

36, 1933

# In the Privy Council.

No. 76 of 1932.

CANADIAN  
LAW  
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APPELLANTS' CASE.

## ON APPEAL FROM THE SUPREME COURT OF CANADA.

IN THE MATTER OF THE INCOME WAR TAX ACT

AND

IN THE MATTER of the Appeal of JOHN B. HOLDEN, of the City of Toronto, in the Province of Ontario, sole surviving Executor and Trustee of the Estate of Duncan McMartin, deceased, late of the City of Montreal in the Province of Quebec.

BETWEEN

JOHN B. HOLDEN, sole surviving Executor and Trustee of the Estate of Duncan McMartin deceased ... .. (Respondent) Appellant,

AND

THE MINISTER OF NATIONAL REVENUE (Appellant) Respondent.

## CASE FOR THE APPELLANT.

1. This is an appeal by special leave from a judgment of the Supreme Court of Canada dated the 15th day of June, 1932, allowing the Respondent's appeal from a judgment of the Exchequer Court of Canada dated the 20th day of October, 1931, and confirming the Respondent's assessments of the Appellant under the Income War Tax Act, 1917, and amending Acts for income tax for the years 1917 to 1928 inclusive upon the undistributed income of the residuary estate under the will of Duncan McMartin deceased. Record. p. 47. p. 13. pp. 10-12.

2. The principal questions in dispute are :—

10 (1) Whether, under the provisions of the Income War Tax Act, 1917, and amendments thereto, so much of the income of the deceased's

Record.

residuary estate bequeathed for the benefit of his three children as had not been applied for their support, maintenance and education is subject to tax in the hands of the Executor for the years 1917 to 1928 inclusive notwithstanding that such children were not resident in Canada ;

(2) Whether in any event such income is taxable subsequent to 4th March, 1925, " the period fixed for the distribution " by the will of the Testator, and

(3) Whether in any case such income being by the terms of the will divisible into three equal parts ought not to have been taxed as 10 three distinct incomes instead of as the income of a single person.

p. 6, l. 30.

p. 7, l. 37.

p. 9, l. 10.

p. 11, l. 22.

p. 11, l. 25.

p. 11, l. 28.

p. 11, l. 31.

p. 10, l. 48—

p. 11, l. 4.

3. The facts are not in dispute. Duncan McMartin died on the 2nd May, 1914, domiciled in the Province of Quebec, survived by a widow and three children. By his will proved in the Province of Ontario he directed his Executors and Trustees to sell and convert into money his residuary estate (except certain shares which were not to be realised), to pay legacies, to invest the balance in investments in which trustees are by the laws of the Province of Ontario permitted to invest trust funds, to pay from income an annuity of \$25,000 to his widow until her remarriage upon which event the annuity was to cease and a capital sum of \$150,000 20 was then to be paid to her. The will further directed the executors and trustees :—

p. 11, l. 34.

" (E) to divide the balance of the income from such investments " or the income, or profits derived from the unrealised portions of my " estate, into three equal parts and to pay or apply one of such parts, " or so much thereof as my executors and trustees in their discretion " deem advisable, in or towards the support, maintenance and educa- " tion of each of my children until they have respectively attained the " age of twenty-five years, or until the period fixed for the distribution " of the capital of my estate, whichever event shall last happen, 30 " provided that any portion of any child's share not required for his " or her support, maintenance and education shall be re-invested by " my said executors and trustees and form part of the residue of my " estate given and bequeathed to such child.

p. 11, l. 45.

" (F) after the death or re-marriage of my wife, whichever event " shall first happen, to divide the residue of my estate equally between " such of my three children as shall attain the age of twenty-five years, " as and when they respectively attain that age, provided that if any " of the said children shall have died before the period of distribution " arrives, leaving a child or children, such children shall take the share 40 " in my estate which his or her parent would have taken had he or " she survived the period of distribution, if more than one, in equal " shares."

p. 7, l. 40.

4. For some time prior to the 1st January, 1917, from which date the Income War Tax Act became operative, the widow and children of Duncan McMartin all resided in the City of New York and at all material times continued to reside there or elsewhere in the United States of America with the exception of the eldest child, Allen A. McMartin, who in January,

p. 7, l. 49—

p. 8, l. 5.

1926, became and thereafter continued resident in Montreal in the Province of Quebec and the possible exception since the 4th March, 1925, of the widow who on that date re-married and on payment, duly made, of \$150,000 ceased to have any interest in the residuary estate or in the income or profits therefrom. Record.  
p. 8, l. 1.  
p. 7, l. 44.

5. Two of the children have attained the age of twenty-five years : Allen A. McMartin on the 4th November, 1928, and Melba McMartin (now Melba Orr) on the 3rd March, 1930. The other child, Duncan McMartin, attained the age of twenty-three years on the 17th February, 1932. p. 8, l. 6.  
p. 8, l. 7.  
p. 8, l. 9.

10 6. Allen A. McMartin was married on the 29th day of August, 1923, and there is no issue of such marriage ; Melba McMartin was married to Leander Lee on the 20th day of September, 1922, and Melba Lee, born on the 23rd May, 1923, is the only issue of such marriage ; Melba McMartin and Leander Lee were divorced, and Melba McMartin was married to T. W. Orr, on the 28th October, 1929, and there is no issue of such marriage ; Duncan McMartin was married on the 1st July, 1931, and there is no issue of such marriage. p. 8, l. 11.  
p. 8, l. 12.  
p. 8, l. 15.  
p. 8, l. 18.

7. The returns required by the Income War Tax Act, 1917, to be made by executors and trustees were each year duly made in respect of the estate of Duncan McMartin and included the undistributed balances now sought to be taxed, but no notices of assessment were served upon the Appellant in respect of the income from the undistributed portion of the residuary estate until 1930. By notices of assessment dated the 1st March, 1930, the estate of Duncan McMartin was assessed for Income Tax upon the undistributed income not used for the support, maintenance and education of the three children of the said deceased under clause (E) of paragraph 9 of the will for the years 1917 to 1928 inclusive. The total income so assessed during this period amounts to \$2,421,685.38, and the tax claimed exclusive of penalties amounts to \$822,866.02. p. 8, l. 40.  
p. 8, l. 37.  
p. 8, l. 20.  
p. 8, ll. 24-36.

30 8. In accordance with the Income War Tax Act, 1917, due notices of appeal dated the 28th March, 1930, against the assessment for each of the said years were duly served upon the Respondent, which assessments were affirmed by the Respondent by notice dated 11th December, 1930. Notice of dissatisfaction dated the 31st December, 1930, was given by the Appellant and the reply of the Respondent dated the 7th January, 1931, denied the facts alleged and confirmed the said assessment. p. 8, l. 42.  
p. 8, l. 44.  
p. 8, l. 45.  
p. 8, l. 46.

9. The Appellant's liability depends on the construction of the Income War Tax Act, 1917, as amended with retroactive effect in 1920, and reproduced without any alteration material to this Appeal in the Revised Statutes of Canada, 1927, chapter 97, hereinafter called " The Act." The principal sections relevant to this Appeal are as follows :—

#### PART I.

##### TAXABLE INCOME.

##### *Taxable Income defined.*

" 3. For the purposes of this Act, ' income ' means the annual net profit or gain or gratuity, whether ascertained and capable of com-

“ putation as being wages, salary, or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be, whether derived from sources within Canada or elsewhere; and shall include the interest, dividends or profits directly or indirectly received from money at interest upon any security or without security, or from stocks, or from any other investment, and, whether such gains or profits are divided or distributed or not, and also the annual profit or gain from any other source including

“ (a) the income from but not the value of property acquired by gift, bequest, devise or descent ;

\* \* \* \* \*

PART III.

CHARGING PROVISIONS.

*Persons Taxable.*

“ 9. There shall be assessed, levied and paid up on the income during the preceding year of every person

“ (a) residing or ordinarily resident in Canada during such year ; or

“ (b) who sojourns in Canada for a period or periods amounting to one hundred and eighty-three days during such year ; or

“ (c) who is employed in Canada during such year ; or

“ (d) who, not being resident in Canada, is carrying on business in Canada during such year ; or

“ (e) who, not being resident in Canada, derives income for services rendered in Canada during such year, otherwise than in the course of regular or continuous employment, for any person resident or carrying on business in Canada ;

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“ a tax at the rates applicable to persons other than corporations and joint stock companies set forth in the First Schedule of this Act upon the amount of income in excess of the exemptions provided in this Act : Provided that the said rates shall not apply to corporations and joint stock companies.

\* \* \* \* \*

PART IV.

SPECIAL PROVISIONS RELATING TO THE INCIDENCE OF THE TAX.

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*Income from Estates and Trusts.*

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“ 11. The income, for any taxation period, of a beneficiary of any estate or trust of whatsoever nature shall be deemed to include all income accruing to the credit of the taxpayer whether received by him or not during such taxation period.

“ (2) Income accumulating in trust for the benefit of unascertained persons, or of persons with contingent interests shall be taxable in the hands of the trustee or other like person acting in a fiduciary capacity, as if such income were the income of an unmarried person.”

Record.

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*Income in Canada of Non-Residents.*

10 “ 24. The income liable to taxation under this Act of every person residing outside of Canada, who is carrying on business in Canada, either directly or through or in the name of any other person, shall be the net profit or gain arising from the business of such person in Canada.”

“ 25. The income liable to taxation under this Act of every person residing outside of Canada, who derives income for services rendered in Canada, otherwise than in the course of regular or continuous employment, for any person resident or carrying on business in Canada, shall be the income so earned by such person in Canada.”

10. The Appellant appealed from the Respondent's confirmation of the assessment to the Exchequer Court of Canada and on the 20th October, 1931, Mr. Justice Audette delivered judgment allowing the appeal and holding that the Appellant was not liable to be taxed in respect of the income of beneficiaries who were non-residents of Canada, and that the corpus of the trust, as well as the income, was the property of non-residents. He further held that the funds in question were not income accumulating in trust for the benefit of unascertained persons, or of persons with contingent interests, and were not taxable in the hands of the Appellant under sub-section 2 of Section 11 of the Act. The learned Judge while allowing the Appeal directed that the interest of Allen A. McMartin be assessed from the date that he became a resident of Canada.

p. 13.  
p. 17, l. 46-  
p. 18, l. 7.  
p. 18, l. 18.  
p. 19, ll. 30-  
48.  
p. 21, l. 18.

11. The Respondent appealed and the Appellant cross-appealed to the Supreme Court of Canada which by a judgment dated the 15th June, 1932, reversed the judgment of the Exchequer Court and confirmed the assessments.

p. 21, l. 29.  
p. 22, l. 21.  
p. 47.

12. Mr. Justice Duff in his reasons for judgment, in which Justices Rinfret, Lamont and Smith concurred, held that under the will of Duncan McMartin, until a child has attained twenty-five years, the destination of the share is uncertain, and the beneficiary is unascertained and unascertainable and that up to that time the accumulated income accumulates as an integer.

p. 48.  
p. 48, l. 11.  
p. 48, l. 15.

13. Mr. Justice Cannon after reciting the facts held that the question of residence or non-residence in Canada does not and cannot arise when the ultimate beneficiary in the accumulating trust fund is not definitely known and determined during the taxation period. In the present case the probable beneficiaries could not be definitely ascertained before the contingency, *i.e.*, their survival until they reached twenty-five years of age, actually took place. Section 11 (being the 1920 Amendment) is a complete

pp. 48-50.  
p. 50, l. 29.  
p. 50, l. 32.  
p. 50, l. 36.

taxing provision taxing in the hands of a resident trustee income accumulating in trust for unascertained persons or persons with contingent interests without distinguishing between residents and non-residents. He felt bound by the *Royal Trust Case*, 1931, Supreme Court Reports, page 485, which followed the case of *McLeod v. The Minister of Customs and Excise*, 1926, Supreme Court Reports, page 457.

14. The Appellant respectfully contends :

(a) That non-residents of Canada are not taxable under the Act (except in special cases not now material) and that the persons for whom the undistributed funds in question were received and held 10 were not resident in Canada.

(b) That section 11, sub-section 2, of the Act is not a substantive taxing provision but merely a direction as to the person accountable for tax otherwise payable. The tax is imposed on persons and not on property, and the words "income . . . taxable" are not apt to impose taxation, but merely indicate income to be included in the taxable income of a person properly taxed under the charging provisions of the Act.

(c) That the undistributed funds in question passed to and were vested in definitely ascertained persons, namely, the testator's three 20 children ; by the will one-third of the income is expressly set aside for each child ; the whole of each child's income may be applied for his or her maintenance, etc. ; such part of a child's income as is not required for maintenance, etc., with accumulations, is, at the date fixed for distribution, to form part of the residue " given or bequeathed to such child " ; hence the surplus income was, during the period in question, accumulated for ascertained persons having vested interests, and section 11 (2) of the Act therefore does not apply. There is nothing in the will to rebut the presumption in favour of the vesting of the 30 income. The postponement of the distribution of the capital until the death or re-marriage of the widow was for the convenience of the estate in order to let in the interest of the wife and to secure that if the widow re-married capital should be in the hands of the executor to pay the legacy conditionally bequeathed to her and such postponement did not have the effect of preventing the vesting of the shares of income. The concluding words of paragraph 9 (E) of the will " given and bequeathed to such child " indicate that each child (or in the event of his death his representatives) was intended to have the accumulated income of his or her share.

(d) That, in the alternative, the funds in question under the 40 will became completely vested in the testator's three children on the date of the re-marriage of the testator's widow, namely, the 4th March, 1925. In the event which happened that date was the " period fixed for distribution " by the testator's will and the postponement of the time of payment of the funds in question until the children had attained twenty-five years did not prevent the vesting as on the 4th March, 1925.

(e) That, alternatively, if the undistributed funds in question were not vested, they were gifts and bequests, and do not come within the definition of "taxable income" contained in section 3 of the Act.

(f) That, contrary to the Respondent's contention in the Courts below, the word "person," as defined under the Act, does not include a "trust" such as that now in question, and the Appellant is not a person liable to be assessed or taxed in respect of the funds in question. Section 2 (d) of the 1917 Act provided :

10 " 2. (d) ' Person ' means any individual or person and any  
 " syndicate, trust, association or other body and any body cor-  
 " porate, and the heirs, executors, administrators, curators and  
 " assigns or other legal representatives of such person, according  
 " to the law of that part of Canada to which the context extends " ;

In the revision of 1927, section 2 (h) provides :

20 " 2. (h) ' Person ' includes any body corporate and politic and  
 " any association or other body, and the heirs, executors, adminis-  
 " trators and curators or other legal representatives of such person,  
 " according to the law of that part of Canada to which the context  
 " extends " ;

It is submitted that the word " trust " as used in section 2 (d) of the 1917 Statute does not apply to a trust such as that constituted by the will, but must be read with the words which follow " or other body and any body incorporate."

(g) That, in any case, the whole of the undistributed income ought not to be taxed as if it were the income of a single person. By the terms of the will, the undistributed income was divisible into three distinct funds and each fund was to be held by the executor for one of the three designated children. Accordingly each fund, if taxable at all, ought to have been taxed as a separate unit.

30 15. The Appellant therefore submits that the judgment of the Supreme Court of Canada was wrong and should be reversed for the following amongst other

### REASONS.

1. Because the persons for whom the undistributed funds in question were received and held were non-residents of Canada, who, under the Act, are not taxable.
2. Because the undistributed funds taxed were not income accumulating in trust for the benefit of unascertained persons or persons with contingent interests.
- 40 3. Because the trust created by the will of Duncan McMartin is not a person liable to income tax.
4. Because the Appellant is not a person liable to assessment and taxation in respect of such undistributed funds.

5. Because in any event subsequent to the 4th March, 1925, such undistributed funds are not subject to taxation.
6. Because, if the undistributed funds in question were not vested, they were gifts and bequests and therefore not within the definition of "taxable income" contained in the Act.
7. Because there are three separate funds which, if subject to taxation, should have been taxed separately and not treated for taxing purposes as a single income.

N. W. ROWELL. 10

FRANK GAHAN.

# In the Privy Council.

No. 76 of 1932.

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*On Appeal from the Supreme Court of  
Canada.*

IN THE MATTER OF THE INCOME WAR TAX ACT

AND

IN THE MATTER of the Appeal of JOHN B. HOLDEN, of the  
City of Toronto, in the Province of Ontario, sole sur-  
viving Executor and Trustee of the Estate of Duncan  
McMartin deceased, late of the City of Montreal in the  
Province of Quebec.

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BETWEEN

JOHN B. HOLDEN, sole surviving Executor  
and Trustee of the Estate of Duncan  
McMartin deceased - - (Respondent) *Appellant,*

AND

THE MINISTER OF NATIONAL REVENUE  
(Appellant) *Respondent.*

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CASE FOR THE APPELLANT.

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