BETWEEN:

WILLIAM H. MALKIN .....APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE ..... } RESPONDENT.

1941
Sept. 23.
1942
June 29.

Revenue—Income tax—Income War Tax Act, R.S.C., 1927, c. 97, s. 2 (l), (r) and (s), s. 3 (e) and s. 34—Income—"Personal and living expenses"—Personal and living expenses when such form "part of the profit, gain or remuneration of the taxpayer, or the payment of such constitutes part of the gain, benefit or advantage accruing to the taxpayer under any estate, trust, contract, arrangement or power of appointment, irrespective of when created"—"The expenses of properties maintained by any person for the use or benefit of any taxpayer or any person connected with him . . ."—"The expenses, premiums or other costs of any policy of insurance, annuity contract or other like contract . . . for the benefit of the taxpayer or any person connected with him"—Rentals received by appellant constitute taxable income although applied to purchase price of rented property by agreement entered into after receipt—"Year"—Fiscal period—Income for two fiscal periods ending in one calendar year assessed for taxation purposes.

Appellant entered into a trust agreement with his four children and a trustee pursuant to the terms of which he transferred to the trustee his interest in a parcel of real estate known as Southlands; certain shares of stock in The W H Malkin Co. Limited; certain life insurance policies on appellant's life in existence at the date of the agreement; and certain new insurance policies issued subsequent to the date of the agreement. Southlands had been owned by appellant and his children. All joined in transferring it to the trustee The upkeep of Southlands was provided by the trustee who was to sell

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it as soon as a reasonable price could be obtained for it. By permission of the children the appellant lived in Southlands without paying rent therefor during the taxation year in question. The trust agreement also provided for the payment of the premiums on the insurance policies. The only income received by the trustee during the taxation year in question was the sum of $5,600. The outlay by the trustee in carrying out the trust was $11,104 13 of which amount the sum of $10,344.68 went for the maintenance of Southlands and the payment of the premiums on the life insurance policies.

On December 1st, 1935, The W. H. Malkin Company Limited sold and conveyed to appellant and his two brothers certain property in Vancouver for the sum of $77,000. The appellant and his brothers rented to the W. H. Malkin Company Limited the said property from December 1, 1935, to November 3, 1938. Appellant received his share of the rentals and for the period from December 1, 1935, to February 28, 1937, reported these as income and paid the tax thereon. He did not report as income his share of the rentals received from March 1, 1937, to November 19, 1938.

On November 3, 1938, the appellant and his brothers entered into a verbal agreement with The W. H. Malkin Company, Limited whereby the property was to be sold and conveyed by the brothers to the Malkin Company for the same price paid for it by the brothers. All rentals received by the brothers since 1935 were to be credited as part payment by the Malkin Company for the property. On November 19, 1938, the property was conveyed to the Malkin Company and the company credited with the rentals received by the transferrors. Appellant contends that these rentals became capital receipts by virtue of the oral agreement and subsequent transfer of the property.

The Commissioner of Income Tax assessed appellant for income tax on the income received by the trustee and also on the rentals received by appellant for the period from March 1, 1937, to November 19, 1938. These assessments were affirmed by the Minister of National Revenue from whose decision an appeal was taken to this Court.

Held: That the expenses of the maintenance of Southlands, or the payment of the insurance premiums under the Trust Settlement do not form part of the profit, gain or remuneration of the appellant nor do they constitute part of any gain, benefit or advantage accruing to the taxpayer under any estate trust, contract, arrangement or power of appointment, irrespective of when created.

2. That all the rental receipts in question constituted income in the hands of appellant and taxable as such.

3. That since appellant had chosen to treat the rentals as a separate business apart from his other interests and had adopted the date of February 28 as being the end of the fiscal year as far as the rentals were concerned, he was correctly assessed for two fiscal periods in the year 1938, namely, the fiscal year ending February 28, and the fiscal period from March 1 to November 19, the date on which the rental business terminated.

APPEAL under the provisions of the Income War Tax Act from the decision of the Minister of National Revenue.

The appeal was heard before the Honourable Mr. Justice Maclean, President of the Court, at Vancouver, B.C.

W. Martin Griffin, K.C., for appellant.

E. Meredith and *A. A. McGrory* for respondent.

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

THE PRESIDENT, now (June 29, 1942) delivered the following judgment:

This is an appeal from the decision of the Minister of National Revenue affirming an assessment for income tax levied against the appellant, by the Commissioner of Income Tax (hereafter referred to as "the Commissioner"), for the calendar year 1938.

On April 29, 1939, the appellant, who is a retired merchant residing in the City of Vancouver, B.C., duly made his income tax return for the taxation year ending December 31, 1938, and, therein, returned a net taxable income of $33,719.78 upon which an income tax of $7,041.11 would be payable. On April 2, 1940, the Commissioner assessed the appellant on a net taxable income of $52,625.41, instead of $33,719.78, upon which there would be payable a tax of $13,459.72, instead of $7,041.11, there being a further tax of $6,418.61; and the said sum of $13,459.72, together with interest amounting to $483.81, making in all $13,943.53, was the income tax levied by the Commissioner against the appellant, for the taxation year 1938.

The additional income for which the appellant was assessed consisted of the following items:—

(*a*) Appellant's proportion of the rents of a certain warehouse, received between March 1, 1937, and November 19, 1938	$13,217 76
(*b*) The income of the Toronto General Trusts Corporation under a Trust Settlement made by the appellant for the benefit of his children, dated November 29, 1934	5,600 00
(*c*) Two small items against which no appeal was lodged by the appellant	87 87

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The amount of additional tax assessed against the appellant in respect of the aforesaid rents ($13,217.76) and the aforesaid income of the Toronto General Trusts Corporation ($5,600) is the sum of $6,390.93.

There are, therefore, two questions involved in this appeal. The one has to do with the amount received by the appellant on account of the rental of the warehouse, and the other is concerned with the amount of $5,600, the income of the Toronto General Trusts Corporation for the year 1938, under the Trust Settlement mentioned, but which income is here assessed as the income of the appellant, namely, as "personal and living expenses of the appellant, as defined in section 3, sub-s. (*e*) of the Income War Tax Act", as stated in the statement of defence of the Crown. It is the latter question which I shall first discuss.

The question as to whether or not the income of the Toronto General Trusts Corporation under the Trust Settlement in question was assessable as income of the Settlor, the present appellant, arose in connection with the assessment of the appellant herein for income tax for the taxation year ending December 31, 1935. In that year the appellant was assessed for the said income of the Toronto General Trusts Corporation, and from that assessment he appealed, and ultimately the matter came, on appeal, before me for decision, and my judgment in that matter will be found reported in the case of *Malkin* v. *The Minister of National Revenue* (1). The facts appearing in that case appear to be sufficiently stated in the head-note of the report of that case and it might be helpful if I should quote the same, and they are as follows:

> Appellant entered into a trust agreement with his four children and a trustee pursuant to the terms of which he transferred to the trustee his interest in a parcel of real estate known as "Southlands" which had been owned by appellant's wife in her lifetime, and on her death had devolved to the appellant as to an undivided one-third interest, and to the children as to the remaining two-thirds; certain shares in the Malkin Company; certain life insurance policies on appellant's life in existence at the date of the agreement, and certain new insurance taken out on appellant's life, subsequent to the date of the agreement. The children joined with appellant in transferring Southlands to the trustee, the upkeep to be provided by the trustee who was to sell it as soon as a reasonable price could be obtained for it. By permission of the children the appellant lived in Southlands without paying rent therefor during the taxation period in question.

(1) (1938) Ex. C R 225

The trust agreement provided *inter alia* for the payment of the premiums on the insurance policies, the upkeep of Southlands, the giving to the appellant of an irrevocable proxy to vote the shares of the Malkin Company, the sale of such shares subject to certain conditions, the investment of the trust moneys, the appointment by appellant of a new trustee and the division of the trust estate at the termination of the trust.

The only income received by the trustee during the taxation period in question was the sum of $6,400 as dividends from the shares of the Malkin Company. The Commissioner of Income Tax assessed the appellant on this income and that assessment was confirmed by the Minister of National Revenue from whose decision the appellant appealed.

I held that the appellant there was not liable for income tax upon the income of the Toronto General Trusts Corporation under any provision of the Income War Tax Act by reason of his occupancy of Southlands during the taxation period there in question, or otherwise. My reasons for judgment will, of course, appear more fully in the report of that case, and from that decision there was no appeal.

In the present case the income of the Toronto General Trusts Corporation under the Trust Settlement for 1938, the taxation year here in question, was $5,600 and the outlay by the corporation in carrying out the trust was $11,104.13. Of this amount the outlay for the maintenance of Southlands and for the payment of the premiums on the life insurance policies was $10,344.68.

There being no material change in the facts appearing in the present case, and those in the former one, it will, of course, follow that, unless there has been some amendment of the relevant sections of the Income War Tax Act since 1936, applicable to the taxation year here in question, my opinion still would be that the income of the Toronto General Trusts Corporation is not assessable as the income of the appellant in the present case, as "personal and living expenses", or otherwise. The relevant and important section of the Act as it stood at the time of the former case, was sec. 3 (*e*) and it read:

> For the purposes of this Act "income" means the annual net profit or gain or gratuity . . . , and also the annual profit or gain from any other source including (*e*) personal and living expenses when such form part of the profit, gain or remuneration of the taxpayer.

This section of the Act was amended by Chap. 46 of the Statutes of Canada for the year 1939, and now reads:

> For the purposes of this Act "income" means the annual net profit or gain or gratuity . . . , and also the annual net profit or gain from any other source including (*e*) personal and living expenses when such form part of the profit, gain or remuneration of the taxpayer *or the*

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payment of such constitutes part of the gain, benefit or advantage accruing to the taxpayer under any estate, trust, contract, arrangement, or power of appointment, irrespective of when created.

The italicized words are those added to the original section by the said amendment.

The same amending statute added to sec. 2 of the Act, as sub-s. (*r*), the following definition of "personal and living expenses", and that sub-s. (*r*) reads as follows:—

(*r*) Personal and living expenses shall include *inter alia*—

(i) the expenses of properties maintained by any person for the use or benefit of any taxpayer or any person connected with him by blood relationship, marriage or adoption, and not maintained in connection with a business carried on *bona fide* for a profit and not maintained with a reasonable expectation of profit.

(ii) The expenses, premiums or other costs of any policy of insurance, annuity contract or other like contract if the proceeds of such policy or contract are payable to or for the benefit of the taxpayer or any person connected with him by blood relationship, marriage or adoption.

The above provisions of this paragraph (*r*) were made to extend to expenses of properties and establishments, maintained by a personal corporation, estate or trust, for the benefit of any of its shareholders or beneficiaries, but that does not seem to concern us here.

The foregoing recited amendments to the Income War Tax Act were made applicable to income of the year 1938 and fiscal periods ending therein, and to all subsequent periods.

The question for decision then seems to be whether the amendments made to the Act in 1939, the amendments which I have recited, have so altered the situation obtaining in 1935, the taxation year considered in the former appeal, that they authorize the assessment of the appellant for the expenses incurred by the Toronto General Trusts Corporation for the maintenance of Southlands, and also for the payment of insurance premiums under the terms of the Trust Settlement, as "personal and living expenses" of the appellant, within sec. 3 (*e*) of the Act. I should perhaps make it clear that the appellant occupied Southlands in 1938 under precisely the same terms and for the same reasons that obtained in 1935, and as explained in my judgment in the other appeal.

It is to be pointed out that the new sub-s. (*r*) of s. 2 of the Act, the Interpretation section of the Act, would appear to have been intended only to define what "per-

sonal and living expenses" shall include, and accordingly it does not say when, or in what state of facts, such "personal and living expenses" would be included as annual net profit or gain and therefore taxable income; in fact, one would not expect to find any such provision in the Interpretation section of the Act, but one would look for something to that effect in sec. 3 of the Act, and there we find that s. 3 (*e*) provides when "personal and living expenses" constitute taxable income. It is difficult to say what meaning is to be ascribed to certain words found in this amending section, s. 2 (*r*), and I have particular reference to the words beginning with "or any person connected with" and then on to the end of both subsections (i) and (ii) of s. 2 (*r*), and which appear as they stand to be not only confusing but incomplete. Any attempt to construe those words literally and without some further statutory provision would appear to lead to some strange results, results which one can hardly believe could ever have been contemplated by the legislature. Then, when we find in the very next section of the Act, s. 3 (*e*), a provision as to when "personal and living expenses" shall constitute taxable income, it becomes all the more difficult to regard or construe s. 2 (*r*) as being intended for any other purpose than a definition of terms, or to read it as a provision enacting when such "personal and living expenses" are to be included as taxable income.

Sec. 3 of the Act is the one which defines in general terms what is "income", and it is only "income" as so defined that is taxable, but of course there are other provisions in the Act which exempt certain incomes from the tax, and which provide for certain deductions and exemptions. The annual net profit or gain made subject to the income tax by s. 3, are made, by the amended sub-s. (*e*) thereof, to include the following: "personal and living expenses when such form part of the profit, gain or remuneration of the taxpayer, or the payment of such constitutes part of the gain, benefit or advantage accruing to the taxpayer under any estate, trust, contract, arrangement or power of appointment, irrespective of when created". Sec. 3 (*e*) thus purports to enact when, and under what state of facts "personal and living expenses", constitute taxable income. Now, I think it is clear that the appellant is not here taxable under s. 3 (*e*) of the

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Act, first, because the expenses of the maintenance of Southlands, or the payment of the insurance premiums under the Trust Settlement, do not form part of the profit, gain or remuneration of the appellant; and, in the second place, because the payment of such expenses by the trustee under the Trust Settlement do not constitute part of any gain, benefit or advantage "accruing to the taxpayer under any estate, trust, contract . . . ." Now if I am correct as to that, and that would seem to be fairly clear, then there is no other provision in the Act which specifically enacts what, or when, "personal and living expenses" are taxable as income. It seems to me therefore that it is only "personal and living expenses" which fall within the terms of sec. 3 (*e*) of the Act that are taxable as income. I do not think therefore that the appellant can be held liable for the particular item of tax assessment under discussion, and which was levied against him. It is quite manifest that it was one of the purposes of the amending statute to capture the tax assessed in this case, but I think the draftsman has not succeeded in doing so. At least that is the conclusion which I have reached and therefore, I think, in so far as this particular item of the appeal is concerned the appellant must succeed.

The second question involved in this appeal is quite separate and distinct from the matter just disposed of. It has to do with the liability of the appellant for income tax on certain moneys received by him by way of rentals.

The appellant and his two brothers were the owners of a warehouse in the City of Vancouver which was rented to The W. H. Malkin Co. Ltd. (hereafter called "the Malkin Company"), during the period with which we are here concerned, that is, from March 1, 1937, to November 19, 1938. The respondent claims that in respect of the fiscal period from March 1, 1937, to February 28, 1938, these three owners received by way of rentals from the Malkin Company the sum of $15,144.55 of which amount the appellant received $9,086.73; and that in respect of the fiscal period from March 1, 1938, to November 19, 1938, the said owners similarly received rentals amounting to $6,885.05 of which sum the appellant received $4,131.03. The appellant was therefore assessed for income tax on $13,217.76, the total rentals received by him in those two periods. The appellant alleges in his statement of claim

and the fact is that on November 3, 1938, a verbal agreement was entered into between the appellant and his two brothers and the Malkin Company whereby the warehouse was to be sold and conveyed by the three Malkin brothers to the Malkin Company, for the same price at which the said brothers had purchased it from the Malkin Company in 1935, namely, $77,000; and they were to credit on the said sales price all rentals received by them since 1935 as part payment of the price payable by the Malkin Company for the said warehouse. The appellant further states that on November 19, 1938, in pursuance of this agreement, the appellant and his two brothers conveyed the warehouse to the Malkin Company and the latter was credited with all rentals received by the three Malkin brothers, just as explained.

In respect of this question certain admissions of fact were made in writing on behalf of the appellant, and for purposes of accuracy it is probably better that they should be recited. They are as follows:

(1) On December 1st, 1935, The W. H. Malkin Company Limited sold and conveyed to Appellant and his two brothers, J. F. Malkin and J. P. D. Malkin, the property located at 57 Water Street, and being Lots 9 and 10. . . . . for the sum of $77,000.

(2) From the date of the said sale and until November 3rd, 1938, the Appellant and his two brothers rented the said property to The W. H. Malkin Company Limited.

(3) The Appellant received as his share of the net rentals of the said property for the period 1st March, 1937, to 3rd November, 1938, the sum of $13,217.76.

(4) Net rentals received by the Appellant in respect of the said property from December 1st, 1935, to February 28th, 1937, were reported by Appellant as income received by him and relevant income tax paid thereon.

(5) The Appellant has not reported as income to him rentals received by him from said property from 1st March, 1937, to November 19th, 1938, nor has he paid any income tax thereon.

The appellant's contention is that while the rentals in question received by him in 1937 and 1938 constituted income, yet by virtue of the oral agreement of November 3, 1938, and the conveyance of the warehouse to the Malkin Company on November 19, 1938, these income receipts were converted into capital receipts. The appellant contends also that in any event only the rentals received in the period from January 1, 1938, to November 19, 1938, should be assessed for income tax for the year 1938. And I understood Mr. Griffin to say that the appeal

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in respect of this particular question should be limited to a consideration of the rentals paid and received in 1938 and if he failed on that the appellant would account for the tax upon the rentals received in 1937.

It seems to me quite clear that the rentals in question as and when received by the appellant constituted taxable income in his hands, and so far as we are here concerned they could not, I think, become anything else. At no stage in the hearing of the appeal in respect of this question could I feel inclined to entertain as at all tenable the argument of Mr. Griffin in support of this point, and I have no doubt he advanced every argument that could possibly be urged in support of his contention. The appellant in his income tax returns made in 1936 and in 1937 treated the warehouse rentals as income, and the question of the resale of the warehouse back to the Malkin Company never arose for consideration until November of 1938. The rentals received by the appellant and his brothers since 1935 might be treated as capital receipts as between themselves and the Malkin Company, by reason of the terms of the contract of sale of the warehouse in November, 1938, but this would not be binding upon the Crown, and particularly in respect of such a subject-matter as the one under discussion. The appellant had the right, of course, to deal with his income as he saw fit after its receipt by him, but such income would remain taxable income under the taxing statute. The appellant could not by any *ex post facto* act alter the destination of these moneys, or the purpose for which they were paid to and received by him. I know of no principle of law or equity which the appellant can summon to his aid to support his contention. I am therefore of the opinion that all the rental receipts in question constituted income in the hands of the appellant and were therefore taxable as such.

Before concluding upon this question it seems necessary that I should discuss the contention advanced by the appellant that in any event he should not be taxed for the rental payments received during the last ten months of 1937, in the calendar year of 1938. This matter is a little complicated and requires a brief reference to certain facts and to certain provisions of the Act which appear to me to be relevant to this contention. Under s. 2 (*l*) of the Income War Tax Act "year" means the calendar

year. Under s. 2 (*s*) of the Act there is such a thing as a "fiscal period", and this means the period for which the accounts of the business of the taxpayer have been, or are ordinarily made up and accepted for purposes of assessment under the Act, and in the absence of such an established practice the fiscal period shall be that which the taxpayer adopts, but it must not exceed a period of twelve months. Then, s. 34 of the Act provides:

> A member of a partnership or the proprietor of a business whose fiscal period or periods is other than the calendar year shall make a return of his income and have the tax payable computed upon the income from the business for the fiscal period or periods ending within the calendar year for which the return is being made, but his return of income derived from sources other than his business shall be made for the calendar year.

Since the warehouse property was sold by the Malkin Company to the three Malkin brothers on November 30, 1935, or thereabouts, the operation of the warehouse has been treated by the appellant and his brothers as a separate business, a partnership business, and as I understand it, they filed a tax return for the fiscal period from November 30, 1935, to February 28, 1936, and this procedure was accepted by the taxing authorities in accordance with the provisions of sec. 34 of the Act. Accordingly, since that time the appellant and his brothers who were individually taxed on their income on a calendar year basis have been taxed on the rental income, for the adopted fiscal period of the warehouse business, which ended within the calendar year, namely, on February 28th, and this was the making of the appellant and his brothers. Whether there existed in fact or law a partnership in respect of the operation of the warehouse is immaterial because such operation was treated by the appellant as a separate business, or a partnership business or as something apart from his other interests from whence came his other income, and which income was reported on the calendar year basis. Accordingly the appellant, and I understand his brothers as well, were individually assessed for the warehouse rentals for the fiscal period ending February 28th of each year subsequent to 1935, and this fiscal period would end within the calendar year. When the warehouse was resold to the Malkin Company in November, 1938, it resulted in a closing of the then current fiscal period pertaining to the business operation of the warehouse, the so-called partnership busi-

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ness, thus ending two fiscal periods within the calendar year 1938; that is, one for the twelve months ending February 28, 1938, and one for the eight and a half months for the period ending November 19, 1938; but this result was, as I have already stated, of the appellant's own making. It seems to me therefore that the taxing authorities were authorized to assess the rental income for those two fiscal periods ending within the calendar year 1938 as they did, and that is all I can usefully say about the matter.

Judgment will therefore be according to the conclusions which I have expressed upon the two questions involved in this appeal. In the circumstances there will be no order as to costs.

Judgment accordingly.