BETWEEN:

HIS MAJESTY THE KING, on the Information of the Attorney-General of Canada ..... PLAINTIFF;

1937
Sept. 27 & 30
1938
Aug. 13.

AND

CANADA RICE MILLS LIMITED.... DEFENDANT.

Revenue—Sales tax—Special War Revenue Act—Liability for tax.

Defendant, a manufacturer of rice and bags, sold its entire output during the period in question herein, to the Canada Rice Sales Company, a partnership, the members of which are, with one exception only, shareholders in defendant company, and in that instance, the partner represents a limited company which is a shareholder in defendant

1938

THE KING
v.
CANADA RICE MILLS LTD.

Maclean J.

company. The partnership purchased from defendant at a price lower than the current wholesale price, and sold at the current wholesale price. The partners divided any profits accruing to the partnership in the proportion of their holdings in defendant company. Defendant was assessed for sales tax upon the selling price of The Canada Rice Sales Company.

Held: That the Canada Rice Sales Company was not an independent trading unit or business enterprise, and defendant is liable for the sales tax and penalty assessed on the selling price of The Canada Rice Sales Company.

INFORMATION exhibited by the Attorney-General of Canada to recover from the defendant sales tax and penalty alleged due the Crown under the provisions of the Special War Revenue Act, R.S.C., 1927, c. 179, and amendments thereto.

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

C. L. McAlpine, K.C. and *J. R. Tolmie* for plaintiff.

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

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

THE PRESIDENT, now (August 13, 1938) delivered the following judgment:

This is an action to recover from the defendant Canada Rice Mills Ld. (to be referred to hereafter as "Rice Mills"), as sales tax, under the provisions of The Special War Revenue Act, the sum of $9,741.55, which with penalty interest amounted to $11,004.87, on November 30, 1936. The taxation period in question is from March 1, 1933, to August 31, 1936.

The issue here arises from the fact that the defendant, a manufacturer of rice and bags, sold its entire output during the period in question to The Canada Rice Sales Company (to be referred to hereafter as "Rice Sales"), a partnership, and Rice Mills was assessed for the sales tax upon the selling price of Rice Sales. This assessment Rice Mills contests and claims it should be assessed on its own selling prices to Rice Sales. No question arises as to the quantity of the sales in question, and Rice Mills admits that if it is obliged to pay the tax on the prices at which Rice Sales sold the goods to wholesalers, then it is indebted to the

plaintiff in the sum of $9,741.55; there is no admission as to the penalty interest, in fact that was not mentioned by either party during the course of the trial.

The purpose of forming the partnership, Rice Sales, its nature and activities, should be explained. The defendant commenced the business of manufacturing and selling rice in 1907, on the Fraser river, some sixteen miles from Vancouver, B.C., where was the office of Rice Mills. In 1932 Rice Mills, on the suggestion of its chartered accountant, first considered the matter of forming some selling organization, and in 1933 there was formed the partnership, Rice Sales, which was to market the products of Rice Mills. One of the purposes in forming the partnership was to separate the accounting of production costs and selling costs, so that Rice Mills might conveniently and accurately inform the Revenue Department as to its production costs, and which would assist the Minister in fixing the fair selling price of Rice Mills as a manufacturer or producer, for the purposes of the tax, in the event of any dispute. It was claimed that at this time Rice Mills was encountering severe competition from rice imported from Oriental countries, and that the sales tax did not fall evenly upon such importations and domestic manufactures of the same product, because in the former case the tax was based only on the foreign or export price plus the duty, without the inclusion of freight and other items of cost which the domestic manufacturer had to incur on the importation of his raw material; and it was claimed by Rice Mills that it paid as sales tax $1.50 more per ton than did importers of Chinese rice; and it was also claimed that the sale of rice manufactured by Japanese residents of British Columbia was in a favoured position so far as the tax was concerned, owing to the conditions under which the same was manufactured, and otherwise, and apparently it was thought that by the separation of the manufacturing and selling ends of the business of Rice Mills, relief would, in some way or other, be afforded it in respect of the sales tax. These were important considerations leading to the formation of Rice Sales.

The members of Rice Sales, the partnership, are, with one exception, shareholders in Rice Mills. One of the partners is a Mr. Ranking, who is not a shareholder in

1938

THE KING v. CANADA RICE MILLS LTD.

Maclean J.

Rice Mills, but it appears that he represents, in the partnership, the firm of Martin and Robinson Ld., which concern is a shareholder in Rice Mills. For our purposes here it may therefore be said that all the partners of Rice Sales are shareholders in Rice Mills. The partners of Rice Sales divide any profits accruing to it, from the business in question, in the proportion of their share holdings in Rice Mills. As Rice Sales only purchases rice from Rice Mills as it sells, its losses are probably negligible, but no mention was made of this. In fact it is not clear by which concern the losses of Rice Sales, if any, are borne.

Rice Mills and Rice Sales occupy the same office premises in the City of Vancouver. The accounting of each concern is kept apart, apparently in separate books, though that is not absolutely clear, but that of itself is not of any moment. The secretary-treasurer of Rice Mills is the book-keeper of both concerns but he is allowed remuneration by Rice Sales for such services as are performed on its account. The wages of Rice Sales employees are said to be paid by Rice Sales. The entire production of Rice Mills, during the period in question, was sold to Rice Sales at an advance of from 5 to 10 per cent above the cost of production, but, it is admitted, at a price below the wholesale prices current at the time of sale; Rice Mills, prior to the formation of Rice Sales, sold its rice, from day to day, at the current wholesale price. Rice Sales sells to wholesalers, retailers, departmental stores, and in fact to any person wishing to buy. The same warehouse is used by both concerns, and apparently—though I am not sure of this—rice there stored on account of either is subject to a lien under section 88 of the Bank Act, for banking advances or credits extended to Rice Mills. There is but one bank account, that of Rice Mills, and drafts, with bills of lading attached, made by Rice Sales upon customers for goods shipped, are at once endorsed over to Rice Mills, and from the proceeds of such drafts cheques are issued by Rice Mills for the difference between its price and the selling price of Rice Sales, directly to the partners of Rice Sales, not the partnership, in the proportions in which they hold shares in Rice Mills. Under this practice it would look as if the partnership, Rice Sales, were never in funds with which to pay any expense of doing business, if so it was

not clearly explained. It is of course claimed by the defendant, that both concerns are independent business enterprises, and the relationship of principal and agent is denied.

Now the facts of this case are quite different from those in other cases which have come before the courts, that is, so far as I am acquainted with them. The plaintiff is not contending that Rice Sales is in any way liable for the tax, in fact it is not even a defendant in this action. The plaintiff takes the position that, for the purposes of the tax at least, Rice Sales is a part of Rice Mills, and that its business activities are but a part of those of Rice Mills. While cases of this kind are never free from difficulties, yet, I think, it is fairly clear in this case that the defendant must be held liable for the tax. Rice Sales was formed at the instance of the directors and shareholders of Rice Mills in the belief that they might thus minimize the sales tax, or, that, in some way or other, they might put themselves on what they thought would be a parity with their competitors so far as the sales tax was concerned; or, that they might induce the Revenue Department to accept a more favourable basis of assessing the sales tax against Rice Mills, as a manufacturer or producer. The formation of Rice Sales does not seem to have been suggested by the usual motives underlying the creation of business enterprises. Mr. Gavin, the president, positively affirms that it was not the directors of Rice Mills who first suggested the partnership, but rather their chartered accountant. And I would expect that what the accountant had in mind was a separation of the accounting of production costs from the selling costs, to assist the Minister in fixing the selling prices of Rice Mills as a manufacturer, under s. 98 of the Act, as apparently was done in the case of other manufacturers. The two concerns occupied the same warehouse, and they occupied the same office building. The intervention of the partnership into the business affairs of Rice Mills did not add to the number of employees or staff, so far as I know; it neither added to nor subtracted from the cost of producing and selling rice; it merely separated the costs incident to production from the costs incident to sales, and this only required two sets of books instead of one. It did not alter the financial position of

1938

THE KING v. CANADA RICE MILLS LTD.

Maclean J.

the shareholders of Rice Mills; the combined profits of both concerns were divided precisely as before, and in fact the profits all went to the shareholders of Rice Mills. It seems to me that Rice Sales was not formed as an independent trading unit or business enterprise, but merely as a paper partnership, to facilitate the purposes which Rice Mills had in mind and which I have already explained. The partners never contributed one dollar of capital to the partnership and I am disposed to suspect that any expenditure made by the partnership was a book-keeping expenditure only. In this case I think it may be said that no real change occurred in the business set-up of Rice Mills, except that some or all of the officers, shareholders and servants, for some purposes, were given the colour of a partnership. The partnership was but another name for that which already existed and was functioning. The same people performed the same services as before, under the colour of a partnership, but nothing more.

I am not relying upon that portion of regulation no. 6, which states that where the vendor and purchaser are associated or affiliated concerns the price at which the goods are sold to *bona fide* independent wholesalers by either of them shall be the value upon which the tax is payable. Mr. Griffin urged that this regulation was *ultra vires* and I am inclined to think that this contention is correct. I am disposing of the case upon the facts here disclosed, and as I weigh them. It was conceded that the goods in question were sold by Rice Mills below the current wholesale prices, and I think the tax must be calculated against the defendant, on the basis of the selling prices of Rice Sales. However, counsel stated that if I reached the conclusion that the defendant were liable for the tax, the amount payable under this judgment would be determined between the parties themselves, and there is no need therefore to add anything further.

The action is therefore allowed and with costs.

Judgment accordingly.