Privy Council Appeal No. 35 *of* 1939

Pioneer Laundry & Dry Cleaners Limited - - - *Appellant*

v.

The Minister of National Revenue - - - - *Respondent*

FROM

THE SUPREME COURT OF CANADA

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 13TH OCTOBER, 1939

Present at the Hearing:

LORD ATKIN
LORD THANKERTON
LORD RUSSELL OF KILLOWEN
LORD WRIGHT
LORD ROMER

[*Delivered by* LORD THANKERTON]

This appeal is taken from a judgment of the Supreme Court of Canada, dated the 12th December, 1938, which affirmed a judgment of the Exchequer Court of Canada, dated the 4th November, 1937, whereby the appellant's appeal from a decision of the respondent, affirming an assessment of the appellant to income tax for the tax year ending on the 31st March, 1933, was dismissed.

The question in the appeal relates to the disallowance by the respondent of certain allowances for depreciation claimed by the appellant. In the return filed by the appellant in July 1933, in compliance with section 33 of the Income War Tax Act, R.S. Canada 1927 c. 97, for the fiscal year ending the 31st March, 1933, the appellant disclosed gross earnings of $171,122·04, and claimed various deductions including allowances for depreciation as follows:—

" Depreciation:—	*Per cent.*	$
Machinery and Equipment	10	14,131.15
Automobiles	20	2,935.08
Horses	10	135.25
Furniture and Fixtures	10	574.07
		$17,775.55 "

On the 19th February the Commissioner of Income Tax sent to the appellant a notice of assessment, in which the appellant's claim in respect of depreciation was disallowed except to the extent of $255·08 under the second item, in respect of two coupés and a truck body, which will be referred to later.

The appellant appealed to the respondent under section 58 of the Act, but the appeal was dismissed by the respondent, and, the appellant having filed a notice of dissatisfaction under section 60, the respondent transmitted the papers to the Exchequer Court in terms of section 63. Pleadings were ordered and filed, and, after trial, the appeal was dismissed by the Exchequer Court (Angers J.) on the 4th November, 1937. On appeal to the Supreme Court of Canada, the case was heard before the Chief Justice of Canada and Crocket, Davis, Kerwin and Hudson JJ., and on the 12th December, 1938, the Court dismissed the appeal, the Chief Justice and Davis J. dissenting.

The relevant facts may be summarised as follows:— The appellant company was incorporated on the 23rd March, 1932, and it acquired the machinery and equipment, etc., in respect of which the claim for depreciation has been disallowed from a company called the Home Service Company Limited, at a price fixed by independent appraisal; the correctness of this valuation has not been challenged by the respondent. The three items in respect of which the claim was admitted, were acquired from other sources.

Home Service Company Limited was incorporated also on the 23rd March, 1932, and on the 1st April, 1932, it acquired all the physical assets of seven companies, including the original Pioneer Laundry & Dry Cleaners Limited, which had gone into voluntary liquidation on the 30th March, 1932. The machinery and equipment etc., here in question were among the assets acquired by Home Service Company Limited from the original Pioneer Laundry & Dry Cleaners Limited.

At this time all the outstanding share capital of the seven companies above referred to, was owned directly or through nominees by a company called Pioneer Investment Company Limited, the assets of which were also acquired by Home Service Limited, with the exception of (*a*) shares owned by the former company i.e. the shares of the seven subsidiaries which, by reason of the liquidation, became unsaleable, and (*b*) amounts owing to the former company by its shareholders. Pioneer Investment Company Limited went into voluntary liquidation on the 7th April, 1932.

The machinery and equipment etc., here in question were fully written off by depreciation while they were in the ownership of the original Pioneer Laundry & Dry Cleaners Limited.

All the share capital of Home Service Company Limited, except forty shares out of 10,000 shares of par value of $100·00 each, was issued or sold to the liquidators of the operating subsidiary companies of Pioneer Investment Company Limited, in consideration for the transfer of the assets of the operating companies to Home Service Company Limited. On the winding-up of the operating companies these shares were distributed to the parent company, Pioneer

Investment Company Limited, and, on the winding-up of that company, were distributed to its own shareholders, with the admitted result that the shareholders of Home Service Company Limited are the same as were the shareholders of Pioneer Investment Company Limited, and their respective holdings in the new company are the same or substantially the same as were their respective holdings in the old company. The forty shares referred to were allotted to Pioneer Investment Company Limited in part payment of the assets acquired from that company.

It is further agreed that during the fiscal year ended the 31st March, 1933, the shareholders of the appellant company were as follows, namely:

	Shares.
Home Service Company Limited	97
Charles H. Wilson	1
Mary E. Stewart	1
Thomas H. Kirk	1
	100

and that the three persons named were during such fiscal year shareholders of the Home Service Company Limited.

The amount of depreciation claimed by the appellant company in its statutory return was in conformity with the rates stated in certain circulars issued by the respondent to local officers of the department (Exhibits 3, 4, 5 and 6), and the appellant sought, because of their being made available to the public, to have them treated as an exercise by the respondent of his statutory discretion as to depreciation. Their Lordships agree with the view of Crocket and Hudson JJ. that these departmental circulars are for the general guidance of the officers and cannot be regarded as the exercise of his statutory discretion by the respondent in any particular case. The other learned Judges of the Supreme Court express no opinion on this point; the Trial Judge had expressed a contrary view.

The main question in the appeal relates to the discretion conferred on the respondent as to allowances for depreciation by the Income War Tax Act, R.S. Canada 1927, cap. 97, the material provisions of which are as follows,

> " 3. For the purposes of this Act, ' income ' means the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be whether derived from sources within Canada or elsewhere;
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> * * * *
>
> " 5. ' Income ' as hereinbefore defined shall for the purposes of this Act be subject to the following exemptions and deductions:—
>
> " (*a*) Such reasonable amount as the Minister, in his discretion, may allow for depreciation, and the Minister in determining the income derived from mining, and from oil

and gas wells and timber limits shall make such an allowance for the exhaustion of the mines, wells and timber limits as he may deem just and fair;

* * * *

" 6. In computing the amount of the profits or gains to be assessed, a deduction shall not be allowed in respect of

* * * *

" (*b*) any outlay, loss or replacement of capital or any payment on account of capital or any depreciation, depletion or obsolescence, except as otherwise provided in this Act;

* * * *

In the first place, as to the nature of the discretion thus conferred on the Minister, Crocket and Hudson JJ. state:

" Reading these sections by themselves and without reference to any outside authorities, it would seem fairly plain that it was the intention of Parliament that there should be no depreciation allowance unless the Minister, in his sole discretion, decided that there should be. There is nothing anywhere to indicate the principle or basis on which the depreciation allowance is to be ascertained. It might vary according to different accounting methods, different economic theories, different general business conditions in the country. Nor is there anything in the statute which denies a right in the Minister to look beyond the legal facade for the purpose of ascertaining the realities of ownership or the possibilities of schemes to avoid taxation, and it would seem to me that it was the intention of Parliament that the Minister, and he alone, could properly estimate these different factors.

" The authorities cited on behalf of the appellant are mostly of statutes, somewhat differently worded from ours, and in effect hold no more than that where the statute gives a discretion to administrative officers and provides an area in time or space for the exercise of such discretion, the Commissioners must take that into account. In the present case, the Minister has exercised his discretion, and, as already stated, the statute does not define or limit the field for operation of such discretion."

Kerwin J. expressed a similar opinion.

Their Lordships are unable to agree with these views, and they agree with the opinion of Davis J., in which the Chief Justice concurred, and in which he states:

" The appellant was entitled to an exemption or deduction in ' such reasonable amount as the Minister in his discretion, may allow for depreciation.' That involved, in my opinion, an administrative duty of a quasi-judicial character—a discretion to be exercised on proper legal principles."

In their Lordships' opinion, the taxpayer has a statutory right to an allowance in respect of depreciation during the accounting year on which the assessment in dispute is based. The Minister has a duty to fix a reasonable amount in respect of that allowance and, so far from the decision of the Minister being purely administrative and final, a right of appeal is conferred on a dissatisfied taxpayer; but it is equally clear that the Court would not interfere with the decision, unless—as Davis J. states—" it was manifestly against sound and fundamental principles."

The decision of the Commissioner of Income Tax in the present case, which is accepted by the respondent as his statutory decision, makes clear the point of principle which

the appellant claims to have been thereby contravened; it is as follows:—

> "The honourable the Minister of National Revenue, having duly considered the facts as set forth in the Notice of Appeal and matters thereto relating hereby affirms the said assessment on the ground that while the company was incorporated and commenced operations during the year 1932 there was no actual change in ownership of the assets purchased or taken over from Pioneer Investment Company Limited by Home Service Company Limited (of which the taxpayer is a subsidiary) and set up in the books of the taxpayer at appreciated values; that in the exercise of the statutory discretion, a reasonable amount has been allowed for depreciation and that the assessment is properly levied under the provisions of the Income War Tax Act."

Their Lordships agree with the Chief Justice and Davis J. that the reason given for the decision was not a proper ground for the exercise of the Minister's discretion, and that he was not entitled, in the absence of fraud or improper conduct, to disregard the separate legal existence of the appellant company and to enquire as to who its shareholders were and its relation to its predecessors. The taxpayer is the company, and not its shareholders. Their Lordships agree with the reasons given by these learned Judges, and their application of the authorities cited by them, and it is unnecessary to repeat them.

It follows that the assessment should be set aside, and the matter should be referred back to the respondent. It becomes unnecessary to consider a further question which was debated, namely, as to whether a taxpayer, who has already received in previous tax years allowance for depreciation amounting to 100 per cent. of the book value of the assets, is entitled to any further allowances.

Their Lordships will therefore humbly advise His Majesty that the decisions appealed from should be set aside, and that the assessment should be set aside and the matter referred back to the Minister. The appellant will have the costs of this appeal and the costs in the Courts below.

(20368—37) Wt. 6375—41 120 10/39 P. St. G. 338

In the Privy Council

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v.

THE MINISTER OF NATIONAL REVENUE

DELIVERED BY LORD THANKERTON

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