BETWEEN:

VANCOUVER TOWING COMPANY LIMITED, ... } APPELLANT,

AND

THE MINISTER OF NATIONAL REVENUE, ... } RESPONDENT.

1946
Oct. 17
Nov. 26

Revenue—Excess Profits Tax—Excess Profits Tax Act, 1940, 4 Geo. VI, c. 32, s. 15 (a)—Controlling interest in company—Distinction between a controlling interest and the controlling interest—Appeals dismissed.

By the Articles of Association of appellant company its managing director was given very extended powers, he having absolute control over the actions of its directors. He also controlled the Vancouver Tug and Barge Company, Limited, which held a majority of the issued shares in the appellant company. At a general meeting of appellant company the voting power is in accordance with the share register and therefore Vancouver Tug and Barge Company, Limited, is more powerful than all the other shareholders put together. On an appeal under the provision of the Income War Tax Act and Excess Profits Tax Act from assessments for the years 1942 and 1943 it was contended that the managing director of appellant company by virtue of the power vested in him by the Articles of Association and his control of Vancouver Tug and Barge Company, Limited, has the controlling interest in appellant company.

Held: That Vancouver Tug and Barge Company, Limited, has *a* controlling interest in appellant company within the intent and meaning of s. 15 (*a*) of the Act, and the appeals from assessments under the Income War Tax Act and the Excess Profits Tax Act for 1942 and 1943 are dismissed.

2. That the person whose shareholding in a company is such that he is more powerful than all the other shareholders in the company put together *in general meeting* has *a* controlling interest in the company.

APPEALS under the provisions of the Income War Tax Act and The Excess Profits Tax Act, 1940.

The appeals were heard before the Hon. Mr. Justice Cameron, at Vancouver.

D. Donaghy, K.C. and *J. A. Macdonald* for appellant.

W. S. Owen, K.C. and *E. S. MacLatchy* for respondent.

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

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CAMERON J. now (Nov. 26, 1946) delivered the following judgment:

This is an appeal from Income Tax and Excess Profits Tax assessments for the years 1941, 1942 and 1943. The usual returns for the various years were made by the appellant, and notices of assessment were mailed to the appellant in each case on March 12, 1945. The appellant gave Notice of Appeal on April 3, 1945, and on November 2, 1945, the Minister gave his decision affirming the assessments throughout. On November 26, 1945, the appellant gave Notice of Dissatisfaction, and on June 12, 1945, the Minister gave his reply affirming all the assessments as originally made. By order of this Court pleadings were directed and a Statement of Claim and Statement of Defence were later delivered.

At the hearing in Vancouver on October 17, 1946, no evidence was taken, the parties agreeing that the allegations in the Statement of Claim admitted in the Statement of Defence should be accepted as the agreed facts.

While the Notices of Appeal and the Statement of Claim indicate that the appeals have to do both with Income Tax and Excess Profits Tax, I am informed that there is now no dispute as to the assessment for Income Tax, and the appeals, therefore, have to do solely with assessments for Excess Profits Tax for the years in question.

It was agreed by Counsel for both parties that the entire problem centred around the interpretation to be placed on Sec. 15 (*a*) of the Excess Profits Tax Act, and in particular on the proper construction of the words "controlling interest" in that section. Sec. 15 (*a*) was added to the Act by Sec. 7, Chap. 13, Statutes of 1943-44, and was made applicable to the profits of the 1942 taxation period, of fiscal periods ending therein, and of all subsequent periods.

Sec. 15 (*a*) is as follows:—

Notwithstanding anything in this Act contained in any case where a company has a *controlling interest* in any other company or companies (hereinafter called controlled company or companies) incorporated in 1940 or thereafter (other than companies incorporated to carry out a contract or arrangement negotiated by the Minister of Munitions and Supply, and in respect thereunder of a management fee or other similar compensation), and the sum of the capital employed by such company and such controlled company or companies at the time of incorporation is not, in the opinion of the Minister of National Revenue, substantially greater than the capital

employed by such first-mentioned company prior to the incorporation of such controlled company or companies, the standard profit of all such controlled companies taken together shall not exceed $5,000 in the aggregate, and shall be allocated to each of such controlled companies in such amounts as the Minister of National Revenue may direct.

In any such case a reference to the Board of Referees shall not be made, notwithstanding the provisions of Sec. 5 of this Act.

It is admitted that the appellant company was incorporated in 1940; and that it was not incorporated to carry out a contract or arrangement negotiated by the Minister of Munitions and Supply. It is also admitted that the sum of the capital employed by the appellant and Vancouver Tug and Barge Company Limited, and Vancouver Tug Boat Company Limited, at the time of incorporation of the appellant is not substantially greater than the capital employed by the two last mentioned companies prior to the incorporation of the appellant company.

I shall deal first with the assessment to Excess Profits Tax for the year 1941. At the hearing it was admitted by Counsel for the respondent that the 1941 assessment as made was made in error, and on the assumption that Sec. 15 (*a*) above recited applied to that taxation year. The department, in making the assessment for 1941, did allow the sum of $5,000 as standard profits for the appellant company, although no fixation of standard profits had then, or has since, been made by the Board of Referees. Because, therefore, of the error in applying Sec. 15 (*a*) to the taxation year 1941, the appellant was deprived of his right under Sec. 5 of the Excess Profits Tax Act to apply to the Board of Referees for the establishment of its standard profits. I think, therefore, that in respect of that year, the appeal must succeed, and the assessment to Excess Profits Tax for that year be set aside.

In respect of the taxation years 1942 and 1943, the appellant's argument is that it is not a controlled company such as is envisaged in Sec. 15 (*a*), that the control of the appellant is not in The Vancouver Tug and Barge Company Limited or the Vancouver Tug Boat Company Limited, but rather in one Harold A. Jones, the Managing Director of the appellant company. This argument is advanced on behalf of the appellant on two grounds. It is alleged first that the Articles of Association by which the appellant was governed were the regulations contained in Table A of the

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first Schedule of The Companies Act as amended by regulations filed and registered with the Registrar of Companies on January 29, 1940, of which the following clauses are a portion of the amendments:—

(*a*) Harold A. Jones shall be the Managing Director of the Company until he resigns his office, or dies, or ceases to hold at least one (1) share of the issued share capital of the Company, and whilst he retains the said office he shall have absolute and sole authority to exercise all the powers, authorities and discretions by these Articles expressed to be vested in the Directors generally, and all the other Directors (hereinafter called "ordinary Directors"), if any, for the time being of the Company shall be under his entire and absolute control, and shall be bound to conform to his directions in regard to the Company's business.

(*b*) If the said Harold A. Jones resigns the office of Managing Director or shall cease to hold at least one (1) share of the issued share capital of the Company he shall become an ordinary Director.

(*c*) If the said Harold A. Jones dies whilst he holds the office of Managing Director, the executor or executors for the time being of his Will, or such other person as the said Harold A. Jones may by his Will appoint as Managing Director (so long as one (1) share of the issued share capital of the Company stands in the name of Harold A. Jones, or in the name of such executor or executors), may exercise the powers vested in the said Harold A. Jones by paragraphs 13 (*a*) and 13 (*f*) hereof.

(*d*) The remuneration of the Managing Director shall from time to time be determined by the Directors of the Company.

(*e*) The qualification of the Managing Director and any ordinary Director shall be the holding of at least one (1) share of the issued capital of the Company.

(*f*) The said Harold A. Jones whilst he holds the office of Managing Director may from time to time, and at any time, appoint any other person or persons to be an ordinary Director or ordinary Directors of the Company, and may define, limit and restrict his, her, or their powers, and may define, limit and restrict his, her, or their remuneration, and duties, and may at any time remove any director howsoever appointed, and may at any time convene a general meeting of the Company. Every such appointment or removal must be in writing under the hand of the said Harold A. Jones.

It will be seen from the above that the Managing Director, Harold A. Jones, by the regulations above recited, has what appears to be absolute control over the actions of the Directors of the appellant company, and throughout the years in question, he was at all times qualified to act as Managing Director as required by the said regulations.

Secondly, it is alleged that the said Harold A. Jones has the controlling interest in the appellant company by reason of the large shareholdings of Vancouver Tug and Barge Company Limited and Vancouver Tug Boat Company

Limited in the appellant company. At all material times there were only 357 shares of the capital stock of the appellant allotted or issued, and they were held as follows:

Harold A. Jones	3 shares
M. T. McLaurin	1 share
Endorsed to and held by the said McLaurin as nominee for Harold A. Jones and controlled by him.	
Vancouver Tug and Barge Company Limited	218 shares
Vancouver Tug Boat Company Limited	135 shares
	357 shares

It will be seen from the above that the Vancouver Tug and Barge Company Limited holds 218 shares out of 357 shares issued by the appellant company, being more than a majority of the said shares.

The Vancouver Tug and Barge Company Limited was incorporated in 1937, and at all material times only 2 shares of its capital were allotted or issued, and they were held as follows:—

Harold A. Jones	1 share
Goldini Webster	1 share
Endorsed in blank and held by the said Webster as nominee for Harold A. Jones and controlled by him.	

It is clear, therefore, that in so far as the Vancouver Tug and Barge Company Limited is concerned, the said Harold A. Jones has what could be called absolute control, and it is argued by Counsel on behalf of the appellant that as Vancouver Tug and Barge Company Limited has the majority of issued shares in the appellant company, and that as Harold A. Jones is in virtual control of Vancouver Tug and Barge Company Limited, that, therefore, Harold A. Jones has a controlling interest in the appellant company, and not Vancouver Tug and Barge Company Limited.

Some reference should also be made to the Vancouver Tug Boat Company Limited which holds 135 shares in the appellant company. That company was incorporated in 1924 and at all material times the said Harold A. Jones had more than a majority of its allotted or issued shares. A further argument of the appellant, therefore, is that since Harold A. Jones has the controlling interest in the Vancouver Tug Boat Company Limited and the Vancouver Tug and Barge Company Limited, that therefore, having control

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of their 353 shares, and three shares issued in his own name, in the appellant company, that he has the controlling interest in the appellant company, and that therefore the appellant company is not such a controlled company as is referred to in sec. 15 (*a*).

The problem, therefore, for decision is to ascertain the true meaning of the words "controlling interest" in section 15 (*a*). Does control of the board of directors mean the same as a controlling interest? Does control by Jones of the Vancouver Tug and Barge Company Limited (the registered owner of the majority of shares in the appellant company) give him a controlling interest in the appellant company? Or is the share register of the appellant company conclusive against the appellant in that it shows the Vancouver Tug and Barge Company Limited to have the majority of the shares and that therefore that company has a controlling interest in the appellant company.

I have not been referred to any cases in our courts where the words "controlling interest" as used in section 15 (*a*) have received judicial interpretation, nor have I been able to find any. But there are several cases in the English courts to which I have been referred and which are of assistance in arriving at my conclusion.

In *B. W. Noble Ltd.* v. *Commissioner of Inland Revenue* (1) the assessment to corporation profits tax had been made by reference to sec. 53 (2) (*c*) of the Finance Act 1920, to include any remuneration in excess of £1,000 per annum paid to a director who has a controlling interest in the company; and on behalf of the company it was contended that none of the directors had a controlling interest in the company within the meaning of the provision referred to. Rowlatt J. in giving judgment says:

> I think that the contention of the Crown is correct. It has been argued by Mr. Konstam with a great deal of ingenuity and industry that the first decision was right, for two reasons. First of all, pointing to a number of the sections, he says that this gentleman was not in a position to control the Company as regards the passing of special resolutions. That is true. Then, secondly, he says that he was not in a position, by virtue of his interest, to control the Board of Directors in the exercise of the powers given to them by the Articles in that behalf. I do not think this Sub-section ((Sub-section) (2) (*c*) of Section 53 of the Finance Act, 1920), is referring to that class of consideration at all. *It seems to me that "controlling interest" is a phrase that has a certain well known meaning;*

(1) (1917) 12 T.C. 926.

it means the man whose shareholding in the Company is such that he is the shareholder who is more powerful than all the other shareholders put together in General Meeting. That is really what it comes to. Now, this gentleman has just half the number of shares, but those shares, in the circumstances of this case, are reinforced by the position that he occupies of Chairman, a position which he occupies not merely by the votes of the other shareholders or of his Directors elected by the shareholders but by contract; and, so reinforced, inasmuch as he has a casting vote, he does control the General Meetings—there is no question about that—and inasmuch as he does possess at least half of the shares he can prevent any modifications taking place in the constitution of the Company which would undermine his position as Chairman.

The above case was referred to in *British American Tobacco Co. Ltd.* v. *Inland Revenue Commissioners* where the judgment of Lawrence J. in the King's Bench Division is reported in (1). In this case the appellant company held shares in eleven companies operating outside the United Kingdom which were therefore not liable to be assessed to the national defence contribution. In the case of four of these companies the appellant itself controlled more than 50% of the votes. In the case of the remaining seven companies more than 50% of the votes were controlled by the appellant company in conjunction with a company or companies in which the appellant company controlled more than 50% of the votes. It was held that on the proper construction of the section in the Finance Act 1937, "controlling interest" in a company *included* an indirect as well as a direct controlling interest and that the appellant company was subject to the national defence contribution.

In his judgment Lawrence J. stated at page 90:

The Attorney-General, on the other hand, contended that the word "interest" is a word of wide connotation. He cited *Lapish* v. *Braithwaite* (1926) A.C. 275 and *Skinner* v. *A.G.* (1940) A.C. 350 and contended that the words "controlling interest" must be interpreted together, that there can be no reason which could have induced the legislature to exclude the case of an indirect controlling interest, that the Finance Act, 1920, shows that the words can equally well be used to include an indirect or a direct controlling interest, and that in their ordinary meaning they include both. I have come to the conclusion that the contention of the Crown is correct. I do not think that it is a proper inference that, because the Finance Act, 1920, mentions expressly a controlling interest, direct or indirect, when the legislature spoke of "a controlling interest" *simpliciter* in 1937, it meant only a direct controlling interest. The word "controlling" is not a term of art, nor is the word "interest" necessarily so, and, when the word "controlling" is used to qualify "interest", I think that the

(1) (1941) 2 A.E.R. 86.

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phrase in its ordinary meaning covers both direct and indirect control. Counsel for the appellants in the second appeal also argued that companies which held only 51 per cent and less than 75 per cent of the shares in a company have not a controlling interest in such company, but it was conceded that upon this point I am bound by the decision of Rowlatt J., in *Mitchell* v. *Noble (B.W.) Ltd.* (1927) 1 K.B. 719. The Crown's appeal will, therefore, be allowed, and the British American Tobacco Co.'s appeal will be dismissed with costs.

This judgment was upheld in the Court of Appeal (1). There it was held that the word "interest" must be interpreted liberally and that when it is used with the word "controlling" it covers an indirect as well as a direct controlling interest.

The appeal to the House of Lords was dismissed (2).

In the judgment of Viscount Simon, L.C. (concurred in by all the other judges) it is there stated:

> But that is to treat the phrase "controlling interest" as capable of connoting only a proprietary right, that is, an interest in the nature of ownership. The word "interest", however, as pointed out by Lawrence J., is a word of wide connotation, and I think the conception of "controlling interest" may well cover the relationship of one company towards another, the requisite majority of whose shares are, as regards their voting power, subject, whether directly or indirectly, to the will and ordering of the first-mentioned company. If, for example, the appellant company owns one-third of the shares in company X, and the remaining two-thirds are owned by company Y, the appellant company will none the less have a controlling interest in company X if it owns enough shares in company Y to control the latter.
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> In my opinion this is the meaning of the word "interest" in the enactment under consideration, and, where one company stands in such a relationship to another, the former can properly be said to have a controlling interest in the latter. This view appears to me to agree with the object of the enactment as it appears on the face of the Act. I find it impossible to adopt the view that a person who, by having the requisite voting power in a company subject to his will and ordering, can make the ultimate decision as to where and how the business of the company shall be carried on, and who thus has, in fact, control of the company's affairs, is a person of whom it can be said that he has not in this connection got a controlling interest in the company.

Counsel for the appellant in the instant case urged upon me that this portion of the judgment was authority for finding that Jones, in full control of the Vancouver Tug and Barge Co. Ltd., which in turn had more than a majority of the shares in the appellant company, had, therefore, the controlling interest in the appellant company. But it must be kept in mind that the sole question in the Tobacco case was whether the controlling interest must be *direct*

(1) (1941) 2 A.E.R. 651. (2) (1943) 1 A.E.R. 14.

ownership or whether indirect ownership of shares would give such *a* controlling interest as would make the Company liable to tax on dividends received by the Tobacco Company from the other companies controlled *indirectly* by shareholding. In the example used, where the appellant company owned one-third of the shares in Company X and the remaining two-thirds were owned by Company Y it is stated that the appellant company would none the less have a controlling interest in Company X if it owns enough shares in Company Y to control the latter. In my view that illustration means only that an *indirect* controlling interest would make the appellant there liable to tax, as well as a holding of sufficient shares in its own name to give it a *direct* controlling interest. I can find nothing in the judgment which states that there is not also a *direct* controlling interest in a company which has registered in its own name a majority of shares of the appellant company.

I am strengthened in my view that this is the proper interpretation of this judgment by the concluding words of the judgment itself which are as follows:

> As to what may be the requisite proportion of voting power, I think a bare majority is sufficient. The appellant company has, in respect of each of the foreign companies referred to in the case, the control of the majority vote. I agree with the interpretation of "controlling interest" adopted by Rowlatt, J. in *Noble* v. *Commissioners of Inland Revenue* ((1926) 2 T.C. 911), when construing that phrase in the Finance Act, 1920, s. 53 (2) (c). He said at p. 926 that the phrase had a well-known meaning and referred to the situation of a man whose shareholding in the company is such that he is more powerful than all the other shareholders put together in general meeting.
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> The owners of the majority of the voting power in a company are the persons who are in effective control of its affairs and fortunes. It is true that for some purposes a 75 per cent majority vote may be required, as, for instance (under some company regulations) for the removal of directors who oppose the wishes of the majority; but the bare majority can always refuse to re-elect and so in the long run get rid of a recalcitrant board. Nor can the articles of association be altered in order to defeat the wishes of the majority, for a bare majority can always prevent the passing of the necessary resolution.

It is to be observed that the interpretation of the words "controlling interest" adopted by Rowlatt J. in the *Noble* case (*supra*) is approved in the House of Lords. There were two propositions put forward by the appellant before the House of Lords. The first one as to indirect control, I have already referred to. The second point was that in

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any event the controlling interest was not constituted by the control of the bare majority of shares (whether directly or through other companies) but that the control must be of such a proportion of shares as will secure the passing of a special resolution for which a special majority is required by the terms of the constitution of the company. The judgment of the House of Lords makes it abundantly clear that the requisite portion of voting power to give a controlling interest is a bare majority. And following the judgment of Rowlatt, J., in the *Noble* case (*supra*) it seems clear that the man (or corporation) whose shareholding in the company is such that he is more powerful than all the other shareholders in the company put together *in general meeting* has *a* controlling interest in the company.

This interpretation of "controlling interest" seems to be a proper and natural one to put on those words as used in the enactment—section 15 (*a*). Scott, J., in the Court of Appeal judgment in the *Tobacco* case (*supra*) sets forth the meaning of the verb "control" and the noun "interest" as found in the Oxford English Dictionary. Moreover, such interpretation seems to meet the situation which section 15 (*a*) was intended to overcome.

Regardless of the very extended powers given to the Managing Director of the appellant Company as above set forth, and of the fact that he, by control of the Vancouver Tug and Barge Company Limited, has indirect control as to how the shares held by the latter company in the appellant company shall be voted, it is abundantly clear to me that at a general meeting of the shareholders of the appellant company the voting power is in accordance with the share register and that the Vancouver Tug and Barge Company Limited is more powerful than all the other shareholders put together. It, therefore, has *a* controlling interest within the intent and meaning of section 15 (*a*).

It should be noted that the words in the section are "*a* controlling interest" not "*the* controlling interest" or "the control". Unquestionably Jones has the ultimate control in the appellant company and has complete control of its board of directors. He also has an indirect controlling interest in the company itself but all the respondent needs

to show is that the Vancouver Tug and Barge Company has *a* controlling interest in the appellant and on the basis of the interpretation given to those words in the cases I have cited and on the agreed facts, I find that such is the case.

Reference may also be made to *Glasgow Expanded Metal Co. Ltd.* v. *The Commissioner of Inland Revenue* (1), and to *Inland Revenue Commissioners* v. *J. Bibby & Sons Ltd.* (2). In the latter case it was held that "controlling interest" referred to the power of controlling by votes the decisions binding on the company in the shape of resolutions passed at a general meeting.

The appeals, therefore, in respect of assessments to Income Tax and Excess Profits Tax for the years 1942 and 1943 will also be dismissed and the assessment confirmed. The appeal as to the assessment to income tax for the year 1941 will also be dismissed and the assessment confirmed. In regard to the appeal in respect of excess profits tax for the year 1941 the appeal will be allowed, the assessment set aside and that item of the appeal will be referred back to the Minister to be dealt with under sec. 5 (2) of the Act, and when the standard profits have been so ascertained, the appellant will be re-assessed to Excess Profits Tax for the year 1941.

Inasmuch as the appellant is only partially successful in its appeal and as most of the argument had to do with matters in which it failed, I am of the opinion that it should be entitled to only one-half of its taxed costs and I so direct.

Judgment accordingly.

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(1) (1926) 12 T.C. 573

(2) (1945) 1 A.E.R. 667.