

BETWEEN:

FREDERICK A. PERRAS APPELLANT;

AND

THE MINISTER OF NATIONAL }
 REVENUE } RESPONDENT.

1953
 Oct. 16
 Nov. 20

*Revenue—Income—The Income War Tax Act, R.S.C. 1927 c. 97, s. 19(1)—
 Winding up—Undistributed income on hand—Meaning of “on hand”
 —Appeal allowed.*

Appellant and another person owned shares in Commercial Hotel Limited the assets of which company were sold, the money received from such sale being held pending the disposition of certain tax appeals instituted by the Company. The Company was liable for certain tax assessments made on it and these assessments were paid. Thereafter the company passed a resolution that it be wound up and a liquidator was appointed. He carried out the liquidation of the company and distributed the balance, after payment of debts, to appellant and the other shareholder. Respondent computed that the Company had on hand undistributed income and added this amount to the income of appellant and the other shareholder. The added assessment was based on the contention that the Company should have had undistributed income on hand from beer sales made during the years for which such sales were assessed against the Company and which were the subject matter of the appeals referred to above. An appeal from such assessments was taken to this Court.

Held: That the undistributed income on hand in s. 19(1) of the Act means the undistributed income the company has *on hand* and that is determined by ascertaining what the company actually did have on hand, not what it should have had on hand; “on hand” means “in the possession or control of” and so available for distribution, and in computing what is on hand there should be taken into account disbursements and losses which may have lessened the amounts of the profits held in reserve.

2. That the assets of the business of Commercial Hotel Limited sold were all capital assets and that any sum of undistributed income which the Company may have had on hand was completely wiped out upon payment of the arrears of income tax and there was not at the time of the winding up any undistributed income on hand.

1953
 PERRAS
 v.
 MINISTER OF
 NATIONAL
 REVENUE

APPEAL from a decision of the Income Tax Appeal Board.

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

J. A. MacInnes, Q.C. and *C. S. Arnold* for appellant.

J. L. Farris, Q.C. and *T. E. Jackson* for respondent.

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

CAMERON J. now (November 20, 1953) delivered the following judgment:

This is an appeal from a decision of the Income Tax Appeal Board dated November 21, 1952, by which it affirmed an assessment made upon the appellant for the year 1948. The appeal involves a consideration of the provisions of s. 19(1) of the Income War Tax Act and its application to the facts of this case. In that year, the appellant, as a shareholder of Commercial Hotel Ltd. received certain amounts from its liquidator, and the respondent, being of the opinion that at the time of the winding up, the company had on hand certain undistributed income, added to the declared income of the appellant (as the owner of one-third of the issued shares of the company), one-third of said amount. The only other shareholder in 1948 was Mrs. Dorothy Johnson who was the owner of the remaining two-thirds of the issued shares of that company; she also received in 1948 certain sums from the liquidator, and to her declared income the respondent added two-thirds of what was considered to be the undistributed income of the company. Both the appellant and Mrs. Johnson were assessed accordingly and their appeals to the Income Tax Appeal Board in respect thereof were dismissed. Both have taken an appeal to this Court and at the hearing their appeals were considered together. The principles involved and the evidence adduced are equally applicable to both cases.

S. 19(1) of the Act is as follows:

19(1) On the winding up, discontinuance or reorganization of the business of any incorporated company, the distribution in any form of the property of the company shall be deemed to be the payment of a dividend to the extent that the company has on hand undistributed income.

The main ground of appeal is that, in fact, Commercial Hotel Ltd. at the time of its winding up had no undistributed income *on hand*. It becomes necessary, therefore, to set out certain facts in relation to Commercial Hotel Ltd. (hereinafter to be called the company).

The company was incorporated in 1927 under the Companies Act of British Columbia. From that date until its assets were sold in 1947 it carried on business in rented premises at Vancouver and had a license to sell beer at retail. From about the year 1938 there were three shareholders of the company, namely, George Johnson (husband of Dorothy Johnson), who was its manager and held approximately one-half of its issued shares; Dorothy Johnson, who held approximately one-sixth of the issued shares and who at no time took an active interest in the conduct of the company's business; and F. A. Perras, the appellant, who was employed as a beer waiter and owned two-sixths of the issued shares.

In August, 1945, the Minister of National Revenue, not being satisfied that the company had filed proper income tax returns for the years 1939 to 1943 inclusive, exercised the powers given him by s. 47 of the Income War Tax Act and determined the income of the company for each of those years and assessed it accordingly. The company appealed, but before it had received the decision of the Minister, George Johnson died. Under his will, all his shares in the company were bequeathed to his wife who thereafter was the owner of two-thirds of the issued shares.

Following the death of the said Johnson in January 1947, his widow and Perras, who were the sole owners of the company, decided to dispose of the hotel business. On April 9, 1947, it was sold to Midtown Holdings Ltd. for \$80,000, the sale price including (a) furniture and equipment, the value of which was fixed at \$17,500; (b) the beer license; (c) goodwill; (d) the name "Commercial"; and (e) the lease of the hotel premises. The proceeds of the sale, which with certain adjustments totalled \$81,223.71, appear to have been paid to the company's solicitors, Messrs. MacInnes and Arnold, and pending the final disposition of the tax appeals then pending, the greater part thereof was placed in Government bonds.

1953

PERRAS

v.

MINISTER OF
NATIONAL
REVENUE

Cameron J.

1953
 PERRAS
 v.
 MINISTER OF
 NATIONAL
 REVENUE
 Cameron J.

In June, 1947, the Minister affirmed the assessments made upon the company for the years 1939 to 1943 and an appeal was taken to this Court. That appeal was dismissed with costs by Mr. Justice O'Connor on December 8, 1947 (1). The company thereby became liable to payment of arrears of income tax, interest thereon, and costs in the sum of \$23,661.31. In order to satisfy the said judgment, the said solicitors sold bonds having a face value of \$25,000 and satisfied the said judgment debt.

Thereafter, and on February 18, 1948, the said company passed a resolution that it be wound up, and appointed William Tomlinson, Esq., C.A., as its liquidator. He took over the remaining assets, paid the debts and expenses and over a period of time distributed the balance between the appellant and Mrs. Johnson in the proportion of one-third and two-thirds. On May 3, 1948, the appellant received \$17,000 in bonds and on the same date Mrs. Johnson received bonds to the value of \$8,500 in respect of her own shares, and \$25,500 in bonds as beneficiary of her husband's shares in the company. According to the computation made by the assessor in the Income Tax office, the company had on hand undistributed income in the sum of \$17,218.74, and under s. 19(1) there was added to the income of the appellant one-third of that amount, and to the income of Mrs. Johnson, the remaining two-thirds.

The books of the company did not show any undistributed income on hand at the time it went into liquidation. The assessments made upon Mrs. Johnson and the appellant were based on a computation of the company's undistributed income made by the witness W. S. Dempsey, an assessor in the Income Tax office at Vancouver. He took into consideration the entire operations of the company since it commenced business as disclosed by its income tax returns, making due allowance for adjustments made at the time of each assessment, and also taking into consideration the income assessed for the years 1939 to 1943 which were later affirmed by the judgment in the Exchequer Court. The basic figures are shown in Ex. A-1, the first page of which is for the period from 1928 to December 31, 1948, the second page bringing the computation up to December 31, 1949. Ex. R-3 is the final computation based

(1) [1948] Ex. C.R. 108.

thereon and it indicates that if the books of the company had been properly prepared and if they had included as taxable revenue the added amounts of income from beer sales for the years 1939 to 1943, which were assessed against the company in those years (\$30,773.03), there should have been undistributed income of \$17,218.74 on hand.

1953
 PERRAS
 v.
 MINISTER OF
 NATIONAL
 REVENUE
 Cameron J.

Counsel for the appellant does not challenge the accuracy of that computation as such. He admits that the company was bound by the judgment in this Court and that the full amount of the assessments for those years was paid. His main contention, however, is that no part of that added income of \$30,773.02 was *on hand* at the time of the liquidation and consequently that none of it was received by either Mrs. Johnson or the appellant. He submits that all the assets sold to Midtown Holdings Ltd. were capital assets; and that as they were sold for a total amount of \$81,223.71, and as the two shareholders received only a total of approximately \$65,000 in the liquidation, the capital assets were, in fact, depleted to the extent of approximately \$16,000.

The onus is upon the appellant and the taxpayer must establish the existence of facts or law showing an error in relation to the taxation imposed upon him (*Johnson v. Minister of National Revenue* (1)). As stated by Rand, J. in that case at p. 489, the onus is upon the taxpayer to demolish the basic fact on which the taxation rested. In this case the basic fact on which the taxation rested was that the company did have undistributed income on hand. Now as I have said, there is no doubt that on the basis of the assessments made upon the company from its inception, the company should have had the sum of \$17,218.74 on hand. But as I read the provisions of s. 19(1), the distribution of the company's assets is deemed to be a dividend, in the circumstances named, only to the extent that "the company has *on hand* undistributed income." That it seems to me is a pure question of fact and is not to be determined by showing what undistributed income the company should have had on hand, but by determining what it actually did have on hand. I do not mean by that, of course, that it must be in the form of cash, for it could be

1953
 PERRAS
 v.
 MINISTER OF
 NATIONAL
 REVENUE
 Cameron J.

on hand in many other forms. In my opinion, "on hand" means "in the possession or control of" and so available for distribution. The tax therefore arises only against undistributed income on hand; and in computing what is on hand, there should be taken into account disbursements and losses which may have lessened the amounts of the profits held in reserve.

Now, as I have intimated above, the entire case put forward by the respondent is based on the assessments made upon the company for the years 1939 to 1943, which assessments were later affirmed in this Court. By those assessments, there was added to the declared income of the appellant the sum of \$30,773.02. Those so-called "arbitrary" assessments were made on the theory that the company had not been reporting in its income the revenue which its purchases of beer suggested it should have reported. Mr. Justice O'Connor, who heard the appeals from those assessments, pointed out in fairness to the company that in presenting its case it was handicapped by the fact that Mr. Johnson, who was the chief shareholder and manager of the company and who knew more about the company's business than any one else, had died before the trial. While he was somewhat doubtful of the weight to be attached to the findings of some of the appellant's witnesses, it would appear that his main reason for dismissing the appeals was that the appellant had not satisfied the onus cast on it, the concluding words of his judgment being, "The appellant has not satisfied me that the actual revenue was less than the revenue estimated by the Minister under s. 47 during the years in question, and the appeal must, therefore, be dismissed with costs."

The effect of that judgment was not to increase the undistributed income actually on hand, but to increase the debts of the company as shown by its books by the sum of approximately \$23,000. That debt was paid in full and it seems to me that on a proper accounting basis it would be right to take into account the payment of such disbursements as a charge on the profits actually held in reserve in determining what undistributed income was actually on hand.

Now, however much in error the books of the company may have been at an earlier stage in the history of the company's affairs, and whatever may be the explanation for the

non-appearance in its books of the sum of \$30,773.02, the history of its affairs from and after the death of George Johnson and up to the time of the final distribution by the liquidator has been made quite clear by the evidence of Mrs. Johnson, Mr. Tomlinson and the appellant. That evidence is sufficient to establish definitely the assets then on hand and the manner in which they were dealt with.

1953
 PERRAS
 v.
 MINISTER OF
 NATIONAL
 REVENUE
 Cameron J.

My first conclusion is that the assets of the business sold to Midtown Holdings Ltd. were all capital assets. That would undoubtedly be the case with regard to the beer license, the lease of the premises, the goodwill and the right to use the name "Commercial." *Prima facie*, also, that would be the case in regard to the furniture and equipment. I have not overlooked the submission of counsel for the respondent that it is a somewhat suspicious circumstance that the total cost of the furniture and equipment as shown by the company's returns, was approximately \$12,300 (practically all of which had been written off to depreciation), and that the price put upon it at the time of the sale was \$17,500. His suggestion is that some of the undistributed profits may have been put into the purchase of additional furniture and equipment. But in view of the effect of inflation on the prices of all such equipment and that the price established thereon at the time of the sale may well have been a purely arbitrary one, I do not think I should draw any such conclusion in regard thereto.

My second conclusion is that on the evidence the appellant has satisfied me that the other assets of the company did not at any material time after the death of George Johnson exceed in value the sum of \$23,661.31, which was paid in satisfaction of the arrears of income tax. Messrs. MacInnes and Arnold, the solicitors for the company, received only the proceeds of the sale of the capital assets, and the remaining assets were taken over directly by the liquidator. I accept the latter's evidence that his total receipts in the winding up proceedings are as shown in para. 17 of the Notice of Appeal. These receipts total \$68,220.85, and excluding therefrom the Victory bonds of a value of \$51,000 and cash amounting to \$649.45 (both of which represent the balance of the proceeds of the sale of capital assets as turned over to him by Messrs. MacInnes and Arnold), the receipts by him of all assets other than of capital assets are shown to be of a value of \$16,571.40.

1953
 {
 PERRAS
 v.
 MINISTER OF
 NATIONAL
 REVENUE
 ———
 Cameron J.
 ———

That amount is made up of \$7,000 in Government Bonds, certain book debts owing by the shareholders, a bank balance and various refunds, mainly of the refundable portion of excess profits tax paid by the company in previous years. Assuming that all these various items are made up of undistributed income on hand in some form, it is apparent that when the debt of \$23,661.31 was paid and charged to profits held in reserve—as I think the company was entitled to do—no undistributed income remained *on hand*.

It is true that the debt of \$23,661.31 was actually paid by Messers. MacInnes and Arnold out of the proceeds of the sale of capital assets. But I do not think that that is a matter of any importance whatever. At the time the judgment was rendered, a liquidator had not been appointed and there were no other liquid assets then available to meet the obligation. It was merely a convenient way of paying the obligation without delay.

My finding on this point, therefore, is that any sum of undistributed income which the company may have had on hand was completely wiped out upon payment of the arrears of income tax; and that upon a proper accounting, there was not at the time of the winding up any undistributed income on hand. It follows that no part of the amounts received by the appellant in 1948 is taxable under the provisions of s. 19(1).

For these reasons, I find that the appellant has satisfied the onus put upon him to establish that on the winding up of Commercial Hotel Ltd., the company had no undistributed income on hand. The appeal will be allowed and the assessment made upon the appellant will be set aside and the matter referred back to the Minister to reassess the appellant upon the basis of these findings.

The appellant is also entitled to his costs after taxation. Inasmuch, however, as the same counsel appeared on behalf of both this appellant and Mrs. Dorothy Johnson, the other appellant, and that the appeals were heard together, I direct that only one set of costs shall be allowed following the service of Notice of Trial, the same to be apportioned equally between this and the Johnson appeal.

Judgment accordingly.
