1957
Apr. 11
Dec. 20

BETWEEN:

WILLIAM G. BRIGGS ....APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Revenue—Income—Income tax—Portion of accounts receivable included in sale of share in partnership—Whether capital payment or income—The Income Tax Act, 1948, S. of C. 1948, c. 52, ss. 3, 4, 6(c), 14(1), 15.

The appellant on retiring from partnership in a firm of chartered accountants on October 31, 1950 was paid pursuant to the partnership agreement his ratio of the profits, and $3,255.51, his share of the accounts receivable to the end of the last fiscal year. The latter amount was assessed by the Minister as taxable income and the assessment upheld by the Income Tax Appeal Board. The appellant appealed from the Board's decision to this Court on the grounds that the sum in question did not constitute income or profit from a business but a capital payment received in a capital transaction, namely the acquisition by the remaining partners of the appellant's interest in the partnership.

Held: That the accounts receivable and accounts collected were nothing but the returns yielded by the fruitful ventures of the firm, in other words, income or profit and under s. 3 of the *Income Tax Act* the accounts receivable accrued to the appellant as income for the taxation year they were paid to him albeit such profits were made during the preceding fiscal period. The assessment was therefore correctly levied upon monies constituting a proportionate share of the partnership earnings up to October 31, 1950.

APPEAL from a decision of the Income Tax Appeal Board.

The appeal was heard by the Honourable Mr. Justice Dumoulin at Vancouver.

C. C. Locke and *W. M. Carlyle* for appellant.

D. T. Braidwood and *F. J. Cross* for respondent.

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

DUMOULIN J. now (December 20, 1957) delivered the following judgment:

This is an appeal from a decision of the Income Tax Appeal Board[1], dated the 12th day of April, 1956, dismissing William G. Briggs' prior appeal from a ruling of the Minister of National Revenue in respect of appellant's income tax assessment for taxation year 1951.

The material facts are quite simple.

William G. Briggs, the appellant, on October 1, 1947, entered into partnership with other members of a chartered accountants firm known as Gunderson, Stokes, Peers, Walton & Company, whose business operations were carried on in the City of Vancouver.

The requisite agreement evidences the rights and obligations of the parties thereto and those, especially, of the appellant. This indenture was filed as Exhibit 1. Clause 8 of this covenant mentions that the second party, i.e. W. G. Briggs, purchases a one-tenth (1/10) interest in the capital and goodwill of the partnership for a sum of $5,000, also outlining the instalment plan set up for payment.

Of greater importance is clause 10 providing for three contingencies of dissolution, and particularly determining the monies to which a partner, either upon voluntary retirement or consequent to his exclusion from the firm, would be entitled.

Since clause 10 contains the crucial point of disagreement, it should be reproduced at length.

10. In the event that any partner shall die or shall retire from the partnership, or in the event that the partnership is dissolved in order to effect the removal of one of the partners and the remaining partners desire to carry on business in partnership then the partner so retiring or excluded

[1] (1956) 10 D.T.C. 176; 14 Tax A.B.C. 453.

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or his estate, as the case may be, shall be entitled to receive the following monies but shall not otherwise participate in any of the capital or profits of the partnership:

(1) His share of the capital of the partnership as shown at the end of the last fiscal year plus his share of any additional capital invested since that date.

(2) His share of the profits since the last fiscal period consisting of;
(*a*) The cash net income received since the end of the last fiscal year,
(*b*) *Accounts receivable,* and
(*c*) 50% of the accrued time charges.

From his share of the capital and profits as above stated shall be deducted any withdrawals since the last fiscal year.

This association, for reasons undivulged, was dissolved on October 31, 1950.

The relevant memorandum dated October 31, 1950, is noted in the record as Exhibit 2.

The conditions agreed upon do not depart in any manner, shape or form, from the stipulations found, and mutually accepted, in the partnership covenant of October 1, 1947, Exhibit 1.

Clauses 2 and 3 of Exhibit 2 clearly settle the terms to obtain in the event of a dissolution, none of which are at variance with clause 10 of Exhibit 1, the Memorandum of Agreement.

A summary of the firm's (a) profits and losses for the month of October 1950, and (b) its Balance Sheet as at October 31, 1950, also form part of Exhibit 2.

These instruments reveal that the outgoing partner, W. G. Briggs, is being refunded or paid back his proportionate share in the joint capital, his ratio of the profits for October 1950, $523.96, and lastly $3,255.51 for accounts receivable.

Appellant reported as income for October 1950, this amount of $523.96. It then seems rather odd that he thereafter objected to the assessment levied by respondent on the further amount of $3,255.51, in respect of taxation year 1951.

At first glance, both sums: $523.96, appellant's profits for October 1950, and $3,255.51 allotted to him for accounts receivable, appear to flow from a self-same source, namely, the earnings realized by the partnership, with merely the

incidental difference that payment was immediately forthcoming in the first case, and would be collected periodically by the continuing partners in the second instance.

The grounds of appeal appear in para. B 2(b) and (c) of appellant's Statement of Facts hereafter quoted:

2. The Appellant intends to submit the following reasons:

* * *

(*b*) The said sum of $3,255.51 was not received by the Appellant as income or profit from or in the course of carrying on the practice of his profession but rather was received by the Appellant in part satisfaction of the monies payable to the Appellant pursuant to the dissolution agreement and in consideration of the matters set out in paragraph A 3 of this Notice of Appeal.

(*c*) The said sum of $3,255.51 was a capital payment received by the Appellant in a capital transaction, namely, the acquisition by the remaining partners of the said partnership of all of the Appellant's interest in the said partnership, other than certain doubtful accounts receivable.

In para. 6, appellant also mentions the fact that, at all material times, he reported his income on a cash received basis.

As for the relevant law, *The Income Tax Act,* 1948, appellant relies upon ss. 3, 6(*c*), 14(1) and 15(1), whilst respondent rests its case upon ss. 3, 4, 6(*c*) and 15.

Respondent did not assess the capital payment made to W. G. Briggs, but only the sum of $3,255.51 representing appellant's share in the accounts receivable.

The matter to be decided then narrows down to this: should the above amount be considered, as contended, in the light of a capital transaction, namely the purchase price of Mr. Briggs' interest in the partnership, or as instalments of accrued corporate income?

The event, whatever it may be, that brought to an end this association after only three years had nonetheless been provided for in the Memorandum of Agreement. Clause 10 of this document does not even allude to an eventual sale of share or interest by a retiring partner, and all conditions according to which the dissolution will be carried out are plainly stipulated. None of the partners can alter or vary the governing factors therein contained.

The usual basic essentials of a sale, that is, the determination by the vendor of a selling price, his complete freedom of selling to A instead of B or C, are lacking. Conversely, a seller cannot force a sale upon a reluctant

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party while, pursuant to clause 10 of the association covenant, Briggs could enforce its terms upon his former associates. Possibly, it should be said that some very special species of transactions are also devoid of these characteristic traits, such as, for instance, in the civil law that particular sale known as *vente à réméré* (sale with a redemption clause) C.C. 1547 *et seq.*, in derogation to the ordinary principles regulating sales.

Mr. Briggs, in para. B 2(*b*), agrees that he received his share of recoverable accounts "in part satisfaction of the monies payable to the Appellant pursuant to the dissolution agreement and in consideration of the matters set out in paragraph A 3 of this Notice of Appeal". As previously mentioned, there is but slight ground, if any, for construing clause 10 of Exhibit 1, (the October 1, 1947 indenture), as implementing a regular sale of a partnership share.

For argument's sake, let us suppose that the instant firm, after paying out to its several members their *pro rata* dues of joint earnings, had, for one reason or another suspended operations during a year and then decided to wind-up. No receivable accounts would exist at the time, for the evident reason that none would have been earned during that period of inactivity. Accounts receivable and accounts collected, it is trite to say, are nothing but the returns yielded by the fruitful business ventures of a firm, company or association, in other words, income or profit.

If the appellant's opinion were the proper one, it would follow that any partnership, at the expiry of a fiscal year, by resorting to some form of dissolution and allotting its accounts receivable, might thereby become immune to income tax.

Had this association endured, appellant assuredly would have found no fault with the propriety of an assessment upon his share of such earnings when paid to him. The only distinguishing factor then is that the disputed sum was received by appellant upon retirement from, instead of, during the partnership. I am unable to perceive in that alone a sufficiently pertinent reason in law to justify appellant's contention.

Section 6(*c*) of the Act reads as follows:

6. Without restricting the generality of s. 3, there shall be included in computing the income of a taxpayer for a taxation year

* * *

(*c*) the taxpayer's income from a partnership or syndicate for the year *whether or not he has withdrawn it during the year.*

Section 3, according to its extensive scope, comes closer to the disputed question when enacting that:

3. The income of a taxpayer for a taxation year for the purposes of this Part is his income for the year from all sources inside or outside Canada and, without restricting the generality of the foregoing, includes income for the year from all

(*a*) businesses
(*b*) property, and
(*c*) offices and employments.

It was argued, if I remember well, that: ". . . income for the year from all (*a*) business . . ." excluded profits distributed outside the fiscal or taxation year they were earned.

I cannot admit of so restrictive an interpretation which, if allowed, would provide an even easier way of thwarting the normal functioning of the Act than was pointed out above in connection with periodical dissolutions of partnership.

As a correct interpretation of s. 3, first paragraph, I would rather hold that accounts receivable accrued to appellant as income for the taxation year they were paid to him albeit such profits were made during the preceding fiscal period.

I therefore reach the conclusion that the assessment, on the sum of $3,255.51 objected to, must be considered as correctly levied upon monies constituting a proportionate share of partnership earnings up to October 31, 1950.

Mention was made by both parties of several precedents amongst which those of *Purchase v. Stainer's Executors*[1], *Bennett v. Ogston*[2] and *Rankine v. Commissioners of Inland Revenue*[3]. These pronouncements of high authority would lend valuable support indeed to appellant's view of the case if only we were dealing with the English Income Tax Act instead of the Canadian Act. The former law

[1] 32 T.C. 367; [1951] 2 All E.R. 1071.
[2] 15 T.C. 378.
[3] 32 T.C. 520-530.

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has many schedules that are not included in our own income tax act. Moreover, the language of our ss. 3, 4 and 6, s-s. (*c*), militates in favour of a different solution.

Two other cases quoted as *No. 333* v. *Minister of National Revenue*[1] and *Wilson v. Minister of National Revenue*[2] are clear instances of partners selling their partnership interest by means of regular and unmistakable sales and therefore should be distinguished from the issue at bar.

A more appropriate precedent is that of *Commissioner of Income-Tax, Madras v. P.R.A.L.M. Muthukaruppan Chettiar*[3]. Upon dissolution of a partnership, the Commissioner of Income Tax purported to assess interest received by the respondent on capital employed in business.

On appeal Lord Atkin held that:

. . . *Being profits of the respondent up to May 31, 1930, how did they alter their character by dissolution?* The account taken on dissolution ascertains what is due to the partners for profits, and what is due for capital. It can hardly be suggested that the partners share according to their capital proportions in the whole assets of the partnership. The sum due for undrawn profits was and remains a sum due by the partners to each partner, and necessarily ranks first before the sums due for capital can be distributed. In other words, on dissolution of a partnership an outgoing partner has the right to receive not as in the case of a shareholder in winding-up a company only a share of the assets, but to receive payment of his profits, *profits which were his before dissolution and do not cease to be his on dissolution.*

For the reasons preceding, the income tax levied for taxation year 1951, on the sum of $3,255.51 received by appellant, was made conformably to law; the appeal is therefore dismissed and respondent is entitled to taxable costs.

Judgment accordingly.

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[1] (1956) 10 D.T.C. 167. [2] (1956) 10 D.T.C. 194.
[3] Gordon's Digest of Income Tax Cases 757.