

58, 1933

No. 72 of 1932.

In the Privy Council.

ON APPEAL

FROM THE SUPREME COURT OF CANADA.

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IN THE MATTER of the INCOME WAR TAX ACT

— AND —

IN THE MATTER of the APPEAL of MRS. CATHERINE
SPOONER of the City of Calgary in the Province of
Alberta.

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BETWEEN :—

THE MINISTER OF NATIONAL REVENUE
(Respondent) *Appellant*

— AND —

MRS. CATHERINE SPOONER
(Appellant) *Respondent*.

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RESPONDENT'S CASE.

RECORD.

1. This is an appeal by special leave from the judgment of the Supreme Court of Canada dated the 28th April, 1931. By the said judgment the Court unanimously allowed an appeal by Catherine Spooner (hereafter referred to as the Respondent) from the judgment of the Exchequer Court dated the 23rd October, 1930, and decided that the Respondent was not liable to pay income tax for the year 1927 for which she had been assessed.

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p. 41.
p. 35.

p. 16.

CASE FOR THE RESPONDENT.

2. The question of liability arises under the Income War Tax Act 7 & 8 Geo. V. Chapter 28, Section 3 (Statutes of Canada 1917) as amended, and the amount of the assessment, \$301.07, was in respect of a sum of \$9570.41 which the Respondent had received under the Agreement hereinafter referred to in respect of part of the consideration payable to her under that Agreement.

3. The material part of Section 3 (1) of Chapter 28 as amended 10 as aforesaid is as follows :—

3. (1) For the purposes of this Act, "income" means the annual net profit or gain or gratuity, whether ascertained and capable of computation 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 * * * * and also the annual profit or gain from any other source * * * * with the following exemptions as deductions :—

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(a) Such reasonable amount as the Minister, in his discretion, may allow for depreciation, and the Minister in determining the income derived from mining, and from oil and gas wells and timber limits shall make such allowance for the exhaustion of the mines, wells and timber limits as he may deem just and fair. (Chapter 55, 9 & 10 Geo. V. (1919) S. 2 (2) a).

* * * * *

p. 15. 1. 3.

4. The Respondent, who has never been a dealer in oil lands or in any way engaged in the business of buying or selling oil land or leases, in the year 1902 purchased from the Canadian Pacific Railway Company certain lands in Alberta for the purpose of conducting ranching operations and she then became owner of the said lands except as to coal therein and thereon. 30

pp. 3-5.

5. In the year 1925 the Respondent agreed to sell a portion of the said lands, viz., the southerly 20 acres of the north-west quarter of Section 13 Township 20 Range 3 west of the Fifth Meridian to Vulcan Oils Limited (hereinafter referred to as the Company). The agreement for sale is dated the 15th April, 1925, and was made between the Respondent of the first part and the Company of the second part and the relative provisions of the said agreement are next referred to. 40

6. By Clause 1 of the said agreement the Respondent sold, assigned, transferred and set over to the Company its successors and assigns all her right, title and interest in the said 20 acres above referred to including all mines and minerals subject to the provisoes, conditions and royalties thereafter reserved. The conveyancer had apparently overlooked the fact that the Respondent was not the owner of the coal but nothing turns upon this omission. p. 3. l. 17.

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7. By Clause 2 the Company agreed in consideration of the sale to it to pay to the Respondent \$5,000 in cash upon the execution of the Agreement and to issue to the Respondent or her nominees 25,000 fully paid shares of a par value of \$1 each, and by Clause 3 it further agreed in consideration of the sale to deliver to the order of the Respondent the royalty thereby reserved to the Respondent, namely, 10 per cent. of all petroleum, natural gas and oil produced and saved from the said lands free of costs to the Respondent on the said premises at least once in every thirty days. p. 4. l. 6.

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8. By Clauses 5 and 6 the Company covenanted to provide the necessary drilling machinery and to drill for oil and gas and to instal and maintain the necessary machinery for pumping and procuring oil or petroleum from wells and delivering it in pipes, reservoirs or tanks as therein provided. p. 4. ll. 38-45.

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9. By Clause 7 it was provided that in the event of oil or gas being discovered in commercial quantities the Respondent as part of the consideration for the Agreement covenanted to transfer to the Company the 20 acres in Section 13 and also 20 acres in Section 24 "reserving always however to the Vendor"—the Respondent, "the said royalty of 10 per cent. of all petroleum, natural gas and oil in respect to" the 20 acres in section 13, and "also free access on and over all the said lands" to the extent therein described. p. 5. l. 5.

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10. In accordance with the said agreement the Company entered upon the property described in the agreement and commenced the operations of drilling for oil with equipment and in a manner satisfactory to the Respondent and during the fall of 1926 the Company struck oil (as referred to in the agreement) "in commercial quantities on the said lands." p. 15. l. 21.

11. Due to the mining operations the whole of the oil produced in the year 1927, the year in question, was sold by the Company and p. 15. l. 30.

out of the moneys received from the sale of the oil (before the Company deducted expenses or made any deductions therefrom) 1-10th of the gross proceeds was paid over to the Respondent.

p. 15. l. 35. **12.** The oil produced by the Company is not in fact physically divided by the Company, nor is it sold in two distinct portions of 90% and 10%, but the whole is handled in bulk. The Company in fact never delivered any of the actual oil to the Respondent but has in fact delivered (as per the said agreement) "to the order of the said Vendor the royalties hereby reserved to the Vendor"—the Respondent, the delivery in fact being effected by payment in cash. The amount received by the Respondent in the year 1927, the year in question, was \$9570.41 the amount upon which the assessment was made (supra paragraph 2). 10

p. 15. l. 10.
p. 16.
p. 16. **13.** The appeal of the Respondent from the assessment was tried in Calgary by Mr. Justice Audette in the Exchequer Court, on the 17th September, 1930, and he gave judgment in favour of the Appellant on the 23rd October, 1930, subject to a deduction to be ascertained for depletion or depreciation but without costs to either party. 20

pp. 17-22.
p. 21. l. 19.
p. 21. l. 25.
p. 21. l. 30.
p. 22. l. 6. **14.** In his reasons for the judgment the learned Judge stated, *inter alia*, that the royalty mentioned in the said agreement was a reservation, operating as an exception out of the demise in favour of the Respondent, of the profits derived from the working and development of the land, and was in its very nature income and could not amount in any sense to capital, and that it was quite variable in quantities and was taxable as income under the Act, and that the reservation of ten per cent. in the said agreement was never sold and never passed out of the hands of the Respondent. He held, however, that before rendering account of the amount of the tax collectible, the Statutory allowance for depletion or depreciation under Section 5 must be ascertained and deducted. The reference by the learned Judge to Section 5 is to Section 5 of Chapter 97 of the Revised Statutes of Canada, 1927, the said section being in the same terms as Section 3 (1a) of Chapter 28 of the Statutes of 1917 as amended by Chapter 55, 9 and 10 Geo. V. (1919) Section 2 (2) (a). 30

15. The Respondent appealed from the Judgment of Mr. Justice Audette to the Supreme Court of Canada. The appeal was heard before Mr. Justice Duff (Acting Chief Justice) and Justices 40

Newcombe, Rinfret, Lamont and Cannon on the 5th and 6th February, 1931, and judgment was given in favour of the Respondent allowing the appeal. p. 35.

16. The reasons which were concurred in by the other Judges were given by Mr. Justice Newcombe. He said, *inter alia*, after referring to Clause 3 of the said Agreement that it suggested a question as to whether the consideration or so-called royalty of ten per cent. of the minerals recovered was validly reserved and then he said that one was concerned to know whether the Respondent had acquired that which was taxable as income: that for the purposes of the Act "income" was defined by the relevant provisions of Section 3 (1) and (3) (1a) (supra paragraph 3): it was, he said, clear that one-tenth of the petroleum, gas and natural oil produced from the lands sold was not profit in the hands of the Company, which was at the expense of producing it and was bound to give it to the Respondent, and so far as the Court knew, the Company did not otherwise make any profit or gain, also, he said, as the Respondent had no reversion and received one-tenth of the specified minerals as part of the consideration of the sale of the inheritance, it was most unlikely that Parliament intended to include the Respondent's tenth as income, within the meaning of Paragraph (a) of Section 3. pp. 36-40.
pp. 36. l. 45.
37. l. 1.

17. Why, said Mr. Justice Newcombe, should a vendor have an allowance for the exhaustion of that which he had sold and been paid for?—the definition clause, he said, must be interpreted in the light of Section 36 of the General Interpretation Act, R.S.C., 1927, Chapter 1, which was in force long before the enactment of the Income War Tax Act, 1917, and it provided that "Definitions or rules of interpretation contained in any Act shall, unless the contrary intention appears, apply to the construction of the sections of the Act which contain those definitions or rules of interpretation as well as to the other provisions of the Act" and thus, he said, it followed that the word "income" in the first line of Section 3 (1) of the Income War Tax Act, 1917, (supra paragraph 3) and the same word in clause (a) of that sub-section were controlled by the same statutory definition: that the stipulated tenth was not rendered annually, but at least every thirty days after production, and that irrespective of whether the operation resulted in profit or loss: it was, he said, by the agreement, for the lack of an apt definition, termed a "royalty", but, whether or not it might appropriately be named a royalty or an annuity, the Statute did not, in terms, charge either royalties or annuities as such: and here the Respondent had p. 38. l. 41.
p. 39. l. 3.
p. 39. l. 10.
p. 39. l. 13.

converted the land, which was capital, into money, shares, and ten per cent. of the stipulated minerals, which the Company might win: what the Respondent would realise, under the covenant, was, of course, uncertain; although it might be ascertained in any event. On the other hand, he said, it might be assumed that if the project should prove unprofitable, the minerals would not be raised and that circumstance, as well as the uncertainty of the extent of the minerals available, contributed to the speculative character of the Respondent's interest; but, nevertheless, the Respondent's receipts would come from a potential source of capital: the taxable commodity, he said, was "income", which meant by the definition, annual profit or gain; and for the Respondent there was no question of profit or gain, unless it were as to whether she had made an advantageous sale of her property.

18. Mr. Justice Newcombe then referred to the judgment of Rowlatt J., in *Jones v. The Commissioners of Inland Revenue*, 1920, 1 K.B., page 711, a case relied upon by the Crown: and said, that the observations of the learned Judge Mr. Justice Rowlatt had their application to the Statutes which were under consideration in that case: but the question in the present case was, did a man take an income within the meaning of the Canadian Act when he sold his land in consideration of a part of the oil and gas to be extracted from it by the purchaser, if, as, he said, was stated in the present case, the Respondent "was not and is not a dealer in or in the business of "buying and selling oil lands or leases", and, when there was no provision for taxing the property delivered by the purchaser to the Respondent, either as annuity or royalty: neither of these words having been used in the Statute to describe any right such as that which the vendor acquired under the agreement.

19. Mr. Justice Newcombe concluded by saying that it was the duty of the Court to ascertain the real nature of the transaction; and that it was argued for the Crown that the Respondent sold her land and joined with the purchaser in the business of recovering the minerals, but, he said, she was clearly not engaged in the business, and that suggestion was excluded by the facts and admissions. The case, he said, was not without its difficulties but he was not satisfied that the Crown had made out its claim, and, "inasmuch as it is the "duty of those who assert and not of those who deny, to establish "the proposition sought to be established. I think the Crown must "fail", referring to *Secretary of State in Council of India v. Scoble*, 1903, A.C. 299.

20. The Respondent humbly submits that the Judgment appealed from of the Supreme Court of Canada dated the 28th April, 1931, is right and should be affirmed and that the Appeal should be dismissed for the following amongst other

REASONS.

- 10 1. Because the Respondent is not engaged in the business of buying or selling oil lands and the assessment is not based on any profit made on the sale.
2. Because if the royalty is a reservation it is a part of the original capital and is merely being realised: and if there had been no reservation the purchase price would have been increased and any such increase in consideration would not differ in principle from the consideration actually received, namely, cash and shares which it is admitted are not taxable.
- 20 3. Because, if the royalty is not a reservation it is part of the consideration for the sale of the land and is not distinguishable in principle from money and shares.
4. Because the provision for a royalty was obviously a device agreed upon by the vendor and purchaser for the purpose of arriving at a fair consideration for the sale, the actual value of the said lands being unknown until production was obtained and depending on the amount of production.
- 30 5. Because any consideration for the sale is, irrespective of the nature thereof, a mere conversion of capital from one form to another.
6. Because on the facts of the case and the application of the law thereto the Respondent is not liable in respect of the assessment.
7. Because the Judgment of the Supreme Court of Canada is right.

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H. S. PATTERSON.

HORACE DOUGLAS.

APPENDIX.

STATUTES OF CANADA 1917 (7-8 GEO. V.).

CHAP. 28.

An Act to authorise the levying of a War Tax upon certain incomes.
(Assented to 20th September, 1917).

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"Income."

3. (1) For the purposes of this Act, "income" means the annual net profit or gain or gratuity, whether ascertained and capable of computation 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; * * * * * and also the annual profit or gain from any other source; * * * * * with the following exemptions and deductions :—

(a) such reasonable allowance as may be allowed by the Minister for depreciation, or for any expenditure of a capital nature for renewals, or for the development of a business, and the Minister, when determining the income derived from mining and from oil and gas wells, shall make an allowance for the exhaustion of the mines and wells;

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STATUTES OF CANADA, 1919, (9-10 GEO. V.).

CHAP. 55.

An Act to amend The Income War Tax Act, 1917.

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(Assented to 7th July, 1919.)

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Income.

2. (1) Subsection one of section three of the said Act is amended by inserting after the word "be" in the ninth line thereof the words "whether derived from sources within Canada or "elsewhere" * * * * *

(2) Paragraph (a) of subsection one of section three of the said Act: paragraph (b) of the said subsection one as enacted by section two of the said statute of 1918, and paragraph (d) of the said subsection one, as amended by section two of the said statute of 1918, are repealed, and the following paragraphs are enacted in lieu thereof :—

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“(a) such reasonable amount as the Minister, in his discretion, may allow for depreciation, and the Minister in determining the income derived from mining and from oil and gas wells and timber limits shall make such an allowance for the exhaustion of the mines, wells and timber limits as he may deem just and fair”;

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REVISED STATUTES OF CANADA 1927 (VOL. 2).

CHAPTER 97.

An Act to authorise the Levying of a War Tax upon Certain Incomes.

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PART. I.

Taxable Income.

Taxable Income Defined.

20 3. For the purposes of this Act, “income” means the annual net profit or gain or gratuity, whether ascertained and capable of computation 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 also the annual profit or gain from any other source * * *

“Income.”

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PART II.

Exemptions and Deductions.

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Deductions and Exemptions Allowed.

5. “Income” as hereinbefore defined shall for the purposes of this Act be subject to the following exemptions and deductions:—

Exemption and Deductions.

40 (a) Such reasonable amount as the Minister, in his discretion, may allow for depreciation, and the Minister in determining the income derived from mining and from oil and gas wells and timber limits shall make such an allowance for the exhaustion of the mines, wells and timber limits as he may deem just and fair;

Depreciations and exhaustion.

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In the Privy Council.

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
Mrs. CATHERINE SPOONER OF
THE CITY OF CALGARY IN THE
PROVINCE OF ALBERTA.

BETWEEN :—

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

— AND —

Mrs. CATHERINE SPOONER
(Appellant) *Respondent.*

RESPONDENT'S CASE.

LAWRENCE JONES & Co.,
Lloyd's Building,
Leadenhall Street,
London, E.C.3.