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Mar. 25

Aug. 27

BETWEEN:

HOME OIL COMPANY LIMITED ..... APPELLANT,

AND

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

Revenue—Income tax—The Income Tax Act, S. of C. 1948, c. 52, s. 11 (1)(b)—Income Tax Regulations, s. 1201—The Income Tax Amendment Act, S. of C. 1949 (2nd S.), c. 25, s. 53 (1)—Allowance in respect of an oil or gas well—Appeal from Income Tax Appeal Board a trial de novo—Act not to be construed by reference to subsequent Act—Meaning of word "well" in s. 11(1)(b) of The Income Tax Act, s. 1201 of the Income Tax Regulations and s. 53 (1) of the Income Tax Amendment Act, 1949—Construction of section permitting deduction—Onus on taxpayer to show entitlement to deduction—Amount of allowance under s-s. (1) of s. 1201 of the Income Tax Regulations fixed by s-s. (4)—"Profits" under s. 1201 of the Income Tax Regulations means aggregate profits from all of taxpayer's wells.

The appellant claimed allowances for 1949 and 1950 under section 11(1)(*b*) of The Income Tax Act and section 1201 of the Income Tax Regulations based on the profits of the oil and gas wells which it operated at a profit on an individual well basis without deducting its exploration, development and other expenditures not related to its profit producing wells, but deducted these expenditures from its gross income under section 53(1) of the Income Tax Amendment Act, 1949 in computing its income for the purposes of The Income Tax Act. The Minister in computing the appellant's profits for the purpose of section 1201 of the Regulations deducted the expenditures which it had not deducted and cut down its allowances accordingly. In assessing

it for 1949 and 1950 the Minister added the amounts which he had disallowed to the amounts of taxable income reported by it on its returns. The appellant appealed to the Income Tax Appeal Board which dismissed its appeals and the appellant appealed from this decision.

Held: That the appeal to this Court from a decision of the Income Tax Appeal Board is a trial *de novo* of the issues involved and it should hear and determine them without regard to the proceedings before the Board and without being affected by any findings made by it. It is not the correctness or otherwise of the decision of the Board or of its reasons for judgment that is before this Court for determination but rather the validity of the assessment appealed against. Consequently, this Court is concerned only with the validity of such assessment and should deal with that question as if there had never been any proceedings before the Board.

2. That in Canada it is not permissible to construe an Act to which the Interpretation Act applies by reference to a subsequent Act unless such subsequent Act directs how the prior Act is to be interpreted.

3. That the word "well" in Section 11(1)(*b*) of The Income Tax Act, section 1201 of the Income Tax Regulations and section 53 (1) of the Income Tax Amendment Act, 1949 should be read as including "wells" and there is no justification for assuming that it was applicable only to wells operated at a profit.

4. That a taxpayer cannot succeed in claiming a deduction from what would otherwise be taxable income unless his claim comes clearly within the terms of the enactment permitting the deduction: he must show that every constituent element necessary to the right of deduction is present in his case and that every condition required by the permitting enactment has been complied with. If he cannot bring his claim within the express terms of the enactment confining the right of deduction he is not entitled to it.

5. That the amount of the allowance to which the appellant was entitled under subsection (1) of section 1201 of the Income Tax Regulations was fixed under subsection (4) by the amount of the expenditures which it deducted under section 53 of the Income Tax Amendment Act, 1949 and that, since it deducted all its exploration and development expenditures under that section, subsection (4) of section 1201 of the Regulations required that the same amount of expenditures must be deducted in computing its profits for the purpose of subsection (1).

6. That the profits contemplated by subsection (1) of section 1201 of the Regulations are the aggregate, over-all profits from the production of oil and gas from all the taxpayer's wells.

APPEAL from a decision of the Income Tax Appeal Board.

The appeal was heard before the President of the Court at Calgary.

R. A. MacKimmie for appellant.

H. W. Riley Q.C. and *J. D. C. Boland* for respondent.

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

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THE PRESIDENT now (August 27, 1954) delivered the following judgment:

This is an appeal from the decision of the Income Tax Appeal Board (1), dated February 3, 1954, dismissing the appellant's appeals from its income tax assessments for 1949 and 1950.

The appellant's complaint against the assessments is that in each one the Minister cut down its claim for an allowance under section 11(1) (b) of The Income Tax Act, Statutes of Canada 1948, Chapter 52, and section 1201 of The Income Tax Regulations, as enacted by Order in Council P.C. 6471, dated December 22, 1949. Since the dispute arises from a difference of opinion on the construction of these enactments their precise terms require careful consideration. Section 11 (1) (b) of the Act, as amended in 1949, read 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 tax-payer for a taxation year:

(*b*) such amount as an allowance in respect of an oil or gas well, mine or timber limit, if any, as is allowed to the taxpayer by regulation;

The applicable regulation referred to in this section is set out in section 1201 of the Regulations. The relevant subsections of this section, as it was in force for the years in question, provided as follows:

1201. (1) Where the taxpayer operates an oil or gas well . . ., the deduction allowed for a taxation year is 33⅓ per cent of the profits of the taxpayer for the year reasonably attributable to the production of oil or gas from the well.

(4) In computing the profits reasonably attributable to the production of oil or gas for the purpose of this section a deduction shall be made equal to the amounts, if any, deducted from income under the provisions of section 53 of Chapter 25 of the Statutes of 1949, Second Session, in respect of the well.

The section referred to is section 53 of An Act to Amend The Income Tax Act and the Income War Tax Act, hereinafter called the Income Tax Amendment Act, 1949, or the 1949 Act, Statutes of Canada 1949, Second Session, Chapter 25, of which subsection 1, as amended by section 46 of Chapter 40 of the Statutes of Canada, 1950, read as follows:

53. (1) A corporation whose principal business is production, refining or marketing of petroleum, petroleum products or natural gas or exploring or drilling for petroleum or natural gas may deduct in computing its income, for the purposes of *The Income Tax Act,* the lesser of

(1) (1954) 10 Tax A.B. c. 61.

(a) the aggregate of the drilling and exploration costs, including all general geological and geophysical expenses, incurred by it, directly or indirectly, on or in respect of exploring or drilling for oil and natural gas in Canada
(i) during the taxation year, and
(ii) during previous taxation years, to the extent that they were not deductible in computing income for a previous taxation year, or

(b) of that aggregate an amount equal to its income for the taxation year
(i) if no deduction were allowed under paragraph (b) of subsection one of section eleven of the said Act, and
(ii) if no deduction were allowed under this subsection,
minus the deduction allowed by section twenty-seven of the said Act.

In the notice of appeal herein as well as during the hearing before me the allowance claimed by the appellant was called a depletion allowance but it should be noted that neither in the Act nor in Regulations is there any reference to it as a depletion allowance. The use of the expression is a loose one.

The parties are in agreement on the facts. The appellant, which has its head office in Calgary, was at all relevant times principally engaged in exploring for and producing petroleum and natural gas and operated oil and gas wells. During the years 1949 and 1950, as well as in other years, it made expenditures in its exploration for oil and natural gas, with some "dry holes" resulting. A "dry hole" meant a hole or excavation in the ground drilled by or on behalf of the appellant in the hope of finding oil or natural gas but where either no oil or natural gas was found or it was not found in sufficient quantities for profitable production.

In its income tax return for 1949 the appellant claimed an allowance under section 1201 of the Regulations of $796,023.22, being 33⅓ per cent of $2,388,069.65, which it considered as its net profits for the year reasonably attributable to the production of oil and gas from the wells operated by it at a profit. In computing these profits it did not deduct its exploration and development expenditures not related to its profit producing wells, including its expenditures on dry holes, a proportion of its general and administrative expenses which it claimed was related to its unproductive wells and its losses from wells operated by it at a loss. The amount of the expenditures which it did not deduct came to $1,424,040.06. The details of how this

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amount was arrived at are given in a statement forming part of the agreement as to facts filed as Exhibit 1. In its income tax return for 1950 the appellant claimed an allowance of $981,738.41, being 33⅓ per cent of $2,945,215.23, which it considered as its net profits for the year reasonably attributable to the production of oil and gas from the wells operated by it at a profit. In computing these profits it did not deduct its exploration and development expenses not related to its profit producing wells, including its expenditures on dry holes. The amount of the expenditures which it did not deduct came to $132,324.94.

It should be noted, however, that, although the appellant did not deduct the exploration and development expenditures referred to in computing its profits for the purposes of section 1201 of the Regulations it did deduct these expenditures from its income under section 53 of The Income Tax Amendment Act, 1949 in computing its income for the purposes of The Income Tax Act.

The Minister, on the other hand, in computing the appellant's profits for the purpose of determining the allowance to which it was entitled deducted the expenditures which it had not deducted and found that it was entitled to an allowance of $321,343.20 for 1949, instead of $796,023.22, and of $937,630.10 for 1950, instead of $981,738.41. In assessing the appellant for the said years the Minister added the amounts which he had disallowed to the amounts of taxable income reported by it on its returns.

The appellant objected to the assessments and appealed to the Income Tax Appeal Board which dismissed its appeals. It is from this decision that the appeal to this Court is brought.

The issue in the appeal turns on how the profits on which the allowance permitted by section 1201 of the Regulations should be computed and, more particularly, what expenditures should be deducted in computing such profits.

Before I deal with the actual dispute herein I have some preliminary remarks to make. In *Goldman* v. *Minister of National Revenue* (1) I held that the appeal to this Court from a decision of the Income Tax Appeal Board is a trial *de novo* of the issues involved. In that case I dealt at length with the reasons which led me to this conclusion and

(1) [1951] Ex. C.R. 274 at 281.

need not repeat them here. There is, I think, general acceptance of this opinion notwithstanding the anomaly that in this Court the parties may put forward a different case from that presented to the Income Tax Appeal Board. *Vide* also *Minister of National Revenue* v. *Simpson's Limited* (1). The hearing before this Court being thus a trial *de novo,* it should hear and determine the issues without regard to the proceedings before the Board and without being affected by any findings made by it. It is not the correctness or otherwise of the decision of the Board or of its reasons for judgment that is before this Court for determination but rather the validity of the assessment appealed against. Consequently, this Court is concerned only with the validity of such assessment and should deal with that question as if there had never been any proceedings before the Board. It seems to me that this must follow from the finding that the appeal to this Court is a trial *de novo.*

There is one other preliminary observation to make. It appeared in the course of the argument that section 1201 of the Regulations was amended in 1951. But we are here concerned with the section as it was in force in 1949 and 1950 and it is not permissible to interpret it in the light of its amendment. I have had occasion to consider this question in a number of cases and am firmly of the opinion that, whatever may be the rule in other countries, in Canada it is not permissible to construe an Act to which the Interpretation Act applies by reference to a subsequent Act unless such subsequent Act directs how the prior Act is to be interpreted: *vide Morch* v. *Minister of National Revenue* (2); *Luscar Coals Ltd.* v. *Minister of National Revenue* (3); *Mountain Park Coals Limited* v. *Minister of National Revenue* (4) and *The Queen* v. *Specialties Distributors Limited* (5). In this case, therefore, section 1201 of the Regulations must be read without regard to its amendment in 1951.

I now come to the specific issue in the present case. Counsel for the appellant argued that it was entitled to an allowance based on the profits of the wells which it operated at a profit on an individual well basis. He built his whole

(1) [1953] Ex. C.R. 93.
(2) [1949] Ex. C.R. 327 at 338.
(3) [1949] Ex. C.R. 83 at 90.
(4) [1952] Ex. C.R. 560 at 565.
(5) [1954] Ex. C.R. 535.

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case on the use of the word "well" in the singular in the relevant enactments. In section 11 (1) (b) the allowance was described as an allowance in respect of *an oil or gas well.* In section 1201 (1) of the Regulations it was provided that the deduction was allowed where the taxpayer operates *an oil or gas well* and the amount of the allowance was 33⅓ per cent of the profits reasonably attributable to the production of oil or gas from *the well.* And in section 1201 (4) there was a reference to the amounts deducted under section 53 of the Income Tax Amendment Act, 1949 in respect of *the well.* The submission was that by the use of the word "well" in the singular Parliament intended that the allowance should be based on the profits reasonably attributable to the production from each well, that, consequently, the only wells to be considered were those that the appellant operated at a profit, that in the case of each of such wells the profits reasonably attributable to the production of oil or gas from it should be computed by charging against the gross receipts from it the expenditures attributable to it, that the appellant was entitled to an allowance for each well based on the profits so ascertained and that the same procedure should be followed for each well operated at a profit. It was urged that if Parliament had intended that the profits should be those of the taxpayer's whole operations in oil and gas production and exploration it could easily have said so by using the word "wells" in the plural, that its deliberate use of the word "well" in the singular made it clear that the profits were to be computed on an individual well basis. It was also argued that the grant of the allowance in cases "where the taxpayer operates an oil or gas well" clearly excluded from the computation of the profits "reasonably attributable to the production of oil or gas from the well" all expenditures attributable to "dry holes" since it could not be said that the taxpayer operated such holes. Consequently, it was said, the appellant was justified in computing its profits for the purpose of section 1201 of the Regulations in excluding from its deduction of expenditures all expenditures that were attributable to dry holes or wells that were not operated at a profit. On this basis the appellant arrived at its profits of $2,388,069.65 for 1949 and $2,945,215.23 for 1950 and its claims for an allowance of $796,023.22 for 1949 and $981,738.41 for 1950.

The Minister, on the other hand, took the position that the profits of the appellant contemplated by section 1201 of the Regulations were its profits reasonably attributable to the production of gas and oil from all its wells, that in computing such profits all its development and exploration expenditures, even those attributable to dry holes, and its losses on unprofitable wells should be deducted and that, in any event, the amount of the expenditures to be deducted should be equal to the amount of the expenditures deducted by it under section 53 of the Income Tax Amendment Act, 1949 in computing its income for the purposes of The Income Tax Act. On this basis the profits of the appellant as claimed by it were reduced by deducting therefrom the amounts of the expenditures which it had not deducted, namely, $1,424,040.06 for 1949 and $132,324.94 for 1950 and the allowances claimed by it were correspondingly reduced by 33⅓ per cent of these amounts.

While the argument advanced for the appellant seems at first to be plausible I have no hesitation in rejecting it.

There is no substance in the contention that because Parliament used the word "well" in the singular it intended that a taxpayer should be able to claim an allowance under section 1201 of the Regulations on the basis submitted by the appellant. The use of the word in the singular does not settle the matter in favor of the appellant for it is provided by section 31 (j) of the Interpretation Act, R.S.C. 1927, Chapter 1, that in every Act, unless the contrary intention appears, words in the singular include the plural and words in the plural include the singular. There are numerous instances in The Income Tax Act where this rule applies and it is, in my opinion, applicable in the present case. Indeed, the appellant's construction of the enactments assumes that the word "well" includes "wells", but only the wells operated at a profit. When section 11 (1) (b) of the Act refers to the allowance as being "in respect of an oil or gas well" it is plain that it is not confined to one well and the expression means "in respect of an oil or gas well or oil or gas wells". Nor was it contemplated by section 1201 of the Regulations that the expression "where the taxpayer operates an oil or gas well" should confine its benefit to the operator of a single well. The expression was merely descriptive of the kind of taxpayer who was entitled to the

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allowance regardless of whether he operated one well or more than one. Nor does the reference in section 1201 to the profits as being those reasonably attributable to the production of oil or gas from the well support the appellant's case. The word "well" in the singular was used because it was grammatically consequential to the use of the singular in the earlier part of the section but the purpose of the expression was to make sure that there should be no allowance on profits that were not attributable to oil or gas production such as, for example, profits from bonds or investments or other sources apart from oil production. The allowance was to be $33\frac{1}{3}$ per cent of the profits of oil production. The use of the expression "in respect of the well" in subsection (4) of section 1201 of the Regulations was for a similar purpose in respect of the income there referred to. There was, in my opinion, nothing in any of the enactments to justify the construction placed on them by the appellant. In my judgment, the word "well" in section 11 (1) (b) of The Income Tax Act, section 1201 of the Income Tax Regulations and section 53 (1) of the Income Tax Amendment Act, 1949 should be read as including "wells" and there is no justification for assuming that it was applicable only to wells operated at a profit.

But there is a much stronger reason for rejecting the appellant's submission. Counsel urged that effect should be given to the plain words of section 1201 of the Regulations and that the appellant's tax liability should be limited accordingly. But section 1201 is not a charging section so that the admonition that there is no tax liability unless the tax is imposed by clear and express terms has no application. On the contrary, the section confers a benefit on the taxpayer to which he would not be entitled apart from it. Such a section should be construed in the same way as an exempting provision of a taxing act. In *Lumbers* v. *Minister of National Revenue* (1) I put the rule of construction of an exempting provision of the Income Tax Act in the following terms:

> A taxpayer cannot succeed in claiming an exemption from income tax unless his claim comes clearly within the provisions of some exempting section of the Income War Tax Act: he must show that every constituent element necessary to the exemption is present in his case and that every condition required by the exempting section has been complied with.

(1) [1943] Ex. C.R. 202 at 211.

Similarly, a taxpayer cannot succeed in claiming a deduction from what would otherwise be taxable income unless his claim comes clearly within the terms of the enactment permitting the deduction: he must show that every constituent element necessary to the right of deduction is present in his case and that every condition required by the permitting enactment has been complied with. If he cannot bring his claim within the express terms of the enactment conferring the right of deduction he is not entitled to it: *vide W. A. Sheaffer Pen Company Limited* v. *Minister of National Revenue* (1).

The onus is thus on the appellant to show that its claim comes clearly within the terms of section 1201 of the Regulations. It is not enough to look at subsection (1) by itself and rely exclusively on the use of the word "well" in the singular in support of the appellant's contention. The amount of the allowance to which it was entitled must be considered in the light of the section read as a whole. When it is so read it becomes clear that the appellant cannot bring its claims within the ambit of section 1201 for subsection (4) defines what deduction of expenditures must be made in computing the profits referred to in subsection (1) and the appellant has not made the required deduction. Subsection (4) specified that in computing the profits referred to in subsection (1) the deduction that was to be made should be equal to the amount of the expenditures deducted from income under section 53 of the Income Tax Amendment Act, 1949. The amount of the allowance to which the appellant was entitled was thus fixed by the amount of the expenditures which it deducted under section 53 of the 1949 Act. Since it took advantage of the right of deduction conferred by this section and in computing its income for the purposes of The Income Tax Act deducted all its exploration and development expenditures, including the amounts of $1,424,040.06 for 1949 and $132,324.94 for 1950, which it did not deduct in computing its profits for the purpose of subsection (1) of section 1201, subsection (4) required that the same amount of expenditures must be deducted in computing its profits for the purpose of subsection (1). The appellant was certainly not entitled to have the benefit of the deduction permitted by section 53 of

(1) [1953] Ex. C.R. 251 at 255.

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the 1949 Act in computing its income for the purposes of The Income Tax Act and at the same time ignore the requirement of subsection (4) of section 1201 of the Regulations in computing the profits on which its allowance was to be based.

Two observations remain to be made. The requirement of subsection (4) of section 1201 that the deduction of expenditures must equal the amount of the deduction under section 53 of the 1949 Act rejects the idea of computation of profits under subsection (1) on an individual well basis for there is no machinery under section 53 of the 1949 Act for the computation of income on such a basis. Thus the profits contemplated by subsection (1) are the aggregate, over-all profits from the production of oil and gas from all the taxpayer's wells. Subsection (4) thus confirms the view that the word "well" in the singular includes the plural.

Counsel for the appellant sought comfort in the concluding words of subsection (4) of section 1201 of the Regulations, namely, "in respect of the well". But the purpose of that limitation is similar to that of the limitation in subsection (1) to which I have referred, namely, that the deduction required to be made for the purpose of determining the profits from oil production, excluding the profits from other sources, should be the same as that made in computing the income from oil production. There might be other deductions to which a taxpayer was entitled in respect of income from sources other than oil production but such deductions were to be excluded in the computation of the profits from oil production on which the allowance was to be based.

If the amounts of the expenditures which the appellant did not deduct in computing its profits under subsection (1) of section 1201 of the Regulations were deducted, as they should have been, the profits would be reduced to those on which the Minister based the allowances which he permitted. The Minister was, therefore, right in assessing the appellant as he did.

Consequently, since the appellant has failed to show any error in the assessments appealed against the assessments stand and the appeal herein must be dismissed with costs.

Judgment accordingly.