfactory. I quote below his evidence on the point with the learned Magistrate's note on it. Tudawe says:—

"I know the accused Mr. John Chellappah. I had not authorised him to appropriate a sum of Rs. 11,643 which was due to me from the Terrazzo Tile Works, under Military Contract D. C. R. E. 565 Madampitiya. I did not agree to his appropriating any sum of money due

to me as a set-off as against any money I owed him. (I should note here that the witness first answered this question by saying ' I don't think ' and then ' I don't remember '.) "

I wish to observe that in the instant case the prosecution appears to have regarded the proceedings under section 87 in the same way as a proceeding to recover tax under the Excess Profits Duty Ordinance. That is an incorrect approach to a prosecution under a highly penal provision. The admissions made by the appellant in proceedings for the recovery of tax cannot by themselves afford proof of a charge under section 87. An offence under section 87 is not easy to establish involving as it does the proof of such mental elements as " wilfulness " and " intention to evade tax ". Those elements have to be proved largely by circumstantial evidence. The prosecution is under a duty to place before the Court facts which lead necessarily to the inference that the accused committed the act alleged with the requisite mental element. The difficulty of proof is no reason for relaxing in a proceeding under section 87 the obligation that lies on the prosecution in all criminal cases.

On a perusal of the documents produced by the appellant I am unable to escape the conclusion that the taxing officers were endeavouring to intimidate the appellant into submission by threatening each time to raise his assessment. The materials relating to the charges have all been obtained from the appellant's books and information furnished by him. Each of his income tax returns contained statements of accounts certified by an approved accountant. Having taken a certain view of his remuneration for supervising the contracts passed on to the Terrazzo Tile Works, Ltd., he kept his accounts in accordance with that view. The system of book-keeping adopted by an assessee does not bind the taxing authorities and an assessee cannot escape tax by adopting a particular method of book-keeping. But he cannot be punished for taking a view of his income which does not accord with that taken by the taxing authorities.

By his conduct the appellant appears to have invited the suspicion of the revenue officers. He seems to have exploited the modern device of the same group of leading members forming separate limited liability companies for carrying on each different branch of their business activities in order to escape the rigour of ever-mounting taxation on income and profits. He was managing director of Terrazzo Tile Works, Ltd. He was managing director of John Chellappah & Co., Ltd. John Chellappah & Co., Ltd., were agents and secretaries for Terrazzo Tile Works, Ltd. His contract business he carried on under his personal name. He assigned contracts to Terrazzo Tile Works, Ltd., and obtained a share of the profits. Documents P 63A, P 63B, and P 63C show that the activities of the appellant as an individual, the Terrazzo Tile Works, Ltd., and John Chellappah & Co., Ltd., were so closely knitted as to appear as the activities of one person. The result is that he has been subjected to the peril of this prosecution.

The appeal is allowed and the accused is acquitted on all the charges.

Appeal allowed.