1937 Sept. 27 & 28. 1938 Sept. 8.

BETWEEN:

W. R. WILSON .... APPELLANT;

AND

MINISTER OF NATIONAL REVENUE... RESPONDENT.

Revenue—Income—Income War Tax Act, s. 1 (i), s. 2 (e), s. 5 (a), s. 6 (a), s. 21 (1, 2 & 3), s. 35 (3)—Premiums received on dividends paid in U.S. funds by mining company constitute "income derived from mining"—Personal corporation—"Disbursements or expenses not wholly exclusively and necessarily laid out or expended for the purpose of earning the income"—Consolidated return—Subsidiary company—Companies not carrying on same class of business—Liability for tax.

Appellant was the principal shareholder in Wilson Mining & Investment Company Ltd., a personal corporation within the meaning of the Income War Tax Act. The company was incorporated in 1929 to acquire the interest of appellant and members of his family in mines, mining lands, companies and ventures, and investments generally in Canada and foreign countries; to carry on *inter alia* the business of a mining and investment company. For the taxation period in question the investments returned by the company had been transferred to it by appellant pursuant to an agreement entered into on September 8, 1931, for a consideration of 45,000 fully paid shares in the company. The income of the company for the same period was derived principally from bonds, dividends paid by Premier Gold Mining Company and premiums upon dividends paid by that company in United States funds.

The appeal is from the decision of the Minister of National Revenue affirming an assessment for income tax levied against the appellant for the 1932 taxation period. There are three grounds of appeal: (1) the disallowance of an operating loss sustained by Pleasant Valley Mining Company, all the shares of which (less directors' qualifying shares) were owned by Wilson Mining & Investment Company Ltd. and which carried on the business of mining coal only; (2) disallowance of a certain sum of money claimed as expenses incurred by the Wilson Mining & Investment Company Ltd. in exploration, prospecting and development work in connection with various mining properties, claims or prospects; (3) the refusal to allow an exemption or deduction for depreciation, authorized in the case of income derived from mining by s. 5 (*a*) of the Act, from the amount received as premiums on the dividends paid by Premier Gold Mining Company.

Held: That the premium received from the dividends paid in United States funds is income derived from mining and the depreciation authorized by s. 5 (*a*) of the Act should be deducted therefrom.

2. That the expenses incurred by the Wilson Mining & Investment Company Ltd., in prospecting, exploration and assessment work were not expenses incurred for the purpose of earning the income in question and consequently were not deductible for taxation purposes.

3. That the Wilson Mining & Investment Company Ltd. and the Pleasant Valley Mining Company Ltd. were not carrying on the same class of business within the meaning of s. 35 (3) of the Act, and, conse-

quently it was not permissible for the Wilson Mining & Investment Company Ltd. to file a consolidated profit and loss statement covering both companies.

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.

A. R. MacDougall for appellant.

Dugald Donaghy, K.C. and *J. R. Tolmie* for respondent.

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

THE PRESIDENT, now (September 8, 1938) 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 W. R. Wilson, the appellant, for the 1932 taxation period. The appellant died in 1937 and the appeal is carried on by the executors of his will. The appellant was assessed for the tax in respect of the income of Wilson Mining & Investment Company Ltd., which company, it was agreed by counsel, is a "personal corporation" within the meaning of the Income War Tax Act. Sec. 21 of the Act provides that the income of a "personal corporation," whether actually distributed or not, shall be deemed to be distributed each year as a dividend to the shareholders. Prior to the date of his death Wilson was the principal shareholder in Wilson Mining & Investment Company Ltd. (referred to hereafter as "the Wilson Company") which had its head office at Vancouver, B.C.

Sec. 1 (*i*) of the Act defines a "personal corporation" as follows:

(*i*) "personal corporation" means a corporation or joint stock company irrespective of when or where created, whether in Canada or elsewhere, and irrespective of where it carries on its business or where its assets are situate, controlled, directly or indirectly, by one individual who resides in Canada, or by one such individual and his wife or any member of his family, or by any combination of them or by any other person or corporation or any combination of them on his or their behalf, and whether through holding a majority of the stock of such corporation or in any other manner whatsoever, the gross revenue of which is to the

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extent of one-quarter or more derived from one or more of the following sources, namely:—

(i) From the ownership of or the trading or dealing in bonds, stocks shares, debentures, mortgages, hypothecs, bills, notes or other similar property,

(ii) From the lending of money with or without security, or by way of rent, annuity, royalty, interest or dividend, or

(iii) From or by virtue of any right, title or interest in or to any estate or trust.

It will be seen that a "personal corporation" is one controlled, directly or indirectly, by a single individual, or by such individual and members of his family, the gross revenue of which is to the extent of twenty-five per cent derived from the sources mentioned in sub-clauses (i), (ii) and (iii). Sec. 2 (*e*) defines "gross revenue," where a personal corporation has revenue from more than one source, as the sum of the net profits from each source. Sec. 21 comprises several provisions in respect of "personal corporations" and subs. 1, 2 and 3 are as follows:

21. The income of a personal corporation, whether the same is actually distributed or not, shall be deemed to be distributed on the last day of each year as a dividend to the shareholders, and the said shareholders shall be taxable each year as if the same had been distributed in the proportions hereinafter mentioned

2. Each shareholder's taxable portion of the income of the corporation deemed to be distributed to him as above provided for, shall be such percentage of the income of the corporation, as the value of all property transferred or loaned by such shareholder or his predecessor in title to the corporation is of the total value of all property of the corporation acquired from the shareholders.

3. The value of the property transferred by each shareholder or his predecessor in title shall be the fair value as at the date of the transfer of such property to the corporation, and the total value of the property of the corporation, acquired from its shareholders shall, for the purpose of determining the percentage referred to in the last preceding subsection, be taken as at the date of acquisition thereof by the corporation; and in ascertaining values under this subsection, regard shall be had to all the facts and circumstances, and the decision of the Minister in that respect shall be final and conclusive.

It may be assumed that the intended purpose of the provisions of the Act regarding "personal corporations" was to overcome the effect of the decisions in cases such as *Salomon* v. *Salomon* (1), and to preserve the personal liability, for the income tax, of the taxpayer who has transferred, wholly or partially, his assets to a corporation which he intends to control. S. 21 provides that the income of a personal corporation shall be deemed to be a dividend to

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the shareholders, whether the same has been distributed or not, and subsections 2 and 3 define how each shareholder's taxable portion of the income of the corporation is to be determined. In this way the liability of the owner of assets transferred to a "personal corporation," and the value of the assets as of the date of transfer, are preserved for the purposes of the income tax, even though the owner's title of the assets has passed to the corporation, and thereafter his interest therein is represented by shares in the personal corporation. What the provisions of the Act respecting "personal corporations" seek to accomplish seems to be quite plain.

The Wilson Company was incorporated in 1929 for various purposes and objects, among them being:

(*a*) To acquire the interest of William Ritson Wilson, of the members of his family and others, in mines, mining lands, mining companies and mining ventures, and investments generally as well in Canada as in foreign countries.

(*b*) 1. To carry on the business of a mining and investment company in all its branches, to acquire by purchase, lease, hire, discovery, location or otherwise, and to hold, work and develop mines, mineral claims, mineral leases, mining lands, prospects, licences and mining rights of every description, and to render the products thereof merchantable, and to buy, sell and deal in the same or any product thereof

The Wilson Company was also empowered to acquire and operate timberlands, to acquire water rights and privileges, patents, patent rights and concessions, to establish and operate stores and hotels and to carry on a general mercantile business, to acquire and operate boats, ships and other vessels, to manufacture fire and building bricks, to take contracts for mining work of all kinds and to accept as the consideration shares, stocks or other securities of any company, to acquire and operate farming lands, and to acquire, hold, sell and dispose of any securities or investments of all classes and description of any company, corporation or trust.

In the taxation period in question the Wilson Company returned as investments Dominion of Canada Bonds, Great Northern Railway Equipment Bonds, Grand Trunk Pacific Railway Bonds, and Province of Saskatchewan Bonds, all of the value of $139,972.40; shares in the Premier Gold Mining Company of the value of $114,769.50, shares in Pleasant Valley Mining Company Ld., a coal mining company, of the value of $409,526, and shares in other mining

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companies; and certain real estate, and mining prospects or equities therein. The total value of all such investments is shown in the return as being $980,929.56. These investments were assigned and transferred by the appellant Wilson to the Wilson Company by agreement dated September 8, 1931, the consideration therefor being the allotment to Wilson of 45,000 fully paid shares in the Wilson Company.

For the same period the total income returned by the Wilson Company was $65.214.93, of which $11,265.73 was derived from the Bonds which I have already described, $45,303.75 as dividends from Premier Gold Mining Company, and $5,675.76 from premiums upon dividends paid by Premier Gold Mining Company in United States funds. The head office of the Premier Gold Mining Company is in New York. The balance of the income was $315.98 received as interest upon moneys deposited in some bank on savings account, and $2,653.71 being the profit on the sale of shares in the McDonnell Coal Company. Whether the latter was in the end treated as an accretion of capital or as income, is not clear. The amount and source of the income is therefore definitely ascertained. The expenses for carrying on the business of the Wilson Company were returned at $19,396.02, most of which were apparently incurred in connection with location, survey, exploration, prospecting and assessment work, carried out on mining claims or properties. The net earnings were returned at $45,818.91.

There were originally four grounds of appeal but one having to do with a farming ranch owned by the Wilson Company, or the appellant, has since been adjusted between the parties, so there remain three grounds of appeal to consider. These are (1) the disallowance of an operating loss sustained in the taxation period in question by Pleasant Valley Mining Company, the appellant claiming that the Wilson Company having elected to file a return for that period in which its profit and loss account was consolidated with that of Pleasant Valley Mining Company, the loss of the latter should be allowed as a deduction in computing the net income of the Wilson Company; (2) disallowance of the sum of $18,303.82 claimed as expenses incurred by the Wilson Company in exploration,

prospecting and development work, carried on in connection with various mining properties, claims or prospects, which expenses were returned as a deduction from the income of the Wilson Company, and which it is claimed by the respondent is not properly allowable as expenses; and (3) the inclusion for taxation purposes of the sum of $5,675.76, being premiums received on dividends paid by Premier Gold Mining Company to the Wilson Company in United States funds, the point in issue being whether the appellant, in respect of such premium income, is entitled to the exemption or deduction for depreciation authorized in the case of income derived from mining by s. 5 (*a*) of the Act.

I propose first to discuss the issue relating to the receipt of premiums derived from the exchange of United States currency into Canadian currency in connection with the dividends paid by Premier Gold Mining Company to the Wilson Company. Sec. 5 (*a*) of the Act enacts that income derived from mining shall be subject to exemptions and deductions in such reasonable amount as the Minister, in his discretion may allow for depreciation, and he may make such an allowance for the exhaustion of the mine as he may deem just and fair. No deduction was allowed for depreciation or exhaustion in respect of the amount of such premiums but a deduction on such account was allowed in respect of the face value of the dividend cheques received from Premier Gold Mining Company by the Wilson Company. The Wilson Company was not a dealer in exchange and neither was Wilson. The question is whether the premiums received from the conversion of United States currency into Canadian currency is subject to the tax without deduction, or whether an allowance for depreciation should be made thereon, just as on the face value of the dividends remitted from New York, and that is the whole point in issue. The claim made on behalf of the Minister is that the cashing of a dividend cheque is a monetary transaction in respect of which depreciation or depletion does not enter. It appears that at one time, in such cases, depreciation was allowed but later that practice was departed from. There is no statutory provision, or regulation, directed to the controversy, and there is no decided authority upon such a point to assist one, at least my

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attention was not directed to any such authority. I was referred to the Australian case of *Payne* v. *Deputy Federal Commissioner of Taxation* (1), but that case is authority only for the proposition that income received as premiums on exchange should be included as income in the return of the taxpayer, and does not touch the question at issue here, namely, whether a deduction for depreciation should be allowed upon income derived from premiums on exchange on account of dividends paid by a mining company.

The premium income here in question constitutes, I think, "income derived from mining"; its source was dividend cheques issued to a shareholder by a mining company, and should, I think, be treated as part of the dividends. There is something, of course, to be said for the respondent's view, but the reasons advanced therefor do not weigh so heavily with me as those advanced for the appellant's contention. If United States funds, in terms of Canadian currency, had been at a discount the Wilson Company would not be taxed on the discount, and the net proceeds of the dividend cheques or warrants would be the dividend income received. To separate the premium received upon the amount of a dividend cheque and give it one name, and to call the balance "the dividend," seems to be to be a rather arbitrary distinction. The Premier Gold Mining Company might have saved the premiums for its treasury by remitting the dividends in Canadian funds but it passed this advantage over to its Canadian shareholders by remitting the same in United States funds. In such a case as this the shareholder would, I think, describe the entire proceeds of each dividend cheque as a "dividend," in his books containing the investment account, and in which account such proceeds would appear as a credit. On the whole, it seems to me that the premiums in question should be treated as part of the income derived from mining, and therefore entitled to the depreciation allowance usual in such cases.

I turn now to the appeal from the disallowance of the sum of $18,303.32, as a deduction, the same being expenses incurred by the Wilson Company in connection with prospecting, exploration and assessment work, carried out upon mining properties, and which properties were, of course,

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not revenue yielding. These expenses were disallowed on the ground that they were "disbursements or expenses not wholly, exclusively and necessarily laid out or expended for the purpose of earning the income," as provided by s. 6 (*a*) of the Act, and which are not allowable "in computing the amount of the profits or gains to be assessed." The revenue of the Wilson Company came almost entirely from two sources, the Bond Investments and Premier Gold Mining Company. No revenue was expected to be earned by reason of the expenditures in question, in the 1932 taxation period; they were in the nature of capital expenditures, and not related in any way to the earning of the income of the Wilson Company. If the mining properties upon which these expenditures were made were later sold the proceeds would, I apprehend, be treated as a return of capital, and would not be taxed as income. Had these expenses been incurred by W. R. Wilson, prior to the organization of the Wilson Company, they would not, I think, have been allowed as a deduction in computing the amount of his profits or gains to be assessed. If the appellant's contention be correct then "personal corporations" would be accorded deductions not allowed other corporations or individuals, and this, I think, is something the Act does not contemplate. A "personal corporation" is relieved of the corporation income tax and its income is to be deemed as a dividend distributed to the shareholder, to him who transferred assets to the corporation, and the distribution is not determined on the basis of the number or value of the shares held by the transferor in the corporation, but on such percentage of the income of the corporation as the value of the property transferred is of the total value of all property of the corporation acquired from the shareholders. That is what distinguishes a "personal corporation" from other corporations. Now I do not understand the Act to mean that a "personal corporation," or a shareholder in a "personal corporation," is to be treated differently from other taxpayers as to the manner of computing the amount of the profits or gains to be assessed. If a personal corporation incurs expenses not wholly, exclusively and necessarily laid out for the purpose of earning the income, I think that s. 6 (*a*) applies to it as well as to any other corporation or individual tax-

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payer. There is nothing in the Act, so far as I can see, which suggests that this provision of the Act is suspended or becomes inoperative in respect of personal corporations, and I am therefore of the opinion that the "expenses" involved in this ground of appeal are to be treated as not having been incurred for the purpose of earning the income here, and for that reason the appellant must fail.

I come now to the last question for decision and that is whether the Wilson Company is to be permitted to file a return in which its profit and loss account is consolidated with that of Pleasant Valley Mining Company. The relevant provision of the Act is s. 35 (3) and which, at the material time, read as follows:

> 3. A company which owns or controls all of the capital stock (less directors' qualifying shares) of subsidiary companies which carry on the same class of business, may elect within the time and in the manner prescribed by regulations, to file a return in which its profit or loss is consolidated with that of its subsidiaries, in which case the tax provided by paragraph D of the First Schedule of this Act shall apply.

If "company" in this section includes a "personal corporation," and if Pleasant Valley Company is a subsidiary of the Wilson Company—neither of which point the respondent contested,—and if the Wilson Company and Pleasant Valley Mining Company carried on the same class of business, then, I think, it was permissible for the Wilson Company to elect to file a consolidated profit and loss statement. The statute enacting sec. 35 (3), Chap. 41, of the Statutes of Canada, 1932-33, provided that this section was to apply "to income of the 1932 taxation period." No regulation was ever enacted, as authorized by that section, prescribing the time and manner in which the consolidated profit and loss statement should be filed, in fact it was virtually conceded by Mr. Donaghy that no regulation had been enacted. At least there was no pretense of showing that one was ever enacted. However, a consolidated statement was filed in respect of the period in question. In any event, no valid regulation could be enacted that would prevent the Wilson Company from filing a consolidated profit and loss statement for the 1932 taxation period, because the statute plainly states that this might be done. Therefore, the filing of such a statement was quite within the terms of the Act and the taxpayer cannot be deprived of the right of doing so, or be deprived of any advantage resulting therefrom, by reason of the

failure to enact any such regulation as was authorized by sec. 35 (3), as was decided in the *Carling* case (1). Therefore, in respect of this point, I would decide that the consolidated profit and loss statement must be considered in determining the assessable income of the Wilson Company unless it be that the Wilson Company and Pleasant Valley Mining Company did not, as required by the Act, "carry on the same class of business," in the period in question. Upon this point the parties are in conflict.

The Income War Tax Act does not in terms define a "subsidiary company" but for the purposes of s. 35 (3) it may be said to mean a corporation the capital stock of which is owned or controlled by another company, usually called a holding company, the business of the holding company and the subsidiary company being of the same class. Sec. 115 of the Dominion Companies Act, 1934, defines a "subsidiary company" but with special reference to the accounting and auditing of holding companies. Ordinarily, a holding company is one which acquires the whole or a controlling interest in the share capital of one or more distinct businesses, thereby for practical purposes effectively amalgamating them and consolidating their interests. The types of business carried on by a holding company and its subsidiaries may vary greatly, and it is not necessary that they be of the same class. The advantages of the summarized picture presented by a consolidated statement of affiliated groups of companies have become well recognized throughout the financial community. Consolidated statements are needed for certain audit purposes, for certain prescribed statutory purposes, and are frequently required by banks and stock exchanges. If the type of business done by a subsidiary company so differs from that carried on as a whole by the holding company, or if there is little or no intercompany business, the consolidation of the figures of the holding and subsidiary companies would lead only to confusion. Consolidated statements in such a case would not likely be expected or required, except perhaps for some special purposes. The taxing statute here recognizes the consolidated statement of a holding company and its subsidiary only when each carries on the same class of business. The reason for that

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is quite obvious. So that the usual consolidated statement of holding and subsidiary companies might mean one thing, and the consolidated statement which s. 35 (3) has reference to would mean another thing.

Here, the Wilson Company owned all the capital stock (less directors' qualifying shares) of Pleasant Valley Mining Company. Therefore one of the conditions precedent to the application of s. 35 (3) in this case is established. But did each company carry on the same class of business? That is the vital and difficult question for decision in connection with this branch of the appeal. In the 1932 taxation period Pleasant Valley Mining Company carried on the business of mining coal, and nothing else. The Wilson Company did not engage in this class of business though it appears it owned or controlled a coal area, called the "Blue Flame," upon which it did exploration and development work for the purpose of making it saleable, but in the practical sense it was not a producing coal mine, and in fact the witness, B. A. Wilson, testified it was never "a coal mine." The business activities of the Wilson Company seem to have been directed to the oversight of its revenue bearing investments, which I have already described, and to investigating, prospecting and exploring undeveloped mining properties, all, I think, being gold mining properties. In any event, I do not think it can be said that the business of mining coal was of the same class as any business carried on by the Wilson Company, however the latter might be described, and as contemplated by sec. 35 (3). The statute here uses the words "carry on the same class of business" for a special purpose. It means that before a consolidated statement might be filed, the subsidiary company must be owned by the holding company, and that the business of each company be of the same class, in the practical sense of course, in which event the profit and loss account of each might, on sound business grounds, or as a matter of fair accounting, be consolidated, that is to say, in the practical sense their business operations were of such a similar character that they might be regarded as the one business concern. That such similarity in the two businesses should exist before it might be expected that, for taxation purposes, a consolidated profit and loss statement would be allowed would seem reason-

able and just what one would expect, and therefore the words "carry on the same class of business" must be narrowly construed. Anything else would not seem reasonable in determining net income for taxation purposes. The words of s. 35 (3) which I am discussing were designedly used to express the idea that before the profit or loss account of a holding company and a subsidiary company might be consolidated, it was necessary that they be, in a very strict sense, carrying on the same class of business. Therefore, it seems to me, and I so hold, that the two companies here were not carrying on the same class of business within the meaning of s. 35 (3) of the Act, and that this provision of the Act was not available to the Wilson Company in computing the amount of its income, though for its own or other purposes this of course might be done. This ground of appeal therefore, in my view, cannot succeed. It is arguable that the word "company" in s. 35 (3) does not include a "personal corporation," and that it was not intended that this provision of the Act should apply to "personal corporations"; I should think it possible that difficulty might be encountered in applying s. 35 (3) to a "personal corporation," in view of the provisions of s. 21. However, that point was not raised before me, and I pronounce no definite opinion upon it, and in my view of the case it is not necessary to do so.

I reserve the matter of costs until the settlement of the minutes.

Judgment accordingly.