THE ELEMENT OF INCOME TAX IN DAMAGES AWARDS FOR PERSONAL INJURIES*

Where a plaintiff is awarded damages for his loss of earnings, should he receive the amount of his gross income or his income after tax? Surely this is a basic question, and one would expect to have found it answered well before 1933—the date of the first reported case on the point.[1] This served as a stimulus to lawyers' minds and cases concerning the point have featured regularly in the Law Reports ever since. Until *British Transport Commission* v. *Gourley*[2] the cases were virtually unanimous that tax was not to be considered in the damages award and that compensation was to be made on the basis of gross income.[3] *Gourley* held otherwise, raising a host of problems that have exercised the minds of judges, practitioners and academics ever since. The decision of the House of Lords has generally been applied,[4] but with the recent decision of the Supreme Court of Canada[5] rejecting the rule, it is opportune to consider the question *de novo*.

In *Gourley's* case the problem was raised in an extreme form. The plaintiff was a highly successful professional man, and his gross loss of earnings for the short time relevant was calculated to be £37,720. But the marginal rate of income tax on Gourley's earnings was 19/- in the £1, so that his after tax loss was a mere £6,695. "Faced by this remarkable illustration of the effects of modern taxation it is hardly surprising that the House felt impelled to decide on the lower figure."[6] The rule has

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* This is a shortened version of a research paper presented by the writer for the LL.M. degree. Sections on the policy considerations and suggestions for reform have been omitted.

1. *Fairholme* v. *Thomas Firth & John Brown Ltd.* (1933) 49 T.L.R. 470.
2. [1956] A.C. 185, H.L.
3. The cases were *Fairholme* v. *Thomas Firth & John Brown Ltd.*, supra n. 1, *Jordan* v. *The Limmer & Trinidad Lake Ashphalt Co. Ltd.* [1946] K.B. 356, *Billingham* v. *Hughes* [1949] 1 K.B. 643, C.A., *Union Steam Ship Co. of N.Z. Ltd.* v. *Ramstad* [1950] N.Z.L.R. 716, C.A., *Fine* v. *Toronto Transportation Commission* [1946] 1 D.L.R. 221, *Bowers* v. *Hollinger* [1946] 4 D.L.R. 186, *McDaid* v. *Clyde Navigation Trustees* 1946 S.C. 462, *Blackwood* v. *Andre* 1947 S.C. 333. The odd-man-out is *McDaid* where Lord Sorn proceeded on the basis that there were no cases on the point. He was plainly in error, but it may be doubted, having regard to the reasoning used, whether knowledge of the previous cases would have made any difference to his decision.
4. The *Gourley* rule is accepted in New Zealand (*Smith* v. *Wellington Woollen Manufacturing Co. Ltd.* [1956] N.Z.L.R. 491, C.A.), Australia (see, for instance, *Black* v. *Mount & Hancock* [1965] S.A.S.R. 167) so far as s. 26 (j) of the Income Tax Assessment Act 1936 does not apply, South Africa (*Pitt*, v. *Economic Insurance Co. Ltd.* 1957 (3) S.A. 284), and Scotland (*Spencer* v. *MacMillan's Trustees* 1958 S.C. 300).
5. *R.* v. *Jennings* (1966) 57 D.L.R. (2d) 644.
6. Lord Justice Clerk Thomson in *Spencer* v. *MacMillan's Trustees*, supra n. 4, at 315. The English Law Reform Committee took much the same view—7th Report, "Effect of Tax Liability on Damages" (1958, Cmnd 501), para. 10.

been accepted by many writers as "impeccable" in law, while others have attacked it on grounds of "equity and practicability."[7] If the rule is found wanting in any of these three respects then there are, it is submitted, grounds for reform of the law.

However, even if such grounds are made out, it should be realised that the only likely method of reform is by the legislature. Despite the fact that the Supreme Court of Canada has chosen to refuse to follow *Gourley*,[8] the New Zealand courts are faced with decisions of the House of Lords and our own Court of Appeal. In the writer's view these authorities will not be departed from in New Zealand unless the House of Lords first alters its own decision. In *Australian Consolidated Press Ltd.* v. *Uren*[9] the Judicial Committee permitted a Commonwealth Court to refuse to follow the House of Lords subject to two conditions: (a) it concerns a matter "considerably . . . of domestic or internal significance",[10] and (b) where the question is "whether the law as it had been settled . . . should be changed to fit with the House of Lords."[11] While the former may be present in the instant matter, the latter certainly is not.

The present study is concerned only with damages for personal injuries. However, it is appropriate to note that the rule has penetrated all types of damages that are measured by reference to income.[12] Equally, the court does not apply the rule where, by the nature of the award, calculation of compensation is made on an after-tax basis.[13]

THE RULE IN LAW

Although there is no express mention of them in *Gourley's* case, there are apparently two pre-conditions to the application of the rule. These conditions may be stated thus:

7. See, for instance, "Notes & Comments" (1956) 30 A.L.J. 90, McGregor, *Mayne and McGregor on Damages* (12th Ed., 1961) para. 268, Street, *Principles of the Law of Damages* (1962) p. 98, and Vineburg, "Case and Comment" (1956) 34 Can. Bar Rev. 940 at 943.
8. Supra n. 5.
9. [1967] 3 W.L.R. 1338 at 1356 et seq., followed by McGregor J. in *Fogg* v. *McKnight* [1968] N.Z.L.R. 330.
10. Ibid. at 1356.
11. Ibid. at 1358.
12. It has been applied in: libel (*Rubber Improvement Ltd.* v. *Daily Telegraph Ltd.* [1964] A.C. 234), sterilisation of minerals (*Thomas McGhie & Sons Ltd.* v. *British Transport Commission* [1963] 1 Q.B. 125), breach of contract (*Julien Praet et Cie, S.A.* v. *H. G. Poland Ltd.* [1962] 1 Ll.R. 566), compulsory purchase (*West Suffolk C.C.* v. *W. Rought Ltd.* [1957] A.C. 403 (H.L.)), wrongful dismissal (*Parsons* v. *B.N.M. Laboratories Ltd.* [1964] 1 Q.B. 95 (C.A.)), capitalisation of pension payments (*In re Houghton Main Colliery Co. Ltd.* [1956] 1 W.L.R. 1219), and trespass (*Hall & Co. Ltd.* v. *Pearlberg* [1956] 1 W.L.R. 244). Not followed in *Spencer* v. *McMillan's Trustees*, supra n. 4, on the facts.
13. See *Lincoln* v. *Gravil* (1954) 94 C.L.R. 430, 442 (Deaths by Accident Compensation Act 1952) and *Head* v. *Hart* [1961] N.Z.L.R. 872 (Workers' Compensation Act 1956, and see Land and Income Tax Act 1954 s. 86 (1) (v)). It may be that if workers' compensation was on the basis of an insurance scheme, the deductions from wages made for premiums would be within the *Gourley* rule—see *Cooper* v. *Firth Brown Ltd.* [1963] 1 W.L.R. 418.

(i) the sums for the loss of which the damages awarded constitute compensation would have been subject to tax;

(ii) the damages awarded would not themselves be subject to tax.[14]

At first glance there appears to be a paradox. To satisfy the first condition the damages are assumed to be income receipts while for the second condition they are capital.[15] With respect, there is really no paradox. One must always distinguish between the nature of the damages and their measure.[16] There would only be a paradox if both pre-conditions referred to measure of the damages or to nature of the damages; in fact the first condition concerns measure, and the second nature. Further, the "paradox" assumes that all capital payments are non-taxable, and all income receipts taxable—this is obviously untrue.[17]

The same sort of reasoning that gave rise to the above argument led to the interesting decision of Donovan J. in *Herring* v. *British Transport Commission*.[18] There the learned judge was awarding damages for loss of profits on the use of one of a fleet of trucks. The damages were based on the excess of receipts over running costs. It was held that there should be no allowance for income tax on the damages since tax is payable only on the "profits of a business", and the profits on one truck are therefore not themselves taxed but simply constitute an element in the final balance sheet, any profit shown in which will be taxed.[19]

It would appear that *Herring's* case was wrongly decided for three reasons. First, the profit that would have been made on the truck would have gone into the profit and loss account and would have been taxed there. On the other hand, the award of damages (since it is *ex hypothesi* not taxable) will not go into the profit and loss account and will not be subject to taxation. Hence, if the *Gourley* rule is not applied the plaintiff

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14. Formulated thus in *Mayne and McGregor on Damages*, supra n. 7, para. 264. The formulation of pre-condition (i) is not accurate as far as damages for personal injuries are concerned. Damages are awarded for loss of earning capacity and not earnings, though they are measured by reference to loss of earnings. This is discussed below.

    It may not be true to say these are universal pre-conditions having regard to *Stewart* v. *Glentaggart Ltd.* 1963 S.C. 300.

15. The argument is developed at length by Jolowicz in "Damages and Income Tax" [1959] C.L.J. 86 at 91-93, and is referred to by Sellers L.J. in *Parsons* v. *B.N.M. Laboratories Ltd.*, supra n. 12, at 119 (dissenting).

16. *Glenboig Union Fireclay Co. Ltd.* v. *C.I.R.* 1921 S.C. 400 & 1922 S.C. (H.L.) 112, 12 T.C. 427.

17. This argument is developed by Tucker, "Damages—Income Tax—A Miracle of Alchemy?" [1959] C.L.J. 185.

    The paradox referred to by Street, supra n. 7 at 88-90 is not that maintained by Jolowicz. Street's paradox involves the simultaneous decision by the court that (a) damages are non-taxable and capital, and (b) damages are exclusively for loss of earnings. This would indeed be a paradox, for (b) means that the damages are of an "income nature", and thus there can, *ex hypothesi* never be these two conditions existing simultaneously in the same set of circumstances.

18. [1958] T.R. 401. Not followed in *Thomas McGhie & Sons Ltd.* v. *British Transport Commission*, supra n. 12.

19. A broadly similar argument was used in *George Thompson & Co. Ltd.* v. *C.I.R.* (1927) 12 T.C. 1091.

will be over-compensated. It would appear to be a vintage *Gourley* situation. Secondly, the learned judge's rationale would apply equally where a plaintiff is injured and is put off work temporarily and happens to be employed in several jobs over the income year. He, like the plaintiff Herring, is not taxed on each individual job: he becomes liable to tax as he derives income, and the tax he finally pays is on the excess of income over deductible expenditure taken over the whole income year. It would scarcely be suggested that the *Gourley* rule should not apply to the plaintiff with two jobs. Thirdly, there is arguably no difference in substance between one of two trucks, nine of ten trucks, ninety-nine of one hundred trucks, and the one and only truck being put out of commission.[20] Of course there *is* a difference between the first three situations and the fourth, but that difference is arguably not one which should give rise to the large difference in quantum of the damages which will usually occur with company tax running at over 40%.

Are the Damages Taxable?

The *Gourley* rule depends upon the damages not being taxable. If they are taxable then a short perusal of the case will show that there is no justification for an application of the rule.[21] Hence, if damages for loss of earnings are income the *Gourley* rule will not apply, for an application of the "hole" test which is considered below would render the damages taxable. If the damages are income, then the *Gourley* rule should not apply, for, even though the Revenue does not in fact collect tax on the damages, its refusal is truly a *res inter alios acta*—it is not for the courts to enforce this sort of *jus tertii* in this way. It is true that a court could adopt Lord Sorn's approach:

> . . . it was said, correctly enough, that in paying an award based on gross wages the defenders would not be paying more than they would have to have had to pay in any case. The resulting benefit to the pursuer, it was said, was not due to the award but rather to the absence of power on the part of the Inland Revenue to collect tax upon it. It was, so to speak, a present subsequently made to the pursuer out of the public purse and something with which the court had no concern—a kind of *res inter alios acta*. This line of reasoning is, however, too refined for me, and I think that, so long as the existing law is to the effect that jury awards are immune from tax, that is something which the court must be deemed to know at the time the award is made and something of which notice ought then to be taken.[22]

20. This raises the old substance versus form argument; compare *I.R.C.* v. *Blott* [1921] 2 A.C. 171 (substance) with *I.R.C.* v. *Duke of Westminster* [1936] A.C. 1 (form). No useful purpose can be served by pursuing the argument further here; judges use whichever approach they consider necessary and appropriate to reach the "right" conclusion in the circumstances.
21. This is subject to *Stewart* v. *Glentaggart Ltd.*, supra n. 14.
22. *McDaid* v. *Clyde Navigation Trustees*, supra n. 3, at 464 f. Read "inclination" for "power" and "practice" for "law" and the statement could be applied to the circumstances presently under consideration.

However, in addition to what has been said above, it should be noted that there is a very great difference between taking notice of the legal situation and taking notice of a decision not to enforce the law, and it is submitted that in the latter situation a court should and would be unlikely to take such notice.[23]

Are, then, the damages for loss of earnings or earning capacity? Through the years, two tests in particular have been used to assist in deciding whether a particular payment or receipt is capital or income. While these are by no means the only tests they are helpful starting-points. The first test is that of Lord Clyde in the *Glenboig Union Fireclay Co. Ltd.* v. *C.I.R.*:[24] if there is injurious affection to a capital asset in such a way as to constitute a "sterilisation" of that asset, then the damages to compensate for that constitute a capital receipt even though it may be measured by income flow. In the context of personal injuries it would be necessary to establish that the injury is in fact to a capital asset and that the injury is such that it can be classified as "sterilisation". The second test is that of Lord Clyde also, enunciated in *Burmah Steam Ship Co. Ltd.* v. *C.I.R.*:[25] where the injury complained of is inflicted on the plaintiff's trading, then damages awarded therefor go to fill a "hole" in the plaintiff's profits and the damages could not in accordance with the principles of sound commercial accounting be put into any account but the profit and loss account (and vice versa). This test presents some difficulty in the present context, and it may be applicable only to commercial enterprises. It should be realised that neither of these tests provides an answer. The "hole" test directs attention to the site of the injury, while the "sterilisation" test directs attention to the degree and effects of the injury. In the context of the "hole" test it is helpful to note that Lord Clyde, in the course of his dictum, compared breach of a charter party with loss of a ship and held the former to be income and the latter capital.

There are three sets of situations to be looked at in the capital/income question: pre-trial and post-trial loss, temporary and permanent loss, and injury to the income earning entity (the human body).

(a) *Pre-trial and Post-trial Loss.*

It has been suggested that there is an income loss in respect of special damages where the plaintiff is permanently injured.[26] On the

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23. Mandamus will not issue to compel the Commissioner of Inland Revenue to collect tax legally due since the Commissioner is an agent of the Crown. Further, it is relevant that the scheme of the Act involves discretion in many areas, and so the only ground available would be misconstruction of the Act. However, liability to tax is imposed by the charging provisions of the tax Act (*Reckitt & Colman (N.Z.) Ltd.* v. *Taxation Board of Review* [1966] N.Z.L.R. 1032 at 1045) so that there would be jurisdiction for the Supreme Court to issue a declaration to the effect that tax is due on the damages award. The Commissioner would presumably comply with such a declaration.
24. Supra n. 16, 1921 S.C. at 406 and 12 T.C. at 448 f.
25. 1931 S.C. 156 at 159 f; 16 T.C. at 71 f.
26. *Billingham* v. *Hughes*, supra n. 3, at 651. See also Jolowicz, supra n. 15.

other hand, there is authority to the effect that the loss is a capital one[27] and this would appear to be the better view.

In the first place, it is submitted that there can be no distinction between pre-trial and post-trial loss. The New Zealand Court of Appeal in *Ramstad's* case[28] refused to distinguish the two situations, as did the Manitoba Queen's Bench in *Soltys* v. *Middup Moving and Storage Ltd.*[29] In both of these cases the loss was held to be capital. Only in *Graham* v. *Baker*[30] have the reasons for this been set out, and they are convincing:

> A plaintiff's right of action is complete at the time when his injuries are sustained and if it were possible in the ordinary course of things to obtain an assessment of his damages immediately it would be necessary to make an assessment of the probable economic loss which would result from his injuries. But . . . it has been found convenient to assess an injured plaintiff's loss by reference to the actual loss of wages which occurs to the time of trial and which can be more or less precisely ascertained and then, having regard to the plaintiff's proved condition at the time of trial, to attempt some assessment of his future loss.[31]

The source of the damage in either case is the same; any distinction is more apparent than real, brought about by the "convenient" division into past and future loss. It would be a very strange result indeed if the taxability of damages was to depend upon an accident of litigation and the crowding of fixture lists.

While it is clear that there is no distinction between pre-trial and post-trial loss there remains the question whether these two losses are capital or income, the answer to which depends on the following paragraphs.

(b) *Permanent and temporary loss.*

It is probably sufficient to say that the great weight of authority is in favour of permanent loss being capital. Indeed, in every case where the *Gourley* rule is applied this must be conceded or the court must so hold, even though the point often passes *sub silentio*. Jolowicz[32] claims that the "weight" of authority is to the effect that the loss is income, and

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27. *Groves* v. *United Pacific Transport Pty. Ltd.* [1965] Qd.R. 62 at 65. Among the doubters are Judson J. in *R.* v. *Jennings*, supra n. 5, at 655 ("the result might well be different").
28. Supra n. 3, at 728.
29. (1963) 41 D.L.R. (2d) 576 at 582.
30. (1961) 106 C.L.R. 340.
31. Ibid. at 346 f. There is also some discussion in *Fletcher* v. *Autocar & Transporters Ltd.* [1968] 2 Q.B. 322, 344, C.A.
32. Supra n. 15 at 94 f. The learned author finds clear authority in one case, indirect authority in another and from the wording of s. 2 (1) of the Law Reform (Personal Injuries) Act 1948.

Bale[33] suggests that there is support in *Gourley's* case itself for its being income. However, with the exception of these views there is unanimity for the proposition that it is capital.[34] If, as is suggested, permanent loss is capital, then pre-trial loss in such a case will also be capital.

Temporary loss is a rather vexing question. The leading case is *London and Thames Haven Oil Wharves Ltd.* v. *Attwooll*.[35] There a jetty owned by the Oil Co. was damaged and put out of use for 380 days. The matter was settled out of court and the Oil Co. was paid an amount for loss of use. Later the Revenue sought to have the damages taxed. In addition to the loss of use, the plaintiff had been required to repair the damage done to the jetty. The Court of Appeal's reasoning may be summarised thus:

(1) the cause of action is injury to the plaintiff;
(2) here there is a twofold injury: damage to the jetty necessitating repairs, and loss of use of the jetty;
(3) the two losses are independent and their taxability can be considered separately, there is no "whole and indivisible" loss;
(4) the damages here are for loss of use involving the failure to receive money from users of the jetty;
(5) had the jetty been usable, receipts for use would have gone into the profit and loss account;
(6) temporary loss is to be distinguished from permanent loss which is a capital loss because it involves abandonment of that part of the trade, involving use of that capital asset, exploitation of which will no longer form part of the profits.

The court also rejected the argument that because the capital asset (the jetty) was physically harmed that harm was the true cause of action. It is submitted that the *London and Thames Haven* case is wrongly decided in that the fact that the jetty was physically harmed did, indeed, render the injury a capital one in entirety. Further, the case has no application to damages awards for personal injuries.

33. Bale, "*British Transport Commission* v. *Gourley*, Reconsidered" (1966) 44 Can. Bar Rev. 66, n. 20. This is, however, a doubtful reading of the case. There is no more than the use of the phrase "loss of earnings" several times in the case, and this is balanced by the number of times "loss of earning capacity" is used. If the case shows anything on this subject it is that the two phrases are used interchangeably. In order to avoid this problem the phrase "earning loss" will be used in this study where it is intended not to indicate capital nature or income nature.
34. Support is contained in *Renfrew Town Council* v. *C.I.R.* 1934 S.C. 468 at 473, 19 T.C. 13 at 19; *Billingham* v. *Hughes*, supra n. 2 at 651; *Soltys* v. *Middup Moving and Storage Ltd.*, supra n. 29, at 582; *R.* v. *Jennings*, supra n. 5 at 655, 656; *Teubner* v. *Humble* (1962-63) 108 C.L.R. 491 at 506, 509; *Groves* v. *United Pacific Transport Pty. Ltd.*, supra n. 27, at 65. And see Vineburg, supra n. 7, at 945; 1st minority of Law Reform Committee, supra n. 6, para. 8; *Mayne & McGregor on Damages*, supra n. 7, para. 269; Street, supra n. 7, at 92. Samuels, "Gourley Revisited and Rejected" (1967) 30 M.L.R. 83 at 84 takes a different view, apparently he accepts that it is capital but attacks the distinction between capital and income.
35. [1967] Ch. 772. In *Renfrew Town Council* v. *C.I.R.*, supra n. 34, at 473 & 19 respectively there are dicta to similar effect. Neither case is one of personal injuries.

First, its application to personal injuries. This is based on the twin cases of *Watson* v. *Powles*[36] and *Fletcher* v. *Autocar and Transporters Ltd.*[37] In the former case Lord Denning M.R. said:

> There is only one cause of action for personal injuries, not several causes of action for the several items. The award of damages is, therefore, an award of one figure only, a composite figure, made up of several parts. . . . At the end all the parts must be brought together to give fair compensation for the injuries.[38]

The reason for this is the chance of "overlapping" of the items which is discussed at length in the *Fletcher* case. Admittedly, the judge may still isolate a sum for "loss of earnings" as was done in *Fletcher's* case,[39] but the figure so set out merely represents "a fair way of dealing with the possibility". If, then, there is but one cause of action and one "sum" of damages, how can the reasoning used in the *London and Thames Haven* case have any application to personal injuries at all? Further, if only one sum is awarded and is not broken down (as in the case of jury awards), how can one part of the undivided sum be income and taxable when the rest is not?

While the *London and Thames Haven* case may not apply to personal injuries, the reasoning of that case sheds some light. The physical harm argument clearly has some relevance to personal injuries, but it fits more conveniently into the third set of situations mentioned above.

(c) *Injury to income earning entity.*

In the *London and Thames Haven* case, counsel for the jetty owners conceded that if the jetty had not been damaged but that the oil tanker had gone aground in such a place as to prevent the jetty being used "a different result might be arrived at".[40] This requires consideration of whether a certain injury impairs a capacity to earn, or merely prevents that earning of income. Obviously, where the capital item is lost or destroyed there is an impairing of capacity to earn—the income earning entity itself is injured. On the other hand, where there is no such injury but use of the still available capacity is prevented then there is an injury only to income. The essential point is that, for it to be capital, the prevention from earning must flow from the injury to the entity, and the damages must be paid for that injury together with its foreseeable consequences. Three examples will show what is meant: (a) tanker collides with the jetty, damaging it, and the jetty has to be closed to repair the damage; (b) tanker collides with the jetty, then, in moving away from the jetty, goes aground preventing the jetty from being used;

36. [1968] 1 Q.B. 596 C.A.
37. Supra n. 31. Both this case and *Watson* are discussed in Walker, "Damages and the Court of Appeal" (1968) 112 Sol.Jo. 164 and noted at (1968) 31 M.L.R. 462.
38. Supra n. 36, at 603.
39. Supra n. 31, at 338 (Lord Denning M.R.) and 349 (Diplock L.J.).
40. Supra n. 35, at 811 f.

(c) tanker goes aground in manoeuvring off the jetty preventing the jetty from being used. It is only in case (a) and so much of (b) as it takes to repair the jetty that there is a capital loss. It is difficult to see any difference between the nature of damages for loss of use where a capital item is lost and where it is merely temporarily "lost". In both cases the measure of damages is based on the time lapse before the plaintiff can be put back in the position he was in before the accident, either by purchase of a new item or "purchase" of the repaired item. Willmer L.J. would appear to be in error when he stated:

> It seems to me that it would be strange if the quality of the damages recovered for loss of use should be held to depend upon the accidental circumstance whether or not there happened also to be physical injury to the jetty.[41]

The physical injury to the jetty is of the very essence of the matter. It is a simple application of normal principles to look first to what happened at the accident. In every case there is a three tier enquiry: (a) what happened at the accident and who is liable? (b) what are the foreseeable consequences of the accident? (c) what is the measure of damages to be awarded in respect of those consequences? In the *London and Thames Haven* case the answers to these enquiries are: (a) defendant's ship struck and damaged the jetty through the defendant's servant's negligence; (b) jetty was damaged and had to be closed during repair; (c) cost of repair and loss of profit respectively. The loss of profit flows from the temporary "sterilisation" of the pier. It is intimately connected therewith and should be viewed as one with it. This is especially so for personal injuries. On the other hand, when there is no "sterilisation" of the pier in the sense of physical injury, there is nothing for the loss of use to be linked with, and the loss is genuinely one of income.

What has been said readily applies to personal injuries. The conclusion may be stated as follows: in the case of temporary "earning loss"[42] damages will be of a capital nature where there has been an injury to the human body, the repair or consequence of injury of which involves the plaintiff's incapacity to earn. On this basis both pre-trial and post-trial loss are capital payments.

It would therefore appear that damages for earning loss are capital payments where there is actual injury to the income earning entity whether the injury causes permanent or temporary earning loss. Nevertheless it must be born in mind that there has been no case establishing that the damages are capital. The question must therefore be regarded as open.

If the damages are capital, then the second pre-condition to the operation of the rule is present. As to the first pre-condition, the measure of the damages is the actual and prospective loss of income, and it becomes necessary to consider the legal justification for using after tax loss rather than gross loss as the measure.

41. Ibid. at 812.
42. See n. 33 supra.

Damages as Compensation

British Transport Commission v. *Gourley*[43] is ultimately based on the proposition that damages are compensatory and not punitive. The court's task is to ascertain as accurately as possible what sum will be necessary to compensate the plaintiff for his loss. In doing so the courts prefer to err on the side of being too low, rather than over-compensating:

> The plaintiff may in certain circumstances receive less than an indemnity, but . . . he should not in general receive more.[44]

It is, of course, sound that damages should provide an indemnity, but that in itself takes the enquiry nowhere; as Donovan L.J. has noted:

> Recognition of this truth does not, however, get one very far. Is it, for example, "punishment" if one asks the defendant to make good the loss he has inflicted without taking into account receipts which the labour, or the thrift and foresight, of the plaintiff alone have secured? Again, the question: "What has he lost?" is not a question the answer to which solves all problems and determines the amount of damages, for one has first to consider the principles upon which the "loss" is to be computed.[45]

To speak simply and with feeling of "punishment" and "unwarranted benefits" is to evaluate the issue.[46] One must isolate the general principles of damages and see how they apply to the situation, and, if necessary, make alterations to fit into the concepts of loss distribution and social justice.

What, then, is the loss for which the plaintiff is to be indemnified? Here it is only earning loss. There are three possible approaches. First, one may ask "What difference did the commission of the act complained of make to the plaintiff?" Secondly, one may ask "What receipts has the plaintiff lost as a result of the injury?" Thirdly, "What is the plaintiff's nett loss after making allowance for expenses necessarily incurred in gaining his income?"

The first approach may be dubbed the "Reid approach", for it was concisely put by that Law Lord in *Gourley's* case where his answer was usable income or income after tax:

> . . . if the respondent had earned the additional sum of £15,220 he would only have benefited from that to the extent of £4,945

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43. Supra n. 2.
44. *Shearman* v. *Folland* [1950] 2 K.B. 43 at 49 (a case on the collateral source rule). This was echoed by Sir Andrew Clark Q.C., counsel for the appellant Commission in *Gourley's* case [1956] A.C. at 188.
45. Dissenting in *Browning* v. *War Office* [1963] 1 Q.B. 750, 763, C.A.
46. See, for instance, Sellers L.J. (*dissentiente*) in *Parsons* v. *B.N.M. Laboratories Ltd.* supra n. 12, at 112. The question is put in focus by Peter Mason in "Damages and Income Tax" (1957) 4 Bus. Law Rev. 242, 252: one has an "uneasy feeling" that *Gourley* makes the strong stronger and the weak weaker, "but is the existence of such an uneasy feeling a good reason for altering the basis on which the computation of damages is made?" See also *Browning* v. *War Office*, supra n. 45, per Diplock L.J. at 764 f.

> because he would have had to pay the rest in tax. £4,945 represents his real loss. . .[47]

However, one must look further than this. If the plaintiff is over-compensated then he may have no means of making good the deficit:

> . . . in assessing a just and fair compensation the purpose is not to attempt by means of money completely to insure that the plaintiff will be placed for the rest of his life in the same position as if he had not sustained his injuries. A full compensation must nevertheless be awarded. It is a compensation once and for all.[48]

In making this compensation once and for all the court awards "full" compensation, endeavouring neither to over nor under-compensate more than is avoidable. In *Gourley's* case the choice between gross and after-tax loss was easily made. If a gross amount had been awarded the damages would be far greater than any imaginable "loss" that the plaintiff might sustain, although it may be asked whether a severely injured plaintiff should not receive such an over-compensation. However, in the case of a worker whose effective rate of tax is about 15c in the $1 the position is not nearly so clear. Increases in the plaintiff's real loss regularly occur, especially where the plaintiff is only partially incapacitated and where the injury may conceivably worsen. Indeed, one can foresee a worsening of injury increasing earning loss by 10% which would make gross loss the more accurate measure; but one cannot foresee the 160% worsening that would have made gross loss the more accurate measure for Gourley. Of course, awards always make allowances for such worsening and, further, under the *Fletcher* case,[49] a round figure is now to be awarded which bears no relationship to strict actuarial calculations. The defect in the Lord Reid approach is that it distracts from the estimatory nature of calculating damages by implying that accurate assessments can be made.[50]

The Lord Reid approach has the ring of validity. If the aim of the damages award is compensation, then one is automatically directed to the plaintiff's loss. But there is a further difficulty inherent in the approach. Lord Reid speaks of the amount by which Gourley would have been "benefited" had he continued to work. If this is to be the test, then very real difficulties arise, especially in connexion with the collateral source rule. The following enquiry becomes necessary: what are the

47. *British Transport Commission* v. *Gourley*, supra n. 2, at 211. See also Singleton L. J. in *Billingham* v. *Hughes*, supra n. 3, at 652—a variation on the same theme. It should be noticed that the Lords in *Gourley's* case allowed that no "calculation" of future loss can be precisely accurate arithmetically—Earl Jowitt [1956] A.C. at 203 f., Lord Goddard at 208, and Lord Reid at 211.
48. *Pamment* v. *Pawelski* (1949) 79 C.L.R. 406 at 410 f.
49. Supra n. 31.
50. See the lengths gone to for the sake of accuracy in *Stewart* v. *Glentaggart Ltd.*, supra n. 14, and *Rakena* v. *Richardson & Co. Ltd.* [1968] N.Z.L.R. 915, C.A. Presumably *Rakena* will be followed throughout New Zealand in cases of special damages. As McGregor J. said at 920, it is not applicable to general damages; however, it does indicate the view of the Court of Appeal that exact compensation is the aim.

needs of the plaintiff and his dependants in his injured state judged by the standard of comfortable living in terms of his previous life? and what are his hopes and likelihood of future income? The amount of the plaintiff's true loss and the amount by which he would have "benefited" is the difference between these two amounts. What justification is there for stopping at income tax and certain living expenses?[51] Difficulty of ascertainment may be suggested, but since a broad assessment of damages is all that is necessary, then these difficulties largely disappear. It may be that the traditional method of calculating damages is on a receipts less expenses basis and not on the Lord Reid basis. However, it remains true to say that the Lord Reid approach is more consistent with the aim of compensation and that stopping short at tax may be justified on the grounds that it gives a reasonable approximation—provided that the *Gourley* rule is in fact treated as providing an approximation only.

The second suggested approach is unacceptable. It was adopted in two cases before *Gourley*[52] and rejected in that case. Suffice it to say that it was rightly rejected; it bears no relationship to practice, and, indeed, could scarcely have been used in the cases where it was adopted since it would involve completely ignoring expenses incurred in gaining the receipts.[53] To adopt this approach is to lose sight of the compensatory object of the damages.

The third approach is based on normal principles; if one is concerned with loss of profits then the measure is gross receipts less expenses necessarily incurred in gaining those receipts. This is the meaning attributed to "profit" in certain tax fields.[54] Income tax, the argument goes, is not an expense necessarily incurred in the production of income but is a "disposition of earnings—however involuntary".[55] If receipts less expenses is the true measure of damages, then the *Gourley* rule cannot be justified on the grounds of legal logic, though it may be justified on other grounds. But it seems to be impossible to determine whether the right approach is that of Lord Reid or this third one. Both may be supported with cogent though brief arguments; both fit into the general pattern of the law; both in the long run become matters of

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51. See *Shearman* v. *Folland*, supra n. 44.

52. *Billingham* v. *Hughes*, supra n. 3, at 648 f, and *Jordan* v. *The Limmer & Trinidad Lake Asphalt Co. Ltd.*, supra n. 3, at 359.

53. For instance, the doctor in *Billingham* v. *Hughes* would have to pay rent, a receptionist, equipment, and so on, some at least of which must have been relevant to the assessment of loss.

54. For instance, the question whether a payment of "interest" is really a distribution of profits—see *British Sugar Manufacturers Ltd.* v. *Harris* [1938] 2 K.B. 220 and *Commissioner of Taxation* v. *Boulder Perseverance Ltd.* (1937) 58 C.L.R. 223.

55. Vineburg, supra n. 7, at 947. See also *R.* v. *Jennings*, supra n. 5, at 656.

attitude. One may take up an attitude and defend it, but one is not driven inexorably by the force of logic to one or the other.[56]

THE PRACTICAL EFFECT OF THE RULE

Since considerations of the legal logic are not coercive of a conclusion on the validity or desirability of the rule in *British Transport Commission* v. *Gourley* the practical consequences of the decision must be considered. It is no answer to the presence of practical difficulties to say with Earl Jowitt:

> I cannot think that the risk of confusion arising if the tax position be taken into consideration should make us hesitate to apply the rule of law if we can ascertain what that rule is.[57]

The practical arguments that will be considered here are: tax complexities in assessing damages, changes in tax rates and structure in the future, possible changes of income pattern and exemptions of the plaintiff, possible changes of residence by the plaintiff with attendant changes in his tax payments, the problem of income slicing, and the question of after-tax equalisation. Other arguments have been omitted from this article.

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56. There are other quasi-logical arguments which can be dealt with shortly. First, long usage (used in *Fairholme* v. *Thomas Firth & John Brown Ltd.*, supra n. 1, and *Jordan* v. *The Limmer & Trinidad Lake Ashphalt Co. Ltd.*, supra n. 3) is no sound reason for rejecting a principle that is valid, and change of which will not seriously disrupt commercial arrangements. This, of course, leaves open the question of *Gourley's* validity. Secondly, it has been said that since income tax is an annual tax, one is usurping the function of Parliament in deducting an amount for tax from a damages award notionally covering a number of years ahead. This argument was used by Lord Keith in *Gourley* [1956] A.C. at 217 f. This would appear to be at least as invalid as an argument that the courts are usurping the function of the Almighty in assuming a certain life span for the plaintiff. In *R.* v. *Jennings*, supra n. 5, at 656, Judson J. laid stress on a "tax policy" of allowing an injured plaintiff the benefit of his gross earning loss:

> It is not open to the defendant to complain about this consequence of tax policy and the courts should not transfer this benefit to the defendant or his insurance company.

This line of reasoning had been refuted earlier by Lord Sorn in *McDaid* v. *Clyde Navigation Trustees*, supra n. 3, at 464 f. By implication, the New Zealand courts have agreed with Lord Sorn. It is doubtful whether the courts would construe even an express exemption from tax as ousting the *Gourley* rule: see *Stewart* v. *Glentaggart Ltd.*, supra n. 14; cf. the American position concerning s. 104 (a) (21) of the Internal Revenue Code 1954 shown in *LeRoy* v. *Sabena Belgian World Airlines* (1965) 344 F. 2d. 266, though some cases have held otherwise (*Floyd* v. *Fruit Industries Ltd.* (1957) 63 A.L.R. 2d. 1378 (S.C.Conn.)).

57. [1956] A.C. at 202 f. This line is echoed by the Law Reform Committee, supra n. 6, at para. 13, and by MacGillivray J.A. in *Jennings* v. *Cronsberry* (1965) 50 D.L.R. (2d) 385 (affirmed by the Supreme Court of Canada sub. nom, *R.* v. *Jennings*, supra n. 5) at 416. Some U.S. courts take the view that there are more than merely practical difficulties in the way of assessment of the incidence of taxation, and that it is really far too conjectural to be considered—see *Stokes* v. *U.S.* (1944) 144 F. 2d. 82, *Southern Pacific Co.* v. *Guthrie*, (1951) 186 F. 2d. 926, 928. Others have opposed this on the ground that it is no more conjectural than any other matters that have to be considered in damages for personal injuries—see *Floyd* v. *Fruit Industries Ltd.*, supra n. 56, 1390.

Tax Complexities in Assessing Damages

With *Gourley's* case, "the assessment of damages", it is said, "comes to depend on questions of tax law which may be quite complex".[58] This was present in the mind of Earl Jowitt at least in the *Gourley* case, and that Law Lord's solution was to assess the incidence of damages on broad principles, and that no calculation should be made to arrive at an exact figure[59]—that is, presumably, when the judge himself is assessing the damages. However, small differences in one year make large ones over forty, and, unless the *Fletcher* case[60] is used liberally, there could be regular examples of gross under- or over-compensation arising from such broad assessments.

Generally these difficulties will not be complexities of tax law but rather factual questions that are difficult to ascertain or predict. There may be, in a small minority of cases (those where the plaintiff is self-employed), questions of deductions, but the main complexity is the capital/income question.[61] Even this complexity may be more apparent than real as a practical matter if the approach of Turner J. in *George Court & Sons Ltd.* v. *Mair & Co. (Importers) Ltd.*[62] is adopted. If it is adopted, the position would appear to be as follows: damages will be assessed on the gross income less costs basis unless the Commissioner of Inland Revenue makes known his attitude, or the Commissioner is a party to the proceedings, or, one may add, the parties agree that the *Gourley* rule applies.[63]

The third is most common, the second never occurs, and the first is something that the defendant may bring into operation if he so wishes.[64] On the assumption that the above approach is adopted as a general rule,

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58. Bale, supra n. 33, at 68. See for a detailing of the various tax problems involved the "Notes and Comments" in (1956) 30 A.L.J. 90.

59. [1956] A.C. at 203. Earl Jowitt's injunction may not have been followed generally. The high-water mark of exact calculations may not even have been reached with *Rakena* v. *Richardson & Co. Ltd.*, supra n. 50. When an Inter-Departmental Committee discussed the question just after *Gourley* was decided, the conclusion was that there should be no legislation. This was arrived at on the basis that tax would only be assessed by the courts in a rough and ready way. The Inland Revenue will not make an accurate assessment for a defendant.

60. Supra n. 31.

61. Considered supra "Are the Damages Taxable?".

62. [1958] N.Z.L.R. 494.

63. Ibid. at 496. Turner J. was in error when he said that the Revenue's attitude was ascertained in *Gourley's case*. There it was a matter of concession that the damages would not be taxed. In *West Suffolk C.C.* v. *W. Rought Ltd.*, supra n. 12, the Revenue's attitude was ascertained.

64. The Inland Revenue readily make available their opinion on whether tax is assessable on whatever damages may be awarded. Such opinion is given to both parties to the case.

the question of whether the damages were capital or income would arise but once—in the first case to which the Commissioner was a party.[65]

Some difficulties of deductions, and perhaps one or two other questions, may still arise, but scarcely often enough to make them a valid objection to the rule.

Alterations of Tax Rates

In estimating the incidence of tax it is not to be assumed that the tax rates may change[66] or that there may be an alteration in the tax structure such as a change in the balance between direct and indirect taxes. There is, of course, no difficulty with special damage awards which are based on the known past rates.[67] However, it has been strongly contended that, whatever the justification for this assumption in the short term, there is no justification in the long run.[68] Peter Mason[69] supports this line and asserts that any significant variation of rates or structures will leave the plaintiff "suffering financially for no reason other than a

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65. The question of onus of proof is discussed at length in Bale, supra n. 33 at 80 to 85. The position would appear to be as follows: it is for the plaintiff to prove his gross and net incomes (*West Suffolk C.C.* v. *W. Rought Ltd.*, supra n. 12, at 413 f.), including any special exemptions or the likelihood of tax saving devices (*McDaid* v. *Clyde Navigation Trustees*, supra n. 3, at 466), while it is for the defendant to establish that the *Gourley* rule applies (*George Court & Sons Ltd.* v. *Mair & Co. (Importers) Ltd.*, supra n. 62, at 496, *Jennings* v. *Cronsberry*, supra n. 57 at 419 f.). *Hall & Co. Ltd.* v. *Pearlberg*, supra n. 12, can be disregarded in this respect, since it was decided only by the Official Referee and then only with hesitation and uncertainty. Upon the defendant's motion the court may order disclosure of particulars of the plaintiff's tax position—*Phipps* v. *Orthodox Unit Trusts Ltd.* [1958] 1 Q.B. 314.

66. See Lord Goddard's model jury direction in [1956] A.C. at 209. The point recently was raised quite acutely in New Zealand. In the 1968 Budget it was announced that revision of tax rates and exemptions would be made commencing on the 1st April, 1969. Now that the appropriate legislation has been passed (the Land and Income Tax (No. 2) Act 1968) it is likely that the courts will calculate the incidence of taxation on the new figures, but up till the passing of the Act the position was rather difficult. Were the courts to take account of the new rates or not? To be realistic the courts should have taken the new rates into consideration, but in the face of Lord Goddard's injunction they may have felt they could not. One experienced Wellington barrister takes the view that the courts will take no cognizance of the new rates until they become effective.

67. *British Transport Commission* v. *Gourley*, supra n. 2, at 208 per Lord Goddard.

68. Bale, supra n. 33, at 85 f.

69. Peter Mason, supra n. 46, at 246.

court's bad guess". One may ask whether that writer is not overlooking the other possibilities. If the court assumes that rates will go up, then the plaintiff loses if they remain constant or go down. If the court assumes that they will remain constant, then the plaintiff loses if they go down and gains if they go up. If the court assumes that they will go down, then the plaintiff will gain if they remain constant or go up. Thus the ideal of compensation is more closely served by assuming that rates and structures will remain constant; the difference that would be made to the plaintiff by any change would be minimised.

There are, however, two further planes at which the assumption of unchanging rates may be justified. First, there is no way of foretelling whether rates will go up or down. There may have been election promises, but these are not sacrosanct; there may have been a Taxation Review Committee, but governments are notorious for shelving reports; tax rates may currently be too high or too low, but can a court say so? This last leads on to the second plane. A prediction of a change in rates involves the courts in commenting on government's present and future policies—a role which the courts are extremely, and possibly wisely, reluctant to undertake. Should or could a court state *ex cathedra* that the government for the time being is taxing too highly, or that it should lower taxation rates? There seems to be no alternative to the assumption of continuing the existing tax rates.

Structure presents a slightly different picture, but even there it would obviously be unrealistic for a court to assume a change in structure unless the manner of that change had already been elaborated and the change itself decided upon.

Unearned Income

The presence of unearned income presents another problem. In *Gourley's* case Lord Goddard divided such income into permanent (e.g. annuities) which may be assumed to continue, and temporary (e.g. shares) which are likely of their nature to be disposed of, and of which little or no notice need be taken.[70] This analysis has been used in at least one subsequent case.[71] Lord Goddard did not mean that the "permanent" income was to be assumed to continue, but merely that "temporary" income could be ignored and that attention should focus on whether the plaintiff can establish that he intended or intends to use the "permanent"

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70. [1956] A.C. at 209.

71. *Beach* v. *Read Corrugated Cases Ltd.* [1956] 1 W.L.R. 807.

income for income-splitting purposes.[72] The question whether the plaintiff will enter into income tax avoidance schemes presents no real difficulty of ascertainment; it is eminently a jury question of the type decided every day. It is, however, yet another consideration made necessary by the decision in *Gourley's* case.

The same applies to the question of a wife's income which may have some effect through the "wife's exemption" and through aggregation and partnership provisions.[73] This aspect has always been recognised.[74]

Difficulties in Actual Assessment

The question of exemptions under the Land and Income Tax Act 1954 raises as many problems as a dragon's teeth. Little more can be done at this point than to mention the difficulties and note one possible solution.

Peter Mason has suggested[75] that it is to be assumed that the plaintiff's current exemptions are to continue, and that it is for the plaintiff to establish that they will increase and for the defendant to establish that they will go down. The initial assumption is sensible and merely reflects the normal legal position where there is no evidence on a point. It is the question of proof that raises the difficulties. Does the test refer to likely changes had the plaintiff not been injured, or to likely changes in his injured condition? If a nineteen-year-old is injured and paralysed, can the court assess damages on the basis that he would marry at age 23, have three children $1\frac{1}{2}$, 3 and 5 years after marriage, but with a deduction of 24% for the chance of not marrying? Can the plaintiff adduce evidence that he believes in large families? Can the defendant adduce evidence that the plaintiff believes in working mothers? The list could be lengthened as far as ingenuity will run.

One solution is to look only to the national averages and existing fact and refuse evidence of personal intention. Like the presumption that the tax rates will remain steady, this is a blunt instrument, but it does minimise the effect of its inaccuracy and it avoids far-ranging, long, and possibly embarrassing inquiries into personal intent.

In fact the New Zealand courts avoid all these difficulties by adopting a most simple and blunt process. Nett income figures for the pre-accident period are adopted and simply continued into the future for the remainder of the plaintiff's "expected" working life on 4%

72. Ibid. This onus has been described as "not great"—Bale, supra n. 33, at 94. The majority of the Law Reform Committee, supra n. 6, compared "real possibility" with "mere existence of the possibility", which also suggests a relatively light burden. So long as it remains light the risk of under-compensation is somewhat reduced.
73. As to the former see s. 81 of the Land and Income Tax Act 1954, and as to the latter see ss. 10 and 104 of the same Act.
74. *British Transport Commission* v. *Gourley*, supra n. 2, at 208 per Lord Goddard. See also *Smith* v. *Wellington Woollen Manufacturing Co. Ltd.*, supra n. 4, at 499.
75. Peter Mason, "Taxation Computation in Claims for Damages" (1956) 106 L.J. 564.

tables.[76] No allowance is made for any changing circumstances of personal life as suggested above.[77] No account is taken of the statistical man—the plaintiff is dealt with as he is. The only enquiry into future occurrences seems to be where employment conditions such as overtime have changed before or after the accident. In such a case counsel adduce evidence as to the likelihood of change in the future.

It will be seen that this process vastly simplifies application of the *Gourley* rule; but in doing so it leaves the ideal of compensation far behind, and emphasises the nature of an award as a guess. The courts would appear to have avoided the practical difficulties of the *Gourley* rule by the simple expedient of ignoring them. However, the whole tenor of the opinion of McGregor J. in *Rakena* v. *Richardson & Co. Ltd.*[78] is such that the current practice for general damages may have to be altered.

Slicing of Income

One of the most thorny problems arising from the decision in *Gourley's* case is the question of slicing. Where the plaintiff's award does not represent his only income, the tax to be deducted from the award may be calculated in three ways: (a) by ignoring the other income and treating the award as being the only income (bottom slicing), (b) by adding the other income to the award, ascertaining the tax on the combined total, and distributing that tax between award and other income *pro rata* (middle slicing), (c) by fiinding the tax on the other income, the tax on the combined total income, and subtracting the former from the latter (top slicing).

The principle of compensation seems to indicate that the top slicing method should be used,[79] but there is some authority for the other methods. Support for middle slicing comes from *In re Houghton Main Colliery Co. Ltd.*[80] This case was not one of personal injuries, but involved the issue of whether tax which would have been paid on instalments of pensions should be taken into consideration when the pensions were capitalised on the liquidation of the employing company. Wynn-Parry J. held that it should be considered. He did not go on to assess the actual amount to be deducted, preferring to let the accountants settle that, but he did imply that there was no need to slice the income:

76. A typical example of the sort of calculation made would be this for a 21-year-old male:

nett earnings prior to accident	$51.32 per week
nett earnings at current employment	$26.84
expected working life	41 years
loss of income	$24.49 per week
present value of loss on 4% tables	$25,962.

This is calculated simply by multiplying the weekly loss by the number of weeks in 41 years, and allowing for 4% compound interest.

77. Any changes in the personal life of the plaintiff that take place before trial are taken into consideration—e.g. if he marries.
78. Supra n. 50.
79. See Vineburg, supra n. 7, at 948 f where an example is used to demonstrate this.
80. Supra n. 12 at 1225.

> . . . it cannot be said that it represents the top slice, or for that matter the bottom slice, of his income; the only effect of making the calculation . . . will be that his income for the relevant period must be treated as larger than in fact it was.[81]

This dictum would have the effect of middle slicing the workers' pension, and for this reason Bale[82] contends that the case was wrongly decided on this point. However, it is by no means clear that Wynn-Parry J. contemplated middle slicing. He did not assess the actual quantum, and the words used can be fitted into top slicing—even though the judge disclaimed any need for slicing.

The case impliedly supporting bottom slicing is *Bold* v. *Brough, Nicholson and Hall Ltd.*[83] which concerned ss. 38 and 39 of the Finance Act 1960 (U.K.) which taxes payments on termination of employment but exempts the first £5,000. Phillimore J. there took the view that *Gourley* applied to the first £5,000 of the damages for wrongful dismissal, but that the £5,000 was to be treated as if it was the only income of the plaintiff.

There is therefore some support for middle or bottom slicing, but the likelihood of the techniques being used is remote for these are the only cases supporting them and the trend in fact seems to be away.[84] Bottom and middle slicing do help to ensure that the plaintiff is not under-compensated and to minimise any under-compensation, but it is rather a "back-door" way of achieving it.

After-Tax Equalisation

The guiding ideal in the *Gourley* case was that of compensation; the plaintiff is to be compensated for his after-tax loss since that most closely approximates his "actual" loss. It arguably follows from this, that, even where tax is due on the damages, it is the duty of the court to ensure that the plaintiff receives no more than this after-tax loss.

One immediately runs up against the two pre-conditions to the operation of the rule in *Gourley's* case, for if the award is taxable in some way then the second pre-condition would seem to be infringed.[85] In the two cases[86] that have adopted the approach indicated above, the second pre-condition was once ignored and once held to be not true in the form in which it has been stated in this study. Where there is clearly no tax then *Gourley* obviously applies, and where there is a real doubt as to whether tax is due or not then there is some authority for the rule not being applied,[87] but the situation here concerned is where there is

81. Ibid.
82. Supra n. 33, at 95 n.
83. [1964] 1 W.L.R. 201.
84. See *Rakena* v. *Richardson & Co. Ltd.*, supra n. 50. Special damages are, however, distinguishable from general.
85. For the pre conditions see supra para. 4.
86. *"Tantalus" (Master & Crew)* v. *"Telemachus", her Cargo and Freight (Owners)* [1957] P. 47 and *Stewart* v. *Glentaggart Ltd.*, supra n. 14.
87. *Spencer* v. *MacMillan's Trustees*, supra n. 4, per Lord Patrick. See also *Hall & Co. Ltd.* v. *Pearlberg*, supra n. 12, at 248.

clearly tax due on the award but it is not such as would have been deducted under the *Gourley* rule. It was in the *Telemachus*[88] that the pre-conditions were ignored. There Willmer J. took the view that tax was in all circumstances to be considered in making awards, and held that salvage awards should be increased to allow for tax that would have to be paid by the salvors. With respect, this is in error. Quite apart from the fact that it flies in the face of the second pre-condition, it ignores the basic inapplicability of the *Gourley* principle to salvage awards. Salvage awards are awards for services rendered, almost a *quantum meruit,* while damages for earning loss are in substitution for a capacity to earn which is measured by actual or prospective loss of earnings. It is arguably natural to take tax into account in the latter situation, but that situation is clearly distinguishable, and there is, indeed, no similar rationale for considering tax in the way Willmer J. did. There has been no support for Willmer J.'s view.[89]

Stewart v. *Glentaggart Ltd.*[90] presents greater difficulties. There is an attraction in Lord Hunter's carrying the compensation principle so far; there is, as has been said, support for it in the recent Court of Appeal case of *Rakena* v. *Richardson & Co. Ltd.*[91] Lord Hunter criticised the two pre-conditions on the ground that they do not appear directly from either *Gourley's* case or the *Rought* case,[92] and on the ground that the over-riding principle of compensation demands that the judge achieve an "after-tax" equalisation by precise calculation, balancing what the uninjured plaintiff would have received after tax against the amount the injured plaintiff will receive in compensation after tax and reaching an exact equality. It is submitted that *Rakena* v. *Richardson & Co. Ltd.* may be distinguished from *Stewart's* case upon the grounds that it does not really concern the same point, and that anyway it was dealing with pre-trial loss. It is further submitted that the English Court of Appeal was right when it doubted and refused to follow *Stewart's* case, regarding it as out of touch with the "rough and ready" assessment prescribed in *Gourley* as well as for practical reasons,[93] and it would not be followed in New Zealand.

It would appear from the above consideration that some at least of the supposed practical difficulties in the *Gourley* rule are not really difficulties at all. However, it is equally plain that at the very least each adds another factor to be considered by judge or jury. Some of them

88. Supra n. 86.
89. *The Telemachus* is criticised in *Island Tug & Barge Ltd.* v. *"S.S. Makedonia" (Owners)* [1958] 1 Q.B. 365 and *The Frisia* [1960] 1 Ll.R. 90, per Hodson L.J. at 94 (there Willmer L.J. at 95 impliedly adhered to his earlier opinion). The case was differed from (though not expressly) in *Julien Praet et Cie S.A.* v. *H. G. Poland Ltd.*, supra n. 12. It is further trenchantly criticised in Hall, "Taxation of Compensation For Loss of Income" (1957) 73 L.Q.R. 212 at 219 f.
90. Supra n. 14.
91. Supra n. 50.
92. Supra n. 12.
93. *Parsons* v. *B.N.M. Laboratories Ltd.*, supra n. 12, per Sellers L.J. at 115 et seq. and Pearson L.J. at 137 et seq.; Harman L.J. did not mention the point.

will require time for argument and, if there is a jury, for direction. A few of them pose real difficulties both in the realm of being argued and considered and in the realm of ascertaining what is to be done about them for a start. It is suggested that the least of these problems are straws in the wind, indicating that there may well be an easier and a better way of dealing with the problem of the measure of damages for earning loss, while the greater of them are genuine arguments against the validity or advisability of having the *Gourley* rule at all.

SUMMARY

The rule in *British Transport Commission* v. *Gourley* is a much-assailed principle, apparently with good reason. However, its defects are not so obvious that it is indefensible. The criticisms made of it on legal grounds may be answered by taking a different though equally justifiable postulate. On balance, it is submitted that the arguments against the rule are slightly weightier than those in favour, but this stems largely from the writer's taking the second possible postulate. Further, in the practical application of the rule there can be seen to be several difficulties that cast doubt on the rule. If a rule is difficult to apply, and doubtful in law, then there are grounds for its reversal.

It is submitted that the difficulties of the *Gourley* decision may be more apparent than real when it comes to future earning loss. All the difficulties are arguably eliminated by the twin decisions in *Fletcher* v. *Autocar and Transporters Ltd.*[94] and *Watson* v. *Powles.*[95] If the heads of damage are not independent but simply guides to a "fair" compensation, then under-compensation on that head does not matter; the only under-compensation that matters is in the final figure. Furthermore, when it comes to assessment of each head as a guide, the enquiry is not one for an exact figure, but rather a broad assessment. An approximate, a very approximate, figure of the plaintiff's tax liability is sufficient; this is all that was intended in the *Gourley* case itself, it is an enquiry well within the scope of a jury's deliberations.

G. D. S. TAYLOR.

94. Supra n. 31.
95. Supra n. 36.