

1964

BETWEEN :

Jan. 23, 24

Apr. 7

THE MINISTER OF NATIONAL }
 REVENUE }

APPELLANT;

AND

ROGER ELKIN CHRISTIE RESPONDENT.

Revenue—Income tax—Income Tax Act R.S.C. 1952, c. 148, s. 12(1)(a) and (b)—Expense incurred to produce income from a business—Deductibility of initiation fee.

In 1959 the respondent, a licensed real estate broker who had been an officer and shareholder of an incorporated real estate brokerage firm carrying on business in London, Ontario, commenced carrying on business as a real estate broker under his own name and on his own account. He had been an active associate member of the London Real Estate Board but, since this class of membership was restricted to employees or salesmen of active members of the Board, he was required to become an active member in order to retain his membership in the Board. To do so he paid the required initiation fee of \$1,000. In computing his 1959 taxable income the respondent deducted the \$1,000 on the ground that payment of the initiation fee was an expense incurred for the purpose of producing income from his real estate brokerage business.

The evidence established that the respondent would have been precluded from using the Board's services, including the cooperative or multiple listing service, if he had not become an active member thereof and paid the required initiation fee and that more than half of his income in 1959 was directly attributable to commissions on sales of properties listed through the Board's cooperative listing service and the balance of his income was indirectly attributable thereto.

Held: That the payment of the initiation fee was not an expense incurred in the course of operations from which the respondent earned his 1959 income but was made at a time anterior to the commencement thereof and accordingly was not the kind of outlay or expense properly deductible in ascertaining his income.

2. That the initiation fee was not paid by the respondent for any particular year or number of years, so that the fee or any proportion thereof cannot have any relationship to the respondent's business in any one year.
3. That the appeal is allowed.

APPEAL from a decision of the Tax Appeal Board.

The appeal was heard before the Honourable Mr. Justice Cattanach at London.

F. J. Dubrule and *M. Barkin* for appellant.

J. H. Gillies, Q.C. for respondent.

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

1964

MINISTER OF
NATIONAL
REVENUE
v.
CHRISTIE

CATTANACH J. now (April 7, 1964) delivered the following judgment:

This is an appeal from a decision of the Tax Appeal Board dated March 16, 1962¹ allowing the respondent's appeal against his income tax assessment for the 1959 taxation year.

In his income tax return for that year the respondent claimed that he was entitled to deduct an initiation fee of \$1,000 paid to The London Real Estate Board for membership therein, as an expense in computing his taxable income from his real estate brokerage business.

In assessing the respondent the Minister by notice of reassessment mailed on February 16, 1961 disallowed the deduction so claimed by the respondent. The respondent objected to the assessment, but the Minister affirmed it. The respondent then appealed to the Tax Appeal Board which allowed his appeal. It is from that decision that the Minister now appeals to this Court.

The deduction was disallowed by the Minister because, in his view, the outlay or expense in question was not incurred by the respondent for the purpose of gaining or producing income from his business within the meaning of section 12(1)(a) of the *Income Tax Act*, 1952, R.S.C., c. 148, but was an outlay or payment on account of capital, within the meaning of section 12(1)(b) thereof.

The respondent contends that section 12(1)(b) is not applicable as the outlay was in no sense an outlay on account of capital, but was clearly one made for the purpose envisaged in the excepting provision contained in section 12(1)(a).

Section 12 reads, in part, as follows:

12. (1) In computing income, no deduction shall be made in respect of
 - (a) an outlay or expense except in the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer,
 - (b) an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part,

¹ 29 Tax A.B.C. 1.

1964
 MINISTER OF NATIONAL REVENUE
 v.
 CHRISTIE
 Cattanach J.

The respondent first entered the real estate business in January 1952 as a salesman licensed under *The Real Estate and Business Brokers' Act* of the Province of Ontario for W. W. Evans and Sons, real estate brokers of London, Ontario. This firm was a member of the London Real Estate Board which at that time was a voluntary association of real estate brokers in the City of London and its environs having been formed in 1921.

On September 17, 1954 the London Real Estate Board (hereinafter sometimes referred to as "the Board") was incorporated pursuant to the laws of the Province of Ontario as a corporation without share capital without the purpose of gain for its members and any profits or accretions to the corporation are to be used in promoting its objects.

The basic objects of the corporation are to advance the interests of those engaged in the marketing of real estate and to establish standards of fair practice and business ethics.

One of the more important functions of the Board is to conduct and supervise a photo cooperative listing service now referred to as a multiple listing service. Under this particular listing service, when a prospective vendor of real estate lists a property for sale the listing broker obtains from the vendor a listing contract, on a standard listing agreement provided by the Board, in triplicate, one copy of which is retained by the listing broker, the second is retained by the vendor and the third is sent to the Board. All listings were for a minimum period of sixty days, which period is now increased to ninety days. Within twenty-four hours of the listing broker's receipt of such signed listing agreement he must forward the third copy to the Board.

The use of this service is obligatory with respect to all properties, other than vacant lands, located within the City of London area.

Each member office and each licensed sales person thereof is entitled to receive a copy of each such listing and such copies are supplied to them by the Board.

Any member office is allowed to advertise a property so listed as soon as a copy of such listing is received in the member's office.

Membership in the Board is divided into five classes, namely, active, probationary active, active associate, associate and honorary.

1964
 MINISTER OF
 NATIONAL
 REVENUE
 v.
 CHRISTIE
 Cattanach J.

Any real estate dealer, broker or duly accredited officer of a corporation or partnership actively engaged in the real estate business or lending institution and who has maintained an office in the City of London or its environs for a period of six months immediately preceding the date of application is eligible for active membership provided the applicant has passed a broker's examination as provided by the Board during the period of probation.

Probationary active membership is limited to brokers who have not been members of the Board. Such membership does not entitle the holder to the benefits of cooperative listing. However, on the expiration of the six month probationary period a probationary active member may make application for active membership.

Active associate membership is restricted to any employee or salesman in the office of an active member.

Persons who are not actively engaged in the real estate business, but who have some connection therewith are eligible for associate membership.

In Article V, section 10 of the by-laws of the Board, provision is made for an initiation fee as follows:

- (a) for active members, \$1,000.00
- (b) for active associate members, \$10.00
- (c) for associate members, \$8.00
- (d) for honorary members, nil.

Section 12 thereof provides for annual membership dues for active members in the amount of \$30.00 and for associate members in the amount of \$10.00, the said annual membership dues to become due and payable in advance as of January 1 each year.

The respondent, while employed as a salesman for W. W. Evans & Sons was a member of the unincorporated Board as an active associate member.

In 1955 the respondent, with two other salesmen in the firm of W. W. Evans & Sons, left that firm and formed a joint stock company under the name of Carruthers, Evans and Christie Limited to carry on a real estate brokerage business.

1964

MINISTER OF
NATIONAL
REVENUE
v.
CHRISTIE

Cattanach J.

In order to comply with the requirements of *The Real Estate and Business Brokers' Act*, 1950, R.S.O. c. 332, the respondent, Carruthers and Evans, the three officers and shareholders of the limited company, were licensed as real estate brokers thereunder.

Active membership in the London Real Estate Board was taken out by the Company in the name of Carruthers, rather than in the corporate name and apparently the respondent became an active associate member of the Board, but it is certain that the initiation fee for active membership was paid by the Company.

The respondent took an active interest in the affairs of the London Real Estate Board, being a director thereof and in 1961 he became the vice-president.

In May 1959 the respondent decided to sever his connection with Carruthers, Evans and Christie, Limited and to carry on business as a real estate broker under his own name and on his own account. Accordingly he applied for and obtained a broker's licence in his own name from the appropriate provincial authority.

He also made application for active membership in the Board. The respondent's application for active membership was given special consideration at a meeting of the directors. It was decided by them that the respondent should be admitted to active membership forthwith and that he would not be required to undergo a six month period of probationary membership.

However, the respondent was required to pay the prescribed initiation fee of \$1,000 which he did by cheque dated June 1, 1959. This is the payment in question in this appeal. The annual membership dues, or any portion thereof, which may have been paid by the respondent in the 1959 taxation year, is not in issue in this appeal, such payment being properly deductible.

The respondent testified that if the probationary period antecedent to active membership in the Board had not been waived, in all likelihood he would not have embarked on this venture. He also considered that active membership in the Board was essential to the success of his business. While it is true that the licence as a real estate broker entitled him to engage in the business of marketing real estate anywhere in the Province of Ontario, nevertheless lack of mem-

bership in the London Real Estate Board would deny him access to cooperative listing therein.

The general manager of the Board testified that the volume of multiple listing sales in the London area in 1960 exceeded \$12,000,000 and in 1961 this volume was in excess of \$17,000,000 which, in each year, was slightly over fifty percent of all real estate sales in the area. He further testified that eighty-seven percent of the real estate brokers in the London area were members of the Board and thirteen percent were not.

The respondent testified that in the year 1959 fifty-three percent of his income was directly attributable to commissions on sales of properties cooperatively listed and the balance of forty-seven percent was indirectly attributable thereto. He also added that of the five hundred listings available to him in 1959, four hundred and eighty-eight were cooperative listings and twelve were exclusive listings.

It is, therefore, obvious that active membership in the Board was particularly valuable and advantageous to the respondent.

The respondent, so long as he remains in the real estate brokerage business in London and maintains his membership in the Board in good standing by payment of the annual membership dues and adherence to the rules of the Board, will not be required to pay the \$1,000 initiation fee again. The respondent is not a member of, nor has he applied for membership in, any local real estate Board in Ontario, other than the Board in London.

In my view the expenditure of \$1,000 for the initiation fee for membership in the London Real Estate Board which the respondent seeks to deduct is not the kind of outlay or expense that can properly enter into the ascertainment of his net profit or gain in the 1959 taxation year or in any other year.

The initiation fee paid by the respondent for active membership was an expenditure antecedent to his membership in the Board and the consequential right to participate in the cooperative listing service and to earn income therefrom. It seems clear to me that an outlay or expense such as this is not expended in the course of operations from which the respondent earned his income, but at a time anterior to the commencement thereof and in order to

1964

MINISTER OF
NATIONAL
REVENUE
v.
CHRISTIE

Cattanach J.

1964
 MINISTER OF
 NATIONAL
 REVENUE
 v.
 CHRISTIE
 ———
 Cattanach J.
 ———

entitle him to participate in the cooperative listing service of the Board from which it follows that this is not the kind of outlay or expense that is properly deductible in ascertaining his income.

Further, the respondent's taxable income for 1959 consisted basically of the commissions received on the sales of real estate effected by him less the costs and expenses of conducting that business. It is not reasonable that the initiation fee which the respondent paid for membership in the Board could properly be offset against receipts for that year. The fee was not paid for any particular year or number of years. Therefore, the fee or any proportion thereof cannot have any relationship to the respondent's business in any one year.

In my view, therefore, the initiation fee so paid by the respondent cannot have been an outlay or expense made or incurred by him for the purpose of gaining or producing income from his business within the meaning of the exclusions outlined in section 12(1)(a).

It was strenuously argued on behalf of the respondent that the facts of the present case are analogous to those prevailing in *The Royal Trust Company v. M.N.R.*¹ decided by Thorson P. There the point in issue was whether the Royal Trust Company could deduct initiation fee paid by it to various clubs, in addition to annual dues, on behalf of its officers to enhance its business. The President held that the initiation fees and annual dues were properly deductible as expenses incurred for the purpose of gaining or producing income from the business of the taxpayer. The distinction lies in the fact that the initiation fees paid by the Company were recurring expenses since they were paid for membership of many employees, in different areas, not for membership of the Company, and when an officer of the Company left the area, the Company would be obliged to pay the initiation fee for membership of his successor, all of which payments were laid out in the course of the Company's business operations.

However, the respondent herein paid the initiation fee once and for all, on his own behalf at a time antecedent to the commencement of his business, active membership in

¹ [1957] C.T.C. 32.

the Board being a condition precedent to participation in the Board's cooperative listing service.

The Minister, was, therefore, right in assessing the respondent as he did from which it follows that the appeal must be allowed with costs.

1964
MINISTER OF
NATIONAL
REVENUE
v.
CHRISTIE
Cattanach J.

Judgment accordingly.