

TAXATION DECISIONS AND RULINGS

The Taxation Division of the Department of National Revenue has adopted a policy of issuing from time to time rulings and directives on the interpretation and administration of the Income War Tax Act, The Excess Profits Tax Act and The Succession Duty Act. These are similar in form and intent to the memoranda formerly issued to Inspectors of Income Tax. It will be recalled that the Taxation Committee of the Canadian Bar Association, along with others, made representations to the effect that these memoranda should be made available to the public. Substantially this is now being done and many of the rulings and directives should be of value and interest to members of the profession.

Apparently the rulings and directives are not being issued in numerical order and some dealing with purely internal matters in the Taxation Division are not being publicized at all. We propose, however, to publish such of those received as seem of direct interest to the legal profession; those which are not of particular interest will be mentioned together with a short statement as to their contents and effect. Anyone desiring fuller information may obtain details from the local office of the Taxation Division.

Tax Ruling No. 1 dated February 24th, 1947, dealt with the exercise of ministerial discretion under section 6, subsections (2) and (3), of the Income War Tax Act with regard to salary allowances. In effect it indicates that the Department proposes in future to exercise its discretion in this regard only after a full and careful consideration of all the facts in the particular case. Ruling No. 2 on pension plans was reprinted in the March issue at page 295. Ruling No. 3 of March 17th concerns the taxation of the remuneration of U.N.R.R.A. employees ordinarily resident in Canada but working in the United States. Ruling No. 4 dated March 20th is published in this issue and Ruling No. 5 has not been received. The subject of Ruling No. 6 of March 28th is "Profits or Losses on Transactions involving Sterling or Foreign Exchange".

Directives No. 7 of April 25th, No. 8 of April 25th, No. 12 of May 1st, No. 15 of May 2nd and No. 17 of May 6th are reprinted in this issue. In addition Directives No. 5, 6 and 13 have been issued. No. 5 concerns the procedure to be followed by taxpayers who wish to present problems at the Head Office in Ottawa. In future such persons will only be heard after the matter in dispute has been discussed fully with the officials in

the local office and these latter have forwarded a report on the facts with their conclusions to the Head Office. The Directive indicates that, while taxpayers or their representatives will still be heard at the Head Office, it is desired to keep their visits to a minimum. Directive No. 6 of April 22nd gives notice that the regulation published in the Canada Gazette on February 26th, 1944, in connection with adjustment to standard profits for the payment of stock dividends has been cancelled. The effect of the cancellation is that, where a stock dividend has been issued, the capital employed in the business may be adjusted accordingly. Directive No. 13 of May 2nd advises that an explanation will be given the taxpayer in every case where the actual tax assessed differs from his own computation on his return. Previously an explanation had been given only where there was an increase in the tax over a minimum amount. In future the explanation will cover any increase or decrease from the taxpayer's own computation.

The tax rulings and directives selected for publication follow:—

Returns of Deceased Persons — Income War Tax Act S. 33(3)
(Tax Ruling No. 4 of March 20th, 1947)

According to the present ruling, when a taxpayer dies after the close of the calendar year but before the 1st May, his executors are nevertheless required to file a return on or before the 30th April for the previous calendar year. It has now been decided that the following will apply, effective 1st January, 1947:

“If death occurs from 1st January until 30th April inclusive, and the taxpayer has not already filed his return for the preceding calendar year, the executors will be allowed four months from date of death to file the deceased taxpayer's return for the previous calendar year, before becoming subject to the penalties as provided in the Act.”

The first paragraph of page 2 of Memo. No. 59 (1944-45) and the last four lines of the last paragraph of page 1 of the same memorandum beginning “but the executors are required” are hereby cancelled.

Assessments — Business Losses — Deceased Taxpayers Estates
(Directive No. 7 of April 25th, 1947)

Questions have arisen concerning the treatment of losses sustained by an estate carrying on a business, including farming,

after the decease of the proprietor. You are advised as follows:

1. The estate is to be deemed to be a new taxpayer.
2. Any loss sustained by the estate in the first year or portion of the first year of its operations will not be permitted as a deduction from the income of the deceased proprietor.
3. Section 5, subsection 1(p) is applicable in the case of an estate carrying on business, but any loss sustained in the first year of the operation of the estate may only be claimed as a deduction from any profits of the following three years.

Assessments — Deductions — Membership Fees
(Directive No. 8 of April 25th, 1947)

It has been the practice of this Department to allow, as deductions from business income, membership fees in Boards of Trade, Chambers of Commerce, Manufacturers' Associations, Credit Men's Associations, Commercial Travellers' Associations, and other similar trade or commercial associations formed for purposes of advancing the collective interests of any particular branch of a trade or commercial enterprise. The number of such associations has increased considerably in the past few years but, so long as the purposes and bona fides are clear, the fees are clearly legitimate expenditures made for the purpose of earning income.

Membership in engineering, scientific and other learned associations and societies clearly belong in the same category.

However, the deduction of these membership fees is permissible only in the case of entrepreneurs and is not allowable against the income of salaried persons. Any well-conducted organization which wishes to have members of its staff belong to such associations will readily arrange an additional membership subscription. Where the employer is not prepared to do so and the employee nevertheless feels that he ought to have a membership, no doubt he considers that this is worthwhile from the standpoint of his future advancement. The cost therefore becomes essentially a personal expense and is something which the individual should absorb out of his own income without expecting a Government contribution thereto by way of a tax concession.

Assessments — Builders' Second Mortgages
(Directive No. 12 of May 1st, 1947)

Questions have arisen as to the method of taxing that part of the sale price of property received by builders in the shape of Second Mortgages. It has been suggested in some quarters that the amount of such Second Mortgages should only be reported as income in the year when such mortgages are actually paid, either at maturity or when sold perhaps at a discount.

Under no circumstances can we accept such a conclusion. The amount represented by the Second Mortgage is, in fact, part of the selling price and must be considered as income of the year in which the transaction takes place. It is an account receivable and should be so reflected in the same manner as a sale of merchandise.

As an account receivable it will be subject to the usual provisions with regard to the allowance of a reserve; whether or not such a reserve in respect thereof is to be admitted will depend upon all the relative facts at the end of the fiscal period. No definite rate of reserve can be laid down; in fact, it will be appreciated that in some cases a reserve should not be admitted at all having regard to the particular circumstances of the case. In other words, the factual situation must govern in determining whether or not a reserve will be allowed.

Assessments — Deduction from Income — Industrial Engineers et al.
(Directive No. 15 of May 2nd 1947)

It is in order to allow as an expense chargeable to income of a business enterprise, any reasonable charges by engineers, efficiency experts and others in the same general class, provided there is satisfactory evidence that the services for which the charges have been made have actually been rendered and were for the purpose of earning or maintaining income and not for capital purposes or related to capital transactions. An engineer's charge in connection with the installation and trial run of a new machine in a factory would be a charge to capital. A survey of a plant preparatory to its sale would be a capital charge also. But an account for a survey of the factory to improve its efficiency might properly be charged to income.

Expenditures which it is determined are admissible as a charge against income may be allowed in full in the year in which made. No pro-rating over several years is necessary although there is no objection to accepting such pro-rating if this is in accordance with a consistent policy on the part of the taxpayer.

This directive cancels memoranda Nos. 79 (1944-45), 96 (1944-45) and 47 (1946-47).

Assessments — Standard Profits Claims
(Directive No. 17 of May 6th, 1947)

The Honourable the Minister of Finance in his budget speech on April 29th proposed that the Excess Profits Tax Act be amended to provide that no taxpayer shall be entitled to make application for determination of his standard profits on or after August 1st, 1947.

On the assumption that this proposal will be implemented by legislation at the present session of Parliament it is deemed expedient to make known to the public at this time the following information which is being transmitted to the Bar Associations, Accountants' Associations, Boards of Trade, etc.

(1) In order to qualify for reference to the Board of Referees a taxpayer must file Form S.P. 1 and Questionnaire combined, in triplicate, with his local Director or Director-General of Income Tax on or before July 31st, 1947.

(2) These forms will not be accepted as having been filed within the time limit unless they have been properly completed and in addition are accompanied by a statement of particulars giving at least the minimum information required as indicated by the instructions printed on page four of the form.

(3) If a claim is filed on or before July 31st, 1947 which is not properly completed, the district office will immediately write direct to the taxpayer concerned advising what further information is required and warning that unless this information is supplied on or before July 31st, 1947, the claim will not be referred to the Board of Referees.

On and after the date of receipt of this Directive District Offices will not forward to Head Office the third copy of any S.P. 1 claim received until such claim is completed. Uncompleted claims will not be taken into account in preparing monthly reports of claims outstanding.

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Ottawa