THE B.C. FIR AND CEDAR LUMBER COMPANY, LTD..... } APPELLANT;

v.

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

1929
Oct. 5.
Dec. 11.

Revenue—Use and Occupancy Insurance—Insurance on Net Profits and Fixed Charges—Income Tax—Profit and Gain.

The appellant carried on the business of manufacturer and dealer of lumber. Besides fire insurance it was insured against loss or damage which it might sustain in the event of its plant, in whole or in part, being shut down or suspended in consequence of fire or damage, which insurance is known as Use and Occupancy Insurance. These policies insured plaintiff for $60,000 in respect of loss "On Net Profits" and $84,000 "On Fixed Charges," the former being defined to mean net profits that would have accrued had there been no interruption of business caused by the fire, and the latter, all standing charges and expenses which must necessarily continue to be paid or incurred by the assured during the time the plant is inoperative.

A fire having occurred in the appellant's premises destroying part of the property, they received from the Insurance Company $43,000 for loss of net profits and $52,427 for fixed charges. This amount, or part thereof, was assessed for income tax. Hence the appeal.

Held, as the amounts constituting Fixed Charges were incurred and paid by the appellant in carrying on its business, and had been allowed as a deduction in determining its net income, that the amounts received

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by it from the Insurance Policies covering Fixed Charges are applicable to such deduction and should be applied in reduction of the deduction claimed.

2. That the amount received for "Net Profits" aforesaid falls within Section 3 of the Income War Tax Act, and is taxable as income. That the said amounts were gain or profit connected with and arising from the business of the appellant. That it was not a receipt or revenue on account of loss or replacement of capital.

APPEAL from decision of The Minister of National Revenue, under the Income War Tax Act, 1917.

The appeal was heard before The Honourable Mr. Justice Maclean, President of the Court, at Vancouver.

C. H. Locke, K.C., for Appellant.

C. Fraser Elliott, K.C., for Respondent.

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

THE PRESIDENT, now (December 11, 1929), delivered judgment.

The appellant company, during the year 1921 and thereafter, carried on its business as a manufacturer and dealer in lumber products in the city of Vancouver, B.C. In the month of March, 1923, the appellant was insured for the period of one year from the said month by some seventeen fire insurance companies against loss and damage to its plant and property by fire, and also by the same companies against loss or damage which might be sustained in the event of its plant, either in whole or in part, being shut down or suspended in consequence of fire and damage, which the latter insurance policies are usually known as Use and Occupancy Insurance. The contracts of Use and Occupancy Insurance insured the plaintiff in the total amount of $60,000 in respect of loss "On Net Profits", and $84,000 "On the Fixed Charges". In these contracts of insurance, "Fixed Charges" is defined to include all standing charges and expenses which must necessarily continue to be paid or incurred by the Assured during the time its plant shall be inoperative; and "Net Profits" is defined to mean net profits that would have accrued had there been no interruption of business caused by the fire.

On August 21, 1923, the plant and premises of the appellant were destroyed by fire; the appellant and the adjuster for the insuring companies agreed upon the period of the interruption of the former's business as being two hundred and fifteen (215) business days, this being the length of time agreed upon as being required for the rebuilding of the plant, and the loss was adjusted upon the following basis:—

Loss of net profits estimated at $317·3263 per day. Insured for and allowed at $200 per day for 215 days.....	$43,000 00
Fixed charges estimated at $243·85 per day. Insured for $280 per day.	
Allowed at the actual estimated loss of $243.85 for 215 days...	$52,427 90

The insuring companies paid to the plaintiff the said sum of $95,427.90.

During a portion of the period of the interruption of the appellant's business, it was able to carry on certain business, namely, the sale of part of its lumber stock and wood which had not been destroyed by fire; and in order to maintain its business connections it purchased certain manufactured lumber in the market and resold it. These operations, it is agreed, constituted but a small fraction of the business which the appellant would ordinarily have carried on but for the destruction of its manufacturing plant and premises.

The appellant in making its return under the Income War Tax Act, charged the premium of $3,828.29 paid for such insurance, under the heading of General Expenses. The respondent, in assessing the income of the appellant for the year 1924, treated part of the moneys received by the appellant from the insurance companies as income for the said year; the appellant treated such moneys as income in its accounts and reported a profit to the Department of Government administering the Act, but it is agreed, that in so doing the company acted without legal advice. Later, upon obtaining legal advice, the appellant informed the Department of National Revenue that these insurance moneys were wrongly included as income. The appellant, in due course, appealed from the assessment made against it, but the Minister of National Revenue dismissed the appeal; the appellant now appeals to this Court and it is agreed that such appeal is properly here. The appellant's contention is that the money received by it from the insur-

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ing companies is not income within the meaning of the Income War Tax Act; the respondent contends that such money is income and was properly assessed as such under the Act.

It was agreed by counsel, upon the hearing of the appeal, that all I need determine was whether or not the moneys received by the appellant company from the insuring companies were income within the meaning of the Income War Tax Act. That question being disposed of, I was informed that in the event of my finding that the moneys in question were properly taxable, the amounts due for the different taxation periods would be amicably reached between the parties.

I think the amounts derived by the appellant, from the Use and Occupancy Insurance policies, constitute income within the meaning of the Income War Tax Act. So far as the amounts received on account of Fixed Charges are concerned, there is little room, I think, for substantial controversy. If the amounts constituting Fixed Charges, were incurred and paid by the appellant in carrying on its business, and have been allowed as a deduction in determining its net income, then the amounts received by it from the insurance policies in respect of Fixed Charges are applicable to such deduction and should be applied in reduction of the deduction claimed. The appellant was, in that amount, recouped for any disbursements made on this account during the period its plant was not in operation. As expressed by Mr. Elliott for the respondent, had the insurance companies themselves paid directly the Fixed Charges as maturing, and the appellant might conceivably have so directed, in that case, the appellant's business accounts would not disclose any receipts or disbursements on account of Fixed Charges, and consequently there would be no income subject to taxation. The result is the same if the appellant received the amounts from the insurance companies on account of Fixed Charges, and disbursed the same on the same account; a deduction must be made for such disbursements, but the appellant's accounts must show the receipt of any amounts derived from the insurance companies on account of Fixed Charges. The appellant having received the benefit of a deduction for Fixed

Charges, an expense for income tax purposes, all receipts coming into its hands on account of Fixed Charges must appear on the other side of the ledger; the difference would be the taxable net income, although in this case the debits and receipts would no doubt be treated as balancing one another. Nothing further need, I think, be said upon this aspect of the case.

Now, as to the remaining point in issue. It seems to me that the amounts derived from the insurance policies, on account of Net Profits, fall within sec. 3 of the Income War Tax Act. The premium paid on account of insurance against loss of Net Profits was claimed as an operating expense and so allowed by the Minister, and this expense was incurred for the purpose of ensuring the earning of net business profits; the contracts of insurance or indemnity make this quite clear, and also that Net Profits mean net profits that would have been earned had there been no interruption of business. Here, a definite portion of the appellant's business was for a fixed period interrupted, and consequently a portion of its usual revenues accruing from the production and sale of its products was temporarily interrupted; but on account of that interruption, and under contracts of indemnity against business interruption, the cost of which was borne by the business interrupted, the appellant received sums of money in substitution of the net profits that otherwise would presumably have been earned. I think such income must enter into the revenue accounts of the business like any other income ordinarily earned, or any other receipt incident to the business, and thus enter into the calculations determining what is the net income of the business, for taxation purposes. The moneys in question were, I think, a gain or profit connected with and arising from the business of the appellant. I cannot conceive of it being anything else. If the same were transferred to a reserve or contingent account no deduction could be allowed upon the ground that it was there so placed. It was not a receipt or revenue on account of loss or replacement of capital. The Act does not seem to have contemplated any exemption or deduction on account of income of this nature.

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Many cases were cited by counsel, but I found little or no assistance from any of them, with one exception, *The International Boiler Works Co.* v. *Commissioner of Internal Revenue* (1). In this case, the income in question was derived from so-called Use and Occupancy Insurance against loss of net profits, and the same was held to be taxable under the provisions of the United States Revenue Act, by the United States Board of Tax Appeals. There is nothing in the United States Revenue Act, so far as I can see, that differentiates that case from the present proceeding under the Income War Tax Act.

I therefore disallow the appeal with costs to the respondent.

Judgment Accordingly.