1946
June 11
1948
April 27

BETWEEN:

EDWARD V. FLINN.....APPELLANT;

AND

MINISTER OF NATIONAL REVENUE..RESPONDENT

Revenue—Income Tax—Income War Tax Act, R.S.C. 1927, c. 97, ss. 3 (1), 12 (1), 58—Income—Taxable income—Dividends are taxable income of the taxpayer in the year in which they are paid—Dividend notes issued by a company in December 1944 for the amount of a dividend and payable in December 1964 are not taxable income until they are paid as they constitute a mere acknowledgment of debt by the company and a claim in favour of the holder of the dividend note—Appeal allowed.

In December 1944 U.S. Corp. Ltd. declared a dividend but postponed payment thereof for a period of 20 years and, as evidence of the right to receive such dividend, issued dividend notes for the amount thereof payable on December 15, 1964, or on such earlier date as in the note provided.

Appellant, a shareholder who received one dividend note for the sum of $47.25, was assessed for income tax thereon for the year 1944. The assessment was affirmed by the Minister and appellant appealed to this Court.

Held: That the dividend note for $47.25 dated December 22, 1944, payable on December 15, 1964, or on such earlier date as in the note provided, received by appellant from the Company, is not "interest, dividends or profits" received from "stocks" during the year 1944.

2. That it will only acquire that quality when it is paid. *Association Insulation Products Ltd.* v. *Golder* (1944) 1 A.E.R. 533; (1944) 2 A.E.R. 203 followed and applied.

3. That presently it merely constitutes an acknowledgment of debt in so far as the Company is concerned and a claim with regard to the appellant.

1948

FLINN
v.
MINISTER OF
NATIONAL
REVENUE

Angers J.

APPEAL under the provisions of the Income War Tax Act.

The appeal was heard before the Honourable Mr. Justice Angers at Halifax.

C. B. Smith, K.C. and *G. S. Cowan* for appellant.

W. C. Dunlop, K.C. and *A. A. McGrory* for respondent.

The facts and questions of law raised are stated in the reasons for judgment.

ANGERS J. now (April 27, 1948) delivered the following judgment:

This is an appeal under sections 58 and following of the Income War Tax Act by Edward V. Flinn, of the Town of Dartmouth, Province of Nova Scotia, against the assessment with regard to income for the year 1944, which appears from the copy of the notice of assessment, included in the file of the Department of National Revenue transmitted by the Minister to the Registrar of the Exchequer Court, to have been mailed on July 21, 1945.

In his notice of appeal dated August 8, 1945, a copy whereof forms part of the record of the Department, the appellant says in substance:

the appellant is an accountant in the employ of Wagner Tours Limited, a body corporate having its head office at Halifax, in the county of Halifax;

in December 1944 he was the holder of 30 shares of the 7 per cent cumulative preference shares of five dollars each in the capital of United Service Corporation Limited, a body corporate with head office at Halifax;

in December 1944 United Service Corporation Limited, being in arrears in respect of the dividends on the said shares, declared a dividend of 31½ cents in respect thereof, but by the provisions of the resolution declaring this dividend postponed the payment thereof for a period of 20 years and, as evidence of the right to receive such dividend, issued dividend notes for the amount of such dividend payable on December 15, 1964, but subject to previous redemption as in the notes provided;

as holder of the said 30 shares the appellant received one of such dividend notes for the sum of $47.25, together with

1948

FLINN v. MINISTER OF NATIONAL REVENUE

Angers J.

a letter from the president of the company outlining the steps taken in connection with the declaration of the said dividend and the issuance of the said notes;

annexed to the notice of appeal are copies of the following documents: (*a*) agreement dated December 9, 1944, between United Service Corporation Limited and Fred C. Manning, one of the holders of the said preference shares acting on behalf of himself and all other holders of said shares; (*b*) resolution of the Board of Directors of the said company passed on December 9, 1944; (*c*) the dividend note received by appellant; (*d*) the letter from the president of the company received by appellant;

the appellant desires to appeal from the said assessment only insofar as the sum of $47.25 has been determined by the Deputy Minister of National Revenue for taxation to be a part of the taxable income of the appellant and insofar as the appellant has been assessed in respect of taxation thereon in the sum of $16.50;

the appellant's reasons for appeal are as follows:

section 12 of the Income War Tax Act specifically provides that dividends shall be taxable income of the taxpayer in the year in which they are paid or distributed and inferentially they are not taxable in any other year;

the said dividend notes are not income within the meaning of any provision of the Income War Tax Act until paid;

the said dividend notes are merely evidence of the right to receive the dividend on the date on which by the terms of the declaration thereof such dividend is payable;

it has been the settled practice of the Minister of National Revenue not to treat the receipt of evidence of indebtedness as receipt of the indebtedness itself and in this regard the appellant craves leave to refer to the rulings of the Minister of National Revenue or the Deputy Minister for taxation in connection with the overdue interest on bonds of Abitibi Power and Paper Company.

The agreement between United Service Corporation Limited and Fred C. Manning, acting on behalf of himself and all other holders of preference shares in the capital stock of the company, after reciting that the capital of the company is divided into 150,000 7 per cent cumulative

preference shares of the par value of $5 each and 35,000 common shares without nominal or par value, that all the preference shares are issued and paid up, that dividends in respect of the preference shares are undeclared and in arrears for the period of four and one half years, that the amount of the said dividends has been earned through the operations of the company, but that it is considered inexpedient to deplete the working capital of the company by the payment of such dividends forthwith, that upon the execution of this agreement the directors of the company propose to declare dividends upon the preference shares in respect of the period of four and one half years, payable in accordance with the terms of certain notes of the company to be issued, that Fred C. Manning is the holder of two of the said preference shares and is contracting on behalf of himself and all other holders of preference shares, that by clause 64 of the articles of association of the company it is provided that if at any time the share capital of the company, by reason of the issue of preference shares or otherwise, is divided into different classes of shares, all or any of the rights and privileges attached to any such class may be modified, commuted, abrogated or otherwise dealt with by agreement between the company and any person purporting to contract on behalf of that class, provided such agreement is ratified in writing by the holders of at least three-fourths in number of the issued shares of the class or by a resolution passed and confirmed at extraordinary general meetings of the holders of such shares, stipulates as follows:

1. THAT the said Fred C. Manning agrees to and with the Company and for and on behalf of himself and all other holders of Preference Shares in the Capital Stock of the Company that if, as and when the Directors of the Company declare dividends upon and in respect of the said Preference Shares in respect of the said period of four and one-half years, for which the said dividends are presently in arrears, the said dividends to be payable according to the terms of, and at the times and in the manner specified in notes of the Company hereinafter described, the said holders of the said Preference Shares, and each of them, will accept postponement of the payment of the said dividends according to the terms, at the time or times, and in the manner specified in the said notes.

2. THAT the said notes referred to in paragraph one hereof, if, as and when issued, shall be unsecured notes of the Company, shall be payable December 15, 1964, unless sooner called for redemption in accordance with the terms thereof, shall bear interest at the rate of 4 per cent

1948

FLINN
v.
MINISTER OF NATIONAL REVENUE

Angers J.

on the principal amount thereof payable half-yearly on the 15th days of June and December in each year until paid, shall be callable for redemption by the Company in whole or in part on any interest date at 102 per cent of the principal amount thereof on thirty days notice to the registered owners thereof, shall be subject to the right of the Company from time to time to purchase all or any of the said notes at prices not exceeding 102 per cent of the principal amount thereof, together with accrued interest, (any notes called for redemption or purchased by the Company to be forthwith cancelled) and shall be registered in the name of the holder thereof from time to time.

3. THAT this Agreement and everything herein contained shall enure to the benefit of and be binding upon the parties hereto and their respective heirs, executors, administrators, successors, and assigns.

Annexed to this agreement is a ratification reading as follows:

WE, the undersigned holders of Preference Shares in the Capital Stock of UNITED SERVICE CORPORATION LIMITED, hereby ratify, sanction and confirm the attached agreement dated the "9th" day of December, A.D. 1944, made between the said Company and Fred C. Manning on behalf of himself and all other holders of Preference Shares in the Capital Stock of the said Company, and we hereby agree with the said Company and with each other to be bound by its terms.

This ratification bears the signature of a large number of shareholders with, opposite their names, the number of preference shares held by each of them.

A certified copy of this agreement was filed as Exhibit 4.

The resolution mentioned in the notice of appeal, after stating that the 7 per cent cumulative preferential dividend on the preference shares in the capital stock of the company is in arrears in respect of a period of four and one half years, that the holders of 75 per cent in number of the said shares have ratified an agreement dated December 9, 1944, between the company and Fred C. Manning, acting on behalf of himself and all other holders of the said preference shares, whereby the holders of the preference shares agree, in the event of the declaration of said dividend, to the postponement of the payment thereof in accordance with the terms of the notes therein and hereinafter referred to, concludes thus:

BE IT THEREFORE RESOLVED that the Directors do hereby declare a dividend in respect of the outstanding preference shares in the capital stock of the Company of thirty-one and one-half per centum (31½ per cent) of the par value thereof, being the amount of the arrears of the said dividend at the rate of 7 per cent for the period of four and one-half years, payable to the holders of the said Preference Shares of record as of the 15th day of December, A.D. 1944, according to the terms

of and at the time or times and in the manner specified in the form of note, a draft of which is attached hereto and initialled by the President of the Company for purposes of identification.

BE IT FURTHER RESOLVED that this Company do issue and deliver on or before the 30th day of December, A.D. 1944, to the holders of the said Preference Shares of record as of the 15th day of December, A.D. 1944, its notes in the form of the aforesaid draft as evidence of the rights of the said holders to the aforesaid dividend to which they may respectively be entitled and in the principal amounts of the said dividend to which they may respectively be entitled, and that the President or the Vice-President and the Secretary or the Assistant-Secretary of this Company be and they are hereby authorized from time to time to execute on behalf of this Company and affix the Corporate Seal of this Company to the said notes, and to do any and all matters and things and execute any and all documents necessary or useful for carrying into effect this resolution.

A certified copy of an extract from the minutes of a Directors' meeting of United Service Corporation Limited held on December 9, 1944, containing the said resolution, was filed as Exhibit 5.

The note received by the appellant, a copy of which is annexed to the notice of appeal, is in the following terms:

No. 33 *UNITED SERVICE CORPORATION LIMITED* $47.25

NOTE

UNITED SERVICE CORPORATION LIMITED, hereinafter called "the Company", will on the 15th day of December, A.D. 1964, or on such earlier date as the principal monies of this note become payable in accordance with the conditions endorsed hereon, pay to Edward V. Flinn of Dartmouth, N.S. or other registered holder for the time being, the sum of Forty-Seven Dollars and Twenty-Five Cents of lawful money of the Dominion of Canada.

The Company will pay to such registered holder interest on the said sum from the date hereof at the rate of four per centum per annum, until this note is paid, by half-yearly payments on the 15th days of June and December in each year, the first of such half-yearly payments to be made on the 15th day of June, 1945.

This note is issued subject to, and with the benefit of, the conditions endorsed hereon which are deemed to be a part of it.

GIVEN UNDER THE CORPORATE SEAL OF United Service Corporation Limited, this 22nd day of December A.D. 1944.

(Sgd.) F. C. Manning, President
George C. Thompson, Assistant Secretary

A certified copy of this note was marked as Exhibit 6.

Attached to the note in question is a document entitled "Conditions", the only provisions whereof offering any interest in the present case read thus:

1. This note is one of a series of Notes payable on the 15th day of December in the year 1964, bearing interest at the rate of 4 per centum per annum.

1948

FLINN
v.
MINISTER OF NATIONAL REVENUE

Angers J.

8. The notes of this series shall be callable for redemption by the Company in whole or in part on any interest payment date at 102 per cent of the principal amount thereof on thirty days notice to the registered holders thereof. In the event that the Company calls for redemption less than the whole of the outstanding notes, the notes to be so redeemed shall be determined by drawing lots, such drawing to be made by a person or persons appointed by the Board of Directors of the Company in such manner as may be determined by the Board. The said notes shall be subject to the right of the Company from time to time to purchase all or any of the said notes at prices not exceeding 102 per cent of the principal amount thereof, together with accrued interest to the date of purchase. Any and all notes redeemed or purchased by the Company as aforesaid shall be forthwith cancelled.

The letter of the president of United Service Corporation Limited to the preference shareholders of the company dated December 23, 1944, a copy whereof is attached to the notice of appeal, explains fully the circumstances in which the dividend note, with which we are concerned, was issued and the conditions of payment thereof. I believe it proper to quote the letter *in extenso*:

Dear Shareholder:

Your Directors have had under consideration for some time the question of payment of the arrears of dividends on the Preferred Shares of the Company in order that the Preference Dividend might be placed on a current basis. Dividends at the rate of 7 per cent per annum have been paid since 1936 but no progress has been made in paying the dividends which were passed for the four and one-half years preceding 1936. Having in mind the plans of the company for post-war expenditures your Directors have felt it inadvisable to reduce the current position of the company by the payment of these arrears at the present time.

On December 9, 1944, Mr. F. C. Manning, acting on behalf of himself and all the other preference shareholders, entered into an Agreement with the company whereby the Preference Shareholders agreed, on declaration of dividends in the amount of the arrears, to postponement of the payment thereof in accordance with the terms of 20-year notes for the amount to be issued by the Company. This agreement was ratified by the holders of more than 75 per cent of the outstanding Preference Shares of the Company and under the articles of association of the company this agreement is therefore binding on all Preference shareholders.

Following the making of the above Agreement the Directors on the 15th day of December, 1944, declared dividends on the Preference Shares covering the arrears and postponing the payment thereof in accordance with the terms of the note which is enclosed.

These notes are payable in twenty years on December 15, 1964, bear interest at 4 per cent per annum and are redeemable by the Company prior to the maturity date in accordance with the conditions endorsed on the note.

In the opinion of counsel for the company under existing legislation delivery of this note to you does not constitute payment of a dividend and is, therefore, not taxable income when the note is received; but when

the note is redeemed by the company, the amount paid will be taxable income in the hands of the registered holder of the note. Interest on this note when paid by the Company constitutes taxable income.

Yours very truly,

(Sgd.) Fred C. Manning
President

UNITED SERVICE CORPORATION LTD.

A certified copy of this letter was produced as Exhibit 7:

A copy of the memorandum and articles of association of United Service Corporation Limited was filed as Exhibit 2. The only article which offers any interest in the present instance is number 64, a certified copy whereof was marked as Exhibit 3; it reads thus:

Modification of Rights of Shareholders

64. If at any time the share capital of the Company, by reason of the issue of preference shares or otherwise, is divided into different classes of shares, in pursuance of the provisions of the next preceding article or otherwise, all or any of the rights and privileges attached to any such class may be modified, altered, varied, affected, commuted, abrogated or otherwise dealt with by agreement between the Company and any person purporting to contract on behalf of that class, provided such agreement is ratified in writing by the holders of at least three-fourths in number of the issued shares of the class or by a resolution passed and confirmed by the same majority and in the same manner as a special resolution at extraordinary general meetings of the holders of shares of that class, and all the provisions hereinafter contained as to general meetings shall, *mutatis mutandis*, apply to every such meeting, but so that the quorum thereof shall be members holding, or representing by proxy, one-half in number of the issued shares of the class. This clause is not by implication to curtail the power of modification which the Company would have if this clause were omitted.

The question at issue is whether or not the dividend note of United Service Corporation Limited for $47.25 dated December 22, 1944, payable to the appellant on the 15th of December, 1964, or on such earlier date as the principal moneys of this note become payable in accordance with the conditions endorsed thereon, received by the appellant from the company, which on the date of the appellant's return of income for the year 1944 had not been paid constitutes an income. Income is defined in section 3 of the Act, the material part whereof reads as follows:

For the purposes of this Act, "income" means the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary, or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be whether derived

1948

FLINN
v.
MINISTER OF
NATIONAL
REVENUE

Angers J.

from sources within Canada or elsewhere; and shall include the interest, dividends or profits directly or indirectly received from money at interest upon any security or without security, or from stocks, or from any other investment, and, whether such gains or profits are divided or distributed or not, . . .

I have to determine if in 1944 the appellant received "interest, dividends or profits" from "stocks or from any other investment".

It is clear to me that the appellant during the year 1944 received only from United Service Corporation Limited note number 33, dated December 22, 1944, for $47.25, which is to mature on December 15, 1964, or on such earlier date "as the principal monies of this note become payable in accordance with the conditions hereon".

As submitted by counsel for appellant the time of payment of a dividend determines the year in which it is assessable to tax.

Subsection 1 of section 12 of the Act indeed enacts:

Dividends or shareholders' bonuses shall be taxable income of the taxpayer in the year in which they are paid or distributed.

The authors and the jurisprudence support the doctrine that it is the time of payment of a dividend which determines the year in which it is subject to assessment.

Plaxton and Varcoe, in their "Treatise on the Dominion Income Tax Law", second edition, make the following comments (p. 168):

Received and Accrued:—In considering this question of the method to determine profits it should be remarked that the Dominion Act imposes the charge simply upon the annual net profit or gain directly or indirectly "received", rather than earned or made, and this provision contemplates the determination of profits by the best accounting system applicable to the particular business in question, and the word "received" must be interpreted to mean "received" in a sense in which it would be used by a business man in referring to the profits of the year of assessment. In many cases it means "accrued" or "earned" so that profits earned, but not actually received or paid, should wherever a business is carried on be regarded as "received" for the purpose of assessment.

In the case of *St. Lucia Usines and Estates Company Ltd. and Colonial Treasurer of St. Lucia*, (1), the headnote, fairly accurate and comprehensive, reads thus:

In 1920 the appellants sold all their property in St. Lucia and ceased to reside or carry on business there. In 1921 interest upon the unpaid part of the purchase price was payable to them, but it was not paid. The appellants were liable to pay income tax for the year 1921 under the Income Tax Ordinance, 1910, of St. Lucia, only if the interest above mentioned was "income arising and accruing" to them in 1921:—

(1) (1924) A.C. 508.

1948

FLINN v. MINISTER OF NATIONAL REVENUE

Angers J.

Held, that though the interest was a debt accruing in 1921 it was not "income arising or accruing" in 1921, and that the appellants were not liable under the Ordinance to pay tax for that year.

Held, further, that the appellant not being liable to assessment at all for 1921, it was not material that by s. 25 of the Ordinance an assessment when entered in the list was to be "final and conclusive".

The following observation by Lord Wrenbury are pertinent and interesting (p. 512):

The words "arising or accruing" occur repeatedly in the Ordinance, e.g., in s. 4, sub-s. 1 (*a*) (*b*) (*c*) (*d*) and (*e*), coupled with the words "and derived from" or "or derived from". Sometimes the expression "derived from" is used alone, s. 5, sub-s. 1 (*a*) (*c*) (*g*) (i) and (ii). The respondent contends that the above interest "accrued" to the company in the year 1921, because it was payable in that year and none the less because it was not paid in that year. Their Lordships do not agree. The words "income arising or accruing" are not equivalent to the words "Debts arising or accruing". To give them that meaning is to ignore the word "income". The words mean "money arising or accruing by way of income". There must be a coming in to satisfy the word "income". This is a sense which is assisted or confirmed by the word "received" in the proviso at the end of s. 4, sub-s. 1. If the taxpayer be the holder of stock of a foreign Government carrying say 5 per cent interest, and the Government is that of a defaulting State which does not pay the interest, the taxpayer has neither received nor has there accrued to him any income in respect of that stock. A debt has accrued to him but income has not.

In re *Cross* v. *London and Provincial Trust, Limited,* (1), the Court of Appeal, affirming the judgment of Finlay, J., held that:

Where a debtor defaults and the appropriate income being money is not changed into something else but remains money which the debtor promises to pay at a later date, it cannot be said that the security has produced any income. The form of the funding bond was nothing but a promise to pay at a future date the interest in respect of which default had been made. The respondent company was not therefore assessable to income tax under Case IV. of Sch. D of the Income Tax Act, 1918, in respect thereof.

At page 796 we find the following relevant comments by Sir Wilfrid Greene, M.R.:

It is not open to question that income can be in the form of money's worth. Nor is it open to question that if the holder of a security, the contractual income from which is money, receives from the person liable to pay that money something of money's worth, namely goods, instead of the money, such goods are income arising from the security. Compare Scottish and Canadian General Investment Co., Ltd. *v.* Easson, (1922) 8 Tax Cas. 265, where debentures of a new company were received in place of interest due on bonds issued by an old company. On the other hand where there is a mere substitution of a promise to pay at a later date for the obligation to make an interest payment presently due, the owner of the security cannot be said to have received income from it. In such a case in truth that is exactly what has not happened, since the payment

(1) (1938) 1 K.B. 792.

1948

FLINN
v.
MINISTER OF NATIONAL REVENUE

Angers J.

has been postponed instead of being made on its due date. Nor do I see how it can make any difference if upon the true reading of the transaction the original obligation is extinguished and the promise to pay at a later date is accepted in its place. If the holder of a mortgage agrees to accept a post-dated cheque in lieu of interest which has accrued due, it would surely be a misuse of language to say that he had received income from the mortgage, and that notwithstanding the fact (which I will assume) that the post-dated cheque was a thing of money's worth. A question of this nature arose under the Indian Income Tax Act (XI. of 1922) in Commissioner of Income Tax, Bihar and Orissa *v.* Maharajadhiraja of Darbhanga, (1933) L.R. 60 I.A. 146, 161.

MacKinnon, L.J., expresses the same opinion (p. 803):

The essential nature of the transaction was that the debtor, avowing his inability to pay what had fallen due, gave instead his written promise to pay at a future date. He might just as well have given his own post-dated cheque. Or, still more simply, he might have written on each of the gold bond coupons a promise to pay it in twenty years, with interest annually until payment.

It is quite true that income may arise by the receipt of money's worth as well as by the receipt of money. And it is equally true that a debtor may pay his debt by giving the promise of a third party to pay; indeed the best form of payment in the world, Bank of England notes, if subjected to the unusual treatment of being read, will be found to be promises by a third party to pay. But I am satisfied that there can never be payment of his debt by a debtor by giving his own promise to pay at a future date. And I am equally satisfied that, though income arises to a creditor from a debtors' having his debt, income does not arise by the debtor's promising that he will pay his debt later on.

The same view was adopted in *Associated Insulation Products Ltd.* v. *Golder* (1).

In the first instance that was a decision of Macnaghten, J., later affirmed by the Court of Appeal (Scott and du Parcq, L.JJ., and Uthwatt, J.). The headnote relating to the judgment of Macnaghten, J., is thus worded (p. 533):

The appellant company was the beneficial owner of a number of shares in a corporation formed under the laws of the United States of America. On Dec. 15, 1936, the American corporation declared a dividend but by a further resolution provided that the distribution of the dividend should be in the form of a certificate of indebtedness to the shareholders payable on Jan. 1, 1940, with interest thereon at a fixed rate until payment. The appellant company contended that it was assessable to income tax in respect of this dividend in the year in which the dividend was declared:

Held: the company was assessable in respect of the dividend in the year in which it was actually paid.

In his judgment Macnaghten, J. makes the following observation (p. 534):

In the computation of the profits of a trade or business, debts due in respect of the trade or business must, no doubt, be included; but dividends are not assessable until they are received. Dividends payable in future are not assessable until they become payable *and are actually paid.*

(1) (1944) 1 A.E.R. 533 and (1944) 2 A.E.R. 203.

Counsel for appellant intimated that the facts in that case are very close to those in the case at bar, noting that the main difference is that the declaration of dividend in the latter was followed by the distribution of notes in compliance with the resolution, whilst in the former the American corporation, after declaring a dividend, provided by a further resolution that the distribution should be in the form of certificates of indebtedness. Counsel's submission that a promissory note is a certificate of indebtedness accompanied by a promise to pay at a later date is, in my opinion, well-founded.

In the Court of Appeal Scott, L.J. expressed this opinion (p. 203):

The only question which I think calls for any consideration is what was the substantial effect of the double resolution of the American company passed on Dec. 15, 1936, and of the similar one passed on Dec. 20, 1937. If those resolutions provided in reality for a distribution by way of dividend not of money but of money's worth, the income tax due in respect of it under case V would be not on the money figure of interest payable on each share, but on the market value of the certificates on the date of their distribution multiplied by the number of shares held. If, on the other hand, the reality of the transaction was the declaration of a money dividend payable not presently, but only on a future date, namely, Jan. 1, 1940, then it follows that till the due date arrived and payment was in fact received by the respondent company as shareholder, no income arose from its foreign possessions.

On the whole I think the latter is the true view of what was done. The first half of the double resolution expresses the real intention rather than the second. The certificates seem to me to have been intended as a consolation for postponement of payment, which would on the one hand assure a reasonable rate of interest during postponement, and on the other give some of the advantages of a security for an existing debt, *debitum in praesenti* though only *solvendum in futuro*: for they would have some—perhaps a high—market value.

du Parcq, L.J. made substantially similar observations (p. 204):

I cannot accept the suggestion put forward by the appellants that the decision in Cross's case (Cross *v.* London & Provincial Trust, Ltd., (1938) 1 K.B. 792) turned on the fact that the promise made under the funding plan was substituted for an earlier promise to pay interest. On the contrary, this court seems to me to have decided as it did, not because of, but rather in spite of, the fact that a new promise had been substituted for the earlier one. The Crown, as I read the report of the argument, was seeking to rely on that fact. The argument was that the old debt had gone, and that the bondholder had taken something marketable in its place. "The interest", it was said, "is discharged and money's worth takes its place". The argument for the subject was that a repeated promise to pay is no more equivalent to payment than the original promise. Promises are not payment. This latter argument prevailed and it was

1948

FLINN v. MINISTER OF NATIONAL REVENUE

Angers J.

held that, when all was said, the funding bond then in question was "nothing but a promise to pay at a future date the interest in respect of which default has been made": see the judgment of Sir Wilfrid Greene, M.R., at p. 800 (1938) 1 All E.R., at p. 433). If the words "in respect of which default has been made" are omitted from that statement, the logic of the proposition and the principle which it states are alike unaffected. To my mind, it is clear from the judgment of Sir Wilfrid Greene, M.R., read as a whole, that a post-dated cheque, or a promissory note, or a promise in the form of the "negotiable instrument" (as it is called) which we have before us in the present case, can never be regarded as "income arising from securities out of the United Kingdom" or (to quote the words now applicable to the case) as "income arising from possessions out of the United Kingdom". They are money's worth, no doubt, but they are not income.

Uthwatt, J. agreed with his colleagues and stated (p. 205):

> The material surrounding circumstances as found by the Commissioners are (i) that the corporation while having a fund of profits available for distribution had not the necessary cash in hand and were unwilling to borrow and that this was the reason for the issue of the certificates; (ii) that while neither resolution used the word "dividend", the circular which accompanied the second distribution records that the directors in their resolution relating to it "had declared a dividend of 16 per cent", and states that "the distribution of 16 per cent is not to be paid in cash but to be in the form of scrip . . . which is in the form of a certificate of indebtedness"; (iii) the accounts of the corporation refer to the two distributions as "dividends" and to the latter distribution as a dividend paid; debit the total amount of their "surplus" and enter the amount payable under the certificates on the liabilities side of the balance sheet along with current indebtedness, but do not treat the sum in terms as loan capital.
>
> To my mind the proper inference is that a distribution of profits as such was intended and made. The substance of the transaction, in my opinion, was the declaration of an ordinary dividend attracted by the stock, such dividend being payable at a future date, and the stockholders' rights in respect of the dividend being for convenience stated in a document which crystallized the position and made their rights conveniently marketable. Taking that view of the transaction, the first point taken by the company fails and upon the second point it follows that upon the authority of Cross' case ((1938) 1 K.B. 792) taxable income did not arise to the stockholders before the due date for payment under the certificates.

The case before me and that of *Associated Insulation Products Limited* v. *Golder* (supra) are very much alike. It would be difficult, I presume, to find two other cases showing so many points of similitude.

In the case of *Associated Insulation Products Limited* v. *Golder,* (supra) the resolution sets out that the Directors of the company have declared a dividend of 16 per cent and that its distribution will not be paid in cash, but in the form

1948

FLINN v. MINISTER OF NATIONAL REVENUE

Angers J.

of a scrip which is equivalent to a certificate of indebtedness, payable on a future date. In the matter now pending United Service Corporation Limited, which had on hand earnings, but not in the form of cash, and wished to pay to its shareholders the dividends in arrears, passed the resolution hereinabove related declaring a dividend payable twenty years later, save in certain contingencies which, by the way, did not materialize. Every condition required to be made in the Associated Insulation Products Limited case in order that a dividend should be paid in the year in which it was actually received and not the year in which the certificates were issued exists in the present case but, judging from the report of the Associated Insulation Products Limited case, the facts herein are more clearly established.

See also *Lambe* v. *Commissioners of Inland Revenue* (1).

There are no judgments of our Courts, as far as I know, in conflict with the decision of the Court of Appeal, which unanimously affirmed the judgment of Macnaghten, J. and I feel that it should be followed.

The balance sheet and the profit and loss statement (Exhibit 8) of United Service Corporation Limited for the year ending December 31, 1944, show the way in which the liability to the shareholders amounting to $236,250.17 was carried.

The same amount appears in the balance sheet and the profit and loss statement for the year ending December 31, 1945, filed as Exhibit 9.

The following decisions, in the same sense, may be consulted beneficially: *Income Tax Case No. 71* (2); *Rand Ropes (Proprietary) Ltd.* v. *Commissioner for Inland Revenue* (3).

In the first case it was held, allowing an appeal, that:

The receipt of a cheque did not result in a receipt of cash by the recipient until the cheque had passed through the bank and the amount had been credited to the payee; consequently on the basis of assessment adopted in respect of the appellant the amount of a cheque which could not be deposited with the bank for collection before the 1st July, 1925, could not be included in his income for the year ended on the 30th June, 1925.

(1) (1934) 1 K.B. 178.
(2) (1926) 3 S.A.T.C., 60.
(3) (1943) 13 S.A.T.C. 1 and (1944), A.D. 142.

1948

FLINN v. MINISTER OF NATIONAL REVENUE

Angers J.

In re White Star Line Ltd. (1) the headnote, after relating the facts in detail, gives a brief but substantial summary of the judgment. I believe it apposite to quote this headnote:

> The R.M. Co. was the holder of a large number of shares in the W.S. Co. Both companies were in liquidation, and a claim was made by the liquidator of the W.S. Co. requiring the payment of £750,990 from the R.M. Co. as contributories in respect of the shares. The R.M. Co. contended that by an arrangement sanctioned by the court the sum of £750,990 was agreed to be satisfied by the issue of deferred creditors' certificates by which the payment of the debt was postponed to an indefinite date, the W.S. Co. together with all other creditors obtaining a certain measure of control over the business of the R.M. Co. and payment of interest in the meantime only out of contingent profits. It was contended that this was a payment in money's worth of the calls upon the shares. The deferred certificates were at all material times worth less than their face value:—
>
> *Held:* on a due consideration of all the facts, money's worth was not given by the issue of the certificates. The consideration for the release of the calls was, therefore, illusory and the transaction did not amount to payment within the Companies Act, 1929, s. 157.

See also *Hope* v. *Minister of National Revenue* (2); *Capital Trust Corporation Ltd. et al* and *The Minister of National Revenue* (3); *Robertson Ltd.* and *The Minister of National Revenue* (4); *Trapp* v. *Minister of National Revenue* (5); Dominion of Canada Taxation Service, H. H. Stikeman, formerly assistant deputy minister of the Department of National Revenue for taxation, pp. 12-2 and 12-3.

It was submitted on behalf of respondent that United Service Corporation Limited was in a position to pay the arrears of dividends which it owed and for which it distributed dividend notes to its shareholders. From this premise counsel concluded that the amount of these notes in the hands of the shareholders constituted income. In his opinion, the agreement between the company and its shareholders was that the company would declare the dividend and that the shareholders would lend the money back to the company and draw interest of 4 per cent per annum on the money so loaned. This would undoubtedly be a very ingenious scheme for evading income tax. The scheme however has not been established and I do not think that, without any evidence to that effect, I should assume

(1) (1938) A.E.R. 607.
(2) (1929) Ex. C.R. 158, at 161.
(3) (1936) Ex. C.R. 163; (1937) S.C.R. 192.
(4) (1944) Ex. C.R. 170.
(5) (1946) Ex. C.R. 245.

that the transaction which intervened between the company and its shareholders was executed for the purpose of avoiding income tax. On the contrary the balance sheet of the company for the year ending December 31, 1944, shows that, at the time the dividend notes were issued, the company had not the available cash to pay the outstanding dividends.

It was the duty of the Crown to establish that the appellant was liable to taxation; this the Crown has failed to do.

I do not think that the judgment in *Waterous* v. *The Minister of National Revenue* (1) cited by counsel for respondent is relevant and has any bearing on the question at issue.

A careful perusal of the Act, of the doctrine and of the precedents has convinced me that the dividend note for $47.25 dated the 22nd day of December 1944, payable on December 15, 1964, or on such earlier date as the principal monies of the note become payable in accordance with the conditions endorsed thereon, received by appellant from United Service Corporation Limited, is not "interest, dividends or profits" received from "stocks" during the year 1944. In my opinion, it will only acquire that quality when it is paid. Presently it merely constitutes an acknowledgment of debt in so far as the company is concerned and a claim with regard to the appellant. Like many other claims it may never be satisfied.

There will be judgment maintaining the appeal, setting aside the assessment for the year 1944 and the decision of the Minister affirming it and ordering that the sum of $16.50 representing the tax on the dividend note aforesaid be struck from the assessment.

The appellant will be entitled to his costs against the respondent.

Judgment accordingly.

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(1) (1931) Ex. C.R. 108.