BETWEEN:

NEW ST. JAMES LIMITED .....APPELLANT;

AND

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

Victoria 1966
May 10
May 19

Income tax—Assessment for loss year—Subsequent years assessed on different basis—Four years lapse from first assessment—Whether loss reassessable—Income Tax Act, s. 46(4).

In assessing appellant for 1955 the Minister allowed a deduction of the full amount spent by appellant in that year on repairs to a building which appellant held under a five-year lease, treating the expenditure as rent paid. In result appellant had a substantial loss in 1955 for income tax purposes. In his assessments of appellant for the four years 1956 to 1959 the expenditure on repairs in 1955 was treated as made on account of a leasehold interest and a deduction of one-fifth of the amount was allowed for each of those years. As more than four years had elapsed between the original assessment for 1955 and the assessments for the later years appellant contended that s. 46(4) of the *Income Tax Act* precluded the Minister from recomputing appellant's 1955 loss in the assessments for the following years.

Held, dismissing the appeal, only the 1955 assessment was affected by the four year limitation of s. 46(4). The assessments for 1956 to 1959 were not affected by s. 46(4).

Income tax—Contract for services—Payment of amount stipulated—Subsequent reduction of amount—Whether rebate deductible.

Appellant agreed to render certain services for an associated company for $2,500 a year and included this amount in computing its income for each of the years 1955 and 1956. In 1957 it was decided that the amount should be retroactively reduced to $500 a year and in its 1957 return appellant claimed a deduction of $4,000 as a rebate.

Held, on appeal from the Tax Appeal Board (*No. 692 v. M.N.R.* 23 Tax A.B.C. 421), as no consideration was given for the rebate it was an incomplete gift, invalid, and not an outlay or expense and therefore not deductible.

APPEAL from decision of the Tax Appeal Board.

Edwin A. Popham for appellant.

D. G. H. Bowman for respondent.

SHEPPARD D.J.:—In this appeal the appellant, New St. James Limited, contends:

(1) that by virtue of Section 46(4) of the *Income Tax Act*, R.S.C. 1952, c. 148 (enacted S. of C. 1960, c. 43, s. 15) the Minister in making assessments for subsequent taxation years is bound by any findings, the basis for his assessment of 1955, and

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(2) that the rebate alleged made in 1957 should be allowed as an expense,

and in a cross-appeal the Minister contends that the portion of the judgment of the Tax Appeal Board allowing a rebate of $2,000 be reversed and the assessment of the Minister be restored.

As to the appellant's contention that by virtue of Section 46(4) of the *Income Tax Act* the Minister is bound by any findings in his assessment for the year 1955 in making assessments for the years 1956 to 1959 inclusive, the facts follow.

At material times the Olympic Properties Limited has owned a hotel in Victoria, British Columbia and has leased it to the appellant. In 1955 the appellant made certain repairs and improvements which the Minister assessed as a rent received by the Olympic Properties Limited and allowed the equivalent amount to the appellant as a rental expense. A notice of assessment and later a notice that no tax was payable for 1955 were sent by the Minister to the appellant.

In March 1960 the Tax Appeal Board on appeal by Olympic Properties Limited (*No. 692 v. M.N.R.*[1].) held that the repairs and improvements were not an additional rent to Olympic Properties Limited, but the Minister made no further reassessment of the appellant for 1955. After the expiry of four years within section 46(4) the Minister made an assessment of the appellant for the taxation years 1956 to 1959 inclusive in which he treated the outlays for repairs and improvements as an allowable capital expenditure and reduced the amount to the actual costs of the outlays.

The appellant contends that under section 46(4) of the *Income Tax Act,* the Minister is bound to accept as an actual loss the amount found in the assessment for the 1955 period. The parties hereto have agreed:

...that the sole issue to be decided on this appeal is whether the Minister of National Revenue is entitled, in reassessing for the 1956, 1957, 1958 and 1959 taxation years and for the purpose of computing the Appellant's taxable income for those years to recompute the Appellant's loss for 1955 on the basis that the sums of $34,541.93 and $1,193.36 referred to above are not deductible in 1955 as rent, but rather, are part of the capital cost to the Appellant of a leasehold interest within the meaning of Class 13 of Schedule B to the Income Tax Regulations, notwithstanding the fact that

[1] 23 Tax A.B.C. 421.

at the date of such reassessment for the 1956, 1957, 1958 and 1959 taxation years four years had elapsed from the date of the original Notice of Assessment for 1955.

Hence the question on appeal is whether or not in assessing for 1956 to 1959 inclusive, the Minister was precluded by Section 46(4) of the *Income Tax Act* from inquiring into the actual loss in respect of which the allowance should be made and in finding that not a rental expense but a capital expenditure.

The appellant stands wholly on the effect of Section 46(4) of which the relevant part reads as follows:

Sec. 46

(4) The Minister may at any time assess tax, interest or penalties under this Part or notify in writing any person by whom a return of income for a taxation year has been filed that no tax is payable for the taxation year, and may

(*a*) at any time, if the taxpayer or person filing the return

(i) ...

(ii) has filed with the Minister a waiver in prescribed form within 4 years from the day of mailing of a notice of an original assessment or of a notification that no tax is payable for a taxation year, and

(*b*) within 4 years from the day referred to in subparagraph (ii) of paragraph (*a*), in any other case,

re-assess or make additional assessments, or assess tax, interest or penalties under this Part, as the circumstances require.

The limitation of section 46(4) only applies when four years have elapsed after the designated notice or notification and that has occurred only in respect of the 1955 taxation year.

Hence section 46(4) imposes no restriction as to any year other than 1955 and therefore not to the subsequent years 1956 to 1959 inclusive to which the four years have not elapsed and the limitation of section 46(4) cannot apply. For these subsequent years section 46(4), having no application, does not preclude an assessment being made in accordance with the provisions of this Statute, including sections 139(1)(*x*) and 32(5). That requires the loss for the years 1956 to 1959 inclusive being taken as provided by the Statute, not as implied in the assessment for the year 1955.

As to the rebate the facts follow.

The Olympic Properties Limited and the appellant agreed that the appellant would perform certain services for the Olympic Company, including paying municipal taxes, keeping records and incidental services, and that the

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Olympic Company would pay for such services the sum of $2,500 each year. Those amounts for the years 1955 and 1956 were treated as an expense of the Olympic Company and as income of the appellant.

In 1957 the appellant purported to reduce the annual charge of $2,500 to $500 and to make the reduction retroactive to 1955. That rebate was made by the appellant debiting its surplus account for 1957 with the rebate of $4,000. In computing its income for 1957 the appellant sought to deduct $4,000 ($2,000 for 1955 and for 1956). The sum of $4,000 was in fact never paid to Olympic Properties Limited.

Watt, the chartered accountant for the companies, testified that Bergman, the controlling shareholder of both companies, decided in 1957 that the amount should be $500 for 1955 and subsequent years and corresponding entries were made in the books of the two companies. In its return for 1957, the appellant sought to charge the sum of $4,000 as an expense and that was disallowed by the Minister. On appeal the Tax Appeal Board held:

> As to 1955, this year is not in appeal before me, however, I do allow a deduction of $2,000 in respect of the appellant's 1956 taxation year.

The appellant contends that the rebate of $4,000 should be allowed as an expense in the taxation year 1957 and the Minister in his cross-appeal contends that the rebate for the year 1956 be disallowed and his assessment be restored. The contention of the Minister should succeed.

Olympic Properties Limited gave no consideration for the rebate, hence it is a gift. The alleged rebate is an incomplete gift and therefore is invalid and not an outlay or expense. In *Milroy v. Lord*,[1] Turner L.J. at p. 274 (1189) said:

> I take the law of this Court to be well settled, that in order to render a voluntary settlement valid and effectual, the settler must have done everything which, according to the nature of the property comprised in the settlement, was necessary to be done in order to transfer the property and render the settlement binding upon him.

Richards v. Delbridge[2].

Upon performing the agreed services in each year, an obligation to pay the appellant $2,500 would vest in the Olympic Company. Before payment that obligation being a

[1] 4 DeG., F. & J. 264 (45 E.R. 1185).
[2] (1874) L R. 18 Eq. 11; 18 Hals. (3rd) 396, para. 755.

chose in action could be discharged by release, but after the contract has been executed by payment or by debiting rent or other monies payable to the Olympic Company, the gift of a rebate would require delivery of monies to the Olympic Company, but not by a mere promise to pay.

In this instance there is no evidence of the release of the obligation nor of delivery of the money. The alleged rebate was carried out by the appellant making a debit entry in its surplus account for the taxation year ending September 30, 1959, which entry is as follows: "Administration costs previously charged to Olympic Properties Limited now rebated—$4,000." That entry could imply an intention to pay that sum or even a promise to pay, but it is without consideration and being without consideration the promise has no binding effect: *Eastman v. Pratchett*[1], Lord Abinger, C.B. at p. 808 (149 E.R. 1302 at p. 1307). It follows that the alleged rebate is ineffective and neither an outlay nor an expense.

The Minister further contends that the alleged rebate, although paid, would not be an outlay or expense "for the purpose of gaining income", and therefore its deduction was prohibited by section 12(1)(*a*) of the *Income Tax Act*. The appellant contends that the purpose of the rebate was to obtain the goodwill of Olympic Properties Limited as a merchant with a customer. In this instance, by reason of Bergman having control of both companies, and his directing the alleged rebate, that contention would mean that Bergman in effect was making the rebate to himself in order to purchase his own goodwill towards himself. Assuming the rebate had been paid by the appellant to Olympic Properties Limited such a purpose for the rebates is not proven, nor is it credible. Therefore the rebate should not be allowed as an expense or outlay, and the judgment of the Tax Appeal Board should be varied accordingly.

In the result, the appeal by the appellant is dismissed, the cross-appeal by the Minister allowed, and the assessment by the Minister for the taxation years 1956, 1957, 1958 and 1959 is restored.

[1] (1834) 1 Cr. M. & R. 798.