

Toronto
1966
Oct. 4-7
Ottawa
Nov. 8

BETWEEN :

COLEMAN C. ABRAHAMS APPELLANT ;

AND

THE MINISTER OF NATIONAL }
REVENUE } RESPONDENT.

(No. 1)

Income tax—Sale of business as going concern—Valuation placed on accounts receivable—Binding effect of on Minister—Contract not validly ratified by purchasing company—Income Tax Act, ss. 17(2), 85D.

Parties—Evidence—Agreement as to facts—Admission of fact made under misapprehension—Duty of court to regard true facts disclosed by evidence

Appellant, who was in charge of the sales organization of a book selling company, was remunerated by a commission on sales from which certain charges were deducted and the resultant balance was payable to him six months after the end of each quarter. In late 1960 or early 1961 appellant discussed with officials and lawyers of his employer the possibility of selling to a company wholly owned by appellant effective April 1st 1961 (a) the property of his "business" as a sales agent,

(b) an office building project, (c) his home, and (d) his car, but the details were not worked out. A draft agreement was put forward in August 1961 but it was not until October 4th 1961 that an agreement dated April 1st 1961 was executed by appellant and a director of the purchasing company purporting to act in its behalf. The agreement then executed differed materially from the earlier draft agreement. The executed agreement listed among the assets, at a valuation of \$5,000, accounts receivable by appellant from his employer amounting to \$208,875, being the amount which would have become payable to appellant after April 1st 1961 under his arrangement with his employer subject to liabilities of approximately \$195,000 which were assumed by the purchaser. Appellant's employer paid the purchasing company \$208,875 on September 30th and October 1st 1961. On March 15th 1962 the agreement executed on October 4th 1961 was approved by resolution of the purchasing company's directors.

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Appellant appealed from an income tax assessment for 1961 contending that in computing his income for that year he was entitled to a deduction of \$208,875 (i.e. the amount of the accounts receivable, \$208,875, less the \$5,000 at which they were valued in the agreement of October 4th 1961) by virtue of s 85D of the *Income Tax Act*. For the purposes of the appeal it was agreed by the parties *inter alia* that if there had not been a sale by appellant to the purchasing company within the meaning of s 85D on or before April 1st 1961 appellant was not entitled to succeed.

Held, dismissing the appeal, appellant and the purchasing company did not enter into a sale contract on or before April 1st 1961. It could not be inferred on a balance of probabilities from the evidence of what occurred before and after April 1st 1961 that a sale had been entered into on or before that date. Not only were the description of the property being sold and its price not settled on April 1st 1961 but there was no corporate act by the purchasing company ratifying the agreement executed on October 4th 1961 until the directors' resolution of 15th March 1962 and therefore no valid sale agreement with respect to the accounts receivable prior to October 4th 1961. There was no evidence that any person engaged in negotiations on behalf of the company before October 4th, 1961 held any office in the company or otherwise had any authority to negotiate on its behalf: a director of a company does not have such implied authority.

Semble. If, as the evidence indicated, appellant was an employee of the book selling company and not, as conceded by respondent, an independent contractor, respondent's admission should be taken to have been made under a misapprehension and the court should have regard to the real facts as shown by the evidence *Sinclair v. Blue Top Brewing Co.* [1947] 4 D.L.R. 561 referred to. This principle applies *a fortiori* where the revenue is involved.

Semble. While s 85D(2) of the *Income Tax Act* declares that a statement of vendor and purchaser of debts as to the consideration is binding on them as against the Minister, the Minister is not prevented from inquiring into the veracity of the statement, and, in this case, from applying s 17(2) of the *Income Tax Act*, under which appellant's appeal would also fall to be dismissed on the ground that he had received fair market value for the debts. There is no conflict between the provisions of s. 17(2) and s. 85D.

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APPEAL from income tax assessment.

John G. McDonald, Q.C. and *M. L. O'Brien* for appellant.

Sydney L. Robins, Q.C. and *T. Z. Boles* for respondent.

JACKETT P.:—This is an appeal directly to this Court from a re-assessment of the appellant for the 1961 taxation year made on February 24, 1965.

The Notice of Appeal sought relief in respect of an alleged benefit included in the appellant's income for the 1961 taxation year by the assessment appealed from under section 8 of the *Income Tax Act* and also claimed a deduction, in computing the appellant's income for that year, of \$203,875.30 by virtue of section 85D of the *Income Tax Act*. At the opening of the hearing, the appellant abandoned its claim for relief in respect of the section 8 benefit. The only relief now sought is therefore the relief under section 85D.

The Notice of Appeal does not comply with the requirement in subsection (3) of section 98 of the *Income Tax Act* that it should contain "a statement of the allegations of fact. . . which the appellant intends to submit in support of his appeal" in that it does not allege "facts" that would entitle it to any relief under section 85D. On the other hand, the respondent did not move for an order under subsection (2) of section 99 nor did he, by his reply, take the position that the Notice of Appeal did not allege facts entitling the appellant to the relief sought. Instead, the respondent, by his reply, specifically denied the existence of certain facts the existence of which, among others, is essential for the appellant to be entitled to the relief sought.¹ The Notice of Appeal and the reply fail, therefore, to define the issues of fact in the manner contemplated by the statute. This did not, however, become apparent to the Court until after the appellant had closed his case.

¹ This was done in such a way as to seem, impliedly, to admit the existence of the other facts necessary for the appellant to be entitled to the relief sought. If the reply did not have the effect of admitting such facts, it was embarrassing.

The parties have now remedied the matter by agreeing upon the issues to be decided by the Court. To understand these issues, it is necessary to have some knowledge of the facts that are not in dispute. I shall therefore defer setting out the issues so agreed upon until I have reviewed the facts that, as I understand it, are not in dispute.

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A company whose name is Encyclopaedia Britannica of Canada, Ltd., a subsidiary of a United States company, Encyclopaedia Britannica Inc., at all relevant times carried on a business of selling books throughout Canada. For this purpose there was a large organization of commission salesmen, supervised by managers of one or more types at different levels of the organization. These salesmen obtained from potential customers signed order forms, which were, in effect, offers to purchase publications of Encyclopaedia Britannica of Canada, Ltd. Each such order was passed by the sales organization to some other branch of the company which investigated the credit rating of the potential customer and, if that was satisfactory, arranged to have the books ordered shipped to the customer. (While, strictly speaking, the sales organization merely obtained the offer to purchase, in the jargon of the business, what they did was referred to as "sales" and "distribution" of the publications. This is a matter of some importance in appreciating some of the evidence.)

From October 1, 1955 until October, 1961 the appellant was in charge of the sales organization for all of Canada. He was extremely effective at recruiting, training and supervising the persons required to carry on the operation effectively and produced results that were very gratifying to Encyclopaedia Britannica of Canada Ltd. He apparently insisted upon being given almost an absolute discretion in running the sales organization and this was accorded to him. So much was this so that, according to much of the evidence, what the sales organization did was regarded by the senior officers of Encyclopaedia Britannica of Canada Ltd. and of the sales organization as being the appellant's business. Nevertheless, the salesmen were employees of the company, the sales organization carried on its activities in

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premises rented by the company and all money, office equipment and other property used by the sales organization belonged to the company. The financial remuneration of the members of the sales organization may be summarized very briefly as follows:

- (a) when a sales order was accepted, the salesman who obtained it was credited with a commission at a scheduled rate, against this were charged back commissions previously credited to him on sales that had since gone bad, and he received payment of the balance so established on a weekly basis;
- (b) when a sales order was accepted, the manager, under whom the salesman who obtained it functioned, was credited with a commission at a higher rate than the salesman but there was charged against his account all the commissions credited to his salesmen, all "chargebacks", and all the other costs of the sales organization in his territory; he was then paid the balance to his credit on a periodic basis; (there may in some cases have been district and regional managers but I propose to ignore this complication as not affecting the outcome of the case);
- (c) when a sales order was accepted, the appellant, who was in over-all control of the organization was credited with a commission which, after 1958, was 45 per cent., and he was debited with all commissions paid to other persons in the sales organization, all "chargebacks", and all other expenses of the sales organization; a balance was struck at the end of each quarter and that balance was payable to him six months after the end of each quarter, during which time it might be reduced by new "chargebacks" arising on sales that had gone bad and, possibly, by "advances" made to him in the meantime.

The scheme envisaged "advances" to members of the organization on the amounts payable to them in the future. The appellant, throughout that period, was paid \$500 a week as an advance of remuneration payable to him in the

future and these advances were deducted in determining the amount payable to him at the end of the six months period.

Necessary records were kept by a group known as the "cashiering department", which department also drew cheques on a company bank account in payment of commissions and other expenses. In 1958, the cashiering department was, for the first time, put under the appellant's control. At that time, an imprest account was set up by the company on which the appellant and persons under his control were given power to draw cheques. This account was maintained at a level necessary to cover the expenses of the sales organization.

After the cashiering department was put under the appellant's control, it kept records of the amounts credited and debited to each of the members of the sales organization other than the appellant. The account of amounts credited and debited to the appellant were kept by a branch of the company outside the sales organization. The weekly advances to the appellant of \$500 were charged in that account. A separate account was kept by the company of other amounts paid to or for the appellant when he was being given financial help by the company in special circumstances; these amounts were regarded by the company officials as "loans" and not "advances".

Quite apart from his work with Encyclopaedia Britannica of Canada Ltd., the appellant owned all the shares in a company known as Coab Holdings Ltd., which carried on no business. That company owned all the shares in Coab Merchandising Co. Ltd. which did carry on a business. This latter company was incorporated on February 9, 1959.

During the latter part of 1960, the President of Encyclopaedia Britannica of Canada Ltd. and the appellant explored the possibility of the appellant selling his "business" in connection with the "sale" of that company's publications to a company the shares of which would all be owned by the appellant. This project was discussed by the appellant and company officials with lawyers and accountants and a firm decision was taken, as far as these gentlemen

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were concerned, either in late 1960 or early 1961, that the appellant would sell (a) the property of that "business", (b) a project he had for building an office building, (c) his private residence, and (d) his automobile, to Coab Merchandising Co. Ltd., *effective April 1, 1961*.¹ It was also decided that that company's name should be changed to Encyclopaedia Britannica Sales Limited. In February, 1961, the accountant who worked under the appellant in the sales organization was instructed to work out the accounting and other details of the proposed sale and details of how the sales organization would operate after such a sale. Steps were also taken to get appraisals of the value of the private residence.

For various reasons, delays occurred in working out the sale arrangements. On July 21, 1961, the name of Coab Merchandising Co. Ltd. was changed to Encyclopaedia Britannica Sales Limited. On August 30, 1961, the solicitor who was drafting the agreement put forward a draft of the

¹ While the evidence is not as precise as might be wished, I find that the agreement at that time was an agreement reached by the parties indicated by the witness Kleeb in the following passage quoted from his evidence:

"Q. . . . When was it agreed that such transfer should take effect and be effective?

A. It was agreed that such transfer should take effect April 1st, 1961.

HIS LORDSHIP: Agreed by whom?

THE WITNESS: It was agreed by the principals involved, that is, Mr. Abrahams and Encyclopaedia Britannica of Canada Limited and as an employee of Mr. Abrahams I was so instructed and it was the result of many discussions between these parties and Mr. McDonald, myself and probably one or two other people."

Reading the evidence as a whole, I find that when the witness Swinton says that "the agreement was made long before the actual effective date", he is speaking of the agreement by the parties enumerated by Mr. Kleeb (which is not an agreement between the appellant and his wholly-owned company) and that, when he says that, from April 1, 1961, he treated the wholly-owned company "as having been substituted for the independent contractor, Abrahams", he meant to convey that the arrangement was worked out with effect from that date (because the necessary arrangements had not been made until months after that date).

agreement. On October 4, 1961, an agreement was executed which was different in material respects from the draft of August 30, 1961, and which read as follows:

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MEMORANDUM OF AGREEMENT made the 1st day of April, 1961

BETWEEN:

COLEMAN C ABRAHAMS, of the Township of Etobicoke in the County of York, in the Province of Ontario, Executive, (hereinafter called the "Vendor")

OF THE FIRST PART

AND

ENCYCLOPAEDIA BRITANNICA SALES LIMITED, (formerly known as Coab Merchandising Company Limited), a company incorporated under the laws of the Province of Ontario, (hereinafter called the "Purchaser")

OF THE SECOND PART

WHEREAS the Purchaser has agreed to buy and the Vendor has agreed to sell, assign, transfer, convey and/or set over unto the Purchaser all the business, undertaking, property and assets relating to the business of sales agent for Encyclopaedia Britannica of Canada Ltd (including the construction, ownership and operation of Britannica House) formerly carried on by the Vendor in the City of Toronto and throughout Canada as the same are shown in the financial statement as at April 1, 1961 which is annexed hereto as Schedule "A", and made a part hereof,

NOW THEREFORE THIS AGREEMENT WITNESSETH THAT:

1 The Vendor hereby sells, assigns, transfers, conveys and sets over unto the Purchaser all the business, undertaking, property and assets of the said business of the Vendor carried on in Canada as at March 31, 1961 as distributor of Encyclopaedia Britannica Publications issued for sale by Encyclopaedia Britannica of Canada Limited, together with all of the assets, rights and interests of the Vendor in and to the building and building project known as Britannica House and located on Bloor Street West in the City of Toronto, at or for the aggregate price or sum of \$471,627 46 representing the sum of the constituent purchase prices of the assets described in Schedule "A"

2. The aforesaid purchase price of \$471,627 46 shall be payable by the Purchaser by the assumption of liabilities in the sum of \$156,688 73 and by delivery to the Vendor of a promissory note payable upon demand in the sum of \$314,938 73.

3. The Purchaser covenants and agrees to pay the sum of not less than \$210,000 00 on or before the 30th day of September, 1961 in partial payment of the unpaid balance of the purchase price secured by the promissory note hereinbefore described

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4. The Vendor covenants and agrees to save the Purchaser harmless of and from all debts, claims or liabilities not disclosed in Schedule "A" hereto that may hereafter arise in respect of the conduct of the business of the Vendor the subject of this sale and purchase prior to the first day of April, 1961.

5. The Vendor covenants and agrees to execute and deliver all such further instruments of conveyance, deeds, bills of sale and other documents required to assure to the Purchaser title to the assets of the business of the Vendor the subject of this agreement of sale and purchase.

6. This agreement shall be binding upon the Vendor, his heirs, executors, administrators and assigns, and upon the Purchaser, and its successors and assigns.

IN WITNESS WHEREOF this agreement has been executed and delivered by the parties hereto as of the day first above written.

SIGNED, SEALED AND DELIVERED

in the presence of (signed) R. M. KLEEB	}	(signed) Coleman C. Abrahams <hr/> Coleman C. Abrahams (seal)
(signed) R. M. KLEEB	}	ENCycLOPAEDIA BRITANNICA SALES LIMITED <hr/> (signed) Kurt R. Swinton

SCHEDULE "A" TO MEMORANDUM OF AGREEMENT DATED 1ST DAY OF APRIL, 1961 BETWEEN COLEMAN C. ABRAHAMS AND ENCycLOPAEDIA BRITANNICA SALES LIMITED

ASSETS PURCHASED

Britannica House—Cash.....	\$ 24,838.33	
Construction in Progress	74,458.55	
	\$ 99,296.88	
Accounts receivable from Encyclo- paedia Britannica of Canada Ltd. (value \$208,875.30)	5,000.00	
Land	\$ 75,000.00	
Buildings	150,000.00	
Furniture and Fixtures 135,000 00	\$ 360,000.00	
Automobile	7,330.58	
	372,330.58	
		\$ 471,627.46

LIABILITIES ASSUMED

Mortgage payable	42,000.00	
Rainy Day Savings Fund— Payable...	65,391.85	
Due E. H. Houghton.....	49,296.88	
	\$ 156,688.73	
Amount due to Coleman C. Abrahams.....		\$ 314,938.73

PAGE 2 TO SCHEDULE "A"

ENCYCLOPAEDIA BRITANNICA SALES LIMITED

Financial Statement showing Assets and Liabilities referred to in Agreement
dated 1st day of April, 1961 between Coleman C. Abrahams and
Encyclopaedia Britannica Sales Limited

ASSETS		LIABILITIES	
CURRENT		CURRENT	
Cash on hand and in bank	\$ 24,838.33	Mortgage payable (see note 1)	\$ 12,000 00
Accounts receivable	5,000.00		
	<hr/>		
	\$ 29,838.33	LONG TERM	
		Mortgage payable	\$ 30,000 00
		(see note 1)	
		Rainy Day Savings Fund	65,391.85
		Due E. H. Houghton	49,296.88
			<hr/>
			\$ 144,688 73
FIXED		OTHER	
Land	\$ 75,000.00	Due Coleman C. Abrahams per agreement.	\$ 314,938.73
Buildings	150,000 00		
Furniture and Fixtures	135,000.00		
Automobile	7,330.58		
Construction in progress	74,458.55		
	<hr/>		
	\$ 441,789.13		
	<hr/>		
	\$ 471,627.46		
	<hr/> <hr/>		<hr/> <hr/>
			\$ 471,627.46

NOTE 1: Total mortgage due \$42,000.00, of
which \$12,000.00 is due and payable within
the current fiscal year.

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On March 15, 1962, the Board of Directors of Encyclopaedia Britannica Sales Limited passed a resolution reading as follows:

PURCHASE OF ASSETS

The Chairman presented to the meeting an agreement made the 1st day of April, 1961, between Coleman C Abrahams and the Company providing for the sale to the Company of all the business, undertaking, property and assets related to the business of sales agent for Encyclopaedia Britannica of Canada Ltd (including the construction, ownership and operation of Britannica House) formerly carried on by Coleman C Abrahams in the City of Toronto and throughout Canada as more particularly described in the said agreement, a copy of which appears as Schedule B hereto

The Chairman also stated that pursuant to the terms of the said agreement the Company had paid the sum of \$260,000 in the aggregate to the vendor hereunder. On motion duly made and seconded and unanimously carried, the following resolution was passed:

BE IT RESOLVED THAT

1. the agreement made the 1st day of April, 1961, between Coleman C. Abrahams and the Company providing for the sale of assets as hereinabove described be and the same is hereby approved

2. the payments made by the Company in the aggregate of \$260,000 pursuant to this agreement be and the same are hereby approved, ratified, sanctioned and confirmed

An agreement bearing date April 1, 1961 was entered into between Encyclopaedia Britannica of Canada Ltd. *et al.* and another wholly-owned company of the appellant called Educational Publications Limited, whereby the latter company was granted "the exclusive right, franchise and licence to distribute and sell" certain of the grantor's publications in consideration of paying to the grantor an amount equal to 55 per cent of "net sales". An agreement bearing the same date was entered into between Educational Publications Limited and Encyclopaedia Britannica Sales Limited whereby it assigned that franchise to Encyclopaedia Britannica Sales Limited in consideration of a promise by the latter company to pay the assignor one and one-half per cent. of the sales. Until October 1961, there was no change in the operations of the sales organization under the appellant. Beginning about that time, changes were made to reflect the fact that the commission salesmen and other employees in the organization had become or were becoming employees of Encyclopaedia Britannica Sales Limited.

An analysis of the sale agreement dated April 1, 1961, whereby the appellant sold the "business, undertaking,

property and assets" of his business as distributor of Encyclopaedia Britannica publications shows that the only asset of the business so sold in respect of which any payment was made was "Accounts receivable from Encyclopaedia Britannica of Canada Ltd. (value \$208,875.30)" which was included in the agreement as being sold for \$5,000. The amount of \$208,875.30 is the amount or the total of the amounts that, in accordance with the arrangements that I have already described would have been payable some time or times after April 1, 1961, in respect of amounts that had been credited to his account before that time subject to

- (a) any "chargebacks" that might have arisen after April 1, 1961,
- (b) a question (raised by the respondent) as to whether certain payments to be made in the future to salesmen under a plan known as the Rainy Day Savings Fund, amounting in all to \$65,391.85, were or should have been charged against the appellant, and
- (c) a question (raised by the respondent) as to whether a balance of \$129,615.25 shown by the "loan" account to be owing by the appellant to Encyclopaedia Britannica of Canada Ltd. should have been charged against the appellant in determining the amount payable by the company to him under the arrangement already described.

On September 30, 1961 and October 1, 1961, the following cheques were issued and delivered:

- (a) Encyclopaedia Britannica of Canada Ltd. to Encyclopaedia Britannica Sales Limited \$208,875.80,
- (b) Encyclopaedia Britannica Sales Limited to the appellant \$210,000.
- (c) the appellant to Encyclopaedia Britannica of Canada Ltd. \$149,615.25.¹

As indicated above, the sale agreement between the appellant and Encyclopaedia Britannica Sales Limited was executed three or four days after this issuance and delivery of cheques.

¹ This amount is in respect of the \$129,615.25 previously referred to as loans made to the appellant by Encyclopaedia Britannica of Canada Ltd. to the appellant prior to April 1, 1961, plus a subsequent loan of \$20,000.

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The Rainy Day Savings Fund, to which reference has already been made, was an arrangement that was in force during the period commencing January 1, 1961, under which, for purposes of current payments to salesmen, they were only credited with 90 per cent. of the scheduled commissions and the remaining 10 per cent. was placed to their accounts for payment to them, subject to the deduction of chargebacks arising in the meantime, several months after the determination of their respective employments. The amounts, so payable to salesmen in the future, that had been credited to salesmen on or before March 31, 1961, totalled \$65,391.85. This amount was not deducted in determining the amount of the receivable of \$208,875.30 that the appellant purported to assign to Encyclopaedia Britannica Sales Limited and was included in the liabilities of the appellant that Encyclopaedia Britannica Sales Limited purported to assume, by the agreement dated April 1, 1961, for the sale to it of the appellant's business.

The above is a sufficient background of the facts that are not in controversy to appreciate the issues upon which the parties have agreed as being the issues, and the only issues, between them in this appeal. These issues have been stated by the parties as follows:

- 1 Whether there was a sale within the meaning of 85*d* on or before April 1, 1961 from Abrahams to E.B.S.L.
- 2 Whether there was a sale at any time of all or substantially all of the business or the property used in carrying on the business.
3. Whether there was at any time a sale of debts that had been or would have been included in computing Abrahams' income tax for 1960 or 1961 and that were still outstanding at the time of sale.
- 4 Whether EBSL continued the business which Abrahams had carried on prior to April 1, 1961.
- 5 If the Appellant is found to have satisfied the provisions of 85*d*, what is the effect of Section 17(2) and Section 23 of the *Income Tax Act*.
- 6 Assuming Section 85*d* applies:
 - (a) whether the Rainy Day Savings Fund of approximately \$65,000.00 was a debt within 85*d* and a debt that had been or would have been included in computing Abrahams' income for 1961 or 1960 and was outstanding at the time of the sale;
 - (b) whether the sum of \$129,000 should be deducted from the sum of approximately \$208,000 to determine the "debts" upon which an election under 85*d* can be made
7. Whether the Respondent had the right to issue a second assessment after Appeal had been filed in respect of the previous assessment.

Counsel for the respondent agreed that, if the issues stated in the first four paragraphs are decided in the affirmative, the appellant is entitled to succeed subject to his being defeated by the decision of the issue stated in paragraph 5 and subject to the amount of his success being diminished by the decision of the issue stated in paragraph 6. It is common ground that, if any of the issues stated in the first four paragraphs are decided in the negative, the appeal must be dismissed subject to a contention put forward on behalf of the appellant after the agreement on issues that, if the evidence establishes that there was such a sale before September 30, 1961, that sale is of the same effect as though there were a sale on or before April 1, 1961.

The issue stated in paragraph 7 has been disposed of by the reasons for judgment that I am issuing concurrently in a companion appeal and need not be referred to further in relation to this appeal.

I propose now to deal with the first issue, namely,

Whether there was a sale within the meaning of 85D on or before April 1, 1961 from Abrahams to E.B.S.L.

“E.B.S.L.” here means Encyclopaedia Britannica Sales Limited, “Abrahams” is the appellant and “85D” is section 85D of the *Income Tax Act* as applicable to the 1961 taxation year, which reads as follows:

85D (1) Where a person who has been carrying on a business has, in a taxation year, sold all or substantially all the property used in carrying on the business, including the debts that have been or will be included in computing his income for that year or a previous year and that are still outstanding, to a purchaser who proposes to continue the business which the vendor has been carrying on, if the vendor and the purchaser have executed jointly an election in prescribed form to have this section apply, the following rules are applicable:

- (a) there may be deducted in computing the vendor's income for the taxation year an amount equal to the difference between the face value of the debts so sold (other than debts in respect of which the vendor has made deductions under paragraph (f) of subsection (1) of section 11) and the consideration paid by the purchaser to the vendor for the debts so sold;
- (b) an amount equal to the difference described in paragraph (a) shall be included in computing the purchaser's income for the taxation year;
- (c) the debts so sold shall be deemed, for the purposes of paragraphs (e) and (f) of subsection (1) of section 11, to have been included in computing the purchaser's income for the taxation year or a previous year but no deduction may be made by the purchaser under paragraph (f) of subsection (1) of section 11 in respect of a debt in respect of which the vendor has previously made a deduction; and

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(d) each amount deducted by the vendor in computing income for a previous year under paragraph (f) of subsection (1) of section 11 in respect of any of the debts so sold shall be deemed, for the purpose of paragraph (f) of section 6, to have been so deducted by the purchaser.

(2) An election executed for the purposes of subsection (1) shall contain a statement by the vendor and the purchaser jointly as to the consideration paid for the debts sold by the vendor to the purchaser and that statement shall, as against the Minister, be binding upon the vendor and the purchaser insofar as it may be relevant in respect of any matter arising under this Act

The general purpose of this section is to change the rules applicable to accounts receivable to which the vendor and purchaser of a business were previously subject. Accounts receivable (for goods sold by a trader) become gross income in the year in which they arise subject, in effect, to a subsequent deduction for such of them as become bad or doubtful in the years in which they become bad or doubtful. Prior to the enactment of section 85D, upon the sale of the assets of a business, including the accounts receivable, as part of the sale of the business as a going concern, there was no allowance for any loss in respect of the sale of the accounts receivable and, of course, there could have been no subsequent occasion for any deduction in respect of any of them becoming bad or doubtful. On the other hand, the purchaser of a business including the accounts receivable was not, prior to that time, required to bring them into the computation of his income from the business and he was not therefore entitled to make any deduction by reason of any of them becoming bad or doubtful. Section 85D makes it possible, if the vendor and purchaser agree, for the vendor to deduct, in computing his income from the business for the year of sale, the amount of his loss upon the sale of the accounts receivable and, in such event, requires the purchaser to take that same amount in as part of his income from the business for that year and then permits the purchaser to make deductions in respect of such of the accounts receivable as become bad or doubtful.

Obviously, in the case of an arm's-length transaction, the provision would seem to be fair from the point of view of not only the vendor and the purchaser, but also from the point of view of the Minister of National Revenue. In the case of a sale to a person with whom the purchaser is not dealing at arm's length, it would seem that any possibility

of the provision being used to avoid tax is defeated by subsection (2) of section 17, which reads as follows:

(2) Where a taxpayer carrying on business in Canada has sold anything to a person with whom he was not dealing at arm's length at a price less than the fair market value, the fair market value thereof shall, for the purpose of computing the taxpayer's income from the business, be deemed to have been received or to be receivable therefor.

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Coming back to the first issue, it raises for determination the mixed question of fact and law as to whether Encyclopaedia Britannica Sales Ltd. entered into a contract with the appellant on or before April 1, 1961, the terms of which are reflected by the written contract between them bearing that date but executed on October 4, 1961.

The appellant does not contend that there is any direct evidence of the two parties having so agreed before that day in the sense that one made an offer to the other that was accepted or in the sense that the terms were written down or otherwise crystallized or enumerated so that both parties could and did manifest an intention of entering into a business agreement on those terms. The appellant does say, however, that a study of what happened in fact during the period preceding and following April 1, 1961, leads to an inference, on a balance of probability, that such an agreement had been entered into on or before that day.

I have not been able to find that the facts lead to any such an inference.

In the first place, vital terms such as the description of the property being sold and the price to be paid therefor were not settled on April 1, 1961. This is apparent from a review of all the evidence. For example, as late as May 30, 1961, as appears from the solicitor's letter of May 31, 1961, the appellant was being advised as to what amount should be put in the agreement as the consideration for the accounts receivable, and, in August, the solicitor submitted a draft of the agreement that differed, so far as material terms are concerned, from the agreement finally executed on October 4, 1961.

In the second place, there is no evidence of any corporate act by Encyclopaedia Britannica Sales Ltd. until the resolution of March 15, 1962, which may be regarded as ratifying the execution of the agreement that was executed on October 4, 1961. There is no evidence that any person who

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was engaged in any of the negotiations before October 4, 1962, held any office in the company or otherwise had any authority to negotiate on behalf of the company.¹ While, as against third parties, the intent of a closely held company is to be judged by the acts of those who are in charge of its affairs and the Court is bound to assume that the owner of all the shares of a company who purports to act on its behalf has taken the necessary steps to give himself the authority he purports to have, when it is a question of establishing, as between such a person and third parties, that he has entered into a contract with a company all of whose shares belong to him, in my view, evidence is required to establish that there has in fact been a formulation and expression of the intent of the company, which is not, after all, a person of flesh and blood having a mind of its own, in one of the modes contemplated by the law, namely, a resolution of the Board of Directors or an act of an officer, servant or agent of the company acting in the course of employment or of the agency. Here, there is no such act established by the evidence (a director being, as such, neither an officer, a servant nor an agent) until March 15, 1962, although it is arguable that the resolution passed then constitutes ratification of the execution of the contract on behalf of the company on October 4, 1961.

This lack of any evidence of any corporate act having effect prior to October 4, 1961, is an insurmountable answer, in my view, to any contention that there was a sale agreement before the \$208,875.30 was paid on September 30, 1961 or October 1, 1961, by Encyclopaedia Britannica of Canada Ltd.²

It becomes unnecessary, therefore, to reach a final conclusion as to whether there is a balance of probability on all

¹ The witness Swinton did say that he was a director of "EBSL." (by which he meant Encyclopaedia Britannica Sales Limited) and that he conferred "on behalf of E.B.S.L." with the appellant, many times, in the preparation of the agreement between "E.B.S.L." and the appellant. There is no evidence of any authority for him, as an individual director, to negotiate such an agreement and, in my view, it is not authority that would be implied in respect of a director. Furthermore, he does not say that he purported to act for "EBSL" in making an agreement on its behalf with the appellant at some time prior to the execution of the written agreement.

² Obviously, once the debt was paid, it could not be the subject of a sale to a third person

the evidence that all the terms of the sale agreement were agreed upon by the individuals concerned at some time between the creation of the draft agreement accompanying the lawyer's letter of August 30, 1961 and the issuance and delivery of cheques which was provided for by a lawyer's letter of August 31, 1961 and carried out on September 30 and October 1, 1961. My view is, however, that the balance of probability is that the various individuals who were advising the appellant and Encyclopaedia Britannica of Canada Ltd. regarded the settlement of all the terms and the creation of the sales agreement between the appellant and his wholly-owned company as mere legal technicalities, the timing of which was of no great significance and proceeded with the more important practical steps in the confident expectation that what they regarded as legal technicalities would be filled in at leisure.¹ I am not convinced, therefore, that the issuance and delivery of the cheques establishes, on a balance of probability, that all the terms of the agreement had already been agreed upon.

Having reached that conclusion, it follows that the appeal must be dismissed.

I do not propose, therefore, to make any finding with regard to the issues in the paragraphs numbered 2, 3 and 4 *supra*. I might make this comment, however, that a discussion of these issues assumes an air of fantasy and unreality when all the evidence² points to the conclusion that the appellant directed the operations of the sales organization that I referred to earlier as an employee of the company while the appellant takes the position, and the respondent concedes, that he did so as an independent contractor. In these circumstances, it would seem that this might be a case where the evidence and the admission made by counsel for the Minister cannot stand together, in which event, the admission should be taken to have been made under a

¹ Compare *Angel v. Hollingworth & Co*, (1958) 37 TC 714, per Vaisey J. at page 723: "In other words, they regarded and treated as an accomplished fact that which was not an accomplished fact but only a well grounded expectation that it would become an accomplished fact, as in due course it did.

² I am ignoring evidence by laymen as to the legal state of affairs at different stages as they were only competent to give evidence of the *facts* as they knew them. I have in mind particularly an employment contract executed on October 1, 1955 between the appellant and Encyclopaedia Britannica of Canada Ltd. which, according to the appellant's answers on discovery, was still in force until April 1, 1961.

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misapprehension and it is the duty of the Court to have regard to the real facts as shown by the evidence. See *Sinclair v. Blue Top Brewing Co.*¹ at page 562. If this principle applies in a cause between ordinary persons, it would seem to have even greater application where the revenue is involved.

With reference to the issue in the paragraph numbered 5 *supra*, I content myself with saying that, as it appears to me, subsection (2) of section 85D makes the statement provided for therein binding on the vendor and purchaser (but only "as against the Minister"). It does not make the statement binding on the Minister. Neither the language nor the scheme of the provision supply any reason for preventing the Minister from inquiring into the veracity of the statement. Furthermore, I see no reason why subsection (2) of section 17—but not section 23—does not apply to the facts of this case. The only submission of the appellant in support of the view that subsection (2) of section 17 does not apply was based on the view that there is a conflict between that provision and section 85D. There is, in my view, no such conflict, and therefore no room for application of the rules as to which of two provisions applies where there is a conflict between them. I should therefore have concluded that the appeal must be dismissed upon a decision of the fifth issue even if I had reached a different conclusion on the first one.

With regard to the sixth issue, if I had to decide it, I should decide that the respondent was correct with regard to both amounts.

The loans or advances, in my view, are advances made in accordance with the contract between the appellant and Encyclopaedia Britannica of Canada Ltd. on October 1, 1955, whether they were made on a regular basis as in the case of the \$500 per week or were special advances in special circumstances. There is no doubt, in my mind, that, if the appellant had sued for the balance owing to him and had objected to the deduction of any of these amounts, Encyclopaedia Britannica of Canada Ltd. would have successfully contended that they were all deducted in accordance with the governing agreement.

The amounts credited to salesmen under the Rainy Day Savings Fund plan, in my view, were amounts payable by

¹ [1947] 4 D.L.R. 561.

Encyclopaedia Britannica of Canada Ltd. to its salesmen, who were its employees, just as were all the other amounts of remuneration payable to them. Those amounts were therefore deductible, in accordance with the governing agreement, in determining the balances owing to the appellant. Whether the payment of the balance without deducting such amounts was the result of a mistake or of an arrangement under which the appellant assumed the responsibility of paying the salesmen, it cannot make such an amount a debt that has been or will be included in computing the appellant's remuneration for the services rendered to the company. (The fact that, in the computation that he filed with his return, the appellant showed a gross amount from which he deducted *inter alia* the amount in question does not establish that such amount was included in computing his income for the year—this was merely the calculation by which one determined the balance payable to him as remuneration for the year.)

Either party may apply for judgment in accordance with these reasons and, at that time, I shall be glad to hear submissions as to costs.

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