BETWEEN:

ARMAND PLOUFFE .....APPELLANT;

AND

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

1963
Apr. 22
1964
Dec. 7

Revenue—Income tax—Income—Purchase of a business—Capital cost allowance—Licence for a limited period—Effect of claiming different amounts for capital cost allowance in notice of objection, notice of appeal and amended notice of appeal—Valuation of leasehold interest —Evaluation of goodwill—Leasehold interest as capitalization over term of lease of premium lessee willing to pay—Income Tax Act, R.S.C 1952, c. 148, ss. 11(1)(a), 20(5)(a) and (6)(g); Regulation 1100(1)(a), (b) and (c) and Schedule B, Clauses 13 and 14—Alchoholic Liquor Act, R.S.Q. 1941, c. 255, ss. 3(4), 35(1) and 36(3).

This action arises out of the purchase by the appellant of a tavern business in Montreal in June 1951 for $186,000, the business sold consisting of goodwill, all existing moveables used for its exploitation, certain merchandise or stock-in-trade and the vendor's right in a liquor licence or permit, as well as an assignment of a sub-lease of the premises which was held by the vendor.

The main issue turns on whether or not and to what extent the expenditure of $186,000 by the appellant constitutes the capital cost of property in respect of which deductions are allowed under ss. 11(1)(*a*) and 20(5)(*a*) of the *Income Tax Act*. The appellant, in his return for 1954 claimed that about 90 percent of the capital cost of the business was expended on depreciable property but the respondent, on reassessment decided that only about 20 per cent of the assets acquired fell within the definition of depreciable property and that the balance represented goodwill, which was a non-depreciable asset. In his notice of objection to the reassessment the plaintiff included a statement showing that of the total purchase price, $48,599 was for furniture and moveables, $3,500 for the sign, $60,750 for leasehold improvements and $58,500 for leasehold valuation. In his notice

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of appeal the appellant alleged that the total price of $186,000 was paid for depreciable property adding to the statement included with his notice of objection $14,650 for the liquor permit and $1.00 for goodwill. The appellant then delivered an amended notice of appeal wherein he alleged that he had paid $48,599 for furniture and moveables, $3,500 for the sign, $60,750 for leasehold improvements and $73,151 for leasehold interest. At the trial the appellant agreed to accept the respondent's allowances of $16,158.91 for furniture and fixtures (including the sign) and $17,285.19 for leasehold improvements, and the only question remaining to be decided, apart from those raised with respect to the liquor licence, is in relation to the amounts, if any, to be apportioned to leasehold interest and goodwill.

Held: That the appellant having claimed in the statement delivered with his notice of objection to the reassessment capital cost deductions on only $171,349 of the total of $186,000 he paid for the business, which creates a presumption that the difference was expended on something in respect of which he was not entitled to any capital cost allowance, the appellant's attempt to add the difference to his original apportionment for leasehold interest cannot succeed in the absence of convincing evidence in support thereof.

2. That the liquor licence issued to the appellant cannot be regarded as a licence "for a limited period" within the meaning of Class 14, Schedule B of Regulation 1100 of the *Income Tax Act* because, by virtue of s. 35(1) of the *Alcoholic Liquor Act*, R.S.Q. 1941, c. 255, the duration of the licence is neither fixed nor determinable, since it may be cancelled at the discretion of the Commission.

3. That although it may be said that nobody should know better than the appellant himself what amount he considered he paid for his leasehold interest, his initial valuation is more accurate and reliable than his subsequent tardy deviations therefrom, which were self-serving and made with the aid of hindsight.

4. That a well-recognized method of evaluating goodwill is to ascertain the net earnings of the business, allow a conservative rate of return on the capital cost of its acquisition and attribute any surplus to goodwill.

5. That in this case the most pertinent evidence as to the existence or otherwise of goodwill is to be found in the profit and loss statements of the business for the taxation years under review which indicate an average annual net profit of $10,691 and an average surplus profit after allowing a 5 per cent rate of return on capital, of $1,391, which could be attributed to goodwill.

6. That since by electing to claim only a fraction of the capital cost allowance to which he is admittedly entitled the appellant could wipe out the relatively small average annual amount of $1,391, which should otherwise be attributed to goodwill, there is sufficient evidence to substantiate the appellant's main contention that goodwill in this case is non-existent.

7. That the apportionment of the purchase price of the business that should be allocated to leasehold interest should be a sum equivalent to the premium which the appellant would be willing to pay rather than part with his lease, capitalized over the term of the lease.

8 That the appeal is allowed in part.

APPEAL under the *Income Tax Act*.

The appeal was heard by the Honourable Mr. Justice Kearney at Montreal.

Redmond Quain, Jr., for appellant.

Paul Boivin, Q.C. and *Claude Guérin* for respondent.

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

KEARNEY J. now (December 7, 1964) delivered the following judgment:

The present appeal is from an income tax reassessment imposed by the Minister with respect to the appellant's taxation years 1954 to 1957 inclusive. As the issues involved are identical in each year, I shall confine myself almost exclusively to a consideration of the appellant's taxation year 1954.

On June 4, 1951 the appellant, by notarial deed effective June 1, purchased for $186,000 a tavern business from Gérard Beaucage which the latter, with the required permission of the Quebec Liquor Commission, was exploiting as the sub-tenant of premises located at 72 Beaubien Street, in the city of Montreal, which was owned by Paul Lalonde. According to the deed, the business sold consisted of goodwill, all existing movables which were being used for its exploitation, certain merchandise or stock-in-trade, and the vendor's right in a liquor licence or permit. Included in the sale price was an assignment of a sub-lease of the premises which the vendor had acquired from Albini Parent, the expiry date of which was June 1, 1964.

The deed makes no mention of the amount of the purchase price attributable to each of any of the aforesaid diversified assets, with the result that the issue turns on whether and to what extent the expenditure of the $186,000 constitutes capital cost of property in respect of which deductions are allowed by virtue of ss. 11 (1) (*a*) and 20 (5) (*a*) of the *Income Tax Act*, R.S.C. 1952, c. 148, Regulation 1100 (1) (*a*), (*b*) and (*c*) and particularly Classes 13 and 14 of Schedule B. The provisions of the Regulations made thereunder reads as follows:

11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year:

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(a) such part of the capital cost to the taxpayer of property, or such amount in respect of the capital cost to the taxpayer of property, if any, as is allowed by regulation.

20. (5) In this section and regulations made under paragraph (a) of subsection (1) of section 11,

(a) "depreciable property of a taxpayer" as of any time in a taxation year means property in respect of which the taxpayer has been allowed, or is entitled to, a deduction under regulations made under paragraph (a) of subsection (1) of section 11 in computing income for that or a previous taxation year;

* * *

REGULATION 1100—(1) Under paragraph (a) of subsection (1) of section 11 of the Act, there is hereby allowed to a taxpayer, in computing his income from a business or property, as the case may be, deductions for each taxation year equal to

Rates

(a) such amounts as he may claim in respect of property of each of the following classes in Schedule B...(Classes mentioned not applicable)

Leasehold Interest

(b) where a taxpayer has property of class 13 in Schedule B which was acquired by him for the purpose of gaining or producing income, such amount as he may claim not exceeding, in respect of each item of the capital cost thereof to him, the lesser of

(i) one-fifth of the capital cost thereof to him, or

(ii) the amount for the year obtained by apportioning the capital cost thereof to him equally over the period of the lease unexpired at the time the cost was incurred,

but the total of the amounts allowed under this paragraph shall not exceed the undepreciated capital cost to him as of the end of the taxation year (before making any deduction under this subsection for the taxation year) of property of the class;

Patent, Franchise, Concession or Licence

(c) such amount as he may claim in respect of property of class 14 in Schedule B not exceeding the lesser of

(i) the aggregate of the amounts for the year obtained by apportioning the capital cost to him of each property over the life of the property remaining at the time the cost was incurred, or

(ii) the undepreciated capital cost to him as of the end of the taxation year (before making any deduction under this subsection for the taxation year) of property of the class;

Classes 13 and 14 of Schedule B read as follows:

CLASS 13

Property that is a leasehold interest except

(a) an interest in minerals, petroleum, natural gas, other related hydrocarbons or timber and property relating thereto or in respect of a right to explore for, drill for, take or remove minerals, petroleum, natural gas, other related hydrocarbons or timber,

(b) that part of the leasehold interest that is included in another class by reason of subsection (5) of section 1102, and

(c) a property that is included in class 23.

CLASS 14

Property that is a patent, franchise, concession or licence for a limited period in respect of property but not including

(*a*) a franchise, concession or licence in respect of minerals, petroleum, natural gas, other related hydrocarbons or timber and property relating thereto (except a franchise for distributing gas to consumers) or in respect of a right to explore for, drill for, take or remove minerals, petroleum, natural gas, other related hydrocarbons or timber,

(*b*) a leasehold interest, or

(*c*) a property that is included in Class 23.

The appellant, in his income tax return for 1954, claimed that about 90 per cent of the capital cost of the business was expended on depreciable property, as defined in the Act, and that he was entitled to deductions accordingly, but the Minister, on reassessment, decided that only about 20 per cent of the assets acquired fell within the definition of depreciable property and that the balance represented goodwill, which was a non-depreciable asset; hence the present appeal.

As appears from the profit and loss statement which accompanied the aforesaid return dated April 30, 1955, the taxpayer elected to claim $7,500 as a capital cost allowance and by reassessment dated April 27, 1959 the Minister reduced it by $5,697.62.

By notice dated July 24, 1959 the appellant objected to the said reassessment and attached thereto a signed statement of facts in which he gave the undermentioned details as to the amount of the capital cost to him of the following items in respect of which he was allegedly entitled to allowances:

(mobilier)	
furniture and movables	$ 48,599
(enseigne)	
sign	3,500
(améliorations locatives)	
leasehold improvements	60,750
(bail)	
leasehold valuation	58,500
total:	$ 171,349

By notice dated October 27, 1961, the respondent advised the appellant that, after having reviewed the assessment and studied the facts and reasons set forth in the appellant's notice of objection, with the exception of $180 which he was

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prepared to allow in respect of capital cost allowances, he ratified and confirmed his previous reassessment; that the sums of $16,158.91 and $17,285.59, representing the capital cost of depreciable property consisting of movables and leasehold improvements, had been correctly determined and were the only amounts in regard to which deductions were allowable; and that the balance of the price paid by the appellant to Gérard Beaucage had not been expended for property susceptible of depreciation within the meaning of s-s. (5) of s. 20 of the *Income Tax Act*.

In a situation such as this, where the contract of sale includes tangibles and intangibles one or more of which may or may not constitute depreciable property as defined in s. 20 (5) (*a*) of the Act *supra* and where the parties have failed to set out in the deed of sale the amount expended on each of any of such items, in my opinion the Court is confronted with a special case such as described in s. 20 (6) (*g*) of the Act, which provides:

> (6) [Special cases.] For the purpose of this section and regulations made under paragraph (*a*) of subsection (1) of section 11, the following rules apply:
>
> (*g*) where an amount can reasonably be regarded as being in part the consideration for disposition of depreciable property of a taxpayer of a prescribed class and as being in part consideration for something else, the part of the amount that can reasonably be regarded as being the consideration for such disposition shall be deemed to be the proceeds of disposition of depreciable property of that class irrespective of the form or legal effect of the contract or agreement; and the person to whom the depreciable property was disposed of shall be deemed to have acquired the property at a capital cost to him equal to the same part of that amount;

The task of leading evidence which will serve to, figuratively, separate the wheat from the chaff and, also, determine what amount can be reasonably regarded as the sale price of the respective assets concerned is admittedly a difficult one. Nevertheless, I feel that the evidence offered on behalf of the parties was noticeably meagre.

The only evidence which might serve to establish the classification or purchase price of the respective tangible and intangible assets acquired consists of the record transmitted in pursuance of s. 100, c. 148, R.S.C. 1952, by the Minister under date of February 27, 1962, the testimony of the appellant, on his own behalf, and the evidence of Jules Dubois, a real estate agent, who was called on behalf of the respondent.

Before making further comment on the said evidence, I think the following extracts from the pleadings and opening declarations by counsel serve to bring the issues into focus and to narrow them considerably.

In a notice of appeal filed on January 25, 1962, the appellant alleged that the entire purchase price of $186,000 paid for the business was a capital expenditure on depreciable property apportioned as follows:

Mobilier	$ 48,599.00
Enseigne	3,500 00
Améliorations locatives	60,750 00
Bail	58,500 00
Permis Commission des Liqueurs	14,650.00
Achalandage	1.00
	$186,000.00

and allegedly made a return of income for the year in question on that basis.

By an amended notice of appeal filed on March 29, 1962 the appellant adopted a new position, as appears from the following extracts:

A—STATEMENT OF THE FACTS

.....

4. The respondent wrongly allocated this cost ($186,000) for purposes of the assessment as follows:

Furniture and fixtures (ameublement)	$ 16,158.91
Leasehold improvements (améliorations locatives)	17,285.59
Goodwill (achalandage)	152,555 50
Total purchase price:	$186,000.00

5. The principal error made by the respondent in the said allocation was in appropriating $152,555.50 of the purchase price to goodwill with the result that no capital cost allowance was allowed to the appellant on any part of this amount as a deduction from his income for the year in question.

C—THE REASONS

.....

6. The appellant's contention is that the proper division is as follows:

Furniture and moveables (Class 8)	$ 48,599
Electric Signs (Class 11)	3,500
Leasehold improvements (Class 13)	60,750
Leasehold interest (Class 13)	73,151
	$ 186,000

10. It is the appellant's contention that nothing was paid with respect to the liquor licence in that a liquor licence is, in the Province of Quebec,

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by its nature not assignable and the said licence was not assigned in the present case.

11. In the alternative, any value that should be placed on the liquor licence situation existing with respect to the lease and premises, should be allocated to Class 13 as part of the price paid for the leasehold interest in that this value was a value attached to the lease itself.

12. In the alternative any value given to the liquor licence situation is properly allocated to Class 14 as "...a franchise, concession or licence, for a limited time..."

The issues were further narrowed when counsel for the appellant in his opening statement declared that the appellant, in lieu of the $52,099 and $60,750 claimed for furniture and fixtures including the sign, and leasehold improvements respectively, was prepared to accept the amounts of $16,158.91 and $17,285.19 allowed by the Minister in respect thereof. Also that, with the consent of his learned opponent, a small sum in connection with "Des marchandises en magasin" or stock-in-trade referred to in item 30, p. 1, Ex. 1, had been settled out of court.

It would appear from the foregoing that apart from the questions raised by counsel for the appellant in his last two alternative submissions in respect of the liquor licence (paragraphs 11 and 12 *supra*) the issues are largely confined to the amount (if any) which should be apportioned to leasehold interests and goodwill respectively.

I shall outline the facts beginning with the deed of sale Exhibit 1 which gave rise to the instant action and the related deeds which preceded it.

It appears that some time prior to May 1949 Paul Lalonde, the owner of the premises, had procured in his own name, a licence from the Quebec Liquor Commission (hereinafter called "the Commission") for the sale of beer and had likewise obtained a permit to carry on this business at 72 Beaubien Street, and on May 17, 1949 Paul Lalonde, while retaining ownership of the premises, by notarial deed sold his tavern business for $90,000 to Albini Parent. On the signing of the aforesaid deed of sale—which was described in Exhibit 1 but not produced—Albini Parent paid $20,500 on account of the purchase price, leaving a balance due of $69,500. On the same date, the vendor granted a 15-year lease of the premises to the purchaser at a rental of $250 a month (Ex. 4). The lease contained a condition that in the event that the purchaser decided to sell the tavern business he would be free to transfer the lease to the new

purchaser provided the latter undertook to fulfil all the obligations contained therein. On January 4, 1950 the above-mentioned parties signed a new lease the only significant effect of which was to raise the rent from $250 a month to $300 a month and to reduce its duration from fifteen years to fourteen years and seven months (Ex. 3).

As appears by s. 3 (4) of the *Alcoholic Liquor Act*, R.S.Q., 1941, c. 255 (hereinafter sometimes referred to as "the Liquor Act"), the word "tavern" means an establishment situated in a city or town and specially adapted for the sale by the glass of beer to be consumed on the premises. The instant tavern was furnished with tables and chairs for the comfort of its patrons. It is admitted that during his tenancy Albini Parent, of his own volition and at his own expense, made alterations to the premises which increased its seating capacity by fifty.

On November 24, 1950, by notarial deed (Ex. 2) Albini Parent sold the tavern business to Gérard Beaucage for $161,000, on account of which the vendor acknowledged to have received $68,000 on the signing of the deed, leaving a balance due of $93,000, whereof $69,500 was payable to Paul Lalonde and the balance of $23,500 to Albini Parent, on terms and conditions which are repeated in Exhibit 1.

This deed which gave rise to the instant contestation contains the following description of the assets sold:

> Le fonds de commerce d'une taverne appartenant au vendeur et exploité par lui au n° 73 est rue Beaubien, à Montréal, et se composant:
>
> 1° De la clientèle ou achalandage.
>
> 2° Des objets mobiliers servant à l'exploitation de ladite taverne, tels que tables, chaises, comptoirs, réfrigérateurs, radios, coffre-fort, enseignes électriques, etc, et généralement tout ce qui se trouve dans la dite taverne et qui sert à son exploitation, sans aucune exception ni réserve, sauf un distributeur automatique de cigarettes, tel que vu par l'acquéreur qui s'en déclare satisfait et qui n'en demande pas plus ample désignation.
>
> 3° Des marchandises en magasin, dont le prix sera payé au vendeur, en sus du prix de vente ci-après mentionné, d'après un inventaire qui sera fait entre les parties aux présentes avant la prise de possession et au prix coûtant.
>
> 4° Du droit au permis ou licence émis par la Commission des Liqueurs de la Province de Québec.

In addition, the deed contains an assignment of the lease described in Exhibit 3 and recites that, commencing with the date of possession (June 1, 1951), the purchaser will

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be required to pay all business taxes and to pay the rent for the premises amounting to $300 a month.

In respect of the purchase price it is stated that the present sale is made for $186,000 on account of which the vendor acknowledged to have received from the purchaser $93,000 and that the purchaser undertook to pay the remaining $93,000, with interest at 5%, by semi-annual instalments payable to the exoneration of the vendor to Paul Lalonde and Albini T. Parent over the term of the lease (See Ex. 1, p. 3).

The deed also contains a resolutory clause whereby the whole transaction would become null and void in the event that the purchaser were unable to procure from the Quebec Liquor Commission (hereinafter referred to as "the Commission") a transfer of the liquor licence; the said clause is drawn in the following terms:

> Il est entendu entre les parties que la présente vente est sujette à l'acceptation, par la Commission des Liqueurs de Québec, du transfert du permis en faveur de l'acquéreur, et à défaut de telle acceptation, la présente vente sera considérée comme nulle et de nul effet, et tous montants versés par l'acquéreur au vendeur en acompte du dit prix de vente devront être retournés et remis à l'acquéreur, et les parties aux présentes seront dans le même état que si le présent acte n'eut jamais été exécuté.

At the conclusion of the deed there is an intervention by Paul Lalonde wherein he consents to the transfer by the vendor to the purchaser of the lease (Ex. 3) which he, as owner of the property, had granted to the vendor, the whole on condition that the latter undertakes to fulfil all clauses and conditions contained in the said lease which then had about thirteen years to run.

I shall now summarize the evidence given by the appellant and Jules Dubois respectively.

At the beginning of his testimony (Transcript, p. 1) the appellant was asked the following question and gave the following reply:

> Q. Prenant comme donnée que dans le prix que j'ai mentionné il y avait trente-trois mille, plus ou moins, et quelques dollars pour des items qu'on peut toucher, comme les meubles, pouvez-vous nous expliquer pourquoi vous avez payé un autre $153,000?
>
> R. C'est parce que je payais le loyer—à mon point de vue—bon marché, le loyer était bon marché et puis j'avais un treize ans à faire, ce qui me permettait de ne pas être ennuyé avec le propriétaire pour continuer à faire les paiements que je devais sur la taverne.

He also declared that he considered that he had acquired an advantageous lease at a low cost, particularly in view of the fact that a year and a half before he leased the property repairs and additions had been made to it which increased its seating capacity; also that his long-term lease brought with it extended and advantageous terms under which he could pay the balance of the purchase price, totalling $93,000, for which he was liable. In addition he was able to rent the upper storey of 72 Beaubien St. for $75 a month; that he took over from Mr. Beaucage a staff of three or four, including a manager, and that at the date of hearing only one of the waiters was still in his employ. He also stated that he removed the inscription "Gérard Beaucage, Prop." from the Neon sign on which the word "Taverne" appeared and replaced it with his own name. Speaking of the annual fees he paid to the Quebec Liquor Commission for his licence, he said he thought they amounted to about $300 or $400.

The witness, after stating that he was not interested in purchasing the property but only the business, was asked on cross-examination (p. 12):

Q. Quand vous achetez un commerce de bière, est-ce que vous n'êtes pas pour vous informer si c'est un commerce prospère?...

R. Comme je vous l'ai dit, j'ai été élevé sur la rue St-Dominique, tout près de la taverne, donc je connaissais la taverne et puis j'avais un bail à long terme qui me facilitait mes paiements et je payais bon marché de loyer, et j'avais des réparations de faites.

Q. Est-ce que ce n'est pas le nombre de barils qui fait la valeur du commerce de bière? Le nombre de barils qui se vendent durant une année?

R. Oui et non—j'ai tenu compte du loyer, ça dépend de la personne qui achète—j'ai tenu compte du loyer et du bail que j'avais à faire, quand j'ai acheté la taverne.

Counsel for the respondent asked the appellant to produce as Exhibit A an extract from the Montreal newspaper "La Presse", dated March 10, 1960, which contained advertisements announcing taverns for sale which, in addition to the sale price and terms of payment, refer to the number of barrels which were sold per annum in each of the premises as well as the rental payable and duration of the lease of the said taverns. The witness in doing so observed that following a change of Government (June 1960) a lot more permits were issued than theretofore, which had the effect of reducing the volume of beer sales. Subsequently, a new

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Liquor Act was passed whereby the *Alcoholic Liquor Act supra* was replaced by the *Quebec Liquor Board Act,* as appears by Statutes of Quebec, 1960-61 (9-10 Elizabeth II), c. 86.

Asked if he were obliged to see his local member in order to obtain the transfer of the liquor licence, he replied that he did not see any person in the government, neither did he have an interview with any official of the Liquor Commission before buying the business and that he had no assurance that he would obtain the transfer of the licence before he signed the deed of acquisition but he expected to obtain it because he had a good reputation insofar as the Commission was concerned; that neither Mr. Beaucage nor anybody else guaranteed the transfer of the licence.

The witness also stated that at the time of hearing he had a clientele about equal to the clientele that he had when he first acquired it. Some patrons moved away and others replaced them.

In his evidence, Jules Boire stated that he had experience from time to time in dealing with purchases and sales of taverns and that he knew the location of the instant tavern.

In his opinion, the purchase price of a tavern such as the appellant's varied a good deal depending on the amount payable by way of yearly rent, but the price which a prospective buyer would have to pay for it would be the equivalent of $120 to $125 for each barrel sold per year. He agreed with the appellant's statement that the rental of the tavern in issue was low and that the normal rental would have been around $350 a month instead of $300 as presently paid by him.

In cross-examination he stated that in buying the instant beer parlour business the purchaser was not buying a building but a tavern business and that the price of the business is established first on the quantity of beer sold in the tavern, secondly on the amount of the rent payable, and thirdly, the length of the lease.

In re-examination the witness explained that the difference between rental normally paid for a tavern and that paid in the instant case was $50, and this was excluding the $75 a month which the appellant obtained from rental of the second floor, which would make a difference of $125

per month, and that by multiplying this by the duration of the lease, which was thirteen years, the figure of $19,500 which he was prepared to allow was arrived at.

As earlier mentioned, the documentary proof contained in the transmitted record includes a signed statement dated July 24, 1959 which the appellant attached to his notice of objection to the Minister's reassessment dated April 27, 1959, in which he attributed the undermentioned amounts as constituting the capital cost to him of the following items on which he was claiming allowances:

(mobilier)	
furniture and movables	$ 48,599
(enseigne)	
electric sign	3,500
(améliorations locatives)	
leasehold improvements	60,750
(bail)	
leasehold valuation	58,500
total:	$ 171,349

The sum of the first three items totals $112,849, and, as previously mentioned, counsel for the appellant declared, at the opening of the case, that the taxpayer accepted, in settlement of this portion of his claim, the $33,444.50 which the respondent had allowed in respect thereof, and I consider that having thus agreed to withdraw the three aforesaid items they are no longer in issue before this Court.

Thus, if the appellant's aforesaid statement be accepted, the only remaining item requiring consideration is the reasonableness or otherwise of the capital cost of $58,500 which he attributed to his lease.

It is however to be noted that, notwithstanding the statement attached to his notice of objection, in his original notice of appeal he attributed an additional sum of $14,650 to the acquisition cost of his liquor licence and $1 as payment for goodwill, thus claiming $186,000, less $1, instead of the $171,349 claimed by his notice of objection as the amount of depreciable property on which he was allegedly entitled to allowances. Later, as appears by paragraph 10 of the reasons given in his amended notice of appeal, he denied having paid $14,650, or any other amount, with respect to the liquor licence, which was non-assignable and was never transferred, and sought in the alternative to add

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it to the $58,500 previously claimed as leasehold interest under Class 13 of Schedule B, thus making a total claim of $73,151 under Class 13; and as a further alternative the appellant submitted that to whatever extent the sum of $14,650, or any part thereof, was not payment for a leasehold interest it must be regarded as payment for a franchise, concession or licence in respect of which allowances are deductible under Class 14 of Schedule B.

I intend to deal immediately with the appellant's two above-mentioned alternative submissions.

I think it is very significant that, as appears by the appellant's original statement of July 24, 1959, he did not claim that he was entitled to capital cost deductions on the whole of the $186,000 which he paid for the business but restricted such a claim to $171,349. This, I believe, creates a presumption that the difference was expended on something in respect of which he was not entitled to any captial cost allowance. In the absence of convincing evidence to the contrary I can place little reliance on the appellant's attempt to add the difference amounting to $14,650 to his original apportionment for leasehold interest, thus raising it from $58,500 to $73,151.

Now, with respect to the concluding submission made by counsel for the appellant, namely, that to whatever extent the expenditure of $14,650 does not fall into the category of Class 13, then it was payment for a concession or licence for a "fixed period of time under Class 14" and is deductible accordingly.

In the first place I think my preceding observations are also applicable to the instant alternative submission, more particularly as the evidence indicates that the only amount expended on the liquor licence consisted of the fees and dues required to be paid by the Commission and which are not in issue.

Secondly, I do not think that the liquor licence issued to the appellant can be regarded as a licence "for a limited period" within the meaning of Class 14 by reason of s. 35 (1) of the *Liquor Act,* which reads as follows:

> 35. 1. Whatever be the date of issue of any permit granted by the Commision, such permit shall expire on the 30th of April following, unless it be cancelled by the Commission before such date, or unless the date at which it must expire be prior to the 30th of April following.
>
> The Commission may cancel any permit at its discretion.

because the duration of the licence is neither fixed nor determinable, since it may be cancelled at the discretion of the Commission.

It was held in *The Minister of National Revenue* and *Kirby Maurice Co. Ltd.*[1] that a franchise was not a franchise within the meaning of Class 14 of Regulation 1100, if it contains a provision that it is cancellable by either party at any time on giving 30 days notice; Cameron J. at page 82 stated:

> But not all franchises are within Class 14; only those that are "for a limited period" are within the class. The intention of Parliament in using these words "for a limited period" seems to me to be quite clear. Unless the duration of the franchise is definitely ascertained and limited there is no yardstick by which the value of the franchise can be ascertained. Further, it would be impossible to ascertain the life of the property or franchise, a matter which must be known in order to make the computation required in para. (i) of s-s. (*c*) of s. 1 of Regulation 1100, namely:
>
> "By apportioning the capital cost to him of each property over the life of the property remaining at the time the cost was incurred."

Another possible explanation as to the reason for paying the sum of $14,650 was put forward in the cross-examination of the appellant by counsel for the respondent by a series of questions directed—but without positive results—to discovering whether the $14,650 or some other amount, was paid to third parties for political influence which would guarantee that he would obtain the licence in issue. If the respondent had been successful in establishing that such were the case, the expenditure would have been disallowed since it was made for personal services, which are non-deductible.

The appellant also denied that prior to the signing of the deed he paid anything for a transfer from Gérard Beaucage of the latter's liquor licence, which is not surprising in view of s. 36 (3) of the *Liquor Act*; it states:

> The Commission must cancel a permit:
>
> .....
>
> (3) If it appears that the permit-holder has, without the Commission's authorization, transferred, sold, pledged or otherwise alienated the rights conferred by the permit.

It was held in *Courey v. Dufresne*[2] that under the Quebec Civil Code any transfer thus made, being contrary to law,

[1] [1958] Ex. C.R. 77, 82. [2] [1956] R.J.Q., C.S. 369.

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was null and void and that the transferee could recover from the transferor the amount paid for the transfer.

It may well be said that nobody should know better than the appellant himself what amount he considered he paid for his leasehold interest, but in my opinion his initial valuation is more accurate and reliable than the above-mentioned tardy deviations therefrom—which were self-serving and made with the aid of hindsight—and his said initial valuation is to be preferred.

For the above reasons I consider that there is insufficient evidence before the Court to enable it to determine with any degree of certainty the purpose or object of the aforesaid expenditure of $14,650 and that the appellant who has the burden of proving that this additional sum represented the cost of depreciable property has failed to do so; *a fortiori* I consider that his previously referred to attempt at trial to raise the value of his leasehold interest to $153,000 is entirely unwarranted.

As regards the case for the respondent, I might here observe that the appellant is not alone in altering an original apportionment.

Although the parties are poles apart in respect of the item of goodwill they find some common ground in regard to leasehold interest valuation, since the respondent acknowledged that his original assumption was unjustified as it is admitted in his answer to plea that the lease in question constitutes depreciable property under the Regulations and Class 13 of Schedule B and in respect of which he was prepared to allow a deduction of $19,500. This amount is the equivalent of a premium of $125 per month capitalized over the duration of the lease and which has been previously denied to the appellant, which had the effect of reducing this item of goodwill from $152,555.50 to $133,055.50. The amount of $58,500 claimed under the same heading by the appellant is the equivalent of $375 a month capitalized over the term of the lease, so that the parties, in terms of monthly rental values, are $250 per month apart.

Whether the sum of $19,500, as submitted by the respondent, is a sufficient leasehold allowance in the circumstances gives rise to the *raison d'être* of the revised

item of $133,055.50 which the respondent later attributed to goodwill.

Counsel were in agreement that two types of goodwill existed, one called "personal", which, in the instant case, would be attached to the vendor Gérard Beaucage and the personnel which he turned over to the appellant, and the other which is called "local" because it is attached to the premises, which, in this case, is the tavern.

Counsel do not dispute it and the evidence indicates that no appreciable amount of personal goodwill is involved in the instant case. Considerable argument, however, was devoted to the following question—

> "To what extent, if any, does goodwill which is attached to the premises, as opposed to personal goodwill, form part and parcel of a leasehold interest?"

It was stated in argument that this is the first time that the above-mentioned question has come before this Court. However, the attention of the Court was drawn to two cases heard before the Tax Appeal Board in which the facts were very similar to the case at bar. In the first of these cases, it was held that "goodwill cannot be made the subject of a capital cost allowance" (*Castellan* v. *Minister of National Revenue*[1]), and the presiding member of the Board, Mr. R.S.W. Fordham, owing to lack of evidence, referred the case back to the Minister for the purpose of ascertaining whether the existence of some goodwill was acknowledged by any of the parties to the transaction and, if so, the value to be assigned to it, and in the event of the parties failing to settle the issue that the record be referred back to the Board for further adjudication. In the other, a more recent decision (*Chartrand* v. *Minister of National Revenue*[2]), the taxpayer had purchased a hotel, including land, buildings, contents, merchandise on hand and goodwill and permit issued by the Quebec Liquor Commission, for $84,000. Mr. Maurice Boisvert held that the Minister erred in imputing $33,173 of the said purchase price to goodwill on the ground that the evidence established it was non-existent.

Section 11 (1) (*a*) states in effect that, in order to ascertain what is depreciable property, one must seek the answer

[1] (1957) 17 Tax A B C 42 at 44. [2] (1964) 35 Tax A B.C. 438

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in the Regulations. It is true that nowhere in the Regulations is any mention made of goodwill. On the other hand, goodwill is not included in the exceptions applicable to leasehold interests referred to in Class 13.

Although the above question raises an interesting issue, I think it will become unnecessary for me to make any finding concerning it if—as in the *Chartrand* case—there is sufficient evidence to justify the main submission of counsel for the appellant that if any goodwill exists, which he denies, its value is negligible.

As appears by a judgment of Noël J. in *Herb Payne Transport Ltd.* v. *Minister of National Revenue*[1], I think a well-recognized method of evaluating goodwill is to ascertain the net earnings of the business, allow a conservative rate of return on the capital cost of its acquisition and attribute any surplus to goodwill.

It sometimes happens that a purchaser pays too high a price for a property and in such cases goodwill is either diminished or extinguished.

In the instant case the notarial deeds filed disclose that on June 1, 1949 the business was sold for $90,000. Eighteen months later, to wit, on November 20, 1950, it was sold for $161,000 and six months later, namely, on June 1, 1951, it was sold for $186,000 (Exhibits 1 and 2).

In other words, the original sale price doubled within two years. True, Albini Parent, who purchased it for $161,000, during his occupancy effected some leasehold improvements. The evidence indicates that the appellant attributed $60,750 of the purchase price to such improvements but rather than attempt to prove such value he accepted $17,285.59 in settlement of this claim.

The next owner of the business, Gérard Beaucage, did nothing by way of improvement to the property, nor did he pay anything on account of the balance of the price owing to the previous owners, Paul Lalonde and Albini Parent, amounting to $93,000. Yet, having held the property for six months he sold it to the appellant for $25,000 more than he had paid for it.

The evidence given by Jules Boire also serves, I think, to establish that the appellant paid more than the going price for the business. As previously stated, he testified

[1] [1964] Ex. C.R. 1 at 10.

that the most important factor in determining a fair market price was the number of barrels sold per annum and that in terms of purchase price each barrel was worth $120 to $125. The witness also established that the number of barrels sold at the instant tavern was 1,400 per annum, which proves he paid the equivalent of over $130 a barrel for the business. Counsel for the respondent filed through the appellant a clipping from the newspaper "La Presse", dated March 10, 1960, and singled out three advertisements offering taverns for sale which he asked the appellant to identify by the letter "X". This exhibit set out the number of barrels sold, the length of the lease and the rent payable in each case, which, as hereunder indicated, showed an average price of less than the $120 to $125 per barrel mentioned by the witness:

Exhibit	*Barrels*	*Lease Terms*	*Rent*	*Per Barrel*	*Sale price*
X-1	925	long		$100	$ 95,000
X-2	1,200	10 yrs.	$250	110	135,000
X-3	1,150	10 yrs.	100	125	145,000
				$335	$ 375,000

AVERAGE PRICE: $112

In my opinion, the most pertinent evidence as to the existence or otherwise of goodwill is to be found in the profit and loss statements for the years 1954 to 1957, inclusive, which appear in the transmitted record and which indicate that, calculated to the nearest dollar, the net profits of the tavern before taking into account any capital cost allowance were as follows:

1954	$ 7,275
1955	9,829
1956	11,393
1957	14,268
total:	$ 42,765

AVERAGE: $10,691 per annum

If the method earlier indicated be applied, based on the average profit of $10,691 and 5 per cent be taken as a reasonable rate of return on the capital expended in acquiring the business, the resulting figure would amount to $9,300 per annum, which, when subtracted from $10,691 would leave an average per annum surplus profit of $1,391 which could be attributed to goodwill.

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As previously noted, the respondent concedes that the appellant is entitled on the undermentioned items to claim the following annual capital cost allowances:

	Value	*C.C.A.*
Furniture and fixtures (20%)—Class 8	$ 16,159	$ 3,232
Leasehold improvements (distributed over 13 yrs.) as per Class 13	17,286	1,329
Leasehold interest (distributed over 13 yrs.) as per Class 13	19,500	1,500
	$ 52,945	$ 6,061

It becomes apparent that the appellant, by electing to claim only a fraction of the capital cost deductions to which he admittedly is entitled, could wipe out the relatively small average yearly amount of $1,391 which could otherwise be attributed to goodwill.

If instead of the respondent's figure of $19,500 for leasehold interest the amount of $58,500—as originally claimed by the appellant—be substituted, this would result in an increased allowance, amounting in round figures to $3,000, to which he would be entitled.

For the above reasons I consider that the evidence is sufficient to substantiate the appellant's main contention that goodwill in the instant case is non-existent and that the assumption by the respondent that the goodwill of the business amounted to $133,000, or any lesser sum, is unrealistic, unwarranted and unreasonable in the circumstances.

Since it is not contested that the appellant, in a *bona fide* transaction entered into at arm's length, paid a global amount of $186,000, or its equivalent, for the tavern business, it should, I think, be borne in mind that Regulation 1100 (1) (*b*) clearly states that the taxpayer is entitled to deductions based on the *capital cost* to him of the leasehold interest which he acquired not from the owner of the property but from Gérard Beaucage, who sold him the business which included an assignment of the lease.

It goes without saying that if Exhibit 1 had stated that the premium price which the appellant paid Gérard Beaucage for the lease in question amounted to $58,500, it is unlikely that this case would ever have arisen, and in my opinion, if the purchaser and the vendor of the business

were *ad idem* as to the amount allocated to leasehold interest and the latter had so testified, such corroboration would have been almost equally conclusive. Notwithstanding the absence of the aforesaid evidence, I am nevertheless convinced that the appellant's original statement as to its value is a reasonable amount in the circumstances, particularly in view of the fact that prior to applying for a permit to sell beer the appellant had the assurance of a lease of premises wherein under previous title-holders a tavern business had been carried on. The aforesaid assurance, I consider, was instrumental to a considerable degree in facilitating the obtainment of his personal licence, gave added value to his leasehold interest and justified a valuation of $58,500, which, in my opinion, must be deemed to be the capital cost to the appellant of the leasehold interest in issue. As previously stated, $58,500 is the equivalent of $375 a month capitalized over the term of the lease and I think this amount should be regarded as what is sometimes called "the premium" (See: Locke J. in *City Parking Ltd.* v. *Corporation of the City of Toronto*[1]) which the appellant was willing to pay rather than part with his lease and that the amount of $125 a month, as submitted by the respondent, is insufficient.

For the foregoing reasons I have come to the conclusion that the appellant is entitled to succeed for the difference between the $19,500 which, as stated in his reply, the respondent was willing to allow as a deduction for leasehold interest and the above-mentioned deduction of $58,500, and I will refer the matter back to the Minister for reassessment accordingly.

The appellant will be entitled to his costs.

Judgment accordingly.

[1] [1961] S.C.R. 336 at 347.