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THE KVP COMPANY LIMITED .....APPELLANT;

AND

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

Revenue—Income—Income Tax—The Income Tax Act, S. of C. 1948, c. 52, s. 12(1)(a) and (b)—The Forest Management Act, Statutes of Ontario 1947, c. 38, ss. 2, 3, 4, 5, 6, 7—Expenses incurred in preparation of a Forest Management Plan not "an outlay or expense incurred by the taxpayer for the purpose of gaining or producing income from the property or business of the taxpayer"—Appeal dismissed.

Held: That expenses incurred by appellant company in the preparation of a Forest Management Plan in compliance with The Forest Management Act, c. 38 of the Statutes of Ontario 1947 and the licensing agreements with the Province of Ontario are, to the extent that they exceed the annual cost of cruises and surveys in the appellant's normal operations, capital expenditures and part of the capital cost of the timber limit or the right to cut timber from a limit and were not made for the purpose of gaining or producing income from the property

or business of the appellant, having been made by appellant in its capacity as owner rather than as trader or operator and not for the purpose of producing profits in the conduct of the business.

APPEAL under *The Income Tax Act.*

The appeal was heard before the Honourable Mr. Justice Cameron at Toronto.

J. R. Tolmie, Q.C. for appellant.

K. E. Eaton and *T. Z. Boles* for respondent.

CAMERON J.:—This is an appeal from assessments to income tax made upon the appellant company for each of the fiscal years ending December 31, 1950, 1951 and 1952. The appeal raises the question as to the deductibility of certain expenses incurred by the appellant in carrying out a timber survey on properties over which it had cutting rights and the preparation of a Forest Management Plan. Such expenses aggregated $176,904.67 in the period 1950 to 1954, inclusive; in each of these years the appellant, in filing its corporation income tax return, claimed as a deduction the following amounts:

1950	$ 60,863.78
1951	62,478.81
1952	36,717.24
1953	16,121.62
1954	723.22
	$176,904.67

In this appeal I am concerned only with the assessment relating to the years 1950, 1951 and 1952, those relating to the years 1953 and 1954 not having been issued at the date of the trial.

In assessing the appellant for the years in question, the respondent disallowed as expenses the following portions of these costs:

1950	$ 48,363.78
1951	49,655.84
1952	20,854.34

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Paragraphs 8 and 9 of the respondent's Reply to the Notice of Appeal, as amended without objection at the trial, are as follows:

8. That of the amounts of $60,863.78, $62,478.81 and $36,717.24, claimed as deductions by the Appellant in computing its income for the taxation years 1950, 1951 and 1952, the amounts, $48,363.78, $49,655.84 and $20,854.34, respectively, were not allowable deductions because they were:

(a) outlays or expenses not made or incurred by the Appellant for the purpose of gaining or producing income from property or a business of the Appellant, within the meaning of paragraph (a) of subsection (1) of section 12 of the Income Tax Act, and

(b) outlays or payments on account of capital within the meaning of paragraph (b) of subsection (1) of section 12 of the Act.

9. That, alternatively, no part of the said amounts which were claimed as deductions by the Appellant should have been allowed as the whole of each of those amounts was an outlay, expense or payment of the kind referred to in subparagraphs (a) and (b) of paragraph 8 hereof.

It is to be noted that although the alternative claim of the respondent in paragraph 9 denies the deductibility of any portion of the amount so expended (notwithstanding the fact that part thereof had been allowed in each of the years), counsel for the Minister stated his purpose in asking for the amendment which included these paragraphs: "The purpose of this Motion is to enable us to be in a position to argue that no part of the costs should have been allowed. We are not asking for any re-assessment or anything like that. We are merely clearing the way for a legal argument."

The appellant company is a Canadian subsidiary of the Kalamazoo Vegetable Parchment Company of Kalamazoo, Michigan, and is engaged in the business of logging and producing pulp and paper in the vicinity of Espanola, Ontario. In 1943 the parent company acquired certain properties from the Abitibi Company (in receivership) and on May 26, 1944, negotiated a timber concession from the province of Ontario (Appendix 1A to the Notice of Appeal) by which the Crown granted to the parent company the right to cut certain species of timber at the rates and subject to the conditions mentioned therein. These cutting rights were assigned to the appellant by the parent company by an agreement dated March 25, 1946, with the consent of the Minister of Lands and Forests. In 1947 the appellant acquired further licences in the same drainage area from the McFadden Lumber Company. Then by an agreement dated

February 27, 1947 (Appendix 1B to the Notice of Appeal), the Crown, in the right of the province of Ontario, entered into a further agreement with the appellant company by which certain cutting rights were granted to the appellant on the terms and conditions therein set forth. The matter is not at all clear but it would appear that the cutting rights so granted covered the areas formerly under licence to the McFadden Lumber Company as well as certain additional properties in the township of Ermatinger, and possibly also the properties referred to in the original agreement of May 26, 1944.

On March 10, 1947, the Minister of Lands and Forests forwarded a letter to the appellant (Exhibit 3) in these terms:

> For your information I am enclosing a copy of the "Manual of Requirements for Working or Management Plans, Operating Plans, Annual Cutting Applications and Forest Surveys".
>
> This manual should be used by you as a guide in the preparation of reports required under the terms of your agreement with the Crown.
>
> Your working plan is due on May 26, 1949.

Subsequently, the date for filing the Working Plan was extended to March 31, 1952.

Exhibit 4 is the "Manual of Requirements" mentioned in that letter. It includes a copy of the *Forest Management Act,* 1947, and a statement of the data which should be included in (1) a Working or Management Plan; (2) an Operating Plan; (3) the annual cutting applications; and (4) a statement of the minimum requirements for summarizing information on forest surveys conducted for the Department of Lands and Forests.

The *Forest Management Act,* 1947, is chapter 38 of the Statutes of Ontario 1947. Inasmuch as the expenditures here in question were made pursuant to its provisions and the regulations established thereunder, it will be helpful to state the operative sections in full:

> 2. (1) Every person who has cutting rights in a Crown timber area shall, when required by the Minister, furnish to him—
>
> (*a*) an estimated inventory of the timber on the Crown timber area with respect to which he has cutting rights, classifying the timber as to age, species, size and type;
>
> (*b*) A proposed master plan for managing the Crown timber area and utilizing the timber thereon; and
>
> (*c*) a map, which shall form a part of the master plan, dividing the Crown timber area into proposed operational units.

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(2) The Minister may approve a master plan as submitted to him or may approve it with such alterations therein as he may deem advisable.

(3) Subject to section 3, a person who has received a request to furnish a master plan shall manage the Crown timber area covered by it and utilize the timber thereon in accordance with the provisions of the approved master plan.

(4) Where conflict exists between an approved master plan and any agreement made or license granted under The Crown Timber Act, the provisions of the master plan shall govern.

3. (1) Every person who is required to furnish a master plan shall annually during the life of such master plan, furnish to the Minister,—

(a) at least sixty days before cutting operations commence, a plan for cutting operations to be conducted during the twelve-month period commencing on the 1st day of April; and

(b) on or before the 31st day of October, a map indicating the cut-over areas together with a statement showing the amount, species and size of timber cut from each cutting area during the twelve-month period ending March 31st of that year.

(2) The Minister may direct such alteration to be made in an annual plan as he deems advisable and where such alteration involves the alteration of an approved master plan, the master plan shall be deemed to be altered accordingly.

4. The Minister may direct the cessation of cutting operations until a master plan has been approved.

5. Where any person fails to comply with an approved master plan, the Minister may suspend or cancel the agreement, or license, or both, under which he derives his cutting rights.

6. The Lieutenant-Governor in Council may make regulations,

(a) prescribing the manner of preparing and the form of inventories, maps and statements required under this Act and governing the accuracy and verification thereof; and

(b) generally for the better carrying out of the provisions of this Act.

7. This Act shall come into force on the 1st day of June, 1947.

It is common ground that Exhibit 4—the Manual of Requirements—constitutes the regulations provided for in section 6 of the Act.

Pursuant to the request of the Minister of Lands and Forests dated March 10, 1947 (Exhibit 3), and in accordance with the provisions of the Act and its regulations, the witness D. W. Gray—who was the assistant woods manager and the logging engineer of the appellant company—proceeded to secure the information necessary to prepare the Forest Management Plan. Certain data were already on hand, some of which had been taken over from the previous owners and some of which had been acquired in previous years by the cruises and surveys carried out by the appel-

lant company itself. This information, however, was insufficient to meet the requirements of the regulations; it was necessary, therefore, to secure further and up-to-date information as to the inventory of timber before the required "estimated inventory", the master plan for managing the timber area, and the map could be furnished to the Minister. There is no precise statement as to the details of this operation, but in the main they consisted of extensive aerial surveys and ground cruises, involving also to some extent the use of office personnel and the preparation of prints and maps. As I have said, the entire operation took about five years to complete, the total cost being $176,904.67; no exception is taken to that amount or as to the proportion thereof expended in each year.

Exhibit 1 is the Forest Management Plan; it is a summary of findings relative to quantity of timber, their location and condition. Exhibits 2(*a*) to 2(*g*) are the operating plans dealing with individual watersheds set up as operating areas by the company; they constitute a broad outline of operating procedure which should be followed in their development.

The evidence indicates that in the years prior to 1947 (when it was required to prepare the Forest Management Plan) the appellant, for its own purposes and in the operation of its business, had expended annually an amount of about $17,000 for surveys and timber cruises, which amounts had been allowed as operating expenses. While the preparation of the Forest Management Plan was undertaken solely for the purpose of meeting the requirements of the Minister of Lands and Forests, part of the information thereby secured was of direct assistance to the company and resulted in a lessening of the cost of the annual surveys and cruises which would normally have been undertaken. While such expense had averaged $17,000 per annum before the preparation of the Plan, it was reduced to about $4,500 per annum after the Plan was undertaken, and the latter amount of normal expenditures was apparently allowed as a proper deduction. In addition, for each of the years in question the Minister, in assessing the appellant, allowed a further sum of $12,500, being apparently of the opinion that $17,000 was a normal and proper deduction

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for such surveys and cruises. In addition, he allowed $322.97 and $3,362.90 as the cost of maps for the years 1951 and 1952 respectively. From the assessments made on this basis, the appellant now appeals to this Court.

For each of the taxation years in question, the following provisions were contained in *The Income Tax Act*:

> 12. (1) In computing income, no deduction shall be made in respect of
> (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer,
> (*b*) an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part.

Briefly, the contention of the appellant is that the whole of the expenditures so incurred was made for the purpose of gaining or producing income from property or a business of the taxpayer and were consequently not barred from deduction by the provisions of s-s. (1)(*a*) of section 12. For the respondent, it is submitted that the outlays were barred from deduction by the provisions of that subsection in that they were not made for the purpose of gaining or producing income from property or a business of the taxpayer; and also that they were barred by the provisions of s-s. (1)(*b*) as being an outlay or payment on account of capital.

Before considering these subsections, it will be convenient to dispose first of one submission made by Mr. Tolmie, counsel for the appellant company. It relates to the evidence of Mr. A. McG. Kennedy, manager of the Toronto office of Ernst and Ernst, accountants and auditors of the appellant company. Mr. Kennedy stated that the outlays in question, under generally accepted accounting principles, would be treated as expenses and charged to operating expenses at the time they were incurred and that he had treated them in that manner. He considered that no portion should be capitalized as he could not find that any capital asset had been created or enhanced in value by the expenditures. In cross-examination, he stated that the absence of any capital asset (as a result of the expenditures) was the sole reason for the opinion at which he had arrived.

It is well settled, however, that an outlay or expense which might be deductible from income on generally accepted accounting principles is not deductible if it be

barred by express provisions of the Act. In the case of *Imperial Oil Ltd. v. Minister of National Revenue* (1), the learned President of this Court stated in reference to the somewhat similar provisions of section 6(*a*) of the *Income War Tax Act*:

> . . . The section directs that such disbursements or expenses are not to be deducted, even although they might be deductible according to ordinary principles of commercial trading or, as it has been suggested "well accepted principles of business and accounting practice". The range of deductibility according to such principles may be wider than that which is inferentially permitted under the section. To that extent they must give way to the express terms of the section, which must, of course, prevail. The result is that the deductibility of disbursements or expenses is to be determined according to the ordinary principles of commercial trading or well accepted principles of business and accounting practice unless their deduction is prohibited by reason of their coming within the express terms of the excluding provisions of the section.

In order to determine whether the outlay was made for the purpose of gaining or producing income from property or a business of the appellant company, it becomes necessary to examine the real nature of the expenses and why they were incurred. It is abundantly clear from the evidence that, had not the appellant been required to prepare the master plan, it would not have embarked on the very extensive woods inventory survey which it actually made; it would merely have continued to make the ordinary annual cruises and surveys necessary for its own logging operations that it had made in previous years. Mr. Gray stated that

> The purpose of this plan was to fulfil the requirements of the Department of Lands and Forests under the Forest Management Act. We already had the information which was sufficient to put our limits on a sustained yield basis . . . The purpose of this plan was to provide the Department of Lands and Forests with information which would enable them to prepare a picture of the forest . . . an inventory of the forest condition in the province as a whole.

This latter view is supported by a statement on page 10 of the Manual of Requirements that

> By following a form such as outlined herewith, basic data from all forest surveys conducted for the Department of Lands and Forests can be amalgamated to form a mosaic of forest conditions over large territories and provide uniform summaries from which to determine the present and future values of the forests of Ontario.

(1) [1947] Ex. C.R. 527 at 530.

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Later Mr. Gray reiterated the point:

> Yet again, if I may repeat, we were under an obligation, and the only reason that this work was undertaken was in order to satisfy the requirements of that manual, which has the effect of being a regulation issued under the Forest Management Act . . . I prepared them (i.e. the cruise regulations) to satisfy the conditions of that manual."

Mr. Avery, president and general manager of the appellant company, was equally emphatic on this point. He stated that the purpose of gathering the data "was to conform with the directions received and the plan was written and submitted in accordance with that." Further, he stated that the company's operations had always been based on a policy of maintaining yields in perpetuity and that the plan which was prepared was not needed to carry out that policy.

> The survey made to secure the data for the plan was merely the carrying out of a duty required under the 1947 legislation. The plan which the company had prepared and used previously, supplemented by necessary annual "current cruising" to ascertain damage by fire and insects and unauthorized cutting, was sufficient to keep the inventory up to date for its own purposes.

In his opinion, the purpose of requiring all licensees in the province to prepare Forest Management Plans was to ensure uniformity of survey throughout the province.

It was undoubtedly necessary for the appellant company to comply with the requirement of the Minister of Lands and Forests that it prepare the Forest Management Plan. If it failed to do so, the Minister under the terms of the Act was empowered to direct the suspension of all its cutting activities. Further, and notwithstanding its general licence from the province, the company was required annually (section 3) to apply for a "cutting permit" over specified areas and in specified quantities, and this cutting permit could also have been withheld had the requirements not been fulfilled. Mr. Avery stated the position of the company as follows:

> As a licensee of the Crown, in order to continue the rights under the licence, we were required to do the work and we had to do it. It would not have been done in this manner had we not been required under the statute to do it.

He admitted that, if the annual cutting permit were denied, the company would be out of business in six months, as its supply of wood would have been cut off.

In these circumstances, it seems to me that the overriding purpose of the appellant company, in incurring these expenses, was not that of gaining or producing income from

its property or business but rather for the purpose of complying with the requirement of the Minister of Lands and Forests, as authorized by the *Forest Management Act* and its regulations, in order to preserve its rights under the licensing agreements which it held. The business operations of the appellant company consisted in acquiring timber, either by cutting on its own limits or by purchase from others, and in processing it into pulp or paper for sale. To the extent that the special surveys made for the purpose of collecting data for the Forest Management Plan exceeded the ordinary annual cruises incidental to the company's normal operations, the sole purpose in undertaking them was to supply data to the provincial authorities for their own use in planning forest management control for the whole of the province and was of benefit only to those authorities. To that extent, the outlays were not made for the purpose of gaining or producing income and were made by the appellant not as trader or operator, but as owner.

While the expenses were incurred in connection with the appellant's business, that is not of itself sufficient to render them deductible. In the case of *Strong & Co. v. Woodifield* (1), Lord Davey said:

> . . . It is not enough that the disbursement is made in the course of, or arises out of, or is connected with, the trade, or is made out of the profits of the trade. It must be made for the purpose of earning the profits.

In *Minister of National Revenue v. The Dominion Natural Gas Co. Ltd.* (2), Duff C.J.C. stated:

> First, in order to fall within the category "disbursements or expenses wholly, exclusively and necessarily laid out or expended for the purpose of earning the income", expenses must, I think, be working expenses; that is to say, expenses incurred in the process of earning "the income".

Reference may also be made to *Montreal Coke and Manufacturing Co. v. Minister of National Revenue* (3) where Lord Macmillan, in the Judicial Committee of the Privy Council, said:

> . . . Expenditure, to be deductible, must be directly related to the earning of income. The earnings of a trader are the product of the trading operations which he conducts.

(1) [1906] A.C. 448 at 453. (2) [1941] S.C.R. 19 at 22.
(3) [1944] A.C. 126 at 133.

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Again, in *Tata Hydro-Electric Agencies, Ltd., Bombay v. Commissioner of Income Tax* (1) the facts, as set out in the headnote, are as follows:

The appellants, a private limited company, who carried on the business of managing agents of A. company, receiving for their services a commission of 10 per cent. on the annual net profits of A. company, with a minimum of Rs. 50,000 whether that company should make any profits or not, had acquired that agency from B. company, their predecessors, under an assignment whereby B. company transferred to the appellants their whole rights and interest as agents of A. company, subject, however, to their (B. company's) obligations under two agreements with D. and E. respectively whereby B. company, who while the managing agents of A. company had borrowed money for that company from D. and E., had to pay to both D. and E., in addition to the interest they would receive from A. company on the loan, 12½ per cent. of the commission earned by them (B. company) under their agency agreement with A. company:—

Held, that in computing their income, profits and gains for tax purposes the appellants were not entitled to deduct the 25 per cent. of the commission earned and received from A. company which they paid over to D. and E. under the agreements. That percentage of the commission paid to D. and E. was not expenditure incurred by the appellants "solely for the purpose of earning . . . profits or gains" of their business within the meaning of s. 10, sub-s. 2 (ix.) of the Indian Income-tax Act, 1922. The obligation to make the payments was undertaken by the appellants in consideration of their acquisition of the right and opportunity to earn profits, that was, of the right to conduct the business, and not for the purpose of producing profits in the conduct of the business.

Lord Macmillan at page 695 said this:

Their Lordships recognize, and the decided cases show, how difficult it is to discriminate between expenditure which is, and expenditure which is not, incurred solely for the purpose of earning profits or gains. In the present case their Lordships have reached the conclusion that the payments in question were not expenditure so incurred by the appellants. They were certainly not made in the process of earning their profits; they were not payments to creditors for goods supplied or services rendered to the appellants in their business; they did not arise out of any transactions in the conduct of their business. That they had to make those payments no doubt affected the ultimate yield in money to them from their business, but that is not the statutory criterion. They must have taken this liability into account when they agreed to take over the business. In short, the obligation to make these payments was undertaken by the appellants in consideration of their acquisition of the right and opportunity to earn profits, that is, of the right to conduct the business, and not for the purpose of producing profits in the conduct of the business.

And at page 696 he stated the test to be as follows:

. . . It is necessary, accordingly, to attend to the true nature of the expenditure, and to ask oneself the question, Is it a part of the Company's working expenses; is it expenditure laid out as part of the process of profit earning?

(1) [1937] A.C. 685.

Applying the principles and tests laid down in these cases, I have reached the conclusion that the expenses in question, to the extent that they exceeded the normal annual expenses for cruising and surveys, were, for the reasons stated, not made for the purpose of gaining or producing income from the property or business of the appellant. They were made by the appellant in its capacity as owner, rather than as trader or operator, and were not made for the purpose of producing profits in the conduct of the business.

While the appellant company, during the years in question, did not attempt to segregate its normal annual operating expenses for surveys and cruises from the total amount expended in preparing the data for the Forest Management Plan, the assessments made in the manner indicated above did provide for such segregation on what appears to be a fair and reasonable basis. In any event, there was no evidence led by the appellant company to indicate that the deductions so permitted were less than should have been allowed for the cost of the normal annual operating cruises and surveys.

I am of the opinion also that the expenses to the same extent as mentioned above were barred from deduction by the provisions of s-s. (1)(*b*) of section 12 of *The Income Tax Act* as being an outlay on account of capital. In the original licensing agreement, dated May 26, 1944, between the province and the parent company (page 10 of Appendix A/1 to Exhibit 1), there are the following provisions:

1. In consideration of the covenants and agreements on the part of the Company herein contained, the Crown, with the approval and consent of the Lieutenant-Governor in Council, and subject to the terms and conditions hereof, doth grant to the Company for a period of twenty-one (21) years from the First day of April, 1943 the sole right to cut and remove the timber specified in Clause 2 of this Agreement in and upon the lands described in Schedule "A" hereto and the lands selected from Schedules "B" and "C" hereto, which Schedules form part of this Agreement.

* * *

11. The Company shall operate in accordance with good forestry practice, and within five (5) years from the date hereof shall file with the Department of Lands and Forests a working plan prepared by the Company, which shall be satisfactory to the Minister, providing a general scheme for the operation and management of the area granted, and providing for the placing of its supply of pulpwood on a sustained-yield basis, to the end that the area will be kept productive and in accordance with the provisions of the Pulpwood Conservation Act.

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29. This Agreement shall be subject to all Acts of the Legislature of the Province of Ontario which are now or which may hereafter be in force and all regulations duly made under the provisions of such Acts, so far as they may be of general application to the cutting, measuring, removing and driving of timber on and from Crown lands throughout the Province, and the same shall be binding upon and ensure unto the Company and shall apply to its operations under this Agreement as fully and effectually as if they had been set forth herein.

* * *

34. The Company hereby covenants and agrees to observe, perform and keep all covenants, provisions, agreements and conditions on its part herein contained.

And in the licensing agreement of February 27, 1947 (Appendix 1B to the Notice of Appeal), after reciting that the 1944 agreement had been assigned by the parent company to the appellant company with the approval of the Minister of Lands and Forests there is the following provision:

It is further agreed by and between the parties hereto that all the terms and condiitons of the 1944 agreement shall apply to and be binding upon this Agreement as fully and effectually as if the area in Schedule "A" hereto had been included in and formed part of the 1944 agreement.

It is apparent, therefore, that the appellant company, by the terms and conditions of its licensing agreements with the province, was bound to submit and conform to all acts of the Legislature, including those that thereafter might come into force, and the regulations made under such acts, such as the *Forest Management Act,* 1947 and its regulations. It seems, therefore, that the obligation to prepare and deposit the Forest Management Plan was assumed by the appellant company in part consideration, at least, of the acquisition of the licences and the opportunity to earn profits therefrom.

In this connection, reference may be made to a portion of the judgment in the *Tata* case (*supra*), where at page 695 it is stated:

. . . They must have taken this liability into account when they agreed to take over the business. In short, the obligation to make these payments was undertaken by the appellants in consideration of their acquisition of the right and opportunity to earn profits, that is, of the right to conduct the business, and not for the purpose of producing profits in the conduct of the business.

In *The Royal Insurance Co. v. Watson* (1), the headnote is as follows:

Upon the transfer of an insurance business the transferees agreed to take into their service the transferors' manager at a fixed salary, with liberty to commute the same by payment to him of a gross sum to be calculated upon life tables. The transferees retained the manager's services for a short time and then paid him a gross sum in commutation of his salary. They claimed to deduct that sum in estimating their profits for income tax:—

Held, that the agreement to pay the commutation money was in fact part of the consideration for the transfer of the business, that the payment was therefore a "sum employed as capital" and could not be deducted.

At page 8 Lord Herschell said:

. . . The payment was made in pursuance of a bargain entered into between the Royal Insurance Company and the Queen Insurance Company, which bargain contained the terms on which the Royal Insurance Company was to become possessed of the business of the Queen Insurance Company. Of course, it could not be disputed for a moment that the price paid to a company whose concern was bought by another company would not be expenditure which could be set against the gains of the year in which the payment was made. It would obviously be capital expenditure; and although in this case the payment was a payment to be made under that agreement to the former manager of the Queen Insurance Company, when the matter is looked at in its substance and essence, I do not think that payment differs from such a payment as I have alluded to. I think it was equally a payment made in pursuance of the obligation contained in the contract by which the business of the Queen Insurance Company was purchased, and, therefore, is properly capital expenditure.

As in that case, I think that the expenditures here made, in so far as they exceeded the normal cost of the annual surveys and cruises of the appellant company in carrying out its operations, were made in pursuance of its obligations in the licensing agreement and were, therefore, capital expenditures.

Reference may also be made to *Robert Addie and Sons' Collieries Ltd. v. The Commissioner of Inland Revenue* (2).

In assessing the appellant, the respondent had treated the expenses disallowed as relating to property subject to capital cost allowances under section 11(1)(*a*) of *The Income Tax Act*; accordingly, he applied the provisions of section 1100(1)(*e*) of the Regulations, which is as follows:

1100. (1) Under paragraph (*a*) of subsection (1) of section 11 of the Act, there is hereby allowed to a taxpayer, in computing his income from a business or property, as the case may be, deductions for each taxation year equal to

(1) [1897] A.C. 1.

(2) (1924) 8 T.C. 671.

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(e) such amount as he may claim not exceeding the amount calculated in accordance with Schedule C in respect of the capital cost to him of a timber limit or a right to cut timber from a limit.

It was suggested in the Notice of Appeal that, if the expenditures disallowed were found to be of a capital nature, the capital cost allowance should have been computed at a rate of 30 per cent. under the provisions of Class 10(1) of Schedule B, which is as follows:

> Property not included in any other class, that is
> (1) property that was acquired for the purpose of cutting and removing merchantable timber from a timber limit and will be of no further use to the taxpayer after all merchantable timber has been removed from the limit, unless the taxpayer has elected to include another property of this kind in another class.

The point was not stressed in argument except for the purpose of suggesting that the capital cost allowance provided for in the assessments was inadequate. It is sufficient to say that in my opinion the expenses incurred, to the extent that they exceeded the annual cost of cruises and surveys in the appellant's normal operations, were capital expenditures incurred pursuant to the terms of its licensing agreements and the *Forest Management Act* 1947, and were part of the capital cost of the timber limit or the right to cut timber from a limit, and consequently fell within the provisions of section 1100(1)(*e*) of the Regulations. It is unnecessary to define the properties which would come within class 10(1) of Schedule B, but it is to be noted that they do not affect "property included in any other class".

For these reasons the appeals will be dismissed and the assessments made upon the appellant for the years 1950, 1951 and 1952 will be affirmed. The respondent is entitled to his costs after taxation.

Judgment accordingly.