BETWEEN:

HARRY C. McLAUGHLIN.....APPELLANT;

AND

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

1952

Mar. 26

Mar. 28

Revenue—Income Tax—Income War Tax Act, R.S.C. 1927, c. 97, ss. 3, 32(2) —Transfer of property from husband to wife—Words of s. 32(2) both precise and unambiguous—Meaning of "substituted property"—Language used in s. 32(2) so explicit as to exclude suggestion it means only substitution made by transferor or those contemplated by transferor and transferee at time of original transfer—Meaning of the words "as if such transfer had not been made"—S. 32(2) does not provide basis of liability to continue to be on the income as it existed at time of transfer—Appeal from decision of Income Tax Appeal Board dismissed.

In 1939 the appellant transferred to his wife 400 preferred shares of McCaskey Systems Ltd. as a gift, but having been assessed and having paid tax on dividends paid by the company on these shares the appellant agreed with his wife to revoke the gift and the wife purchased the same shares for which she gave a promissory note for $40,000 to her husband. Because of the admission made by the appellant that this agreement in no way affected his liability to tax on income derived from such shares the Court was not called upon to determine whether or not a bona fide sale of property from husband to wife is within s. 32(2) of the Income War Tax Act. In 1942 one C. sold to the appellant 500 common shares of Whitehall Machine and Tools Ltd., part of the consideration therefor to C. being the 400 preferred shares of McCaskey Systems Ltd. that the appellant's wife transferred to C. in exchange of 400 shares of the Whitehall stock. In 1948 the appellant's wife received $30,000 in dividends on these 400 shares, which amount was added to the appellant's declared income for 1948, on the ground that it was taxable as part of his income as being "income derived from property substituted for that which he had transferred to her in 1939". The appellant appealed to the Income Tax Appeal Board which dismissed his appeal.

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Held: That the words of section 32(2) of the Income War Tax Act, R.S.C. 1927, c. 97 are both precise and unambiguous. "Substituted property" means that property which replaces, or takes the place of, that property which was originally transferred.

2. The language used in the section is so explicit as to exclude the suggestion that it can mean only substitutions made by the transferor or substitutions contemplated by the transferor and transferee at the time of the original transfer. To limit the interpretation in that manner would make it necessary to read into the section words which Parliament has not seen fit to include, nor intended should be included.

3. That by virtue of section 32(2) the appellant was liable to be taxed in respect of that income "as if the transfer to his wife had not been made".

4. That the provisions in section 32(2) of the Act that the transferor shall be liable to be taxed "as if such transfer had not been made", means that he shall be liable to be taxed as though the property transferred or that which was substituted for it, were his property and not that of the transferee.

5. That section 32(2) of the Act also means that, while the property originally transferred remains in its original form, the income therefrom shall be taxable as income in the hands of the transferor, but that, if other property be substituted therefor, then the income from such substituted property shall be taxable as income in the hands of the transferor.

APPEAL from the decision of the Income Tax Appeal Board dismissing the appellant's appeal against his 1948 assessment.

The appeal was heard before the Honourable Mr. Justice Cameron at Toronto.

E. Bristol, Q.C. for appellant.

J. de N. Kennedy, Q.C. and *J. E. Jackson* for respondent.

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

CAMERON J. now (March 28, 1952) delivered the following judgment:

This is an appeal from a decision of The Income Tax Appeal Board dated August 28, 1951, by which that Board dismissed the appellant's appeal from a Notice of Assessment dated June 30, 1950, for the taxation year 1948.

In that Notice of Assessment, the respondent had added to the appellant's declared income, the sum of $30,000, which amount was received by the appellant's wife—and

not by the appellant personally—by way of dividends on certain shares under the circumstances presently to be mentioned.

It may be noted here that the appellant, under protest, has paid the full amount of the assessment, including interest accrued.

In 1939 the appellant, a resident of Galt, Ontario, was vice-president of McCaskey Systems, Ltd. From the Statement of Facts contained in the notice of appeal to this court, it is shown that on January 24, 1939, the appellant transferred from his own name to that of his wife 400 preferred shares of McCaskey Systems, Ltd., such transfer being made as a gift, the purpose being to bring about a possible savings in succession duties for his estate, if he should survive the statutory period.

It is also shown that, in 1939, that company paid a substantial dividend representing accumulated arrears on its preferred shares and under section 32, of subsection 2, of The Income War Tax Act, the appellant was assessed for and paid tax thereon as though he had personally received such dividend.

In view of that situation, that is, that the appellant was required to pay income tax on the stocks which he had transferred to his wife, the appellant and his wife agreed verbally to revoke the earlier gift, and his wife agreed to purchase the same shares from the appellant at their par value of $100. As a result thereof, his wife gave to the appellant her promissory note dated April 15, 1940, for $40,000 payable on demand and without interest. Exhibit "B" is an agreed copy of that note.

Section 32, subsection 2 of The Income War Tax Act, Revised Statutes of Canada 1927, chapter 97, as it was from 1927 to December 31, 1948, was as follows:

> 32(2). Where a husband transfers property to his wife, or vice versa, the husband or the wife, as the case may be, shall nevertheless be liable to be taxed on the income derived from such property or from property substituted therefor as if such transfer had not been made.

Certain other facts will be later referred to, but I considered it advisable to quote the section at this point because of certain admissions made at the hearing.

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Counsel for the appellant, for the purposes of this case only, has admitted

(*a*) that had nothing further occurred beyond the facts which I have above stated, the transaction would have fallen within the provisions of Section 32, subsection 2, and the appellant would have been personally assessable to tax on dividends received by his wife from the 400 shares of McCaskey stock so transferred to her: and

(*b*) that the agreement with his wife to revoke the original gift, and to sell the shares to her for $40,000 in no way affected the appellant's liability to tax on income derived from such shares, inasmuch as he was satisfied that the word "transfer" was wide enough in its meaning to include a "sale" for value.

Because of that admission I am relieved of the necessity of determining whether or not a bona fide sale of property from husband to wife is within Section 32, subsection 2.

There were certain other occurrences, however, on which the appellant relies.

A short time prior to April 11, 1940, the appellant heard that one, A. G. Colvin, was desirous of selling his controlling interest in Whitehall Machine & Tools Limited. He felt that, if he could gain control, and bring Whitehall under his own efficient management, it would turn out to be a successful investment. Negotiations to that end were entered upon, and in the result Colvin and the appellant entered into an agreement on April 11, 1940—Exhibit "A". By that agreement Colvin agreed to sell, and the appellant to purchase, 500 shares, fully paid common stock of Whitehall. The consideration payable therefor to Colvin was 400 shares of the 7 per cent cumulative preferred stock of McCaskey Systems Ltd. and $35,000 payable as therein provided. The appellant, however, then owned no preferred stock in McCaskey. He states that, in agreeing to convey 400 such McCaskey shares to Colvin, he was acting on behalf of and with the approval of his wife, and that it was her 400 shares in McCaskey that were to be transferred to Colvin. He states also that, when his wife heard of the negotiations with Colvin, she desired to participate therein, and that she insisted that she receive an equal

number of Whitehall shares for her 400 McCaskey shares. Presumably this agreement between the appellant and his wife was arrived at prior to April 11, 1940, the date of the agreement with Colvin, and, therefore, before the date of the note—Exhibit "B".

A disagreement arose between Colvin and the appellant, the details of which are not here of importance. After a long period of litigation, the agreement of April 11, 1940, was specifically carried out in June, 1942. At that time Colvin received Mrs. McLaughlin's 400 preferred McCaskey shares, together with dividends which had accrued, and the balance of the expressed consideration. Mrs. McLaughlin received 400 shares of Whitehall stock, the remaining 100 shares going to the appellant or his nominee.

Under the appellant's management Whitehall apparently prospered, but no dividends were paid on its stock until December, 1948, when Mrs. McLaughlin received $30,000 in dividends on her 400 shares.

It was the amount of that dividend which was added to the appellant's declared income for 1948, on the ground that it was taxable as part of his income, as being "income derived from property substituted for the property which he had transferred to her in January, 1939."

It is shown that, in December 1949, the note given by the appellant's wife to him, was paid in full, together with one year's interest. I do not think, however, that that fact is of any importance in this case in view of the admissions made, nor do I think it is of any importance to determine in this case the precise value of the 400 McCaskey shares which Mrs. McLaughlin received from the appellant, or the value of the 400 Whitehall shares which she got in exchange therefor.

The sole point I am called upon to decide is whether the sum of $30,000 was properly added to the appellant's income.

The submissions on behalf of the appellant may be best expressed by quoting a portion of his Notice of Appeal.

Paragraph 2 of the reasons are as follows:

2. (a) The Income War Tax Act does not, by Section 32 or otherwise, in clear and express terms impose a tax upon the appellant in respect of income derived by his wife from the Whitehall Company shares substituted for the McCaskey shares transferred to her by the appellant unless it is

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shown that the appellant at the time or by the terms of the transfer from him to her was a party to such substitution:

(*b*) The uncontradicted evidence clearly establishes that the said substitution took place long after the transfer of the McCaskey shares from the appellant to his wife, and was not contemplated by either of them at the time of said transfer, that said substitution was made by the wife as her own act, and that the appellant was not a party thereto:

(*c*) If the word "substituted" in Section 32(2) does not mean substituted by the husband or by agreement with the husband made at or before the time of transfer, it would mean that the husband might be liable over an indefinite period and even after the death of his wife, in respect of any number of substitutions made by her or her personal representatives or heirs.

In support of this submission, there is cited the case of *Attorney General* v. *Eyres* (1). That was a case under the English Succession Duty Act, 1853, in which the Court was called upon to determine whether the compensation payable to a substituted trustee of a trust settlement was a disposition of property "by way of substitutive limitation". With respect, I do not think that the interpretation placed on the words "substitutive limitation" under that English Act, affords any guide to the meaning of the words "or from property substituted therefor" as found in Section 32, subsection 2 of the Income War Tax Act.

In the case of *Commissioners* v. *Pemsel* (2), Halsbury, Lord Chancellor, stated in a few words the basic principle to be applied in the interpretation of Statutes, where, at page 543, he said:

> The only rule for the construction of Acts of Parliament is, that they should be construed according to the intent of the Parliament which passed the Act.
>
> If the words of the Statute are in themselves precise and unambiguous, then no more can be necessary than to expound those words in their natural and ordinary sense. The words themselves alone do in such cases best declare the intention of the law-giver.

That precept of the Lord Chancellor is, in my view, particularly appropriate to the circumstances of this case, for, in my opinion, and so far at least as this problem is concerned, the words of Section 32, subsection 2 are both precise and unambiguous. The subsection provides, in the clearest terms, that, when a husband transfers property to his wife, or vice versa, the transferor shall be liable to be taxed on the income derived from the property so transferred, or, if other property be substituted for that originally

(1) (1909) 1 K.B. 723. (2) (1891) A.C. 531 at 543.

transferred, then upon the income derived from such substituted property. "Substituted property" means that property which replaces, or takes the place of, that property which was originally transferred. In my view the language used is so explicit as to exclude the limitations suggested by the appellant, namely, that it can mean only substitutions made by the transferor or substitutions contemplated by the transferor and transferee at the time of the original transfer. To limit the interpretation in the manner suggested, it would be necessary to read into the section words which Parliament has not seen fit to include, and which I do not think it intended should be included.

The intent of the subsection is clearly discernible, namely, that the national revenue to be derived from income shall not be lessened by transfers of property between husband and wife. It provides, therefore, that if such a transfer took place, the transferor shall continue to be liable on income arising from the property so transferred "as if such transfer had not been made." No doubt realizing that, if the provision went no further than that, its intention could be completely frustrated by a quick sale or exchange of the property transferred, Parliament did go further, and provided that the same results would follow in respect of income from property substituted for that originally transferred.

Now in this case it is admitted that the 400 McCaskey shares transferred by the appellant to his wife constituted a transfer of property within the provisions of Section 32, subsection 2. The evidence establishes that the 400 shares of Whitehall stock, later received by Mrs. McLaughlin, constituted property substituted for the original property transferred; that the $30,000 received by Mrs. McLaughlin in December, 1948, represented income from such substituted property.

By virtue of the subsection, therefore, the appellant was liable to be taxed in respect of that income, "as if the transfer to his wife had not been made."

A further minor point is raised by the appellant in paragraph 2(*h*) of his reasons, as follows:

> 2. (*h*) In any event, Section 32(2) while saying that the husband is "liable to be taxed on the income derived" from the substituted property, does not state or provide, as in other sections of the Act, that such income shall be deemed to be received by, or deemed to be income of, the husband.

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With that submission I cannot agree.

The subsection provides that the transferor shall be liable to be taxed "as if such transfer had not been made", which means, I think, that he shall be liable to be taxed as though the property transferred or that which was substituted for it, were his property and not that of the transferee. Being his property the income derived therefrom would constitute "income" as defined in Section 3 of the Act.

Finally, it is contended in the alternative, that, if the appellant be liable in respect of any income from the property transferred, it would be limited to the sum of $2,800, that being the annual dividend of 7 per cent payable on the 400 McCaskey shares.

It is pointed out that the subsection provides that the transferor shall be liable to be taxed "as if such transfer had not been made". Those words, however, refer to both situations previously mentioned, namely, the property originally transferred, and to the property substituted therefor. The section does not provide that the basis of the liability shall continue to be on the income as it existed at the time of the transfer. It means merely that, while the property originally transferred remains in its original form, the income therefrom shall be taxable as income in the hands of the transferor; but that, if other property be substituted therefor, then the income from such substituted property shall be taxable as income in the hands of the transferor.

It may be noted that, in the present case, no income was derived from the Whitehall stock for the years 1940 to 1947, and, therefore, the appellant was not liable throughout that period in respect of any income from the property transferred or property substituted therefor.

In my opinion this appeal must fail. The appeal will be dismissed and the assessment affirmed. The respondent is entitled to costs after taxation, and there will be judgment accordingly.

Judgment accordingly.