BETWEEN:

MONTREAL TRUST COMPANY (Trustee of LODESTAR DRILLING COMPANY, a bankrupt) ... APPELLANT;

1960 Apr. 4

1961 May 9

AND

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

Revenue—Income—Income tax—Sale of mineral rights by oil drilling company—Whether proceeds income or capital—Charter powers—Amended tax return not filed within statutory delay—Discretionary power of Minister—The Income Tax Act, S. of C. 1948, c. 52, ss. 3, 4, 20(1)(d), 40(1)(a) and 42(4A) as enacted by S. of C. 1951, c. 51, s. 14—The Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4 and 46(5).

The Lodestar Drilling Co. which carried on the business of drilling by contract, was empowered by its charter to acquire and sell mineral rights. In 1952 it sold a one-half interest in an oil lease for $27,500 and treated the sum received as a capital receipt. In filing its income tax return for its taxation year ending March 31, 1952 the company declared a profit of some $114,900 and for 1953 a loss of some $3,500. On September 30, 1953, it filed an amended tax return and claimed as a deduction from its income for 1952 the loss suffered in 1953. By notice of re-assessment dated April 28, 1955 the Minister added the $27,500 to the declared income for 1952 and allowed less than one-third of the loss claimed. In October 1953 the company made an assignment in bankruptcy and the Trustee after revising the company's accounts to provide for additional capital cost allowance not previously claimed, on June 2, 1955 filed amended tax returns for 1952 and 1953 in which a loss of some $53,000 alleged to have been incurred in 1953 was claimed as a deduction from the 1952 income. Subsequently the Trustee filed a notice of objection to the assessment in respect of 1952 and the Minister by notice dated August 28, 1956 confirmed the assessments. In an appeal from a decision of the Income Tax Appeal Board upholding the assessment, the appellant contended that the $27,500 payment constituted a capital receipt which should not have been included in its income, and that by reason of the increased capital cost allowance now reflected in its books, the deduction in respect of loss incurred in 1953 should be increased accordingly.

Held: That the $27,500 payment was properly assessed as income since it was a gain made in the operation of a business in carrying out a scheme for profit-making which the company by its charter had power to undertake.

2. That since the amended tax return filed by the Trustee was not, as required by s. 42(4A) of the *Income Tax Act, 1948,* filed within one year from the day on or before which the taxpayer was required by s. 40(1) of the Act to file the original return, it was within the discretionary powers of the Minister to refuse to re-assess beyond the allotted delay.

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APPEAL from a decision of the Income Tax Appeal Board[1].

The appeal was heard before the Honourable Mr. Justice Dumoulin at Calgary.

R. A. MacKimmie, Q.C. and *F. R. Mathews* for appellant.

R. L. Fenerty, Q.C. and *T. E. Jackson* for respondent.

DUMOULIN J. now (May 9, 1961) delivered the following judgment:

This is an appeal from a decision of the Tax Appeal Board[1] dated February 6, 1958, affirming the income tax re-assessment, on April 28, 1955, of Lodestar Drilling Company Ltd., for taxation year 1952.

Lodestar Drilling Company Ltd. (formerly of Calgary, Alta., hereinafter called the Company) was incorporated on March 17, 1949, and, since that date, carried on, as a contractor, the business of drilling petroleum and natural gas wells for owners of petroleum and natural gas rights.

This Company, for the fiscal years ending March 31, 1952 and 1953, declared its income to be:

Year ended March 31, 1952 (ex. 1) ....$114,916.05 Income
Year ended March 31, 1953 (ex. 2) ....$ 3,516.00 Loss.

Lodestar's T2 return for 1952 shows that this global income of $114,916.05 comprises a provision of $51,185.24 for tax liability to the Dominion Government (Cf. ex. 1).

In February, 1952, the Company ceded to another western concern, Realty Oils Ltd., at a price of $27,500, an undivided one-half interest in presumably oil bearing properties it had acquired from Trans Empire Oils Ltd. (through the nominal intermediary of its own President and agent, Mr. William Ford) the same month and year, also for a consideration of $27,500. These three transactions are related in exhibits 7, 8 and 9.

In computing its income for the 1953 fiscal year, the Company did not include this 1952 receipt of $27,500 from Realty Oils, nor, and this omission is more readily understandable, did it make any mention of its purchase from Trans Empire Oils Ltd.

[1] 18 Tax A.B.C. 18; 58 D.T.C. 131.

By September 1953, the Company's financial condition had precariously deteriorated, and on September 30, it filed an amended return for 1952 (ex. 3) pursuant to s. 46(5) of the Act, claiming, as a deduction from income for that year, a loss of $3,516 incurred during the 1953 period, thereby reducing the taxable income of $114,916.05 reported on the original return, (ex. 1) to $111,400.05.

Notices of re-assessment in respect of years 1952-1953 were sent the Company on April 28, 1955, one of two crucial dates in the determination of the instant case, and the taxable income was then set out as hereunder:

Taxation year 1952

Taxable income previously assessed:	$114,916.05
Add: Proceeds of sale of interest in Farmout from Trans Empire Oils:	27,500.00
Revised assessed income:	$142,416.05
Deduct: 1953 loss applied	1,073.15
Revised taxable income:	$141,342.90

This re-assessment allowed less than one third of the $3,516 loss to which the Company laid claim for 1953, and inserted as a revenue item the full amount, $27,500, received by appellant from Realty Oils Ltd.

No further steps were taken about the matter until practically two years later. Meanwhile, the Company, on October 22, 1953, made an assignment under the provisions of the *Bankruptcy Act* appointing Northern Trust Co. Ltd. as Trustee, to be replaced in such capacity with the bankrupty Company by Montreal Trust.

Appellant next alleges that in June 1955, the Trustee revised the accounts of the defunct Company for its 1953 fiscal year "to provide for an additional provision for depreciation of $51,885.42 and caused revised financial statements to be prepared . . ." reflecting this heretofore undisclosed provision for depreciation.

Conformably to this revision, and I now quote s. A (i) of Appellant's Notice of Appeal:

"The Trustee *'then prepared and filed an amended return'* (italics are mine throughout) of the Company's income for the 1953 fiscal year reflecting the above adjustment, and *'at*

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the same time' the Trustee filed a revised amended return for the Company's income for the 1952 fiscal year", detailed as follows:

	1952 Income	1953 Loss
Taxable income or loss as assessed	$141,342.90	$ 1,073.15
Add additional provision for depreciation recorded in the Company's accounts		$ 51,885.42
	Income	Loss
	$141,342.90	$ 52,958.57
1953 loss applied	52,958.57	
Revised income:	$ 88,384.33	

The italics are intended to emphasize that expressions such as "then" and "at the same time" must necessarily relate to the preparation and filing of the amended 1952-1953 returns at some undisclosed date of June 1955, since, in the paragraph preceding A (*h*), appellant avers it revised the Company's accounts "in June 1955". Later still, the exact date remaining unspecified, the Trustee "filed Notice of Objection to the assessment in respect of the 1952 fiscal year and by notification by the Minister, *dated August 28, 1956,* the assessment was confirmed".

The appellant, then, bases its appeal on two grounds, namely: (cf. Statement of Facts). B.(1) (*a*) that "the proceeds of sale of one-half of the Company's interest in the Farmout Agreement above mentioned in the sum of $27,500 added to the Company's income in the said assessment represents a capital receipt which should not be included in its income", and; 2. "The deduction allowed in respect of loss incurred in the 1953 fiscal year should be increased by $51,885.42 to $52,958.57 by reason of the increased capital cost allowance now reflected in the books of the Company and as disclosed in the amended Return for the 1953 fiscal year filed by the Trustee".

Regarding its first objection, appellant argues that the $27,500 obtained for the assignment of a one-half interest in the petroleum leases to Realty Oils Ltd. (ex. 9) ". . . represents a capital receipt, properly excluded from income for the 1952 fiscal year . . .", that the asset derived by the Company via the Farmout Agreement of February, 1952 (ex. 7), is ". . . an income producing property which would be a capital asset held for investment"; finally, that

the Company not being in the business of buying and selling natural gas leases or rights to acquire the same, any such rights obtained or sold by it ". . . were not trading assets".

The "Reply to Notice of Appeal" could well have endured more explicitness. Perfunctory denials are mostly vague and seldom helpful or convincing. It so happens, however, that paragraph "13" of the Reply raised in clear enough terms a point which, if well taken, would preclude the appellant from successfully prosecuting its twofold complaint. Respondent contends that the Company is disentitled to any of the redresses sought for ". . . by virtue of s-s. (4A) of s. 42 of *The Income Tax Act* (1948) . . . in respect of the further 1953 loss claimed in the amended tax return for its 1952 taxation year, which was filed by it *in the month of June 1955, since that return was not filed within one year from the day on or before which the Appellant was required by subsection (1) of section 40 to file its return for the 1952 taxation year*".

In the closing paragraphs of these notes, reasons for considering this objection a peremptory one will be dilated upon. Even so, I had as well afford appellant the melancholy comfort of holding that none of his claims on their merits, or more precisely demerits, could otherwise be allowed.

The recent case of *Western Leaseholds Ltd. v. Minister of National Revenue*[1] decided by Mr. Justice Cameron of this Court, dealt with problems very closely allied to the instant matter arising from the assignment of a one-half interest in the drilling of natural gas wells to Realty Oils Ltd. Large sums of money received in 1949 and 1950 by Western Leaseholds Ltd. from Imperial Oil and Barnsdall Oil under options exercised and also for leasing agreement were held to be ". . . income from a business and therefore within the definition of income in s. 3(1) of the *Income War Tax Act*".

A comparison, which it suffices to suggest, between Western Leaseholds' Memorandum of Association, reproduced on page 287 of the official report, and our Lodestar Drilling Company's own memorandum (ex. A), especially

[1] [1958] Ex. C.R. 277 at 287.

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paragraph 3(*d*), would reveal a striking similarity in both these empowering covenants. In the former case, page 292, Cameron J. wrote as follows:

> In my view, no distinction can be drawn between the five items of profit now under consideration. They are all gains which fall within the test laid down in *Californian Copper Syndicate v. Harris*, 5 T.C. 159, namely whether the amount in dispute is "a gain made in an operation of business in carrying out a scheme for profit-making".

The Supreme Court of Canada[1] unanimously affirmed this decision, Mr. Justice Locke approvingly quoting, *inter alia*, this passage of the judgment appealed from:

> Generally speaking, a business is operated for the purpose of making a profit and the pursuit of profits may be carried on in a variety of ways and by different operations. In the instant case, it seems to me that the business of Leaseholds was carried out in two stages and involved two different operations. While the purpose of ultimately developing its own resources may have been kept in mind throughout, the first operation necessarily consisted of the acquisition and disposition of mineral rights so as to acquire funds with which to enter into the second stage, namely, the drilling for and operation of oil and gas wells on its own account. The possibility of disposition of the mineral rights had been contemplated since the company was formed. In dealing with its mineral rights in this fashion, it did not do so accidentally but as part of its business operations, and although possibly that line of business was not of necessity the line which it hoped ultimately to pursue, it was one which it was prepared to undertake, and, by its charter, had power to undertake.

The above analysis fits in to a nicety with the particular transactions performed by Lodestar Drilling Company and Realty Oils Ltd.

Coming now to the second element in dispute, the increase to $52,958.57 of the allegedly permissible deduction in respect of loss incurred during the 1953 fiscal year, only meagre material was adduced in support.

Donald Archibald MacGregor, the sole witness, who commented on this moot point, is a member of an important Calgary firm of chartered accountants. Mr. MacGregor prepared the Company's annual returns, both the regular and amended ones, viz. exhibits 1, 2, 3, 4, and 5 for fiscal years 1952-1953. He expresses the opinion that "a drilling company is allowed to deduct its normal business expenditures, plus depreciation on drilling equipment, and drilling performed on its own account". Deductions for 1953, would consist in a $1,073.15 loss allowed by respondent, plus a

[1] [1960] S.C.R. 10 at 21.

$51,885.42 depreciation. All of this too summary information might otherwise be correct, if it did not suffer from overconciseness that deprives it of probative weight unless and until reasonably particularized. Assertions that drilling costs, pursuant to the Farmout Agreement (ex. 7), "amounted to $51,800 in 1952 and $10,900 in 1953", or, again "that a 20% depreciation instead of a 30% one was entered for the Company's fiscal year terminating March 31, 1953", surely require some elaboration. "The reason for omitting to claim the entire 1953 depreciation ratio of 30%, pursues the witness, was the Company's intention to pay a dividend for that year, an impossible policy had it asked for this full $52,000 depreciation". We already know that 1953 was the year of the Company's financial discomfiture, officially declared on October 22. Nonetheless, by October 30, 1952, a $30,000 dividend issued to shareholders of record on October 17, same year, prompted apparently by highly wishful but equally dubious assumptions.

My somewhat copious notes are silent on the topic of coupling this subsequent charge for depreciation with any correspondingly specific expenditures. A similar observation qualifies the five income tax returns of record, wherein a "wealth" of entries is offset by a dearth of suitable identifications. This deficiency was not remedied by the evidence of the Company's past president and manager, the last witness to testify, Mr. William Ford.

Since the appellant must rebut the statutory presumption, then, at best, the decision might well reside in a Scotch verdict of "Not proven".

I expatiated at greater length than I intended on aspects devoid of objective significance, since the language of the *Income Tax Act,* in s. 42 (4A), added by c. 51, s. 14 of 1951, seems to justify respondent's plea of prescription.

So as to reach this opinion, one should minutely review the chronological sequence of the Company's filing of its regular and amended income tax returns for fiscal years 1952-1953 (exhibits 1 to 5 inclusive), and the statutory steps thereupon taken by respondent. Although tedious, such a task cannot be avoided. Section 42 (4A) reads thus:

> Where a taxpayer has filed the return of income required by section 40 for a taxation year and, *within one year from the day on or before which he was required by section 40 to file the return for that year,* has filed an

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amended return for the year claiming a deduction from income under paragraph (*d*) of subsection (1) of section 26 in respect of a business loss sustained in the taxation year immediately following that year, the Minister shall reassess the taxpayer's tax for the year.

A twelve-month period being thus extended, from the date of the prescribed annual report, to produce an amended return of which the Minister "shall" take due cognizance, let us inquire whether the taxpayer at bar complied with this requirement.

Exhibit "1", the Company's return for its taxation year ending March 31, 1952, was received at the Calgary National Revenue office *on October 1, 1952*, according to the day-stamp affixed. It acknowledges a taxable income of $114,916.05.

Exhibit "2" is the 1953 return listing a loss of $3,516; it reached the Calgary office *on September 30, 1953*.

Exhibit "3", also dated the same day, viz. *September 30, 1953*, purports to be an amended return for 1952, intended to bring about a re-assessment of this latter year and have deducted therefrom a 1953 deficit ($3,516) as permitted by ss. 26(1)(*d*) and 42 (4A).

Paragraph A(*f*) in Appellant's "Statement of Facts" recites that "on April 28, 1955, Notices of Re-Assessment were mailed to the Company in respect of years 1952 and 1953 . . ."

Exhibit "5" should be summarized before exhibit 4, since it is the amended report *for 1953*, but dated *June 27, 1955, precisely two (2) months after the Minister's Notice of re-assessment of April 28, 1955*. This "corrected" statement increases to $52,958.57 the former loss of $3,516 appearing on exhibit 2, and would have it deducted from the 1952 profits (ex. 1).

Exhibit "4" is a second revised return for taxation year 1952 (the first 1952 amended report being exhibit 3), *dated June 27, 1955*. An attempt is made to set at $61,957.48 the 1952 taxable income which, in exhibit 1, reads $114,916.05. In the instant occurrence, as for exhibit 5, the day of filing, *27th June, 1955*, exceeded by two months the official re-assessment notification of *April 28*.

When the Minister re-assessed on April 28, 1955, in respect of the years 1952-1953, the only returns in his possession at that time were:

(a) exhibit 1, received October 1, 1952

(b) exhibit 2, received September 30, 1953 and,

(c) exhibit 3, also received September 30, 1953.

We know that exhibits 4 and 5 reached the respondent after June 27, 1955.

Therefore, one must conclude that, *as of April 28, 1955,* the re-assessment date, the only loss about which respondent had any information was, and could be, no other than the $3,516 one disclosed in exhibit 2.

Subsequently to June 27, 1955, the re-amended returns, exhibits 4 and 5 being received, the Minister, by notification dated August 28, 1956, took a negative attitude, simply adhering to his assessment of April 28, 1955.

Such are the facts; now, appellant strives, in law, to have the ministerial decision rescinded and obtain a second re-assessment.

Section 42 (4A) does not give rise to any ambiguity; amended income tax returns must be forwarded at the latest one year after the statutory mailing date of each annual statement (cf. Ch. 52, 1948, s. 40 (1) (*a*)).

September 30, 1953, appearing on exhibits 2 and 3 as the time of receipt, the Company had until October 1, 1954, and not up to June 27, 1955, to submit for appraisal its re-amended returns, exhibits 4 and 5.

It possibly lies with the Minister to excuse a bar of limitations due to tardiness, but this does not constitute my problem. Requested to compel the respondent, no convincing argument was suggested whereby the Court could coerce the Minister to re-assess beyond the allotted delay, if, for motives within his discretionary powers, he deems fit to refuse.

For the reasons above, this appeal is dismissed, with taxable costs against the Appellant Company.

Judgment accordingly.