BETWEEN:

YARDLEY PLASTICS OF CANADA LIMITED ..... APPELLANT;

AND

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

Toronto 1966 March 30, 31

Ottawa April 21

Revenue—Income—Income Tax Act—Sections 39(3), 39(4)(b), 39(4a)(c), 139(5a), 139(5d)(a)—Corporations being controlled by the same person or group of persons, associated with each other within the meaning of section 39(4)(b) of the Income Tax Act—Failure of the appellant to have successfully challenged the assumptions of fact that both corporations were under a common management coupled with the controlling group being common share-holders in both corporations—Appeal dismissed.

Appeal from the assessment of the appellant for the 1961 taxation year whereby a tax of $1,460 42 was levied on the basis that the appellant as well as a corporation called Canadian Mouldings Ltd., being controlled by the same group of persons, were therefore associated with each other within the meaning of section 39(4)(*b*) of the *Income Tax Act* and the appellant's tax was therefore determined in accordance with the provisions of subsection (3) of section 39 of the Act.

Section 39(4)(*b*) of the Act provides that corporations bear a tax rate of 18% on their first $35,000 profit and $6,300 plus 47% of the amount by which the amount taxable exceeds $35,000 if the amount taxable exceeds $35,000.

This, however, does not prevail if one corporation is associated with one or more other corporations at any time during the year when the 18% rate must be allocated to one of them or shared between them in some agreed proportion.

The sole issue in the present appeal is whether the appellant and Canadian Mouldings Ltd. are associated or not under section 39(4) of the *Income Tax Act* read in conjunction with sections 39(4)(*a*) and 139(5d)(*a*) of the Act.

The meaning of control of a corporation is not defined in section 39(4) and reference should be made in this regard to page 507 in *Buckerfield's Ltd. et al v. M.N.R.* [1964] C.T.C., Jackett P.:

> "...section 39 of the *Income Tax Act*, the word "controlled" contemplates the right of control that rests in ownership of such a number of shares as carries with it the right to a majority of the votes in the election of the board of directors. See *British American Tobacco v. C.I.R.* [1943] 1 All E R. 13, where Viscount Simon L.C., at page 15 says:
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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'."

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The concept of control in section 39(4) of the Act has been expanded somewhat through section 39(4a)(*c*) which makes section 139(5d) applicable to section 39(4) of the Act and subsection (*b*) of section 139(5d) in the cases therein contemplated even makes mere factual control or even potential control sufficient within the meaning of control in section 39(4) so as to associate two or more corporations.

Held, That the appellant has not succeeded in its submissions because although section 139(5d) and its subsections directly affect section 39(4) in extending the meaning of control therein, they do not restrict its meaning.

2. That, although section 139(5d)(*a*) creates a statutory fiction in deeming that a related group in a position to control is a related group that controls a given corporation whether or not it is part of a larger group by whom the corporation is in fact controlled, it does so for the sole purpose of assisting in the construction of the words "related group" found in sub-paragraphs (iii) and (v) of section 139(*a*) as well as paragraph (*e*) of subsection 4 of section 39 of the Act, and does not create a statutory fiction in relation to the corporations controlled by an unrelated group as provided for in subsection (*b*) of section 39(4) of the Act, nor does section 139(5d)(*a*) eliminate the possibility of another group being held to control thereunder.

3. That section 139 (5d)(*a*) may become useful in a given case to determine when a related group may be declared to control but does not do away with or exclude or preclude the holding of an unrelated group as controlling two corporations when such a group does so control even when conditions are such that they happen to also meet with the requirements of the above section.

4. That section 139(5d)(*a*) indicates that the artificial construction was directed at the concept of a related group and would apply only when the statutory fiction of control created by the section and made available to the Minister as a possible basis of claim, from a revenue point of view, was required to bring into association two or more corporations controlled by related groups who otherwise would not fall within the strict conditions as set down, for instance in some of the subsections of section 139(5a)(*c*) of the Act.

5. That, when dealing with groups, it is always a question of fact as to whether any "group of persons" who own the majority of the voting power in a company are in effective control of its affairs and fortunes.

6. That "the appellant and Canadian Mouldings Ltd. were both, at some time in the taxation year 1961, controlled by a group comprised of F. B. Hill, F. B. Hill III, R. H. Wycoff, F. R. Daymond and W. E. Jacobson and that by virtue of paragraph (*b*) of s.s. (4) of sec. 39 of the *Income Tax Act,* the appellant and Canadian Mouldings Limited were associated in 1961"

7. Failure by the appellant to have successfully challenged the assumption of fact upon which the assessment was based and in view of the circumstances surrounding the origin of both corporations which were under a common management and the fact that the group chosen by the Minister as the controlling group were common shareholders in both corporations all lead to the conclusion that the group chosen is a group as contemplated by section 39(4)(*b*) of the Act.

8. That the appeal be dismissed with costs.

APPEAL from a decision of the Tax Appeal Board.

J. M. Shoemaker for appellant.

G. W. Ainslie and *Bruce Verchere* for respondent.

NOËL J.:—This is an appeal from a decision of the Tax Appeal Board[1] which confirmed a re-assessment of the appellant for the 1961 taxation year whereby a tax of $1,460.42 was levied on the basis that the appellant as well as a corporation called Canadian Mouldings Ltd., being controlled by the same group of persons, were therefore associated with each other within the meaning of section 39(4)(*b*) of the *Income Tax Act* and the appellant's tax was therefore determined in accordance with the provisions of subsection (3) of section 39 of the Act.

The above section provides that corporations bear a tax rate of 18% on their first $35,000 profit and $6,300 plus 47% of the amount by which the amount taxable exceeds $35,000 if the amount taxable exceeds $35,000. This, however, does not prevail if one corporation is associated with one or more other corporations at any time during the year when the 18% rate must be allocated to one of them or shared between them in some agreed proportion.

The shareholdings of the companies for the year 1961 (common as well as preferred both of which ranked equally for purposes of voting) were as appear in Schedule "A" produced hereunder:

SCHEDULE "A"

	CANADIAN MOULDINGS LIMITED			YARDLEY PLASTICS OF CANADA LIMITED		
	Common	Preferred		Common	Preferred	
Shareholder	Shares	Shares	%	Shares	Shares	%
F. B. Hill	1	162	4.6	5,321	53	28.0
F. B. Hill III	665	—	18.6	4,276	42	22.5
R. H. Wycoff	666	102	21.7	2,090	21	11.0
F. R. Daymond	669	102	21.7	2,660	27	14.0
A. Strachan	666	102	21.7	—	—	—
C. A. Ebner	—	—	—	3,231	33	17.0
W. E. Jacobson	333	81	11.7	1,425	14	7.5
	3,000	549	100%	19,003	190	100%

[1] 38 Tax A.B.C. 137.

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The respondent in its assessment assumed that the appellant and Canadian Mouldings Limited were both at some time in the taxation year 1961 controlled by the following group of persons in Schedule "D" hereunder, which comprises all the shareholders of both corporations who are common to both companies and therefore excepting therefrom A. Strachan who holds shares in Canadian Mouldings Limited only and C. A. Ebner, who holds shares in Yardley Plastics of Canada Limited only:

SCHEDULE "D"

MINISTERIAL GROUP
SHAREHOLDINGS OF THE COMPANIES—1961

	CANADIAN MOULDINGS LIMITED			YARDLEY PLASTICS OF CANADA LIMITED		
	Common	Preferred		Common	Preferred	
Shareholder	Shares	Shares	%	Shares	Shares	%
F. B. Hill	1	162	4.6	5,321	53	28.0
F. B. Hill III	665	—	18.6	4,276	42	22.5
R. H. Wycoff	666	102	21.7	2,090	21	11.0
F. R. Daymond	669	102	21.7	2,660	27	14.0
W. E. Jacobson	333	81	11.7	1,425	14	7.5
	2,334	447	78.3%	15,772	157	83.0%

At the hearing counsel for both parties agreed that the evidence in this appeal would be restricted to that of Mr. C. R. Hunter before the Tax Appeal Board to be found in the transcript at pp. 9 to 21 inclusive, that Schedules "A" and "D" produced by the appellant represent truly the holdings in both corporations, that two of the shareholders of both corporations, F. B. Hill and F. B. Hill III, are respectively father and son and are, therefore, related persons within the meaning of the provisions of section 139 of the *Income Tax Act* and that the other shareholders of the group chosen by the respondent are not related persons within the meaning of the Act. Counsel for the Minister finally admitted that the shareholders of both corporations which appear on Schedule "D" were the absolute and beneficial owners of all of the shares which appear opposite their names and that there was no arrangement contractual or otherwise which would bind any of the shareholders as to the manner in which they would cast or exercise their votes at any meetings of shareholders of either of the corporations.

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Mr. Hunter, the controller of Daymond Company, which administers the appellant corporation as well as Canadian Mouldings Ltd., stated that the Daymond Company Limited was incorporated around 1942 by a Mr. F. R. Daymond, father of the F. R. Daymond whose name appears as a shareholder of both the appellant company and Canadian Mouldings Ltd. The Daymond Company was engaged in the wholesale distribution of building materials as well as of plastic and aluminum products. When Canadian Mouldings Ltd. was formed in 1945, it purchased the assets of the metal moulding business which had been carried on by Mr. F. R. Daymond personally. When Yardley Plastics of Canada Limited was incorporated in 1947 it purchased assets from Yardley Plastics of Columbus, Ohio, including tools, jigs, dies and certain form manufacturing techniques. The Daymond Company Limited has continued its wholesale business, which consists of buying and reselling both plastic and aluminum products. The accounting, and administration of the various companies, is carried on at the office premises of the Daymond Company Limited, where each company has certain of its employees stationed for that purpose.

The sole issue in the present appeal is whether the appellant and Canadian Mouldings Limited are associated or not under section 39(4) of the *Income Tax Act* read in conjunction with sections 39(4a), 139(5a) and 139(5d)(*a*) of the Act, the relevant parts of which I have underlined. These sections read as follows:

39(4).

(4) For the purpose of this section, *one corporation is associated with another in a taxation year if, at any time in the year,*

(*a*) one of the corporations controlled the other,

(*b*) *both of the corporations were controlled by the same person or group of persons,*

(*c*) each of the corporations was controlled by one person and the person who controlled one of the corporations was related to the person who controlled the other, and one of those persons owned directly or indirectly one or more shares of the capital stock of each of the corporations,

(*d*) one of the corporations was controlled by one person and that person was related to each member of a group of persons that controlled the other corporation, and one of those persons owned directly or indirectly one or more shares of the capital stock of each of the corporations, or

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(e) each of the corporations was controlled by a *related group* and each of the members of one of the related groups was related to all of the members of the other *related group,* and one of the members of one of the related groups owned directly or indirectly one or more shares of the capital stock of each of the corporations.

39(4a).

(4a) *For the purpose of this section,*

(a) one person is related to another person if they are "related persons" or persons related to each other within the meaning of subsection (5a) of section 139;

(b) "related group" has the meaning given that expression in subsection (5c) of section 139; and

(c) *subsection (5d) of section 139 is applicable mutatis mutandis.*

139(5a).

(5a) For the purpose of subsection (5), (5c) and this subsection, *"related persons"* or persons related to each other are,

(a) individuals connected by blood relationship, marriage or adoption;

(b) a corporation and

(i) a person who controls the corporation, if it is controlled by one person,

(ii) a person who is a member of a related group that controls the corporation, or

(iii) any person related to a person described by subparagraph (i) or (ii);

(c) any two corporations

(i) if they are controlled by the same person or group of persons,

(ii) if each of the corporations is controlled by one person and the person who controls one of the corporations is related to the person who controls the other corporation,

(iii) *if one of the corporations is controlled by one person and that person is related to any member of a related group that controls the other corporation,*

(iv) if one of the corporations is controlled by one person and that person is related to each member of an unrelated group that controls the other corporation,

(v) *if any member of a related group that controls one of the corporations is related to each member of an unrelated group that controls the other corporation,* or

(vi) if each member of an unrelated group that controls one of the corporations is related to at least one member of an unrelated group that controls the other corporation.

139(5d).

(5d) For the purpose of subsection (5a)

(a) *where a related group is in a position to control a corporation, it shall be deemed to be a related group that controls the corporation whether or not it is part of a larger group by whom the corporation is in fact controlled;*

It will be useful at this point to consider the meaning of control of a corporation and as it is not defined in section 39(4), reference should be made to what the President of this Court said in this regard at p. 507 in *Buckerfield's Limited et al. v. M.N.R.*[1]:

> Many approaches might conceivably be adopted in applying the word "control" in a statute such as the *Income Tax Act* to a corporation. It might, for example, refer to control by "management", where management and the board of directors are separate, or it might refer to control by the board of directors. The kind of control exercised by management officials or the board of directors is, however, clearly not intended by Section 39 when it contemplates control of one corporation by another as well as control of a corporation by the individuals (see subsection (6) of Section 39). The word "control" might conceivably refer to *de facto* control by one or more shareholders whether or not they hold a majority of shares. I am of the view, however, that in Section 39 of the *Income Tax Act*, the word "controlled" contemplates the right of control that rests in ownership of such a number of shares as carries with it the right to a majority of the votes in the election of the board of directors. See *British American Tobacco v. C.I.R.*, [1943] 1 All E.R. 13, where Viscount Simon L.C., at page 15 says:
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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."

I might enlarge somewhat upon these comments by saying that it appears to me that the concept of control in section 39(4) of the Act has been expanded somewhat through section 39(4a)(*c*) which makes section 139(5d) applicable to section 39(4) of the Act and subsection (*b*) of section 139(5d) in the cases therein contemplated even makes mere factual control or even potential control sufficient within the meaning of control in section 39(4) so as to associate two or more corporations when it states that:

> (*b*) a person who had a right under a contract, in equity or otherwise, either immediately or in the future and either absolutely or contingently, to, or to acquire, shares in a corporation, or to control the voting rights of shares in a corporation, shall, except where the contract provided that the right is not exercisable until the death of an individual designated therein, be deemed to have had the same position in relation to the control of the corporation as if he owned the shares.

Counsel for the appellant presented two rather ingenious submissions with which I will now deal. His first can be stated simply as follows: a related group composed of F. B. Hill and F. B. Hill III, father and son respectively, is deemed by section 139(5d)(*a*) to control Yardley Plastics

[1] [1964] C.T.C. 504.

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and since Hill and Hill III do not control Canadian Mouldings Ltd., the two corporations cannot be held to be in association. There is no doubt that as F. B. Hill and F. B. Hill III own 28.00% and 22.5% respectively of the voting shares of Yardley Plastics of Canada Limited, they are "in a position to control a corporation" and, therefore, as set down by subsection (*a*) of section 139(5d) they form a related group which, because of this same section, is "deemed to be a related group that controls the corporation" and this, according to the appellant, becomes an irrebuttable situation which would prevent the respondent from choosing another group as the controlling group under section 39(4)(*b*) of the Act. The appellant in order to succeed on this point had to establish that section 139(5d)(*a*) can change and restrict the natural meaning of the words found in paragraph (*b*) of subsection 4 of section 39 of the Act which sets out that "one corporation is associated with another in a taxation year if, at any time in the year...

(*b*) both of the corporations were *controlled* by the same person or *group of persons*."

(the emphasis is mine.)

The appellant has not, however, succeeded in this regard because although section 139(5d) and its subsections directly affect section 39(4) in extending the meaning of control therein, they do not restrict its meaning. Indeed, although section 139(5d)(*a*) creates a statutory fiction in deeming that a related group in a position to control is a related group that controls a given corporation whether or not it is part of a larger group by whom the corporation is in fact controlled, it does so for the sole purpose of assisting in the construction of the words "related group" found in sub-paragraphs (iii) and (v) of section 139(5a) as well as paragraph (*e*) of subsection 4 of section 39 of the Act, and does not create a statutory fiction in relation to the corporations controlled by an unrelated group as provided for in subsection (*b*) of section 39(4) of the Act nor does section 139(5d)(*a*) eliminate the possibility of another group being held to control thereunder. Section 139(5d)(*a*) therefore may become useful in a given case to determine when a related group may be declared to control but does not do

away with or exclude or preclude the holding of an unrelated group as controlling two corporations when such a group does so control even when the conditions are such that they happen to also meet with the requirements of section 139(5d)(*a*) such as we have in the present case.

I am further confirmed in this view by the language used in the above section which places an artificial construction on the words "related group" and not on the word "control" by repeating the words "related group" when it states that "where a related group is in a position to control a corporation, it shall be deemed to be a related group that controls the corporation" instead of merely saying as it could have that "it shall be deemed to control". This indeed indicates that the artificial construction was directed at the concept of a related group and would apply only when the statutory fiction of control created by the section and made available to the Minister as a possible basis of claim, from a revenue point of view, was required to bring into association two or more corporations controlled by related groups who otherwise would not fall within the strict conditions as set down, for instance in some of the subsections of section 139(5a)(*c*) of the Act. It, however, does not have the effect of eliminating the right of the Minister to adopt another basis of claim which flows from another section and which is given in the clear words of section 39(4)(*b*) in a case where a larger unrelated group controls.

It therefore follows that if a case be found to come within subsection (*b*) of section 39(4) of the Act, it is not necessary for the purpose of association to look any further and enquire as to whether it might fall (because it has one or two persons related amongst the group who own more than 50% of the voting shares of one company) in a class covered by section 139(5d)(*a*) of the Act because this section is merely supplementary and an expansion of the cases where control of two or more corporations may be found for the purpose (through section 39(4a) of its subsections) of ascertaining the associated status of corporations under section 39(4) of the Act.

I cannot indeed come to the conclusion, upon a reading of all the sections which deal with associated corporations, that the natural meaning of the words used in section 39(4)(*b*) in the present case are altered or modified so as to

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exclude an unrelated group common to both corporations every time one finds amongst such a group as here two persons who are related and who own more than 50% of the voting shares of one corporation, but less than 50% of the other corporation, nor can I accept that because of this it would not be permitted to look at any other unrelated group common to two corporations and which controls both of them.

The appellant's second submission is that under section 39(4)(*b*) for the purposes of association, where corporations are controlled by the same group of persons, this group must have the right to effectively control the corporations and if it does not, then it cannot be considered as the group contemplated in the section.

Counsel for the appellant relies in this respect on the decision of the President of this Court and the expression quoted therein of Viscount Simon L.C. at p. 15 *in re British American Tobacco Co. v. C.I.R.*[1] where he says:

> 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.

(the emphasis is mine.)

Counsel for the appellant, referring again to the *Buckerfield's case* (*supra*) states that the President of this Court when referring to the word "controlled" used in section 39 (and not control), has defined it as the right of control which means the right to exercise effectively the ultimate decision as to the carrying on of the business of the corporation. He relies on a further decision of the President of this Court in *Dworkin Furs (Pembroke) Limited v. M.N.R.*[2] which also indicates that "controlled" means something more than "control" when at p. 468 of the above decision it is stated that:

> ...One corporation cannot, in my view, be said to be "controlled" by another in any possible sense of that word unless that other can, over the long run, determine the conduct of its affairs.

He then concludes that "controlled", when control by a group is involved, is therefore something more than mere "control", i.e., a holding which might carry the majority of votes but must be the group that effectively controls and carries with it the power to determine the conduct of the corporation's affairs over the long run.

[1] [1943] 1 All E.R. 13. [2] [1965] C.T.C. 465.

As, according to counsel for the appellant, the group chosen by the Minister herein as the group that controlled is not the only group that could have been chosen (Schedule "B" produced by the appellant indeed pointed out five other combinations of groups which could also have been taken and which all would have held a majority of the voting power) it cannot have effective control of the corporations nor determine their affairs over the long run and, therefore, cannot be the group that effectively controlled the corporations.

I do not believe, as submitted by counsel for the Minister, that the latter is allowed to choose out of several possible groups any aggregation holding more than 50% of the voting power, even if the members of the group are common shareholders in both corporations and that such a group then becomes irrebuttably deemed to be the controlling group for the purposes of section 39(4) of the Act as this could lead to an absurd situation where no two large corporations in this country would be safe from being held to be associated.

I would indeed hold that when dealing with groups it is always a question of fact as to whether any "group of persons" who own the majority of the voting power in a company are in effective control of its affairs and fortunes following in this regard the dictum of Jackett P. in *Buckerfield's Ltd. et al v. M.N.R.* (*supra*) at p. 508 where he stated:

> Where, in the application of Section 39(4), a single person does not own sufficient shares to have control in the sense to which I have just referred, it becomes a question of fact as to whether any "group of persons" does own such a number of shares.

In the instant case, however, because of the history of both corporations, Yardley Plastics of Canada Limited and Canadian Mouldings Ltd., and in view of the fact that both, for many years, have been administered by the same corporation, Daymond Company (incorporated by the father of one of the shareholders of both companies, F. R. Daymond) it is not too surprising that the Minister in assessing the appellant and in his reply to the notice of appeal assumed, at paragraph 6 thereof, the following facts on which he based the assessment:

> 6. The Respondent says that the Appellant and Canadian Mouldings Limited were both at some time in the taxation year 1961 controlled by a group comprised of F. B. Hill, F. B. Hill III, R. H. Wycoff, F. R. Daymond

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and W. E. Jacobson and that by virtue of paragraph (*b*) of s.s. (4) of sec. 39 of the *Income Tax Act*, the Appellant and the Canadian Mouldings Limited were associated in 1961.

It then follows, referring to the dictum of Rand J. in *Johnston v. M.N.R.*[1] that:

> Every such fact found or assumed by the assessor or the Minister must then be accepted as it was dealt with by these persons unless questioned by the Appellant.

The appellant here could have (as pointed out by Cattanach J. in *M.N.R. v. Pillsbury Holdings Ltd.*[2]) met the Minister's pleading that in assessing it he assumed the facts set out in paragraph 6 of his reply to the notice of appeal by

(*a*) challenging the Minister's allegation that he did assume those facts;

(*b*) assuming the onus of showing that one or more of the assumptions were wrong, or

(*c*) contending that, even if the assumptions were justified they do not of themselves support the assessment.

The appellant here attempted to challenge the assumptions of fact of the Minister by merely pointing out that several other combinations or groups could be held to have controlled the corporations during the year without, however, discharging the burden it had, and can exercise, by putting evidence before the Court to establish that the group assumed by the respondent to control the corporations was not the group that controlled the corporations, as it had to do in order to succeed herein.

It then follows that because of the failure of the appellant to have successfully challenged the assumptions of fact on which the assessment is based and also because of the circumstances surrounding the origin of both corporations, their being under a common management, coupled with the group chosen by the Minister as the controlling group being common shareholders in both corporations, I must and do find the said group so chosen to be a group as contemplated by section 39(4)(*b*) of the Act.

The appeal is dismissed with costs.

[1] [1948] S.C.R. 486.

[2] [1964] C.T.C. 294 at 302.