

BETWEEN:

BESSIE L. SHAW ..... APPELLANT;

AND

MINISTER OF NATIONAL REVENUE.. RESPONDENT.

1938  
 May 5.  
 —  
 Nov. 23.

*Revenue—Income tax—Income War Tax Act, s. 3 (b), s. 5 (k)—“Income from but not the proceeds of life insurance policies”—“Income”—Liability for tax.*

The Sun Life Assurance Company of Canada issued a policy of insurance upon the life of appellant's husband, appellant being named the owner and beneficiary therein. The policy was described as “Guaranteed Income Life—Monthly Instalments—Annual Dividend Plan” and provided that on the death of the assured the company would pay to the beneficiary mentioned therein “the sum of Seven Hundred Dollars and a like monthly instalment on the same day in each succeeding month until one hundred and twenty monthly instalments in all shall have been paid . . . The company further agrees that if the beneficiary . . . shall still survive after the payment in full of the one hundred and twenty monthly instalments . . . the company shall continue to pay to the said beneficiary the sum of Seven Hundred Dollars monthly on the same day in each month . . . so long as she may survive thereafter; . . . It is further agreed that when the first instalment under this policy becomes due, as above, the person or persons legally entitled to receive said first instalment shall have the option of commuting all instalments into a single cash payment of Seventy-One Thousand Four Hundred Dollars and the payment of this amount shall completely discharge the company from all liability in connection with this contract.”

Appellant, upon the death of the assured, did not elect to accept the cash payment of \$71,400, and the monthly instalments stipulated in the contract have been paid to and received by her since that time. In the year 1934 she received the sum of \$8,400 which was assessed for income tax. The assessment was affirmed by the Minister of National Revenue from whose decision appellant appealed.

*Held:* That such monthly payments constitute “income” and appellant is liable for tax thereon.

2. That the contract herein is not like the annuity contracts mentioned in s. 5 (k) of the Act and the appellant is not entitled to any exemption or deduction.

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APPEAL under the provisions of the Income War Tax Act from the decision of the Minister of National Revenue.

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

*I. F. Hellmuth, K.C.* and *H. C. F. Mackridge* for appellant.

*F. P. Varcoe, K.C.* and *J. R. Tolmie* for respondent.

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

THE PRESIDENT, now (November 23, 1938) delivered the following judgment:

This is an appeal from the decision of the Minister of National Revenue affirming an assessment for income tax levied against the appellant under the Income War Tax Act, for the 1934 taxation period. The pleadings and a Statement of Admitted Facts disclose that the appellant is the widow of the late Mr. G. B. Shaw, of Toronto, who died on or about November 23, 1933; and that before the decease of Mr. Shaw a policy of insurance was taken out on his life, with the Sun Life Assurance Company of Canada, upon the application of his wife, the appellant, who paid the annual premiums thereon, amounting to \$6,265, except that all dividends earned by the policy during the lifetime of the husband were from time to time, on the election of the appellant, applied in reduction of the annual premium. The contract of insurance provided that the appellant should be paid, on the death of her husband, the sum of \$700 per month for a guaranteed term of one hundred and twenty consecutive months, and should she survive that term she was to be paid the same monthly instalment so long as she lived, but she had the option of commuting all such monthly instalments into a single cash payment of \$71,400.

The principal provisions of the contract are brief and had better be recited. They are as follows:

Sun Life Assurance Company of Canada hereby agrees that on receipt and approval at its Head Office in Montreal of the proofs of the fact and cause of the death of GEORGE BALDWIN SHAW of Toronto, Ontario (herein called the assured) and of the title of the claimant, it will pay to BESSIE LOUISE SHAW (herein called the owner) (herein called the beneficiary) the sum of SEVEN HUNDRED DOLLARS and a like monthly instalment on the same day in each succeeding month until

one hundred and twenty monthly instalments in all shall have been paid.

Each instalment payable by the Company under this policy shall be paid to the said BESSIE LOUISE SHAW.

The Company further agrees that if the beneficiary above described by name shall still survive after the payment in full of the one hundred and twenty monthly instalments mentioned above, the Company shall continue to pay to the said beneficiary the sum of SEVEN HUNDRED DOLLARS monthly on the same day in each month as that on which the preceding instalments became due, so long as she may survive thereafter; provided always that satisfactory proof in writing be furnished to the Company that the said beneficiary be still living at the time each such subsequent payment becomes due, and in default of such proof, no further payment (fractional or otherwise) shall be made.

It is further agreed that when the first instalment under this policy becomes due, as above, the person or persons legally entitled to receive said first instalment shall have the option of commuting all instalments into a single cash payment of SEVENTY-ONE THOUSAND FOUR HUNDRED DOLLARS and the payment of this amount shall completely discharge the Company from all liability in connection with this contract; provided always that this option cannot be exercised by the beneficiary or payee unless the owner shall have filed with the Company a written request to that effect, or shall have so expressed his desire by will.

The insurance policy is described at the foot of the first page, and in the endorsement on the back, as "Guaranteed Income Life—Monthly Instalments—Annual Dividend Plan." The policy was to participate in profits at the expiration of each year from the date on which the first premium fell due, and such profits were to be allotted to the policy in one of four forms, one of which was "as a reduction of the premium for the ensuing year." Dividends accrued under the policy in the aggregate sum of \$6,815.15 and were applied in reduction of the annual premiums from time to time, from the date of the contract until the death of Shaw, some six or seven years thereafter. The appellant did not, upon the death of her husband, elect to exercise the option of commuting the monthly instalments into a single cash payment of \$71,400, and consequently the monthly instalments stipulated in the contract have been paid to and received by the appellant since the death of her husband. In the year 1934 she received the sum of \$8,400, which was assessed for the income tax, and the appeal herein is in respect of such assessment.

There are two points for decision in the case. First, is the sum of \$8,400, the annual amount of the monthly instalments, subject to the income tax, in addition to the

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other income of the appellant from other sources, and secondly, if this amount is to be treated as taxable income is it subject to a deduction of \$5,000, or \$1,200, or any sum?

The relevant section of the Income War Tax Act in this dispute is s. 3 and ss. (b). Together they read as follows:

For the purposes of this Act income means the annual net profit or gain or gratuity . . . , and also the annual profit or gain from any other source including (b) the income from but not the proceeds of life insurance policies paid upon the death of the person insured, or payments made or credited to the insured on life insurance endowment or annuity contracts upon the maturity of the term mentioned in the contract or upon the surrender of the contract.

It is evident that s. 3 (b) contemplates the taxation of "income" derived from life insurance policies or annuity contracts. In this case we are concerned with a life insurance policy or contract, the main provision of which provided that if the appellant survived her husband she would be entitled to a monthly payment of \$700, for one hundred and twenty consecutive months, and similarly so long thereafter as she continued to live. The payment of one hundred and twenty instalments was guaranteed and in respect of those instalments the appellant is described in the policy as the "owner," and therefore she could dispose of the same as she might any other property which she owned. The policy itself, as I have already pointed out, is described by the company issuing the same as "Guaranteed Income Life," payable in monthly instalments, and the policy was entitled to participate in profits after the end of the first policy year and during the lifetime of the assured, all of which means that if the appellant survived her husband she was to be paid, as owner, a monthly sum of \$700, for one hundred and twenty months, and if she survived that period the insuring company agreed to pay her the same monthly instalment so long as she lived.

The taxable "income" referred to in s. 3 (b) whatever it may comprise, provides for no exemption or deduction, but the section, for the purposes of clarity and greater certainty states that certain payments or receipts, flowing from life insurance policies or annuity contracts, are not to be included as "income" within the meaning of s. 3 (b). In the first place the proceeds of a life insurance policy paid upon the death of the person insured are not to be construed as income; such proceeds are to be regarded as capital and not income, in the hands of the recipient. In

the next place payments made or credited to the insured on "life insurance endowment or annuity contracts" upon the maturity of a term or terms mentioned in the contract are not to be treated as "income." This may be illustrated by reference to a life insurance endowment contract where, for example, the face of the policy was \$5,000, but at the end of a stated term the payments to be made or credited to the insured under the policy, or to a beneficiary, might, by reason of the accumulation of profits, reach the sum of say \$7,000; in that case the payment or credit of the accumulation of profits, \$2,000, is not to be treated as "income," at least that is my view in such a case. That illustration would be applicable to life insurance annuity contracts if similar payments or credits were made, or earned, and the words of the section read "life insurance endowment or annuity contracts." That is the kind of payment or credit to which, I think, the section refers. Payments made or credited to the insured here mean, I think, a distribution of profits at the end of a term or terms, or a payment made on the surrender of a policy, neither of which would be income within the meaning of s. 3 (b).

Now, was the \$8,400 received by the appellant in the 1934 taxation period "income" from the insurance policy in question here? It was not, I think, the proceeds, or a part of the proceeds, of the policy. The appellant might have commuted the monthly instalments or income, surrendered the contract, and received a single cash payment of \$71,400, which, I think, would be the "proceeds" of the life insurance policy. But the appellant did not exercise her option to do this and therefore the insuring company at once commenced to pay to her, on the death of her husband, the monthly sum of \$700, as it was obligated to do. Some \$43,000 had been paid in the way of premiums to ensure the payment of this monthly income to the appellant, upon the death of her husband. It matters not whether the obligation of the insuring company be called a life insurance annuity contract or a plain annuity contract. We are here concerned only with the true nature of the insurance contract in question and particularly the nature of the payments made thereunder to the appellant; the contract required the insuring company to pay to the

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appellant a fixed monthly sum if she survived her husband, virtually for the balance of her life, and the question is whether or not that is "income" from a life insurance annuity contract. We need not really be concerned about the words "payments made or credited to the insured," because in point of fact no payments were ever made or credited to the insured, and therefore no difficulty arises on that account. In this case any dividends or profits paid or credited on the maturity of any term, went in reduction of the annual premium payable by the appellant.

The words "payments made or credited to the insured" do not therefore, in my opinion, occasion any real difficulty here, and do not seriously enter into the debate. Further, this is not a case of the surrender of a life insurance contract. It seems to me that this insurance contract was entered into expressly for the purpose of giving the appellant a monthly income during her life, in the event of her surviving her husband, and really that is what the contract states. That is the sense and real purpose of the contract. The appellant did not elect to take the proceeds of the policy, the capital worth of the policy, she preferred to take the income. I think therefore that such monthly receipts constitute "income," and that the appellant is subject to the income tax upon the monthly instalments received by her in 1934.

There remains the further question as to whether the appellant is entitled to any exemption or deduction under the provisions of ss. (k) of s. 5 of the Act, or any corresponding section earlier enacted and repealed. An annuity contract with the Dominion Government cannot be issued on the life of any one other than the actual annuitant, and therefore such a contract is not "like" the policy or contract of life insurance under which an annuity, or income, is now being paid to and received by the appellant, and therefore I do not think that the appellant is entitled to any exemption or deduction. The reason for the distinction between a Dominion Government Annuity Contract and the contract in question here, in respect of exemptions and deductions, is not for the court to explain.

This is a case of first impression, and one in which I think I would be fully justified in refraining from making any order as to costs.

*Judgment accordingly.*