

1939

BETWEEN:

Oct. 18-20,
23-27.

DOMINION TEXTILE COMPANY }
LIMITED

APPELLANT;

1940

May 13.

AND

THE MINISTER OF NATIONAL }
REVENUE

RESPONDENT.

*Revenue—The Business Profits War Tax Act, 1916, 6-7 Geo. V, Chap. 11—
An Act to revive and amend The Business Profits War Tax Act, 1916,
1 Geo. VI, Chap. 19—The Income War Tax Act, R.S.C. 1927, Chap. 97
—Valuation of capital stock of company under the provisions of The
Business Profits War Tax Act, 1916—Statute not retroactive unless
expressly so provided—Appeals allowed.*

Section 3 of The Business Profits War Tax Act, 1916, imposed a tax upon the profits earned in any business, owned by an incorporated company, in excess of 7 per cent per annum upon the capital employed in such business. The first accounting period thereunder began on January 1, 1915. S. 3 ceased to be in force after December 31, 1920. S. 7 of the Act also provided: (ss. 1) "For the purpose of this Act the capital employed in the business of an incorporated company . . . shall be the amount paid up on its capital stock: (ss. 3) . . . the amount paid up on the capital stock of a company shall be the amount paid up in cash. Where stock was issued before the 1st day of January, 1915, for any consideration other than cash, the fair value of such stock on such date shall be deemed to be the amount paid up on such stock . . . In estimating the value of stock issued for any consideration other than cash, regard shall be had to the value of the assets, real and personal, movable and immovable, and to the liabilities of the company at the date as of which such value is to be determined. In no case shall the value of the stock be fixed at an amount exceeding the par value of such stock: (ss. 4) For the purposes of this Act, the actual unimpaired reserve, rest or accumulated profits, held at the commencement of an accounting period by an incorporated company shall be included as part of its capital as long as it is held and used by the company as capital, and dividends paid during an accounting period shall be considered as a reduction of unimpaired reserve, rest or accumulated profits." S. 13, ss 3 of the Act as amended by Chap. 34 of the Statutes of Canada for the year 1923 reads as follows: "Any person liable to pay the tax shall continue to be so liable and in case any person so liable shall fail to make a return as required by this Act, or shall make an incorrect or false return, and does not pay the tax in whole or in part, the Minister may at any time assess such person for the tax, or such portion thereof as he may be liable to pay, and may prescribe the term within which any appeals may be made under the provisions of this Act from the assessment or from the decision of the Board."

Appellant company was incorporated in 1905. The capital stock of appellant company was issued for a consideration other than cash. It was assessed for business profits tax for the years 1915 to 1919, both inclusive, and for income tax for the years 1920 to 1934, both

inclusive. These taxes were paid by appellant. The company was further assessed in 1937, for the years mentioned, under the authority of Chap 19 of the statutes of Canada for the year 1937, by which The Business Profits War Tax Act, 1916, and all amendments thereto, were revived and the provisions of The Income War Tax Act, R.S.C. 1927, Chap. 97, relating to appeals from assessments thereunder and the procedure connected therewith were made to apply *mutatis mutandis* to and in respect of appeals from assessments made under The Business Profits War Tax Act, 1916, and to the hearing and determination of such appeals. These assessments were confirmed by the Minister of National Revenue from whose decision the company appealed to this Court.

1940
 DOMINION
 TEXTILE CO.
 LTD.
 v.
 MINISTER OF
 NATIONAL
 REVENUE.

The Court found that the fair value of the common shares of the company on January 1, 1915, was their par value; that there should be considered as part of the company's capital for the purposes of The Business Profits War Tax Act, 1916, the sum of \$829,379 65 to the credit of profit and loss account on March 31, 1914, together with \$500,000 put to reserve prior to March 31, 1914, and the further sum of \$759,822 79 which was an additional reserve created by reason of the readjustment of inventory values made by the Department of National Revenue in its 1937 assessments, and now the subject of agreement between the parties; that the sum of \$500,000 put to reserve by the company in the 1919 taxation period as a protection against inventory losses due to an expected decline in the price of raw cotton and which operated as a reduction in the net profits for that period, had been considered and allowed by the taxing authorities and could not now be disturbed.

Held: That the value of the stock issued for a consideration other than cash should be estimated in a practical manner, with due regard to all the circumstances attending its issue, and on a basis not unfair, and perhaps even generous, to the taxpayer.

2. That where common shares issued as fully paid up are supported by net assets approximating their par value and have paid substantial dividends for eight consecutive years, at the same time leaving a substantial sum to the credit of profit and loss, such shares should be valued at their par value for the purpose of ascertaining the amount of capital employed in a business, under the provisions of The Business Profits War Tax Act, 1916.
3. That The Business Profits War Tax Act, 1916, as revived, has no retroactive effect.
4. That since the company made no inaccurate or false return and had fully paid any tax assessed upon it during any of the taxation periods in question, The Business Profits War Tax Act, 1916, s. 13 (3), did not authorize the assessments made by the Minister in 1937 pursuant to the provisions of an Act to revive and amend The Business Profits War Tax Act, 1916, being Chap. 19 of the Statutes of Canada for the year 1937.

APPEALS under the provisions of The Income War Tax Act and of an Act to revive and amend The Business Profits War Tax Act, 1916, from the decision of the Minister of National Revenue.

1940
 DOMINION
 TEXTILE CO
 LTD.
 v.
 MINISTER OF
 NATIONAL
 REVENUE.

The appeals were heard before the Honourable Mr. Justice Maclean, President of the Court, at Ottawa.

W. N. Tilley, K.C. and C. G. Heward, K.C. for appellant.

L. M. Gouin, K.C., B. Bourdon, K.C. and W. S. Fisher for respondent.

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

THE PRESIDENT, now (May 13, 1940) delivered the following judgment:

These are appeals, consolidated, from decisions of the Minister of National Revenue affirming assessments made in 1937 upon the Dominion Textile Company Ltd., hereafter to be referred to as "the Company," under The Business Profits War Tax Act, 1916 (hereafter to be referred to as "the Business Profits Act"), for the years 1915 to 1919, both inclusive, and under The Income War Tax Act for the years 1920 to 1934, both inclusive. The Company had been assessed for the business profits tax and the income tax for the years just mentioned; the said assessments for such taxes were in due course paid by the Company; the assessments herein appealed from were in the nature of revisions of those assessments and it will be convenient to refer to them as such even if that be not strictly accurate. The revision of the assessments for the business profits tax purport to have been made under the authority of Chap. 19 of the Statutes of Canada for the year 1937, entitled "An Act to revive and amend The Business Profits War Tax Act, 1916" (hereafter to be referred to as "The 1937 Act"), and the Business Profits Act, and the revision of the assessments for the income tax purport to have been made under the provisions of The Income War Tax Act.

Generally, it is the contention of the Company that it had been already assessed for the business profits tax and the income tax for the respective periods mentioned; that the said taxes were in due course paid and the receipt therefor acknowledged on behalf of the Minister of National Revenue (hereafter to be referred to as "the Minister"); and that there were no grounds of fact or law

for the revision of the assessments for the business profits tax made upon the Company because that tax had already been assessed in conformity with the statute and paid. It is also the contention of the Company that if the Minister is authorized to open up any assessments made under the taxing statutes mentioned and which assessments of the tax had been paid, the Company is, of right, entitled to raise any question of fact or law relative to such assessments, and that does not appear to be contested.

I might observe that the result of the revision of the assessment made in each of the twenty accounting periods mentioned was that in nine accounting periods the Company's assessment was reduced below the amount of the original assessment, and in the remaining eleven periods it was increased.

The inventories of the Company, a manufacturer of textiles, normally consisted of three classes, namely: raw cotton and other raw materials, goods manufactured and goods in process of manufacture, and stores and supplies. The officers of the Minister in revising the assessments in controversy departed from the method pursued by the Company throughout the years in question in valuing its inventories, and they valued such inventories, including goods in process of manufacture, on the basis of the lower of cost or market. The Company, in respect of its raw cotton inventories, followed the method which it had pursued prior to the introduction of the Business Profits Act in 1916, but, as I understand it, a different method was followed in respect of goods in process of manufacture, and, I think, goods manufactured. It is not necessary now to describe the method pursued by the Company in respect of the valuation of its inventories, and I would infer that it makes little difference in practice what reasonable method is adopted provided consistency is observed in the application of the method. Accordingly, the Company's method of valuing its inventories being varied by the Minister in the course of revising the assessments for each of the accounting periods in question, the amount of the capital employed by the Company in its business, the annual profits earned by it, and ultimately the amount of the tax assessed against the Company, would be varied up or down by this change in the method of inventory

1940
DOMINION
TEXTILE CO.
LTD.
v.
MINISTER OF
NATIONAL
REVENUE.
Maclean J.

1940
 DOMINION
 TEXTILE CO.
 LTD.
 v.
 MINISTER OF
 NATIONAL
 REVENUE.
 Maclean J.

valuation. The correctness of the basis employed by the Minister in the revaluation of the Company's inventories, the Company in its notice of dissatisfaction contested, and this issue threatened a protracted inquiry upon the appeals. At an early stage in the hearing of the appeals the parties very properly attempted to agree upon some basis for the valuation of all the Company's inventories, including goods in process of manufacture, for the whole period from March 31, 1915, to March 31, 1934, and in the end an agreement was reached and the same was committed to writing, and it is as follows:

With the approval of the Court, the parties herem agree as follows:

(1) That for the whole period comprising the Appellant's financial years ending March 31st, 1915, to March 31st, 1934, both inclusive, all Inventories of the Appellant, including goods in process, be valued at the lower of cost or market and that, in relation to such inventories, the Respondent's figures as to the market price per pound and the cost price per pound (as shown in column headed "Average Inventory price as adjusted by Dept." in Exhibit No. 1 filed with the Answer of the Respondent) be adopted, the whole without prejudice to and under reserve of all the other contentions of the parties, whether of fact or of law, including but without limiting the generality of the foregoing, the contentions of the parties in regard to the invested capital of the Appellant and the contentions of the parties in regard to the amount of \$500,000 for 1919 mentioned in par. 40 of the Answer of the Respondent.

(2) That if the result of the valuation of the inventories on the foregoing basis and of the adjudication of the Court upon the other contentions of fact and of law of the parties is that, in respect of the whole period under review, the Appellant owes any balance of taxes to the Crown, the Appellant will pay such balance forthwith after such valuation and adjudication, and if the result is a credit in the Appellant's favour the amount of that credit will be credited against Income Taxes for years subsequent to 1934. Should any amount be thus found due by the Appellant, it will bear interest at five per cent per annum from August 6th, 1937.

(3) The parties agree that the quantities or volumes of raw cotton, dealt with in the assessments before the Court, include the quantities or volumes mentioned in Exhibit "A," attached hereto and do not include the quantities or volumes referred to in the next succeeding paragraph.

(4) That the quantities of raw cotton in public warehouses in 1927, 1929, 1930, 1931, 1932 and 1934 are not included in the inventories referred to in the immediately preceding paragraph.

It will be seen from this agreement that the inventories of the Company, including goods in process, from March, 1915, to March, 1934, both inclusive, are to be valued at the lower of cost or market, but without prejudice to all the other contentions raised by the parties, whether of

fact or of law, including the contentions of the parties in regard to the invested capital of the Company, and in regard to the amount of \$500,000 mentioned in paragraph 40 of the Answer of the Respondent. I was led to expect that the parties would be able to agree in the result of the valuation of the inventories upon the basis indicated in the agreement, and there should be no reason for their not being able to do so; however, in the event of the parties failing to agree in the result of a revaluation of the inventories of the Company, on the basis provided by the agreement, I now direct a Reference to the Registrar for that purpose, and the matter of costs of that Reference will be reserved pending the Report of the Registrar. That, for the present at least, will dispose of that issue.

The other questions of fact or law to be decided here have reference to (1) the amount of capital employed by the Company in its business, including unimpaired reserves, rest, or accumulated profits, under the Business Profits Act, (2) whether an amount of \$500,000, put to reserve by the Company in the accounting period of 1919, in view of anticipated losses in raw cotton inventories, was considered and allowed by the taxing officers of the Minister for taxation purposes in the assessment for that period under the Business Profits Act, and if so whether or not that allowance may now be disturbed, and (3) whether the 1937 Act, and the Business Profits Act which the former purports to revive, authorize a reconsideration and revision of any assessment levied against and paid by the Company under the Business Profits Act, in the periods from 1915 to 1919 inclusive. Should I find that the assessments for the business profits tax made upon the Company, for the periods mentioned, cannot be opened up and fresh assessments made, then the questions raised for determination and which I have just above numbered (1) and (2) will disappear, but that will not disturb the results deriving from the revaluation of the inventories under the agreement mentioned. However, I propose discussing and pronouncing upon the first two points, and in the order stated, regardless of the construction to be put upon the 1937 Act and the Business Profits Act, the third point. In the event of an appeal I think it is desirable that I pursue such a course.

1940

DOMINION
TEXTILE Co.
LTD.v.
MINISTER OF
NATIONAL
REVENUE.

Maclean J.

1940
DOMINION
TEXTILE Co.
LTD.
v.
MINISTER OF
NATIONAL
REVENUE.
Maclean J.

It will be desirable to refer to the origin and early history of the Company and it will be convenient to do so at this stage. This is of importance because the favourable development of the financial position of the Company from its inception in 1905 down to January 1, 1915,—the latter an important date, as will later appear—enters into one or more of the issues here to be decided. This requires a reference to four textile companies, operating, I understand, chiefly in the Province of Quebec, the control of which concerns was acquired by the Company in 1905 in the manner I am about to relate. Late in 1904 a group of men formed a syndicate for the purpose of making an offer to the shareholders of the four textile companies to purchase their shares in the capital stock of such companies. These four companies were the Dominion Cotton Mills Company Ltd., the Merchants Cotton Company Ltd., the Montmorency Cotton Mills Company Ltd., and the Colonial Bleaching & Cotton Company Ltd. The Syndicate deposited with The Royal Trust Company the sum of \$1,000,000 as evidence of good faith and ability to implement the terms of the offer about to be made. The offer of the Syndicate, made early in 1905, through the agency of the Royal Trust Company, was to purchase the said shares at a stated percentage of their par value, which varied according to the company to which the offer applied, paying for the same in the bonds and preference shares of a new company to be formed, in designated proportions. It was also a term of the offer that the Syndicate would purchase for cash, at their par value, preference shares of the Company to be formed in the total amount of \$500,000, and would also pay to the new company the sum of \$500,000, both of which sums were to be paid out of the \$1,000,000 deposited with the Royal Trust Company. In due course the offer was submitted to the shareholders and the Syndicate acquired a majority of the shares in each of the four companies, or the right to acquire the same, and a new company was formed under the name of the Dominion Textile Company Ltd., the Company herein.

The Syndicate then offered to sell to the Company 24,467 shares of the capital stock of the Dominion Cotton Mills Company Ltd., out of a total issue of 30,336 shares;

14,118 shares of the capital stock of the Merchants Cotton Company Ltd., out of a total issue of 15,000 shares; 9,693 shares of the capital stock of the Montmorency Cotton Mills Company Ltd., out of a total issue of 10,000 shares; and 2,368 shares of the capital stock of the Colonial Bleaching and Printing Company Ltd., out of a total issue of 3,000 shares, all the shares of the said four companies being of the par value of \$100 each, and further to pay to the Company the sum of \$500,000 in cash; in consideration therefor the Company was required to issue, allot and deliver to the Syndicate, or its nominees, 12,222 fully paid-up and non-assessable preference shares of the Company of the par value of \$100 each (in addition to the 5,000 preference shares which the Syndicate was to purchase and pay for in cash, \$500,000), \$2,759,000 of the Company's six per cent twenty-year bonds, and 50,000 of the Company's fully paid-up and non-assessable common shares. The offer of the Syndicate was accepted and in due course carried out. Apparently the \$500,000 which the Syndicate agreed to pay to the Company was treated as part of the consideration for the 50,000 common shares of the Company to be allotted and delivered to the Syndicate. It was so treated in the accounting of the Company, and so described to me by counsel on the hearing of the appeals. Whether that view is in conformity with the agreement between the Syndicate and the Company is doubtful, but that is of little consequence, because, in any event, the Syndicate was to receive, in addition to the bonds and preference shares mentioned, the Company's total issue of common shares, fully paid up and non-assessable, in consideration for the shares in the four old companies to be sold and transferred to the Company, and the total issue of the Company's common shares was transferred to the Syndicate or its nominees.

When the agreement between the Syndicate and the Company had been fully consummated the shareholders of the old companies held the bulk of the Company's senior securities, and the members of the Syndicate all the shares of its capital stock. Thereafter the Company acquired from time to time the balance of the outstanding shares of the four textile companies. Complete ownership of all the shares of the Montmorency Cotton Mills Com-

1940
 DOMINION
 TEXTILE CO.
 LTD.
 v.
 MINISTER OF
 NATIONAL
 REVENUE.
 Maclean J.

1940
 ~~~~~  
 DOMINION  
 TEXTILE CO.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 \_\_\_\_\_  
 Maclean J.

pany Ltd., and the Colonial Bleaching & Printing Company Ltd. was acquired by March 31, 1906, of the Merchants Cotton Company Ltd. by December 31, 1912, and of the Dominion Cotton Mills Company Ltd. by December 22, 1916. By January 1, 1915, the Company had acquired 98 per cent of the issued shares of the Dominion Cotton Mills Company Ltd., and the remaining two per cent was acquired by December 22, 1916.

It was a term of the agreement between the Syndicate and the Company that if the former transferred to the latter a larger amount of the shares in each or any of the four textile companies than that stipulated in the offer of the Syndicate, the Syndicate was entitled to receive an additional amount of the bonds and preferred stock of the Company, proportionate to the additional number of shares so transferred by the Syndicate. As the complete ownership of the shares of each of the four old companies was acquired, the assets and liabilities were taken into the accounts of the Dominion Textile Company Ltd. at the amounts in which they were formerly carried in the accounts of the subsidiary company.

From an exhibit put in evidence on behalf of the Minister it would appear that in 1904 the financial position of the four textile companies mentioned was not very satisfactory. While the four companies showed a combined surplus of \$932,831.72, and a combined net worth of capital and surplus amounting to \$6,770,631.72, yet the net working capital position showed a deficit of some \$108,000, they were each heavily indebted to the banks, and apparently an attempt to bring in fresh capital had proven unsuccessful. The earnings and dividend record of the four companies was not an encouraging one. The Dominion Cotton Mills Company had paid no dividend since 1902, the Merchants Cotton Company none for several years, the Montmorency Cotton Company only one payment of 1 per cent since 1901, and the Colonial Bleaching & Printing Company only one payment of 6 per cent since its incorporation in 1899. During the calendar year 1904 the Dominion Cotton Mills Company had operated for ten months of its fiscal year, as I understand it, at a loss of \$164,000 in round figures; the Merchants Cotton Company at a loss of \$277,000 during twelve months of

operation; the Montmorency Cotton Company at a loss of \$148,000 during five months' operation; and the Colonial Bleaching & Printing Company at a profit of \$477 during a period of nine months' operation. As of March 31, 1905, the combined fixed assets of the four companies were carried in the several balance sheets at \$10,892,706.17, their combined bonded indebtedness was \$4,013,660, and their combined issued capital stock was \$5,837,800.

The Company, having acquired the control of each of the four old companies, through a holding of a majority of shares in each of them, went into operation in April, 1905. It had control of over \$10,000,000 worth of land, buildings and machinery, other assets in a substantial amount, and it had in its treasury a working capital of \$1,000,000 in cash received from the Syndicate; that is to say, \$500,000 from the sale to the Syndicate of 5,000 preference shares, and \$500,000 paid the Company in cash by the Syndicate for the consideration I have already mentioned and explained.

For the fiscal year ending March 31, 1915, the nearest accounting period to January 1, 1915, when it became necessary to estimate the value of the shares of the capital stock of the Company under the provisions of The Business Profits Act, as I shall later explain, the balance sheet of the Company showed the total assets at \$15,276,538.84, which included \$10,775,941.40 for "land, buildings, machinery, stock of the Dominion Cotton Mills Company, and good will"; \$2,295,801.40 for raw cotton, stock manufactured and in process of manufacture, and \$2,239,795.80 in open accounts, cash on hand and supplies, etc., and there was to the credit of profit and loss account \$881,926.30, after payment of interest on bonds, dividends on preference stock, and a dividend of six per cent on the common stock. The Company at that date being in possession of but 98 per cent of the capital stock of the Dominion Cotton Mills Company, a minority interest of two per cent having refused to exchange their shares of the capital stock of that corporation for the securities of the Company, the Company was obliged to put through an arrangement whereby it leased the mills of the Dominion Cotton Mills Company for operating purposes, until such time as all the shares therein were surrendered. It was for this reason

1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

1940  
DOMINION  
TEXTILE CO.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.

that the Company's balance sheet for that year was obliged to reflect this situation by including with land, buildings and machinery, the shares of the capital stock of the Dominion Cotton Mills Company acquired and held by it on the asset side of the balance sheet. The evidence would seem to indicate that the Company gave a book value of approximately \$2,228,000 to "good will." At this time the outstanding bond issue of the Company (including a bond issue of the Montmorency Cotton Mills Company) was \$3,697,775, and its issue of preferred stock was \$1,925,975.

The principal issues to be decided here arise under the provisions of the Business Profits Act. It will be necessary now to refer to the material provisions of that Act which imposed a tax upon the profits earned in any business, in excess of seven per cent per annum upon the capital employed in that business. While the Business Profits Act was enacted in May of 1916 the first accounting period thereunder began on January 1, 1915. Section 3 provided that:

There shall be levied and paid to His Majesty a tax of twenty-five per centum of the amount by which the profits earned in any business exceeded, in the case of a business owned by an incorporated company, the rate of seven per centum per annum, and, in the case of a business owned by any other person, the rate of ten per centum per annum upon the capital employed in such business. Such tax shall be levied against and paid by the person owning such business for each and every accounting period ending after the thirty-first day of December, one thousand nine hundred and fourteen.

Sec. 3 was amended by Chap 6 of the Statutes of Canada, 1917, so as to provide that where the profits exceeded fifteen per centum per annum, the tax was to be fifty per centum with respect to all profits in excess of the said fifteen per centum but not exceeding twenty per centum per annum, and where the profits exceeded twenty per centum per annum the tax was to be seventy-five per centum with respect to all profits in excess of the said twenty per centum. Sec. 3 of the Act ceased to be in force on December 31, 1920, and to this I shall have occasion to refer later.

Sec. 7 relates to the matter of capital and reserves and s.s. (1), (3) and (4) are of importance here, and, as amended, by Chapter 6 of the Statutes of Canada, 1917, and Chap. 10 of the Statutes of Canada, 1918, read thus:

1. For the purpose of this Act the capital employed in the business of an incorporated company having its head office or other principal place of business in Canada shall be the amount paid up on its capital stock.

\* \* \* \*

3. For the purposes of this Act the amount paid up on the capital stock of a company shall be the amount paid up in cash. Where stock was issued before the first day of January, one thousand nine hundred and fifteen for any consideration other than cash, the fair value of such stock on such date shall be deemed to be the amount paid up on such stock; and where stock has been issued since the said first day of January for any consideration other than cash, the fair value of the stock at the date of its issue shall be deemed to be the amount paid up on such stock. In estimating the value of stock issued for any consideration other than cash, regard shall be had to the value of the assets, real and personal, movable and immovable, and to the liabilities of the Company at the date as of which such value is to be determined. In no case shall the value of the stock be fixed at an amount exceeding the par value of such stock.

4. For the purposes of this Act, the actual unimpaired reserve, rest or accumulated profits, held at the commencement of an accounting period by an incorporated company, shall be included as part of its capital as long as it is held and used by the company as capital, and dividends paid during an accounting period shall be considered as a reduction of unimpaired reserve, rest or accumulated profits.

Sec. 7, as amended, makes it clear that "the actual unimpaired reserve, rest or accumulated profits, held at the commencement of an accounting period \* \* \*" shall be included as part of the capital of an incorporated company as long as it is held and used by the company as capital, but any dividend paid during an accounting period shall be considered as a reduction of unimpaired reserve, rest or accumulated profits. This section required, it will be observed, that the common shares of the Company be valued as of January 1, 1915, the beginning of the first accounting period under the Business Profits Act, because such shares were issued for a consideration other than cash. That valuation was necessary in order to determine precisely the amount of capital employed in the business of the Company.

Sec. 10 of the Act required every person liable to taxation thereunder to make a return, on or before the first day of July in each year, to the Minister, in the form prescribed, for each accounting period for which he was liable to taxation. Sec. 11 empowered the Minister to require a further return, or additional information, or the production of account books, invoices, statements, etc., if he so desired. Sec. 13 required the Minister, on or before

1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

1940  
 DOMINION  
 TEXTILE CO.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

the first day of September in each year to determine the amount payable for the tax, and to send by registered mail a notice of assessment to the taxpayer notifying him of the amount payable for the tax. Sec. 13 (3) as originally enacted provided that "any person liable to pay the tax shall continue to be so liable for the period of three years from the time at which such tax would have been payable." This subsection as amended by Chap. 34 of the Statutes of Canada, 1923, reads as follows:

Any person liable to pay the tax shall continue to be so liable and in case any person so liable shall fail to make a return as required by this Act, or shall make an incorrect or false return, and does not pay the tax in whole or in part, the Minister may at any time assess such person for the tax, or such portion thereof as he may be liable to pay, and may prescribe the time within which any appeals may be made under the provisions of this Act from the assessment or from the decision of the Board.

Sec. 9 of the Act provided that the Governor in Council might appoint a Board of Referees, and s. 15 provided that this Board should act as a Court of Revision, and should hear and determine any appeal made by a taxpayer under the Act. Sec. 16 provided that:

Any person objecting to the amount at which he is assessed, or as having been wrongfully assessed, may, personally or by his agent, within twenty days after the date of mailing of the notice of assessment, as provided in section thirteen of this Act, give notice in writing to the Minister in form K of the schedule to this Act that he considers himself aggrieved for either of the causes aforesaid, otherwise such person's right to appeal shall cease and the assessment made shall stand and be valid and binding upon all parties concerned notwithstanding any defect, error or omission that may have been made therein, or in any proceeding required by this Act or any regulation hereunder: Provided, however, that the Minister, either before or after the expiry of the said twenty days, may give a taxpayer further time in which to appeal.

No appeals, during the accounting periods in question, were made by the Company.

One of the questions to be decided here relates to the matter of the amount of capital employed by the Company in its business at the beginning of each accounting period during which the Business Profits Act was in force, and particularly at the beginning of the first accounting period, March 31, 1914, to March 31, 1915. If this is correctly determined as of the beginning of the first accounting period, no difficulty should arise in the following periods as any alterations would involve only subtractions for deductions in the capital employed, or additions on account of sur-

pluses earned and reinvested in the business, less of course any dividends paid out of such surpluses. The determination of the quantum of capital employed in a business, under the Business Profits Act, was always of the greatest importance to the taxpayer because it was to his interest that the capital employed should be computed as high as possible, for the reason that the capital employed was exempt from the business profits tax to the extent of seven per cent thereon, annually. In computing the capital employed by the Company for the first accounting period, from March 31, 1914, to March 31, 1915, it became necessary under the provisions of the Business Profits Act, to estimate the fair value of the shares of the Company's common stock as of January 1, 1915, because they had been issued in 1905 for a consideration other than cash. It was also necessary to ascertain the amount of any "actual unimpaired reserve, rest or accumulated profits" reinvested in the business because, under s. 7 (4) of the Act, the same was to be included as part of the Company's capital. And it is the question of the quantum of capital employed by the Company in its business, in its first accounting period, that I am about to discuss, and this involves a consideration of (1) the fair value of the Company's issued common stock (there being no question as to the preference stock), the shares of which the Company claims should be valued at par, and (2) the quantum of actual unimpaired reserves and accumulated profits used in the Company's business, all as of the beginning of its first accounting period. The amount of the unimpaired reserves and accumulated profits, the Company claims, should include the surplus to the credit of the profit and loss account on March 31, 1914, which, it is claimed, was in the sum of \$829,379.65: the amount of \$500,000 put to a special reserve, "raw cotton reserves," some years prior to the introduction of the Business Profits Act; and the sum of \$759,822.79 which emerges as an addition to the Company's inventory values as of March 31, 1914, resulting from the revaluation of such inventories on the basis now set forth in the agreement between the parties, which addition would increase the amount of the unimpaired accumulated profits employed as capital in the business for the accounting period ending March 31, 1915, and which inventory readjustment is to be found in the Minis-

1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

1940  
 DOMINION  
 TEXTILE CO.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

ter's assessment made in 1937, in practically the same amount as that claimed by the Company. Now, all these items are to be considered in ascertaining the quantum of capital employed in the first accounting period, and the Company claims that these amounts should now be allowed if the assessments made upon it throughout the years mentioned, and paid, are to be opened up and readjusted. When the Company filed its first return, for the period ending March 31, 1915, under the Business Profits Act, it showed, in the form prescribed, its paid-up capital stock to be as follows: preferred stock \$1,925,975, common stock \$5,000,000, and it returned its unimpaired reserve, rest or accumulated profits at \$1,381,926.30, making a total of \$8,307,901.30 for its paid-up capital stock and its unimpaired reserves and accumulated profits. It will be seen therefore that the Company then valued its shares of common stock at par, \$100 each. When the Company was assessed for this period the paid-up capital stock was computed at \$5,675,975, this sum being reached by valuing the issued preference shares at par, and the common shares at \$75 per share, and at that it apparently remained until the assessment made in 1937. Notwithstanding that the Business Profits Act plainly enacted that the unimpaired accumulated profits should be included as part of the Company's capital, this seems to have been entirely disregarded by the taxing authorities when the assessment for the 1915 period came to be made. Any conjecture as to why this was permitted to occur without serious controversy would be unprofitable. So therefore there is now to be considered whether the value of the shares of the Company's common stock should be increased to their par value as claimed, and whether the surplus account, the raw cotton reserve, and the additional reserve created by the inventory adjustments, should be included in the unimpaired accumulated profits and therefore included as part of the Company's capital, all as of the beginning of the first accounting period, April 1, 1914.

I come now to the question as to what was the fair value to be given the fifty thousand common shares of the Company as of January 1, 1915. As already stated, the fair value of the common shares was estimated—arbitrarily, I think, in the first assessment at \$75 per share, the difference between that amount and the par value being \$1,250,000,

which represents the amount in dispute in respect of this point. The Act provided that the fair value of any issued capital stock, on January 1, 1915, should be deemed to be the amount paid up on such stock, if the same had been issued for a consideration other than cash, before that date. In estimating the value of capital stock issued for a consideration other than cash, the Act provided that regard should be had "to the value of the assets, real and personal, movable and immovable, and to the liabilities of the Company," but that would not exclude any other consideration properly applicable to that valuation. The Company was required to state separately in its return, the amount of its unimpaired reserves and accumulated profits, which it did, as I have already stated. All that the first assessment reveals is that the value of the capital stock was fixed at \$5,675,975, which amount was made up by valuing the preference shares then issued at par, and the common shares at \$75 per share. There is nothing to indicate therein that in reaching the value of the capital stock for taxation purposes the amount of any unimpaired accumulated profits was considered at all.

1940  
 DOMINION  
 TEXTILE CO.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

It was the contention of the Company that on the basis of net asset value, including a certain allowance for goodwill, and a 98 per cent interest in the capital stock of the Dominion Cotton Mills Company, less the bonded indebtedness, all other liabilities, and the preference shares, the fair value of the common shares of the Company, on January 1, 1915, would be their par value, \$100 per share, beyond which they could not be valued. The Company's valuation of its common shares, on this basis, was put before me in the form following, and as of January 1, 1915:

|                                                                                                                                          |                |
|------------------------------------------------------------------------------------------------------------------------------------------|----------------|
| Fixed assets and shares in the Dominion Cotton Mills Ld. (representing substantially the mills and equipment owned by that Company)..... | \$8,547,773 00 |
| Goodwill .....                                                                                                                           | 2,228,168 00   |
| Other assets, including inventories valued at not more than market value.....                                                            | 5,787,943 00   |
|                                                                                                                                          | <hr/>          |
| Gross assets .....                                                                                                                       | 16,563,884 00  |
| Deduct, liabilities .....                                                                                                                | 7,468,637 00   |
|                                                                                                                                          | <hr/>          |
| Net assets .....                                                                                                                         | 9,095,247 00   |
| Deduct, preferred shares .....                                                                                                           | 1,925,975 00   |
|                                                                                                                                          | <hr/>          |
| Net value common shares.....                                                                                                             | 7,169,272 00   |
| Net value per share.....                                                                                                                 | 143 40         |



1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

I might add that early in 1915 the fixed assets of the four textile companies ultimately acquired were appraised at \$10,872,133.68 by the Canadian Appraisal Company, and this included only lands, buildings, machinery and mill equipment, allowance being made for depreciation and obsolescence, but nothing for goodwill.

It was also the submission of the Company, that, on the basis of net asset value, but excluding any allowance for the intangible asset of goodwill, which would amount to about \$44 per share, the common shares would have a value only slightly below par, about \$99 per share. I refrain from engaging in a discussion of "goodwill," always difficult of valuation, particularly where there was no specific sale and purchase of "goodwill." In this case goodwill arises from a voluntary writing up of its capital by the Company above the amount which it gave for the assets acquired. However, I am far from saying that the capital assets of the Company were not of a greater value on January 1, 1915, than when they were acquired from the four old textile companies, including the 98 per cent interest acquired in the capital stock of the Dominion Cotton Mills Company at that date, but in my view of the matter it is not necessary to attach any definite value to any "goodwill," in disposing of the point presently under discussion.

It will be proper to look at the dividend record of the common stock of the company. The first common stock dividend was paid in the fiscal year ended March 31, 1908, being at the rate of five per cent. This rate remained in effect for the succeeding four years. In 1913 the common dividend was increased to 5½ per cent, and to 6 per cent in 1914 where it remained during the war years. Interest payments on the bonds and preferred stock were met during the first and subsequent years. In all the years, practically from the beginning of the Company's career, substantial amounts of surplus earnings were held and used in the business to build up reserves, the Company observing the practice of most industrial managements in paying out in dividends only a part of earnings realized, and reinvesting the balance in the expansion or improvements of productive facilities, or for other purposes of the Company. The common shares were quoted on the Montreal

Stock Exchange where they were listed, at an average price of \$82.75 throughout the year 1913 and quotations reached as high as \$89.50 per share in one week of that year. In the year 1914, from January 1 to July 28, the average quotation was \$76.75. On the latter date the Montreal Stock Exchange closed for business and did not reopen until January 25, 1915. It is possible, if not probable, that the war would have a disturbing effect on the market quotations of many listed shares, including that of the Company. In any event stock exchange quotations would not necessarily afford a reliable index of the fair value of the common stock of the Company, as of January 1, 1915.

In my opinion the fair value of the common shares on January 1, 1915, was their par value. The fact that substantial dividends were paid on such shares for the fiscal years 1908 to 1915, both inclusive, is, I think, alone pretty conclusive of the matter, and the net annual earnings were not only ample to pay such dividends but they were sufficient to enable the Company to add substantially to the credit of the profit and loss account, each year. It was not, I think, intended by the Act that the estimated fair value of the common shares should be determined on any narrow basis, or that the same should be ascertained by a meticulous appraisal of gross and net assets. That stock was issued as fully paid up, for what the Syndicate would at the time probably regard as a substantial consideration, in a transaction that could not be said to have been fictitious. I would interpret the Act as meaning that the value of the stock issued for a consideration other than cash should be estimated in a practical manner, with due regard to all the circumstances attending its issue, and on a basis not unfair, and perhaps even generous, to the taxpayer. If common shares issued as fully paid up are supported by net assets approximating their par value, and they have paid substantial dividends for eight consecutive years and at the same time leaving a substantial sum to the credit of profit and loss, as was the case here, that would appear to me to afford ample ground for valuing such shares at their par value for the purpose of ascertaining the amount of capital employed in a business, under the provisions of the taxing statute in question. My conclusion is that the common shares of the Company should

1940

DOMINION  
TEXTILE Co.  
LTD.

v.

MINISTER OF  
NATIONAL  
REVENUE.

Maclean J.

1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

have been valued at par from the beginning of the first accounting period and onwards, under the Business Profits Act.

The other three amounts which I have already mentioned as being claimed by the Company as proper additions to its "unimpaired reserve, rest or accumulated profits," as from the beginning of the first accounting period under the Business Profits Act, and therefore to "be included as part of its capital" under s. 7 (4) of the Business Profits Act for the same period, may, I think, be disposed of in brief terms. The Company contends that if the original assessments made upon it under the Business Profits Act may now be reopened and revised at all, then these amounts are now properly open for adjudication, and I see no successful answer to that contention. First, as to the amount of \$829,379.65. That amount was the balance at the credit of the audited and verified profit and loss account on March 31, 1914, and as such it appears in the annual statement of the Company for the year ending March 31, 1915, but the same was not included as capital in the first accounting period, in either the original or the revised assessment. There is no suggestion that this amount did not represent unimpaired accumulated profits used in the business. I cannot perceive of any sound reason why this amount should not have been included in the computation of the Company's capital, in the accounting period beginning March 31, 1914, and ending March 31, 1915. The Act, in the plainest terms possible, directs that this should be done, and I think it must now be done. And the same thing is to be said regarding the second amount of \$500,000, an amount put to a special reserve apparently some years before the Business Profits Act was enacted. It was an unimpaired reserve, and it was not suggested that at the beginning of the first accounting period and onwards that this amount was not used in the business of the Company; that amount must now, I think, be included as part of the capital of the Company, as at the beginning of the first accounting period, for the purposes of the Business Profits Act.

There is left, then, for consideration the third amount, approximately \$759,822.79. The Minister having adjusted, in the 1937 assessments, the amount allowed as capital

employed by the Company in the original assessment under the Business Profits Act, by adding approximately the sum just mentioned to the inventory values in the first accounting period, and which amount had its genesis in the adoption of the method of valuing the inventories now embodied in the agreement between the parties, it is now claimed that this amount must be included in the capital employed in all the accounting periods under the Business Profits Act. The effect of the stipulated method of valuing the inventories of the Company did, it is agreed, result in an addition to the unimpaired accumulated profits of the Company, as at the beginning of the first accounting period under the Business Profits Act, and it is claimed that this amount must now be considered as part of the Company's capital for the purposes of that Act, and with that I agree.

The three amounts mentioned must therefore, in my opinion, be considered as part of the capital of the Company for the purposes of the Business Profits Act, and these amounts cannot be extinguished or diminished by apportioning any of them, or portions of them, towards the valuation of the preference or common shares, as is suggested to have been done in the second and subsequent assessments under the Business Profits Act; this, in my opinion, could only be done in contravention of the express terms of the Act. There is no suggestion of this having been done in the first assessment, and it may in fact be said that it was not done. The first and last amounts above mentioned may not be strictly accurate though the first would not appear to be open to question; the last-mentioned amount closely approximates the amount mentioned in the assessment of 1937 as being in addition to the inventory values in consequence of the new method adopted for valuing the same. In any event there would not appear to be any reason why the parties should fail to agree upon the figures of the last amount, and the first as well if it should be in dispute. Should the parties fail to agree upon those two amounts they will be treated as falling within the Reference to the Registrar already mentioned, and what I there said as to costs will apply to those matters.

There is another important question for decision. For the accounting period of 1919, under the Business Profits

1940  
DOMINION  
TEXTILE Co.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.

1940  
DOMINION  
TEXTILE CO.  
LTD  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.

Act, the Company put to reserve out of profits the sum of \$500,000, referred to as a raw cotton reserve, in view of apprehended inventory losses chiefly in the next accounting period, and this was an addition to the raw cotton reserve of \$500,000 which I have already mentioned and discussed. It is not, of course, contended that the Company might not do this. It is always recognized that a prudent commercial man may put part of his profits made in one year to reserve, and carry forward that reserve to the next year, in order to provide against an expected or inevitable loss which he foresees will fall upon his business during the next year. The process is a familiar one. In practice, a raw cotton reserve, or any reserve, would be set up by a process of deduction from the inventory values, which would be reflected in the net profits for the accounting period concerned, the same being diminished by the amount put to reserve, but if that reserve were held and used in the business it would form part of the unimpaired reserves or accumulated profits under the Business Profits Act, and would for taxation purposes be considered as part of capital employed in the business. The immediate reason for putting to reserve the amount mentioned here was the imminence and almost certainty of a decline in the Company's raw cotton inventory values in 1920, the year in which the Company would normally make its return for the accounting period of 1919, under the Business Profits Act. I do not doubt that the Company was right in considering that a very substantial loss was inevitable in its cotton inventories in 1920. The price of raw cotton was as high as 42 cents per pound in April, 1920, and soon thereafter deflation set in and by the month of November of the same year it had fallen to about 17 cents. This alone involved an inventory loss of about two and a half million dollars to the Company. In April, 1919, the Company commenced reducing the selling price of its manufactured goods, and it also felt obliged to reduce the invoice prices of goods already sold and delivered, and, I think, the prices of goods under contract for future delivery. This was necessitated by the disturbed state of the raw cotton market. In point of fact this severe decline in cotton inventory values occurred before the Company had been assessed in 1920 for the 1919 period, but after

it had made its return for the 1919 period. Now the problem here is whether this reserve, made in view of apprehended future losses but which had not been suffered in the 1919 accounting period, can be claimed by way of a deduction in profits for the 1919 period.

The Company now claims that the amount of this reserve was upon consideration allowed as a deduction in net profits for the 1919 accounting period and is reflected in the assessment made for that period, and that as the tax was paid on the basis of this assessment it cannot now be disturbed. When the Company made its return for the 1919 period its balance sheet for the same period accompanied the return as was required, but not what is called its "trading account." In the preceding accounting periods it was the practice of the taxing authorities to request of the Company its trading account, some time after the receipt of its return and before proceeding to make the assessment; and the officers of the Company were aware that this would be required of them for the 1919 period, and, as expected, a request was made for the trading account early in November, 1920. With this furnished the taxing authorities would then have before them the Company's return, its balance sheet, and its trading account, for the 1919 period. The Company asserts that the amount in question put to reserve was orally explained to the Minister's principal taxing officers; that an examination of the balance sheet and the trading account would disclose it; that it was by the taxing officers considered and in due course allowed; that the computation of the assessment for the 1919 period included the allowance of this reserve made by the process of a reduction in inventory values and consequently by a deduction in profits for the same amount; that the tax was fully paid shortly after notification of the assessment, and that no question was ever raised concerning the basis of this assessment until 1937, seventeen years thereafter. The Company therefore claims that the assessment was made after a compliance with all the requirements of the statute on its part, after a full disclosure of all the relevant facts concerning the Company's computation of net profits for the 1919 period, and that the same is now binding upon all the parties concerned and is not now open to review.

1940  
DOMINION  
TEXTILE Co.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.

1940  
DOMINION  
TEXTILE CO.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.

It is claimed on behalf of the Minister that the amount in question put to reserve was without the knowledge of the Minister's taxing officers, without disclosure being made to them, and that the same was not knowingly allowed in calculating the assessment; and for such reasons it is claimed that the revision of the original assessment made in 1937 was authorized by the Business Profits Act, and that it properly excluded the allowance of this reserve. This issue would seem to be largely a question of fact, and the facts must therefore be carefully examined.

The Company's balance sheet for the 1919 period would not by itself disclose that \$500,000 had been put to reserve but an examination of that balance sheet along with the trading account for the same period, as seems to have been the usual practice, would do so. The trading account is a document showing on one side the stock of raw material and manufactured goods on hand at the beginning of any period, the additions thereto during the same period, and the working expenses for the whole of the period; on the other side of the trading account there will be shown the amount of goods and merchandise sold during the period, and the amount of raw material, and goods manufactured or in process of manufacture, on hand at the end of the period. At the top of the left-hand side of the trading account in question is to be found the value of the stock of raw cotton and goods manufactured or in process of manufacture, on hand at the beginning of the accounting period, and the working expenses of the period. On the right-hand side of the trading account is to be found the value of goods and merchandise sold during the period, and the value of the stock of raw cotton, and goods manufactured or in process of manufacture, on hand at the close of the accounting period. The difference between both sides of the trading account would indicate the profits for the 1919 accounting period. On the right-hand side of the trading account we find the stock of raw cotton on hand at the end of the period to be valued at \$2,807,754.79. When we turn to the balance sheet for that period we find the raw cotton was valued at \$1,807,754.79, precisely \$1,000,000 less than the value stated in the trading account.

This would show that the raw cotton inventory had been reduced by \$1,000,000, that is, by the addition of the new reserve of \$500,000 to the old reserve of \$500,000 which was set aside sometime prior to 1916, making altogether a raw cotton reserve of \$1,000,000. This addition to the raw cotton reserve would, I think, be obvious to any person conversant with such matters, and who would be obliged to make an examination of the balance sheet and trading account in the course of making the assessment in question. It is difficult to believe that such a person could fail to observe this.

I should point out that the Company in its tax return for 1919 was claiming as a working expense the sum of \$400,000 expended in the reconstruction of a dam at one of the Company's mills, at Magog, P.Q., which had been swept away or damaged, and also a reduction in its raw cotton inventory values in the sum of \$439,943, which amount was based on a reduction of 4 cents per pound in the value of raw cotton on hand, as a provision against possible shrinkage in values. The Company was therefore at this time making three different claims for consideration by the taxing authorities,—that is to say, the addition of \$500,000 to the raw cotton reserve, an allowance of \$400,000 for expenses incurred in the restoration of the Magog Dam, and a reduction in its raw cotton inventories in the sum of \$439,943, in making the assessment against the Company for the 1919 accounting period.

The Company's officers were of the view that it would be necessary for some one to appear before the taxing officers, on behalf of the Company, in order to explain and support the three different matters or claims referred to, and accordingly its General Manager, Mr. Daniels, and its Secretary, Mr. Webb, proceeded to Ottawa in November, 1920. The Company claims that a conference then took place between the Minister's senior taxing officers and those two officers of the Company, and it claims that these three matters were subjects of discussion between such parties, but without any final conclusion then being reached. Within a few days after such conference the Company was notified in writing of the assessment for the 1919 period. The assessment allowed a portion of the

1940  
DOMINION  
TEXTILE Co.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclelean J.



1940  
DOMINION  
TEXTILE CO.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.

claim in respect of the Magog Dam expenditures; it disallowed the item of \$439,000 in respect of the reduction in raw cotton inventories, and apparently assented to the action of the Company in putting to reserve the amount of \$500,000, which had the effect of reducing the net profits for the 1919 period by that amount. The Company accepted the assessment; at least it did not appeal therefrom, and within a week or so the Company paid the amount assessed, and there the matter stood unquestioned until 1937.

There is some evidence upon this point which must be referred to. When Mr. Daniels and Mr. Webb proceeded to Ottawa for the purpose mentioned they took along with them the trading account for 1919, which had been a little earlier requested by the taxing authorities, and without which an assessment could hardly be made, and they then interviewed Mr. Breadner, the Commissioner of Taxation, and Mr. McLaughlin, the Chief Auditor of Taxation. Mr. Breadner and Mr. Daniels are now both deceased, but Mr. Webb appeared as a witness upon the hearing of the appeal, and he testified that he discussed the matter of the expenditures made in connection with the Magog Dam with Mr. McLaughlin alone, and that the latter agreed to a certain disposition of this item, subject however to the approval of Mr. Breadner. Mr. Webb stated that with the Magog Dam item tentatively disposed of, he and Mr. McLaughlin proceeded to the office of Mr. Breadner where they found Mr. Daniels discussing with Mr. Breadner the matter of the \$500,000 reserve, and the item of \$439,000 pertaining to the reduction of 4 cents per pound in the raw cotton inventories. Mr. Webb testified that he heard Mr. Daniels discussing those two items with Mr. Breadner, and that Mr. Breadner in the end promised consideration would be given the same, and so these matters stood over for further consideration. I unreservedly accept the evidence of Mr. Webb, and I might add that he, having taken pension some years ago, is no longer Secretary of the Company. In the end, as I have already stated, when the assessment was made the item of \$439,000 was not allowed. The Magog Dam item was allowed to the extent of \$200,000, it being agreed that a further amount would be

allowed in the next accounting period, and no restoration of the \$500,000 reserve to the Company's assets, or its net profits, for the purposes of taxation, was made or in any way suggested. The Company accepted the assessment to mean that the amount of \$500,000 put to reserve had, for taxation purposes, the approval of Mr. Breadner.

1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.

Maclean J.

In the Company's trading account for 1919, which was left with Mr. Breadner or Mr. McLaughlin on the occasion referred to, there is to be found the notation in pencil: "Carried on Balance Sheet at \$1,807,754.79," and this notation was directed to those figures in the trading account which state the value of the stock of raw cotton on hand at the end of the 1919 period, namely, \$2,807,754.79. There is also the notation: "Increase is caused by addition Cotton Reserve \$1,000,000," which would clearly indicate that the raw cotton reserve had been increased to \$1,000,000, and this would mean that the raw cotton on hand at the end of the period was carried on the balance sheet at \$1,000,000 less than in the trading account; the word "increase" in this notation would indicate that there was an addition of \$500,000 to the old raw cotton reserve. These notations, whoever made them, clearly show that the author was aware of the existence of a raw cotton reserve account, and the addition of \$500,000 to it in the 1919 period, making altogether \$1,000,000. Mr. Tilley contended that these notations were made by Mr. McLaughlin when the assessment for the 1919 period was under preparation, and that the same appeared to be in the handwriting of Mr. McLaughlin. Mr. Sharp, presently Assistant Chief Auditor, thought that these notations were made by him at the time the assessment revisions of 1937 were being considered, which, of course, is quite possible. If these notations were made by Mr. McLaughlin then the contention made on behalf of the Minister that the existence of the reserve in question was unknown to the taxing officers, or that it was ever brought to their attention, would, in my opinion, fall to the ground.

I cannot say that the notations on the 1919 trading account were made by Mr. McLaughlin, in view of the evidence of Mr. Sharp. I cannot form any opinion worth while from a comparison of the handwriting of Mr.

1940  
DOMINION  
TEXTILE Co.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.

McLaughlin and that of Mr. Sharp, such as there is before me. Mr. McLaughlin was not called at the hearing of this appeal, and while he was then no longer in the service of the National Revenue Department, yet he was available to the Minister as a witness. Mr. Tilley openly called my attention to the fact that Mr. McLaughlin was present in Court during the hearing of the appeal, and this remark was not at the time controverted by counsel for the Minister. In the circumstances, I think, Mr. McLaughlin should have been called on behalf of the Minister; he was the only person alive, with the exception of Mr. Webb, who would likely know whether Mr. Breadner had been informed of the reserve in question in the manner related by Mr. Webb, and whether or not Mr. Breadner had considered the same and had directed that it was to enter into the computation of the Company's net profits, for taxation purposes, in the period in question. It is of some significance that on the trading account for the preceding accounting period, 1918, we find the notation, "\$500,000 carried as a secret reserve since prior to taxation period," under which appear the initials of Mr. McLaughlin; this notation would go to show that Mr. McLaughlin was aware of the existence of the old raw cotton reserve in the accounting of the Company, and this he would no doubt ascertain by examining together the trading account and the balance sheet for that period, and he would no doubt then also learn that the balance sheet would show that the raw cotton inventories were carried at \$500,000 below the value stated in the trading account. I think it is therefore not unfair to assume that Mr. McLaughlin would not, in 1919, fail to see that this reserve account had been increased by \$500,000, by the familiar process, when the assessment for the 1919 period was being made. And the evidence would go to show that Mr. McLaughlin would become aware of this addition to the raw cotton reserve account through Mr. Daniels' discussion of the matter with Mr. Breadner; I cannot but believe that he knew it was the subject of discussion between Mr. Breadner and Mr. Daniels, and he would know of Mr. Breadner's final decision in the matter.

On the ground of probability there is, I think, some support for the claim that the amount of the reserve in

question was brought to the attention of the taxing officers for consideration, and that a decision for allowance or disallowance was expected. When the Company made its return in June of 1920, its officers had, as I have already stated, very strong grounds for apprehending a very substantial decline in the value of cotton stocks on hand, and they would, I think, be amply justified in regarding such a decline as inevitable. That would be the situation then confronting most all other large business concerns in Canada, and there is evidence to show that the creation of reserves from profits was then being allowed business concerns by the taxing authorities just to meet that situation, but apparently this was officially approved for taxation purposes only in cases where the reserve was set up in the accounting period in which the inventory losses were actually sustained. In the circumstances it would be probable, and not unexpected, that the Company would make an effort to minimize the effect of its apprehended inventory losses in the manner it did. Moreover, the Company, and other commercial concerns, had reasons for hoping that the Business Profits Act would not remain in force after the accounting period of 1919, and that there would be no further opportunity of putting to reserve out of profits any amount to mitigate the anticipated future losses. The 1919 accounting period was in fact the last under which the Company was taxed under the Business Profits Act, because thereafter its assessment under the Income War Tax Act exceeded any tax exigible under the Business Profits Act, and therefore it was the Income War Tax Act that applied to the 1920 and subsequent accounting periods.

I therefore feel bound to hold upon the material before me that the matter of the reserve in question was brought to the attention of the taxing officers, by officers of the Company, and particularly was it brought to the attention of Mr. Breadner by Mr. Daniels, before the assessment for the 1919 period was made, on the occasion mentioned by Mr. Webb. I have no doubt that if this matter were given favourable consideration by Mr. Breadner the same would be communicated to Mr. McLaughlin before the assessment was made, and that both Mr. Breadner and Mr. McLaughlin would at once realize that to allow this

1940

DOMINION  
TEXTILE CO.  
LTD.

v.

MINISTER OF  
NATIONAL  
REVENUE.

Maclean J.

1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

reserve, for taxation purposes, would involve a corresponding reduction in inventory values, and in the net profits, for the 1919 period. I think it must be assumed that Mr. Breadner decided to allow the amount of this reserve to enter into the Company's computation of profits for the 1919 period, as a provision against anticipated losses in inventories, though not then actually incurred, and which anticipated losses Mr. Breadner would then view as inevitable. Had the amount put to reserve in this period been unknown to Mr. Breadner and his assistants, and had not been put before Mr. Breadner for consideration, it is possible that I would feel obliged to reach another conclusion upon this point, on the ground that the reserve was set up in view of an apprehended future loss which the Company had not actually suffered in the accounting period in which the amount was put to reserve out of profits. The amount of the reserve having been allowed for taxation purposes, and so understood by the Company, as I hold, and the assessed tax having been paid, I think the assessment must now stand and cannot be disturbed. That is my conclusion upon this point.

The final point upon which I am required to make a pronouncement is whether or not the Business Profits Act, as revived, empowered the Minister to reassess the Company for the several accounting periods for which it had already been assessed under that Act. If I conclude that there were no grounds for so doing, then, what I have hitherto said need no longer be considered, except as to any findings of fact which are relevant to the point I am about to discuss. If the assessments made prior to the enactment of the 1937 Act, are not open to review at the instance of the Minister, they are not open to review at the instance of the Company because it never appealed therefrom within the time and in the manner prescribed by the Business Profits Act. This refers only to the assessments made under the Business Profits Act, and would not disturb the terms of the agreement entered into between the parties in respect of the revaluation of inventories, or its intended consequences.

Section 1 of the Act of 1937, entitled "An Act to revive and amend The Business Profits War Tax Act, 1916," reads as follows:

1 Notwithstanding the provisions of sections two and five of chapter sixty-five of the statutes of 1924, entitled "An Act respecting the Revised Statutes of Canada," and the inclusion in Schedule A to the certified printed roll of the Revised Statutes of Canada, 1927, of The Business Profits War Tax Act, 1916, and of the amendments thereto, the said The Business Profits War Tax Act, 1916, and all amendments thereto, are hereby revived and shall have the same force and effect to all intents as if the said Revised Statutes of Canada, 1927, had not come into force and taken effect as law; and all proceedings, transactions, matters or things, had, done, made or completed, or purporting to have been had, done, made or completed under and in accordance with the provisions of The Business Profits War Tax Act, 1916, and the amendments thereto, on or after the first day of February, one thousand nine hundred and twenty-eight, are hereby validated.

1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

Section 2 of this Act repeals the provisions of the Business Profits Act relating to the procedure for appeals from assessments made thereunder, and s. 3 provides for the substitution therefor of certain provisions of the Income War Tax Act, and s. 4 of the 1937 Act provides that sections two and three thereof shall be applicable to all appeals under the Business Profits Act then pending or thereafter instituted. It will be observed therefore that the 1937 Act purports merely to revive the Business Profits Act and to provide a new procedure for appeals from assessments made under that Act, and nothing else. It creates no new duties, obligations or liabilities, so far as the taxpayer is concerned, nor does it deprive him of any legal rights subsisting or acquired under the Business Profits Act, prior to its revival. In other words, the Business Profits Act as revived has no retroactive effect, and could have none unless it contained express words or there were the plainest implication to that effect.

Sec. 1 of the 1937 Act, I might observe, seems to suggest that it was the enactment of the Revised Statutes of Canada, 1927, that terminated the useful life of the Business Profits Act. It seems to me that this result was effected by the enactment of Chap. 10 of the Statutes of Canada, 1924, which provided that s. 3 of the Business Profits Act should not continue in force after December 31, 1920. In the Revised Statutes of Canada, 1927, at the beginning of Volume 5, will be found a table, Appendix 1, giving the "history and disposal" of Acts enacted between 1906 and 1927, and there the Business Profits Tax Act, 1916, is described as "spent," which means that

1940  
 DOMINION  
 TEXTILE CO  
 LTD.  
 v  
 MINISTER OF  
 NATIONAL  
 REVENUE  
 Maclean J.

it had become "obsolete," and "obsolete" is a term applied to laws which have lost their efficacy without being repealed. Therefore it appears to me that if the Act were "spent" it was by reason of Chap. 10 of the Statutes of Canada, 1924, and not because of the Table or Appendix referred to, which was something introduced into the Revised Statutes of Canada, 1927, for historical purposes, and I assume for the sake of convenience as well. However, this is not of any practical importance.

Sec. 1 of the 1937 Act provides that "the Business Profits War Tax Act, 1916, and all amendments thereto, are hereby revived and shall have the same force and effect to all intents as if the said Revised Statutes of Canada, 1927, had not come into force and taken effect as law." One of the amendments to that Act was that enacted by Chap. 10 of the Statutes of Canada, 1924, and s. 1 thereof is as follows:

1. The Business Profits War Tax Act, 1916, and amendments, shall be construed and have effect and be deemed to have had effect since its enactment, without lapse or interruption, as if section twenty-six when first enacted had provided as follows:—

"The provisions of section three of this Act shall not continue in force after the thirty-first day of December, one thousand nine hundred and twenty";

and anything enacted inconsistent therewith shall be deemed to have been superseded, amended or repealed, as the circumstances may require, and all taxes, interest and penalties payable under the said Act and amendments shall remain a tax owing to His Majesty until fully paid and satisfied.

It would appear therefore that while the Business Profits Act was revived, so also was the amendment just recited, the result apparently being that s. 3 of the Act is not now in force. On its face, the 1937 Act has every appearance of a legislative lapse, and the Business Profits Act would seem to be still "spent" and inoperable for taxation purposes as from December 31, 1920. However, it may be that the amendment mentioned is still effective and that s. 3 of the Act is to be regarded as in force, but only in respect of persons who were liable to pay the tax prior to December 31, 1920; this construction is perhaps possible. If by the Act of 1937 it were intended to revive the Business Profits Act and to make it effective as a taxing instrument from the date of its enactment and onwards,

without any limitation as to time, and that by implication the amendment mentioned stands repealed, then it would seem that we have the anomalous and confusing situation that there is presently in force the Business Profits Act and the Excess Profits Tax Act, enacted by Chap. 4 of the Statutes of Canada, 1939, which one can hardly imagine to have been contemplated. However, this point did not arise for discussion on the hearing of the appeal and therefore I have not had the benefit of the views of counsel thereon. I do not intend therefore making any definite pronouncement upon the point, and in my view of the case it is not necessary to do so.

1940  
 DOMINION  
 TEXTILE CO.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.  
 Maclean J.

The only provision of the Business Profits Act, and all amendments thereto, that purports to authorize the assessments here appealed from is, I think, to be found in s. 13 (3) of that Act, and it is the contention of the Company that upon the facts here disclosed this provision of the Act did not authorize, and does not sustain, the assessments in question, and that this alone is conclusive of the whole controversy here. Sec. 13, s.s. (3), as amended by Chap. 34 of the Statutes of Canada, 1923, reads thus:

Any person liable to pay the tax shall continue to be so liable, and in case any person shall fail to make a return as required by this Act, or shall make an incorrect or false return, and does not pay the tax in whole or in part, the Minister may at any time assess such person for the tax, or such portion thereof as he may be liable to pay . . . .

This section originally provided that "any person liable to pay the tax shall continue to be liable for the period of three years from the time at which such tax would have been payable." The limitation of three years was repealed by Chap. 34 of the Statutes of Canada, 1923, and this repeal was made retroactive. But the section as amended still authorizes the Minister, in certain events to assess any person liable for the tax, and in such cases he might prescribe the time within which any appeal might be made from that assessment. The section provides that "in case any person so liable (for the tax) shall fail to make a return as required by this Act, or shall make an incorrect or false return, and does not pay the tax in whole or in part, the Minister may at any time assess such person for the tax, or for such portion thereof as he may be liable to pay . . ." Those words are, I think, to be



1940  
 DOMINION  
 TEXTILE Co.  
 LTD.  
 v.  
 MINISTER OF  
 NATIONAL  
 REVENUE.

construed as meaning that if a person liable for the tax has made the return that was required of him by the Act, and that such return was not inaccurate or false, and that he had paid fully the tax assessed upon him, the liability for the tax ceased and the Minister was not empowered to open up or review such assessment.

Macleane J.

It is quite clear that it was under the words of s. 13, s.s. (3), of the Business Profits Act just referred to that the assessments in question were made. The decision of the Minister states that the Company filed returns for the several taxation periods under the Business Profits Act, but that following an investigation additional taxes were found owing by the Company for the same taxation periods. The assessments in question must therefore have been made upon the Company on the ground that it had not wholly paid the taxes for which it was assessed or liable under the Business Profits Act, or, that it had made inaccurate or false returns for the taxable periods under that Act. Those grounds must therefore be established or the assessments in question must fail and the Company's appeals succeed.

The Company, I find upon the evidence, made its return for each accounting period under the Business Profits Act and this is admitted; it did not make any incorrect or false return, and there is no evidence to support the suggestion that it concealed any facts that should have been disclosed relative to its profits, or its liability for the business profits tax, in any taxation period; it was assessed for the tax in each of such periods upon the basis of its returns duly made, and the facts known or made known to the taxing authorities; and it fully paid the taxes assessed upon it for each of such taxation periods, and within the time prescribed by the Act. The Minister, I think, has failed to establish the grounds upon which the assessments in question were made, and the Company has satisfied me that it made no inaccurate or false return and that it fully paid any tax assessed upon it during any of the taxation periods in question, under the Business Profits Act.

I am of the opinion therefore, that upon the facts here disclosed s. 13 (3) of the Business Profits Act did not

authorize the assessments made by the Minister there-  
under in 1937. And that, I think, is conclusive of the  
matters here in dispute and arising under that Act. It is  
unnecessary, I think, to say anything concerning the income  
tax assessments in question into which there does not enter  
the matter of the capital employed by the Company in  
its business, or concerning the method employed by the  
Company in valuing its inventories as all debate on that  
point has been closed by the agreement entered into  
between the parties.

If I am correct in holding that upon the facts here  
disclosed there were no grounds for making the assess-  
ments here in question, under the Business Profits Act,  
then, as already stated, the conclusions earlier expressed  
upon the various other points argued on this appeal need  
no longer be considered, except to the extent already  
indicated, and for the reasons already mentioned. In case  
I have failed to appreciate accurately all the implications  
of the agreement entered into between the parties in  
respect of the valuation of the Company's inventories and  
have overlooked any point incidental to that agreement  
and upon which a pronouncement should be made, such  
matters are reserved until the settlement of the minutes  
of judgment, when they may be mentioned to me by  
counsel.

I reserve the matter of the costs of the appeals until  
the settlement of the minutes of judgment.

*Judgment accordingly.*

1940  
DOMINION  
TEXTILE CO.  
LTD.  
v.  
MINISTER OF  
NATIONAL  
REVENUE.  
Maclean J.