BETWEEN:

NICHOLSON LIMITED ..... APPELLANT;

AND

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

1943
Sept. 29
1945
Oct. 5

Revenue—Income Tax—Income War Tax Act, R.S.C. 1927, chap. 97, secs. 6 (2), 6 (3), 58-69, 75 (2)—Disallowance of excessive expense—Discretionary powers vested in the Minister—Discretion to be exercised on proper legal principles—Duty of supervision by the Court—Appellate jurisdiction of the Court—Appeal to the Court is an appeal from the assessment and does not involve an appeal from the Minister's determination in his discretion—Minister's determination in his discretion under section 6 (2), if discretion exercised on proper legal principles, not open to review by the Court.

Certain amounts of the salaries paid to executive officers of the appellant were disallowed as deductible expenses by the Commissioner of Income Tax under the authority of section 6 (2) and section 75 (2) of the Income War Tax Act, as being in excess of what was reasonable or normal expense for the business carried on by it and the amounts so disallowed were added to its taxable income in the assessments levied against it.

Held: That the duty cast upon the Minister by section 6 (2) is an administrative duty of a quasi-judicial character, requiring that the discretion vested in him should be exercised in the manner prescribed by law. The discretion must be exercised on proper legal principles. *Pioneer Laundry and Dry Cleaners, Limited,* v. *Minister of National Revenue* (1940) A.C. 127 at 136 followed.

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2. That the appeal to the Exchequer Court provided by the Income War Tax Act is not an appeal from any decision of the Minister but an appeal from the assessment made by him in the course of his functions in respect thereof and it is incorrect to describe it as an appeal from the decision of the Minister.

3. That the sole issue before the Court in an appeal under the Income War Tax Act is whether the "assessment under appeal" is correct in fact and in law.

4. That the opening words of section 66 "Subject to the provisions of this Act" require the Court to apply and give effect to all the sections of the Act, including section 6 (2).

5. That the correctness of the amount of excessive expense to be disallowed under section 6 (2) depends, not upon the amount that is in excess of what is reasonable or normal as a matter of fact, but on the amount determined by the Minister in his discretion; the amount so determined is the correct one and an assessment in which such amount has been included is, to the extent of such inclusion, correct in fact. Being made as the law requires, it is also correct in law.

6. That the right of appeal to the Court conferred by the Act does not carry with it any right of appeal from the Minister's determination in his discretion under section 6 (2).

7. That it is the duty of the Court to supervise the manner in which the Minister exercises his discretionary powers, but there its function stops; with the quantum of such exercise the Court is not concerned.

8. That when the Minister has determined in his discretion under section 6 (2) of the Income War Tax Act the amount of excessive expense to be disallowed to a taxpayer as a deduction from his income and has exercised his discretion on proper legal principles, the amount so determined is not open to review by the Court; and an assessment in which a disallowance so determined has been included cannot, to the extent of such inclusion, be successfully attacked as incorrect either in fact or in law in an appeal to the Court under the Act. *Pioneer Laundry and Dry Cleaners, Limited* v. *Minister of National Revenue* (1939) S.C.R. 1; (1940) A.C. 127 discussed and *Dobinson* v. *Federal Commissioner of Taxation* (1935) 3 Australian Tax Decisions 150 distinguished.

APPEAL under the provisions of the Income War Tax Act.

The appeal was heard before the Honourable Mr. Justice Thorson, President of the Court, at Vancouver.

Hon. J. W. de B. Farris K.C. and *J. L. Lawrence* for appellant.

Dugald Donaghy K.C. and *H. H. Stikeman* for respondent.

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

THE PRESIDENT now (Oct. 5, 1945) delivered the following judgment:

This appeal from the assessments for income and excess profits tax for the taxation years ending January 31, 1940 and 1941, is brought by the appellant because certain amounts of the salaries paid to its executive officers were disallowed as deductible expenses by the Commissioner of Income Tax.

The appellant carries on the business of printing at Vancouver, British Columbia. It does some job printing but the bulk of its business consists of specialty printing, such as street railway tickets and transfers, steamship tickets, theatre, exhibition, bread and milk tickets and coupon books for transportation, fishing and logging companies. This requires special equipment and special qualifications on the part of its employees. During the years in dispute the appellant had four executive officers, who were also its directors, and fifteen employees. Each of the officers in addition to performing executive duties did other work. The appellant's business increased rapidly with an increase in profits and, since it was not possible to obtain additional staff, both employees and officers were called upon for overtime work. The directors, on the recommendation of the general manager, declared a salary bonus of $3,600 for 1940 and $3,575 for 1941. In each year $1,800 of such bonus was distributed among the officers and the balance among the employees, the reason for such equal distribution being that "the wages of the employees just about broke even with the salaries paid the other four members of the firm." The salaries of the directors prior to the bonus, the distribution of it among them and the amount of salary disallowed in each case are set out in a table filed as Exhibit 4.

The amounts of the disallowances were determined by the Commissioner of Income Tax under the authority of section 6 (2) of the Income War Tax Act, R.S.C. 1927, chap. 97, reading as follows:—

6. 2 The Minister may disallow any expense which he in his discretion may determine to be in excess of what is reasonable or normal for the

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business carried on by the taxpayer, or which was incurred in respect of any transaction or operation which in his opinion has unduly or artificially reduced the income.

and section 75 (2) by which the Minister may authorize the Commissioner of Income Tax, now the Deputy Minister of Taxation, to exercise such of the powers conferred by the Act upon the Minister, as may, in his opinion, be conveniently exercised by the Commissioner of Income Tax. The necessary authority was given on August 8, 1940; *Vide* Canada Gazette, September 13, 1941, page 852. For the sake of convenience the discretionary powers in question will be referred to as those of the Minister and their exercise as his.

Before any determination was made, the Inspector of Income Tax at Vancouver notified the appellant on October 27, 1942, that discretion was about to be exercised in the matter of the salaries paid to its directors and invited it to submit its representations for final consideration and either arrange for an authorized person to attend the Vancouver office in person or submit its representations in writing as soon as possible. The appellant accepted this invitation and made lengthy representations in writing through its representative, Income Tax Specialists Limited, of Vancouver, by letter dated October 29, 1942, in which the facts regarding it were fully set out and justification for the salary increases was put forward, such as increased business and profits, limit of plant capacity, impossibility of extension and need for additional effort and overtime on the part of employees and executive officers. On January 12, 1943, the Commissioner of Income Tax determined that the salaries of the directors were in excess of what was reasonable for the business carried on by the appellant and disallowed $1,050 in 1940 and $1,811.50 in 1941 as deductions from income. On January 26, 1943, notices of assessment were given to the appellant, adding the amounts disallowed to its taxable income. From such assessments the appellant appealed to the Minister. In its notice of appeal the appellant sought to justify the increased salaries on the same grounds as those advanced by its representative. No new facts were put forward for the consideration of the Minister that had not been referred to in the representations already made on its behalf. The decision of the

Minister, to which reference will be made later, affirmed the assessments and the appellant now brings its appeal from them to this Court.

This appeal raises squarely for the first time in Canada the question whether the Court under its appellate jurisdiction may review the actual exercise of discretionary powers vested by the Act in the Minister where such exercise may affect the assessment under appeal and substitute its own opinion for the Minister's discretion. The question is one of major importance in view of the many sections in the Income War Tax Act by which wide discretionary powers that may affect an assessment are conferred upon the Minister.

It is first necessary to deal with the appellant's submission that the Minister's discretion under section 6 (2) of the Act must be confined to a determination of what is in excess of reasonable or normal expense but that what is reasonable or normal expense is a question of fact in respect of which the Minister has no discretion. I am unable to adopt this view. In my opinion, the Minister's discretion extends not only to a determination of what is in excess of reasonable or normal but also to a determination of what is reasonable or normal. This is, I think, the true meaning of the section, for without such meaning it would not be possible to carry out what appears to be the policy of Parliament. Parliament decided as a matter of policy that excessive expenses should not be allowed as deductions from taxable income; it realized that in many cases it would be difficult, if not impossible, to determine what was reasonable or normal expense as a matter of fact and that without such determination it would not be possible to determine what was an excessive one and, therefore, decided to leave the determination of the amount of excessive expense to be disallowed to the discretion of a person in whom it had confidence, namely, the Minister of National Revenue, who was responsible to it for the administration of his department; then by section 75 (2) it allowed the Minister to authorize a specified officer, namely, the Commissioner of Income Tax, now the Deputy Minister of Taxation, the permanent head of the taxing authority, to

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exercise such of the powers conferred by the Act upon the Minister, as might, in the Minister's opinion be conveniently exercised by the Commissioner.

The duty cast upon the Minister by section 6 (2) is an administrative duty of a quasi-judicial character requiring that the discretion vested in him should be exercised in the manner prescribed by law.

The courts have always jealously supervised the manner in which administrative bodies have exercised the discretionary powers vested in them, so far as they are of a judicial nature, whether the Act conferring them granted an appeal from the decision of the body or not, in order to ensure their exercise in a proper manner, but there is no case of which I am aware in which the court has gone beyond such supervision and assumed the exercise of such powers itself in the absence of specific statutory authority enabling it to do so.

Where there has been no provision for appeal the supervision has been mainly by writ of certiorari or mandamus. The judgments dealing with the matter phrase the requirements for the proper exercise of such discretionary powers in varying terms but the necessity for acting judicially runs through them all. This broad requirement was stated in *Local Government Board* v. *Arlidge* (1), where Viscount Haldane L. C. fully discusses the manner in which an administrative body should perform its judicial duties. In an earlier case, *Board of Education* v. *Rice* (2) Lord Loreburn L. C. emphasized that such a body "must act in good faith and fairly listen to both sides, for that is a duty lying upon everyone who decides anything". This was approved in the *Arlidge Case* (*supra*) and in *The King* v. *Noxzema Chemical Company of Canada, Limited* (3). It is obviously essential to the proper performance of its judicial duty by an administrative body that before it decides a person's case it should afford such person an opportunity of placing his side of the case before it; it cannot act judicially unless it does so. In *Leeds Corporation* v. *Ryder* (4), Lord Loreburn L.C. stated that persons exercising discretionary powers must act honestly and endeavour to carry out the spirit and purpose of the statute. In *Hayman*

(1) (1915) A.C. 120 at 132
(2) (1911) A C. 179 at 182
(3) (1942) S C.R. 178 at 180
(4) (1907) A.C. 420 at 423

v. *Governors of Rugby School* (1) it was laid down that such powers must be fairly and honestly exercised. In *The Queen* v. *Vestry of St. Pancras* (2) Lord Esher M. R. stated that the persons exercising discretion should exercise it fairly and not take into account any reason for their decision which is not a legal one and that if they do so then in the eye of the law they have not exercised their discretion. These statements of the manner in which administrative bodies should discharge their judicial duties should not be regarded as statements of independent principles governing them but rather as particular applications of the general principle that they must act judicially. If they do, their exercise of discretion will not be disturbed; if they do not, the Courts will interfere by writ of certiorari, mandamus or other appropriate remedy.

It was contended for the appellant that these decisions, being in certiorari or mandamus proceedings, have no application in the present case, since an appeal is provided by the Income War Tax Act, and that the Court under its appellate jurisdiction is not restricted to supervision over the manner of exercise of the Minister's discretion under section 6 (2) but may and should review such exercise itself and substitute its own opinion of the amount of expense to be disallowed, if any, for the determination by the Minister. Proper disposition of this contention requires careful consideration of the scheme of appeal provided by the Act, the subject matter of the appeal and the nature and extent of the Court's jurisdiction.

The Act affords the taxpayer two opportunities for relief from the assessment levied against him. He may appeal to the Minister and then, if he is dissatisfied with his decision, he may bring his appeal to this Court; in each case the appeal is from the assessment.

Part VIII of the Act deals wth the subject of appeals and procedure. Section 58 (1), prior to its amendment in 1944, read as follows:

58. Any person who objects to the amount at which he is assessed, or who considers that he is not liable to taxation under this Act, may personally or by his solicitor, within one month after the date of mailing of the notice of assessment provided for in section fifty-four of this Act, serve a notice of appeal upon the Minister.

(1) (1874) 18 Eq. 28 at 68. (2) (1890) 24 Q.B.D. 371 at 375.

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The taxpayer may thus appeal on grounds of fact as well as of law. The notice of appeal must be in writing, be served by mailing it by registered post addressed to the Minister of National Revenue at Ottawa and set out clearly the reasons for appeal and all facts relative thereto. Section 59 sets out the duties of the Minister as follows:

> 59. Upon receipt of the said notice of appeal, the Minister shall duly consider the same and shall affirm or amend the assessment appealed against and shall notify the appellant of his decision by registered post.

From this it appears with certainty that what is before the Minister on the appeal to him is "the assessment appealed against", together with the notice of appeal from it. The sole issue before him is whether the assessment is correct. If it is, he must affirm it; if it is not, he is required to amend it. The requirement that the Minister shall affirm or amend the assessment is consistent with the scheme of the Act which assigns the function of assessment to him.

The sections following section 59 prescribe the procedure to be followed before the appellant can have his appeal to the Court heard. This appeal has frequently been referred to as an appeal from the decision of the Minister but such a description of it is incorrect. What is before the Court is not the decision of the Minister but the assessment. Examination of the Act makes this quite clear. Section 60 provides that if the appellant, after receipt of the Minister's decision, is dissatisfied with it, he may, within one month from the date of the mailing of the decision, mail to the Minister by registered post a notice of dissatisfaction stating that he desires his appeal to be set down for trial. With such notice of dissatisfaction he must forward a final statement of the facts, statutory provisions and reasons which he intends to submit to the Court in support of the appeal. Section 60 thus contemplates that the appellant may carry his appeal beyond the Minister's decision and bring it to this Court; the only appeal thus far referred to is the appeal mentioned in the notice of appeal, namely, an appeal from the assessment; the appeal throughout the whole scheme of the Act is from the assessment, first to the Minister and then to the Court. Section 61 provides for the giving of security for costs of the appeal and section 62 requires that upon receipt of the notice of dissatisfaction and statement of facts the Minister shall reply thereto by

registered post admitting or denying the facts alleged and confirming or amending the assessment or any amended, additional or subsequent assessment. The purpose of sections 60 and 62 is to ensure that all the facts, statutory provisions and reasons which the appellant intends to submit to the Court shall first be brought to the attention of the Minister so that he may deal with the assessment as required, since the making of the assessment or its amendment if necessary is exclusively his function under the Act. The appeal is then ready to be launched in this Court. Section 63 requires that, within two months from the date of mailing the reply, the Minister shall cause to be transmitted to the Registrar of the Exchequer Court of Canada, to be filed in the said Court, typewritten copies of certain specified documents; these include the appellant's income tax return, the notice of appeal, the Minister's decision, the notice of dissatisfaction and the Minister's reply thereto, but special reference should be made to the following other specified documents, namely:

(*b*) The Notice of Assessment appealed;

and

(*g*) All other documents and papers relative to the assessment under appeal.

This makes it clear that the appeal to the Court is an appeal from the assessment. Section 66 then sets out the Court's appellate jurisdiction as follows:

66. Subject to the provisions of this Act, the Exchequer Court shall have exclusive jurisdiction to hear and determine all questions that may arise in connection with any assessment made under this Act and in delivering judgment may make any order as to payment of any tax, interest or penalty or as to costs as to the said Court may seem right and proper.

The Court is given jurisdiction over the assessment because that is the subject matter of the appeal before it. It is not concerned with the decision of the Minister as such; the question which it must consider is the correctness of the assessment "under appeal". Finally, section 69 concludes Part VIII of the Act with the provision that if a notice of appeal is not served or a notice of dissatisfaction is not mailed within the time limited therefor, the right of the person assessed to appeal shall cease and the assessment shall be valid and binding notwithstanding any error, defect, or omission therein or in any proceedings required by the

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Act. From this it is clear that if the appeal goes no further than to the Minister and no notice of dissatisfaction is mailed within the time limited, it is the assessment and not the decision of the Minister that is made binding. Nowhere in the Act is the appeal to the Court referred to as an appeal from the decision of the Minister. It is, I think, beyond dispute that the appeal to the Exchequer Court provided by the Income War Tax Act is not an appeal from any decision of the Minister but an appeal from the assessment made by him in the course of his functions in respect thereof. The exact nature of the subject matter of the appeal to the Court must be kept clearly in mind if confusion of thought is to be avoided.

Counsel for the appellant argued that the appeal under the Act involves an appeal from the exercise of the Minister's discretion; that the purpose of the appeal to the Minister is to enable him to review such exercise and that he must do so; that his failure to do so would deprive the appellant of a right to which it is entitled under the Act and make the assessment before the Court an improper one; and that the Court under its appellate jurisdiction has the same power of review and is under the same duty to exercise it as the Minister, since it is the same appeal that is carried throughout. I am unable to accept these contentions. They are, I think, based upon a misconception of the nature of the appeal.

The decision of the Minister on the appeal to him was given in the following terms:—

> The Honourable the Minister of National Revenue having duly considered the facts as set forth in the Notices of Appeal and matters thereto relating hereby affirms the said Assessments on the ground that Section 6 (2) of the Act provides that the Minister may disallow any expense which he in his discretion may determine to be in excess of what is reasonable for the business carried on by the taxpayer; that in the exercise of such discretion he has determined that the salaries paid or credited to four employees of the taxpayer were to the extent of $1,050.00 in 1940 and $1,811.50 in 1941 in excess of what is reasonable for the business carried on by the taxpayer and has disallowed as an expense of the taxpayer the said amounts so determined and therefore the Assessments are accordingly affirmed under and by reason of the provisions of the said section 6 (2) and other provisions of the Income War Tax Act in that respect made and provided.

The Minister put his decision squarely on the ground that he had determined the amount of excessive expense

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to be disallowed in his discretion under section 6 (2) and confirmed the assessments accordingly. I see no failure of duty on the Minister's part in taking this ground. It is not the purpose of the appeal to the Minister to enable him to review the exercise of his discretion and there is nothing in section 59 requiring him to do so. The question before him is whether "the assessment appealed against" is correct in fact and in law and he must "duly" consider the notice of appeal in the light of such question. This requires consideration of the various items involved in the assessment and whether they have been properly included. The only item against which complaint is made is the amount of expense that was disallowed. If this has been lawfully determined, no exception can be taken to the assessment in respect of such item. The Minister was, in my opinion, quite within his rights in confirming the assessment on the ground taken by him and if his discretion was exercised judicially his decision in confirming the assessment on such ground was a sound one. He owed no duty to review his exercise of discretion; the appellant has suffered no loss of legal right by his not doing so and has no cause for complaint against him on such score. It may, indeed, be open to doubt whether the Minister, while acting under his appellate jurisdiction, had any right to review the exercise of discretionary powers vested in him in his administrative capacity. But whether that be so or not, and even if the Minister on the appeal to him, while not obliged to review the exercise of his discretion is not precluded from so doing, it by no means follows that the Court may do so. There is a *non sequitur* in this line of reasoning, for the Act specifically vests the discretionary powers in the Minister and there is no such vesting in the Court.

The extent of the Court's jurisdiction under section 66 of the Act is very wide. Subject to the provisions of the Act it has exclusive jurisdiction to hear and determine all questions that may arise in connection with the assessment. It may, therefore, deal with issues of fact as well as questions of law. Nor is its jurisdiction restricted to questions arising subsequent to the assessment; it may deal with all questions, whether they arise before or after the assessment, provided they are connected with it.

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The wide extent of this jurisdiction led counsel for the appellant to the argument that the appeal to the Court is in the nature of a trial *de novo* and that it may examine all the facts that were before the Minister prior to his determination in his discretion since such facts are connected with the assessment and draw its own conclusions from them. There is, I think, a fallacy in this argument. It is true that section 63 (2) provides that when the necessary documents have been transmitted to the Registrar of the Exchequer Court the matter shall thereupon be deemed to be an action in the said Court ready for trial or hearing, but this is mainly for procedural purposes to enable proceedings such as discovery to be had, witnesses to be subpoenaed and the like, and does not affect the nature of the issue before the Court. But it is not correct to say that the facts before the Minister prior to his determination are facts connected with the assessment. A clear distinction must be drawn between the Minister's determination and the assessment; they are not the same; the determination must be made before the assessment can be levied. The facts before the Minister do not enter into the assessment; it is the Minister's determination that does so. The determination itself is, therefore, a fact connected with the assessment. The facts before the Minister are connected with his determination but not with the assessment. The issues before the Minister on his determination and the Court on the appeal to it are not the same. I can find no support anywhere for the view that the Court may try *de novo* matters left by Parliament for determination by the Minister in his discretion. What is before the Court is an appeal from the assessment, not an appeal from the Minister's determination. The sole issue before the Court in an appeal under the Income War Tax Act is whether the "assessment under appeal" is correct in fact and in law. If it is, the appeal must be dismissed; if not, it must be allowed. It will be remembered that section 59 requires the Minister after duly considering the notice of appeal to confirm or amend the assessment appealed against and that section 62 imposes similar requirements upon him in his reply to the notice of dissatisfaction. No similar duty is cast upon the Court. The reason is clear; it is no part of the duty of the Court to make, confirm or amend an

assessment or perform any administrative act that may affect it; such functions, under the Act, belong exclusively to the Minister. All the Court is concerned with is the correctness of the "assessment under appeal". That question is solely a judicial one.

The Court's jurisdiction is by section 66 made "subject to the provisions of this Act". Counsel for the appellant sought to narrow the meaning of these opening words. He referred to section 6 (3) which reads as follows:

> 6. (3) For the purpose of determining earned income the Minister may reduce the amount of any salary, wages, fees, bonuses, gratuities or honoraria, which, in his opinion, are not commensurate with the services actually rendered, and the amount of such reduction shall be treated for the purposes of this Act as investment income. The decision of the Minister on any question under this subsection shall be final and conclusive.

and argued from the fact that no sentence similar to the last sentence in section 6 (3) appears in section 6 (2) there is by implication an appeal from the Minister's determination under section 6 (2); and that the opening words of section 66 must be limited to provisions of the nature of the final sentence in section 6 (3). It is, I think, open to serious doubt whether the final sentence of section 6 (3) adds anything to the effect of the Minister's acts under the powers vested in him by it. I am inclined to the view that it does not, but, in any event, the appellant's argument puts an unwarranted limitation upon the opening words of section 66. In my opinion, they require the Court to apply and give effect to all the sections of the Act, including section 6 (2). The general words conferring the appellate jurisdiction are, in my view, specifically made subject to the provisions of the Act. Even if this were not so, they would, I think, have to give way to a specific enactment such as section 6 (2), under the maxim *generalia specialibus non derogant*. This is particularly so where Parliament, as in section 6 (2), has expressly specified the manner in which a particular item which may affect an assessment is to be determined and has done so as a matter of policy because of the difficulty or impossibility of having it ascertained otherwise. If such an item, determined in accordance with Parliament's policy as expressed in clear and specific terms, is included in an assessment, how can the Court properly hold that the assessment is erroneous

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in fact or in law because of such inclusion? To that extent the assessment is in accordance with the law as laid down by Parliament.

There is another way of looking at the matter. The Court has jurisdiction over questions of fact as well as of law. What is the question of fact before the Court into which it must enquire before it can decide whether the assessment is correct in fact or not? The only complaint the appellant has against the assessment is the amount of expense that was disallowed. The only issue of fact connected with the assessment that is before the Court is, therefore, whether the amount of the disallowance was correct or not. If it has been determined in accordance with the law, how can it be found to be incorrect? When counsel for the appellant contends that the Court may look into all the facts that were before the Minister prior to his determination in his discretion and draw its own conclusion from them as to the correct amount of expense to be disallowed, he misapprehends the nature of the issue of fact before the Court. The correctness of the amount of excessive expense to be disallowed under section 6 (2) depends, not upon the amount that is in excess of what is reasonable or normal as a matter of fact, but on the amount determined by the Minister in his discretion; the amount so determined is the correct one and an assessment in which such amount has been included is, to the extent of such inclusion, correct in fact. Being made as the law requires, it is also correct in law.

The purpose of granting a right of appeal from an assessment is to ensure to the taxpayer that it shall be a correct one. It is not to be assumed that Parliament in granting such right meant that the Court should apply a different standard for adjudicating as to the correctness of the assessment under appeal from that laid down for its correct levy by the Minister in the discharge of his functions. The Court must apply the law and section 6 (2) is binding upon it. The Court may not, therefore, substitute its own opinion as to the correct amount of expense to be disallowed for the amount determined by the Minister in his discretion under section 6 (2). The amount so determined is not open to review by the Court. The right of appeal to

the Court conferred by the Act does not carry with it any right of appeal from the Minister's determination in his discretion under section 6 (2).

The Minister's discretion under section 6 (2) must be exercised in a proper manner. If in making his determination he has not acted judicially, within the meanng of the cases cited, he has not exercised the discretion required by the section at all, and if his determination so made is included in an assessment the assessment is, to such extent, incorrect. Whether the discretion has been exercised in a proper manner is, therefore, a question connected with the assessment over which the Court has jurisdiction. Indeed, the Court owes a duty of supervision over the manner of its exercise in order to ensure that the Minister acts as the law ordains. The fact that it has appellate jurisdiction does not alter the nature of the principles to be applied in its duty of supervision; they are the same as those applied by the courts in the certiorari and mandamus cases. This was settled in *Pioneer Laundry and Dry Cleaners, Limited* v. *Minister of National Revenue* (1) where, at page 136, Lord Thankerton, in delivering the judgment of the Judicial Committee, adopted the statement of Davis J. in the Supreme Court of Canada that the exercise of the discretionary powers of the Minister under section 5 (*a*) of the Act involved:—

> an administrative duty of a quasi-judicial character—a discretion to be exercised on proper legal principles.

The statement that the discretion of an administrative officer in the discharge of his quasi-judicial duties must be exercised on proper legal principles is, in my judgment, just another way of stating as Viscount Haldane L.C. did in *Local Government Board* v. *Arlidge* (*supra*), that he "must act judicially".

Much of the argument on the hearing before me centred around the *Pioneer Laundry Case* (*supra*) and it would not be proper to conclude my reasons for judgment without discussing it. Its importance in Canadian income tax law has not been eliminated by the fact that the immediate effect of the judgment has been nullified by amendment of the Act, but there has been considerable misunderstanding of it, and it is desirable to ascertain what it actually decided

(1) [1939] S.C.R. 1; [1940] A.C. 127.

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so that its continuing effect may be appreciated. The facts were that the appellant had claimed depreciation allowances in respect of certain second hand machinery and equipment which had formerly belonged to a company that had gone into voluntary liquidation; that it was controlled by the same shareholders who had formerly controlled such company; and that the machinery and equipment, while owned by such company, had been fully written off by depreciation. Under these circumstances, the Commissioner of Income Tax disallowed the claims for depreciation altogether. An appeal to this Court was dismissed by Angers J. and his judgment was affirmed by the Supreme Court of Canada, with Duff C. J. and Davis J. dissenting. Its judgment was reversed by the Judicial Committee of the Privy Council, which adopted the dissenting opinion in the Court below, expressed by Davis J., speaking for the Chief Justice and himself. The Court had to consider section 5 (*a*) of the Income War Tax Act, reading as follows:—

> 5. "Income" as hereinbefore defined shall for the purposes of this Act be subject to the following exemptions and deductions:—
>
> (*a*) Such reasonable amount as the Minister, in his discretion, may allow for depreciation, ...

and the question before it was whether the Commissioner had been right in disallowing altogether the claims for depreciation made under the circumstances mentioned. It was held that he had been wrong in two respects. In the first place, he had misconstrued the effect of section 5 (*a*); while he had a discretion as to the amount to be allowed for depreciation, his discretion did not extend to deciding whether any depreciation should be allowed or not; the taxpayer had a statutory right to an allowance in respect of depreciation and the Minister had a duty to fix a reasonable amount in respect of such allowance. The second ground of error assigned was that he had acted on wrong legal principles in that he had disregarded the fact that the appellant had a separate legal existence from that of its shareholders and that it was the appellant company, and not its shareholders, that was the taxpayer. The Judicial Committee accordingly set the assessment aside and referred the matter back to the Minister. The judgment must, I think, be taken as a decision that the Minister in failing

to act on proper legal principles had not exercised the discretion contemplated by the Act at all, and that in such a case the proper course for the Court to take is to refer the matter back to the Minister for the exercise of his discretion in the manner required by law, namely, its exercise on proper legal principles. This view of the decision makes it one of continuing important effect.

Counsel for the respondent submitted that the *Pioneer Laundry Case* (*supra*) had decided the question now under review. There are, undoubtedly, statements in that case which lend support to the view that if the Minister exercises his discretionary powers under the Act on proper legal principles his exercise of them is not open to review by the Court. Counsel for the appellant submitted that the questions raised by him in this appeal, such as whether the appeal from the assessment involves an appeal from the Minister's determination in his discretion, and whether the appeal to this Court is in the nature of a trial *de novo* enabling it to go into all the facts that were before the Minister, draw a conclusion from them and substitute its own opinion for the determination of the Minister, were not before either the Supreme Court of Canada or the Judicial Committee and were not argued before either of them; and contended that, under the circumstances, many of the statements in the case were *obiter dicta* and that it should not be regarded as an authority against him. In the main, I agree with his contentions; a number of the statements are clearly *obiter dicta* and have no binding authority; but, although that is so, they are not without persuasive effect. The misunderstanding of the case to which I have referred is in part due to some of these statements which, unfortunately, are not couched in the precise and accurate terms that might have been expected if the questions now under review had been argued, and some discussion of them is required.

In the Supreme Court of Canada, Davis J., after stating that section 5 (*a*) placed upon the Minister "an administrative duty of a quasi-judicial character—a discretion to be exercised on proper legal principles", went on to say, at page 5:—

> Section 60 of the Act entitles a taxpaper, after receipt of the decision of the Minister upon appeal from an assessment, if dissatisfied therewith,

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to appeal to the Court. The decision is appealable; but the exercise of the discretion will not be interfered with unless it was manifestly against sound and fundamental principles.

Sound and fundamental principles must mean the same thing as proper legal principles. If the purported exercise of discretion is "manifestly against sound and fundamental principles" it is not the exercise of discretion as contemplated by law at all and the interference by the Court is not really interference with the exercise of the discretion, but rather a finding that it has not been exercised. Later, Davis J. said, at page 8:—

> *The Income War Tax Act* gives a right of appeal from the Minister's decisions and while there is no statutory limitation upon the appellate jurisdiction, normally the Court would not interfere with the exercise of a discretion by the Minister except on grounds of law.

The introduction of the word "normally" is confusing for it makes the statement seem to qualify the earlier one and suggests that there might be cases in which the Court would interfere with the exercise of the discretion, otherwise than on grounds of law, without indicating the kind of cases in which it would do so. If the statement implies that the Act gives a right of appeal from the Minister's decision on the exercise of his discretion, it is clearly not in accord with the Act, which expressly makes the appeal an appeal from the assessment. Davis J. clarified the position when he held that the Commissioner, acting for the Minister, had exercised a discretion upon what he considered to be wrong principles of law and said, at page 8:—

> it is the duty of the Court in such circumstances to remit the case, as provided by sec. 65 (2) of the Act, for a re-consideration of the subject matter, stripped of the application of these wrong principles.

It would, I think, be a reasonable inference from his statements as a whole that Davis J. was of the opinion that, if the Minister on his reconsideration of the matter exercised his discretion on proper legal principles, the quantum of his allowance for depreciation would not concern the Court, but this is a matter of inference of his opinion only, since the question was not before him for judicial decision.

Some of the remarks of Lord Thankerton in the Judicial Committee also require comment. After deciding that the taxpayer had a statutory right to a depreciation allowance,

and that the Minister was under a duty to fix a reasonable amount of such allowance, he went on to say, at page 136:—

> so far from the decision of the Minister being purely administrative and final, a right of appeal is conferred on a dissatisfied taxpaper; but it is equally clear that the Court would not interfere with the decision unless—as Davis J. states—"it was manifestly against sound and fundamental principles."

In this passage Lord Thankerton seems to speak of the right of appeal as being from the decision of the Minister and the only decision to which reference is made is that of the Minister in fixing a reasonable amount for depreciation allowance. I confess that I am unable to reconcile the two statements contained in the passage, having regard to their respective implications. It must follow, I think, from the second statement that if the Minister's decision was not "manifestly against sound and fundamental principles" but was made on proper legal principles the Court would not interfere with it; in such a case the decision of the Minister would be final, since the Court would not interfere. Conversely, if the Minister's decision is not final since there is a right of appeal from it, it must be contemplated that the Court may interfere with the discretion for, otherwise, the right of appeal would be meaningless. The two statements are thus in conflict with one another. Two explanations are possible. One is that Lord Thankerton meant that the Minister's decision was not final if it was against sound and fundamental principles. The other is that the first statement in the passage must be modified in view of the fact that the right of appeal conferred on a dissatisfied taxpayer is a right of appeal from the assessment, as analysis of the Act would have shown if the exact nature of the appeal conferred by the Act had been before the Court. If the first statement is modified, as it should be, then the second can stand unaltered with its necessary implication as it was clearly intended it should do. That this is so is made clear by the course taken in remitting the matter back to the Minister for the exercise of his discretion on proper legal principles with the implication involved therein that such exercise would not be interfered with.

After the Judicial Committee had referred the matter back to the Minister the Commissioner fixed the depreciation allowance to the appellant at the sum of $1 and the

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matter came before this Court again in *Pioneer Laundry & Dry Cleaners Limited* v. *Minister of National Revenue* (1). Robson J. held that such allowance was not the exercise of discretion at all. At page 180, he said:

> I cannot think that this mere allowance of a nominal sum was a possibility within the contemplation of the learned Lords when they referred the question back to the Minister. I have to say, with deference, that I think the course pursued was not a consideration of a reasonable amount for depreciation within the intention of the Act. I have not the benefit of any explanation, simply the Minister's decision.

He allowed the appeal and referred the matter back to the Minister for further consideration of reasonable allowance within the Act. It is suggested that the last sentence in the passage cited implies a right in the Court to review the amount of the allowance to determine whether it was reasonable or not if there had been more facts before the Court by way of explanation. I am unable to read any such view into the judgment. It is clear that Robson J. considered that the allowance of a merely nominal sum was not the exercise of the discretion contemplated by section 5 (*a*) at all. If any inference is to be taken from the judgment, a fair one would be that if the allowance made had been other than a nominal one the amount of it would not have been questioned.

The action taken by the Courts in the two *Pioneer Laundry Cases* (*supra*) in sending the matter back to the Minister for the exercise of his discretion on proper legal principles is, in my opinion, even more important than the statements in them which I have discussed. It is clear from such action that the Court assumed that the proper person to exercise the discretion called for by section 5 (*a*) was the Minister himself—and not the Court, even under its appellate jurisdiction. If the Court did not consider it proper to exercise discretion where the Minister had failed to exercise his in the manner contemplated by law, surely it would not be proper to do so where the Minister has exercised the discretion vested in him on proper legal principles. The reason for the action taken is sound; the exercise of the discretion vested in the Minister is his function in the course of his administrative duties; it is the duty of the Court to supervise the manner of its exercise, but there its function stops; with the quantum of such

(1) (1942) Ex. C.R. 179.

exercise the Court is not concerned. When the judicial or quasi-judicial requirements of the Minister's duty have been satisfied all that remains is administrative. The Court is a judicial body, not an administrative one; it must keep within the confines of its own jurisdiction and be careful not to arrogate to itself functions which Parliament has clearly entrusted to the Minister.

Such careful consideration as I have been able to give to the *Pioneer Laundry Cases* (*supra*) strengthens me in the conclusion that I have reached in this appeal that when the Minister has determined in his discretion under section 6 (2) of the Income War Tax Act the amount of excessive expense to be disallowed to a taxpayer as a deduction from his income and has exercised his discretion on proper legal principles, the amount so determined is not open to review by the Court; and an assessment in which a disallowance so determined has been included cannot, to the extent of such inclusion, be successfully attacked as incorrect either in fact or in law in an appeal to the Court under the Act.

If there is any suggestion in the first *Pioneer Laundry case* (*supra*) that the Court, while it will not interfere with the exercise of the discretion vested in the Minister except on certain grounds, has the right of such interference except on certain grounds but will not exercise it, then the conclusion I have reached goes farther, for it is that, if the requirements of section 6 (2) are fully met, the Court has no right to interfere at all, under the Act as it now stands.

In this connection reference may be made to the decision of the Supreme Court of New South Wales in *Dobinson* v. *Federal Commissioner of Taxation* (1). This is the only case, of which I am aware, in which the Court on an appeal from an income tax assessment has substituted its own opinion for that formed by the Commissioner under his statutory powers. In that case the Commissioner was of the opinion that a partnership which the appellant had entered into with his wife had been formed for the purpose of relieving him from a liability to which he would have been otherwise subject and, on the basis of such opinion, assessed the partnership as if it were a single person. He had statutory authority for forming his opinion and making

(1) (1935) 3 Australian Tax Decisions 150

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the resulting assessment under section 29 (2) of the Commonwealth of Australia Income Tax Assessment Act, 1922-1933. At the hearing of the appeal from the assessment, the appellant, his wife and their accountant gave evidence that the partnership was not entered into for the purpose of relieving the husband of any liability to taxation to which he would otherwise have been subject. Jordan C. J. accepted this evidence, came to a conclusion different from the opinion formed by the Commissioner and allowed the appeal. This decision was made under quite a different state of law from that which obtains in Canada. While sections 50, 51 and 51A of the Commonwealth of Australia Income Tax Assessment Act, 1922-1933, contained provisions for appeal by a dissatisfied taxpayer from the assessment made by the Commissioner, in several respects similar to those in the Canadian Income War Tax Act, there was also a special section, enacted in 1930, for which there is no counterpart in the Canadian Act. This was section 51B which read as follows:—

> 51B. Notwithstanding anything contained in this Act a taxpayer who is dissatisfied with any opinion, decision or determination of the Commissioner under section twenty-one A, paragraph (n) of sub-section (1) of section twenty-three, or subsection (2) of section twenty-nine of this Act (whether in the exercise of a discretion conferred upon the Commissioner or otherwise) and who is dissatisfied with any assessment made pursuant to or involving such opinion, decision or determination shall, after the assessment has been made, have the same right of objection and appeal in respect of such opinion, decision or determination and assessment as is provided in sections fifty, fifty-one and fifty-one A of the Act.

It is clear from the judgment of Jordan C. J. that it was only because of this special section that the Court was able to review the opinion of the Commissioner and substitute its own opinion for that formed by him under section 29 (2), and that without such section it could not have done so. At page 151, he said:

> In certain special cases, however, the fact that the Commissioner entertains a particular opinion is made the criterion of the existence of liability. In such cases there can, obviously, be no appeal from his opinion unless the Act gives an appeal, although the opinion can be examined within certain limits.

Jordan C. J. is here clearly referring to the opinion of the Commissioner under section 29 (2) and its binding effect in the absence of an appeal from it. Then he continued:—

> Section 51B provides in terms that a taxpayer shall have the same right of appeal in respect of any opinion of the Commissioner under s. 29

(2) and in respect of any assessment made pursuant to or involving such opinion as is provided in ordinary cases. I think it follows from this that the appellate tribunal must consider for itself such material as is placed before it with respect to matter as to which the Commissioner's opinion was formed, and that it is intended that the opinion of that tribunal should be substituted for that of the Commissioner as a criterion of liability if it forms an opinion different from his.

In my judgment, the *Dobinson Case* (*supra*) supports the conclusion that, since the Income War Tax Act provides specifically for an appeal from an assessment and makes no provision for any appeal from the Minister's determination under section 6 (2), there is no appeal from the latter, and that, before the Court could try *de novo* the facts that were before the Minister prior to his determination and substitute its own opinion as to the amount of excessive expense to be disallowed, if any, for the amount determined by the Minister in his discretion under section 6 (2), there would have to be specific statutory authority enabling it to do so, similar in effect to that given by section 51B of the Australian Act. There is no such authority in the Income War Tax Act, as it now stands.

It was not argued before me that the Minister in making his determination under section 6 (2) had not exercised his discretion on proper legal principles and there is nothing in the case to indicate or suggest that he did not do so. The determination cannot be challenged on any such ground. Counsel for the appellant argued on the facts that the Minister did not correctly exercise his discretion in that he did not give proper consideration to the increase in the appellant's business and profits and did not make a fair allowance for overtime work by the directors. The appellant had the fullest opportunity of placing its case before the Minister and the facts were all before him before he made his determination. The matters referred to by counsel are among the very considerations that Parliament has left to the discretion of the Minister. The conclusion which he reached after exercising his discretion on proper legal principles is not open to review by the Court.

The appellant has failed to show that the assessments under appeal were incorrect either in fact or in law and its appeal must be dismissed with costs.

Judgment accordingly,