About ten years have passed since the House of Lords in British Transport Commission v. Gourley\(^1\) held that the income tax liability of the plaintiff is a relevant consideration in assessing damages for loss of earnings. This decision has promoted much controversy\(^2\) and has prompted much legal writing.\(^2\) Before this decision it was settled law in the Commonwealth\(^4\) with the exception of Scotland\(^5\) that the court was not concerned with the plaintiff's liability to in-


\(^{2}\) It caused the Lord Chancellor to refer the matter of the relevance of income tax liability in the assessment of damages to the Law Reform Committee. In Scotland, the Lord Advocate referred this matter to the Law Reform Committee for Scotland. The Gourley decision formed the basis for a panel discussion entitled, Taxation in the Computation of Damages at the annual tax Conference of the Canadian Tax Foundation in 1964.

\(^{3}\) Some of the most significant articles are:


\(^{5}\) The conflicting Scottish cases were M'Daid v. Clyde Navigation Trustees, [1946] S.C. (Ct. of Sess.) 462 and Blackwood v. Andre, [1947] S.C. (Ct. of Sess.) 333. The first case held that the plaintiff's income tax liability should be taken into account. The second case was consistent with other Commonwealth decisions in holding that income tax should not be taken into account.
come tax in the assessment of damages. It is proposed to consider the difficulties which arise out of the Gourley case and the status of the Gourley principle in Canada.

British Transport Commission v. Gourley was a striking case. A very successful civil engineer was negligently injured while travelling by train. If the award for loss of earnings were granted without taking into account the plaintiff’s income tax liability, it would amount to £37,720. While if the award for loss of earnings were made on the basis of earnings after deduction of the income tax, it would amount to only £6,695. The House of Lords started from the premise that the function of the law of damages is to compensate the plaintiff for his loss. Their Lordships were then faced with the real question of whether the plaintiff’s liability to pay tax was to be regarded as too remote when determining what he has lost as a result of the accident. By a six to one decision, the House of Lords reversed the decision of the Court of Appeal and held that in assessing damages for loss of earnings, allowance must be made for the income tax liability which the plaintiff would otherwise have incurred. The decision of the Court of Appeal in Billingham v. Hughes which held that income tax considerations should be ignored as they were res inter alios acta was overruled.

Lord Goddard expressed surprise about the lack of authority and remarked that such an issue has never been before this House nor was there any decision in the appellate courts of the other Commonwealth countries or of the United States on the matter. This was an accurate statement with regard to the law in Canada. In Ontario, there appear to be only three trial court decisions prior to British Transport Commission v. Gourley. They are Fine v. T.T.C., Bowers v. J. Hollinger & Co. Limited and Anderson v. International Waxes Limited. In each case, tax liability was not taken into account in the assessment of damages for loss of earnings. However, the New Zealand Court of Appeal decision in Union Steam Ship Company of New Zealand Limited v. Ramstad apparently was not brought to Lord Goddard’s attention. The New Zealand Court of Appeal followed Billingham v. Hughes and held that social security tax on wages should be left out of account in assessment of damages for loss of earnings. The Ontario cases

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6 Supra, footnote 4. 7 Ibid. 8 Ibid. 9 Ibid. 10 Ibid. This case was subsequently overruled by the New Zealand Court of Appeal in Smith v. Wellington Woolen Manufacturing Co. Ltd., [1956] N.Z.L.R. 491 (C.A.). The New Zealand Court of Appeal considered that it was bound to follow the House of Lords’ decision in British Transport Commission v. Gourley, supra, footnote 1.
of Fine v. T.T.C. and Bowers v. J. Hollinger & Co. Limited were discussed and approved by the New Zealand Court of Appeal.

I. Difficulties Arising out of the Gourley Case.

1. Conditions precedent to an application of the Gourley principle.

One of the problems which confronts a court is to determine when the Gourley case is applicable. This is, of course, a problem common to all cases. However, the Gourley case does impose problems of a greater magnitude. It has been established that there are two conditions precedent to an application of the Gourley case. First, the award of damages must represent compensation for loss of income which, if it had been received by the plaintiff in the ordinary course, would have been subject to tax. Secondly, the award of damages itself must not be liable to tax. If these two conditions are satisfied, the award of damages is computed on an after tax basis.

The Gourley case deposits the complexities of tax law upon the doorstep of the ordinary practitioner. The assessment of damages comes to depend on questions of tax law which may be quite complex. This difficulty is compounded by the fact that in Canada these questions of income tax law will come before a trial court and a provincial appellate court that have previously not been burdened with income tax matters. The provincial trial court and provincial appellate courts might interpret the Income Tax Act differently than the Tax Appeal Board and Exchequer Court. Since the Supreme Court of Canada is the ultimate court in the hierarchy of both systems of courts, it might reasonably be hoped that any conflicting lines of decision would be eliminated. Nevertheless, conflicting lines of decision could exist for some time adding complications to a complex branch of the law.

It might be argued that the tax considerations arising out of the application of the Gourley principle are not difficult. In the Gourley case itself, there was no doubt about satisfying the first condition precedent. Damages were being awarded for the loss of professional income which if it had been earned would have been subject to tax. However, the matter is not always that easy. For example, the action for damages may be for a breach of contract of sale of land or shares as in Spencer v. Macmillan's Trustees. It would then be necessary to determine the often intricate question of whether or not the plaintiff was a trader in land or securities.

\[11\] Income Tax Act, R.S.C., 1952, c. 148, s. 86, 91, & 98.

If he were not, the gain on the transaction would represent a capital gain. As this would not be subject to tax, the first condition precedent to the application of the Gourley principle would not be fulfilled. As to the second condition precedent, in the Gourley case, counsel agreed that the award of damages itself would not be subject to taxation. Earl Jowitt commented that he thought they had rightly agreed. However, in Jennings v. Cronsberry, MacKay J.A. and Kelly J.A. considered that there was no certainty that an award of damages to compensate for a permanent loss of earnings was not taxable under the Canadian Income Tax Act and held that the award should have been made without deduction of income tax. It cannot be said that the two conditions precedent do not involve difficult tax matters.

2. Revenue not bound.

Another difficulty, arising out of the Gourley principle is that plaintiff might suffer tax twice over since a decision of the court in regard to taxation will not bind the Minister of National Revenue when he has not been a party to the decision. The court in awarding damages might apply the Gourley deduction on the basis that what is being compensated for would have been taxable if received in the ordinary course of events but that the award of damages would not itself be subject to tax. The Minister of National Revenue might successfully contend in other courts that the award of damages is taxable. This has led to suggestions that the Revenue be made a party to such proceedings. The English Law Reform Committee asked the Board of Inland Revenue to consider this suggestion. The Board was opposed to it on the basis that it would be costly to the Revenue and would lead to delays in the assessment of damages. The Board also indicated that it was to the advantage of the plaintiff to contend that the award of damages

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18 Supra, footnote 1, at pp. 197 (A.C.), 799 (All E.R.).
16 The serious and irreparable harm which could be inflicted on the plaintiff is discussed in Spencer v. Macmillan's Trustees, supra, footnote 12, at p. 305. In this case, opinions were reserved as to whether in the absence of the Inland Revenue, proof would be competent of the Revenue practice with regard to taxing damage awards.
In George Court and Sons v. Mair & Co., [1958] N.Z.L.R. 494 (S.C.), the plaintiff was suing for damages which included damages for loss of profit. The plaintiff sought leave to argue a question of law before trial which was whether damages should be awarded on the basis of gross loss of income or of the net loss after deduction of tax. It was held that this question could not be answered in the absence of the Commissioner of Inland Revenue in that the answer to this question depended on whether tax will and can be levied upon the damages awarded.
would itself be subject to taxation and, if the issue had been genuinely contested and the plaintiff were unsuccessful, the Revenue would rarely wish to challenge the result by taxing the award of damages.\textsuperscript{17} If the \textit{Gourley} principle is accepted, the result appears to be that either you have a costly and cumbersome procedure for the assessment of such damages or you must rely on the administrative discretion of the Revenue.

3. \textit{The scope of the Gourley principle.}

It has been said that the \textit{Gourley} case depends on a paradox. This reputed paradox is:

For the purposes of Revenue law the damages received by the plaintiff were regarded as having been awarded in respect of a capital loss. Otherwise they would have been taxable in his hands. For the purpose of assessing the damages, however, what the plaintiff had lost was income, for how otherwise could his liability to income tax be in the least degree relevant.\textsuperscript{18}

Is this in reality a paradox?\textsuperscript{19} For the purpose of the argument, it will first be assumed that in the \textit{Gourley} case what the plaintiff was being compensated for was the loss of a capital asset, his earning capacity.\textsuperscript{20} If this is so, it follows that the award of damages should not itself be assessed to income tax. The next matter is the mode of assessing the damages. In the case of a capital asset, such as earning capacity, its value can only be determined by discounting to the present the income flow which it will produce. The next issue is whether you discount the gross income flow or the income flow after deduction of tax.\textsuperscript{21} This income flow but for the breach of duty on the part of the defendant would have been subject to tax. Thus, if one wishes only to make good the financial loss which the plaintiff has suffered, the capital asset, earning capacity, will be valued by discounting the after tax flow of income which it would have produced. You do not have to

\textsuperscript{17} \textit{Ibid.}

\textsuperscript{18} Jolowicz, \textit{loc. cit.}, footnote 3, p. 91.

\textsuperscript{19} Professor Street does not believe that there is a paradox. See Street, \textit{Principles of the Law of Damages} (1962), pp. 89-90.

\textsuperscript{20} It is submitted that Gourley was being compensated for loss of earnings not for a reduction in his earning capacity. Only the dissenting judge, Lord Keith of Avonholm, states explicitly that what the plaintiff is being compensated for is loss of wage-earning capacity. Lord Goddard does, however, refer to compensation for loss of earning power on one occasion. Nevertheless, Lord Goddard and the other judges in the majority seem to treat the claim as one for loss of earnings.

\textsuperscript{21} Lord Keith of Avonholm in \textit{British Transport Commission v. Gourley}, \textit{supra}, footnote 1, at pp. 217 (A.C.), 811 (All E.R.), said: "The whole issue in this case boils down to the question whether a man is to be compensated for loss of wage-earning capacity on the basis of gross earnings, or net earnings after deduction of tax."
assume that he lost was income. There is no paradox. Income tax becomes relevant when a capital loss can only be determined by capitalizing income which would have been subject to tax.22

As a general rule, damages retain the characteristic of the assets which they replace.23 If it is assumed that Gourley was being compensated for loss of income, it would be reasonable to assume that the damage award would itself be taxable. However, it appears that, by concession of the Revenue, damages for loss of earnings are not taxed. This is so even though the loss of earnings is temporary and therefore is analogous to a revenue receipt. Gale J. said in Posluns v. Toronto Stock Exchange:24 "It is by no means clear, however, that damages for temporary loss of earnings are tax free in Canada, even though in practice taxes on them have apparently not been exacted by the Crown... a strong case may be made for the contention that in Canada damages in lieu of earnings are taxable even though by administrative tolerance, the tax is never levied." This appears to be the case in both Canada and England.25 Thus, there is not necessarily any paradox. If Gourley was being compensated for the loss of a capital asset, earning capacity, tax becomes relevant in valuing that asset without having to assume that when awarding damages you are compensating for loss of income. If, however, Gourley was being

22 This was recognized by the Scottish Law Reform Committee in their Sixth Report (1959), Cmnd. 635, p. 6. The Committee said, "The fact that damages for loss of earnings in certain cases, e.g. where there is permanent incapacity, may properly be regarded as being given for the loss of earning capacity may be a reason why the damages awarded should be treated for income tax purposes as capital and not subjected to tax in the hands of the recipient. The damages must, however, be based on an estimate of the earnings which have been lost and we do not think it necessarily follows the liability to tax which the recipient would have incurred if he had received the lost earnings should be ignored in assessing the damages to compensate him for his loss."


25 In Renfrew Town Council v. I.R.C. (1934), 19 T.C. 13, at p. 19, [1934] S.C. (Ct. of Sess.) 468, at p. 473, it was observed that if a person were permanently disabled the damages for loss of income would appear to be a capital receipt in the hands of the plaintiff but if it were only a temporary disability, the damages would be analogous to a revenue receipt and thus taxable. This statement was obiter dictum. It may reflect what the law is but it does not reflect the practice of the Revenue. In West Suffolk County Council v. W. Rought Ltd., [1957] A.C. 403, at p. 410, counsel contended that: "There was never a case in which the income tax authorities made a claim for tax in respect of damages for tort." This may state the concession too broadly.
compensated for the loss of income, tax becomes relevant in that, by concession, the Revenue do not tax an award of damages for loss of income. In the latter case, it means that the Revenue are not being consistent about treating an award for damage in the same way as the claim it replaces. A minor inconsistency in the field of tax law hardly warrants being branded as paradoxical.

Although I do not believe that there was any paradox in the Gourley case, the argument does indicate limits to the applicability of the Gourley principle. If the plaintiff is suing for loss of a capital asset, tax will only become relevant if the capital asset can be valued with reference solely to income which otherwise would have been taxable. In this category, are actions for damages for breach of a contract of employment. The loss which he suffers is loss of office, which is regarded as a capital asset. It is a capital loss which can only be assessed by determining the present value of a flow of income which would have been subject to tax. This explains the application of the Gourley principle in Beach v. Reed Corrugated Cases, Ltd., Phipps v. Orthodox Unit Trusts Ltd., Walker v. Copp Clark Publishing Co. Ltd., and Widrig v. Strazer. Posluns v. Toronto Stock Exchange was an action for damages for inducing the breach of a contract of employment. Gale J. said: "... the damages are not taxable because they are not granted in lieu of income that would otherwise have been earned but are awarded as compensation for the destruction of a capital right, the right to serve and receive remuneration to the end of a contractual term." This capital loss could only be valued by reference to income which would have been taxed and thus Gale J. would have applied the Gourley deduction. However, he found that there was justification for inducing the breach of contract and therefore no damages were awarded.

The Gourley principle was also applied in Re Houghton Main Colliery Co. Ltd. Mr. Brass and Mr. Francis had a contractual right to a pension and they claimed in voluntary liquidation. The value of the loss of the right to receive a pension could only be assessed on the basis of the flow of income which it would produce and which would be taxable. In West Suffolk County Council v. W. Rought Ltd., it was held that compensation for loss of

30 Supra, footnote 24.
business resulting from a compulsory acquisition of factory premises was subject to the Gourley deduction. It would appear that this was a case where damages were being awarded for loss of profit and, consequently, the Gourley deduction should not be made as the award itself should be taxable. However, a letter from a District Valuer indicated that the Board of Inland Revenue did not regard such compensation as taxable. This opinion was based on *I.R.C. v. Glasgow and South-Western Railway Co.* in which it was held that in the case of compulsory acquisition of land, the sum allowed as compensation for loss of business was part of the sale price. It would seem that the compensation for loss of business resulting from a compulsory acquisition was not a revenue receipt but part of a capital receipt. It was, however, a capital receipt that could only be measured with reference to income which, after deduction of expenses, was subject to tax. The Gourley principle was applicable.

If, on the other hand, the plaintiff is suing for the loss of income, the Gourley principle will not be applicable, unless by law...
or by concession of the Revenue, no tax is levied on the award for damages even though it represents compensation for the loss of income. This heading accounts for those cases where damages have been awarded for loss of income flowing from personal injuries caused by the negligence of the defendant.\textsuperscript{36} \textit{Thomas McGhie & Sons Ltd. v. B.T.C.}\textsuperscript{36} is a case where a mine owner became entitled to compensation for being required to leave minerals unworked. Phillimore J. stated that what is being compensated for is not value of the minerals or for the sterilization of a capital asset but for the loss of leaving the minerals unworked. It appears to be compensation for loss of income and one would have expected that the award itself would be subject to tax. However, it was agreed that the award of damages would not be taxable but why this was admitted by the plaintiff does not appear. The \textit{Gourley} principle has been held applicable in an action for damages for libel. Lord Reid said:\textsuperscript{37} "The injury need not necessarily be confined to loss of income. Its goodwill may be injured. But in so far as the company establishes that the libel has, or has probably, diminished its profits, I think that the \textit{Gourley} case is relevant." The relevance of the \textit{Gourley} case must stem from the fact that even though the damages are awarded for loss of income, the award itself is by concession not taxed. The concession appears to be that damages awarded in a tort action are not taxed.\textsuperscript{38} Where there is a breach of an ordinary commercial contract, and the plaintiff is a trader in the subject matter of the contract, the \textit{Gourley} case is not applicable.\textsuperscript{39} This is because the award of damages will be taxable in his hands.

In discussing the scope of the \textit{Gourley} principle, it is also necessary to consider whether it applies solely to income tax liability or whether other prospective liabilities of the plaintiff should also be taken into account in assessing damages. In \textit{Cooper v. Firth Brown Ltd.},\textsuperscript{40} it was held that the \textit{Gourley} case should be


\textsuperscript{38} \textit{Supra, footnote 25.}

\textsuperscript{39} \textit{Diamond v. Campbell-Jones}, [1961] Ch. 22, [1960] 1 All E.R. 583 (Ch.D.); \textit{Spencer v. Macmillan's Trustees, supra, footnote 12, at p. 316.}

\textsuperscript{40} [1963] 2 All E.R. 31 (Sheffield Ass.).
extended to apply to national insurance contributions. Lawton J. assessed the damage for loss of earnings after deduction of income tax and the employee's national insurance contribution. It is submitted that the case is wrong and that the employee's national insurance contribution should not be deducted even though it is paid under a compulsory government scheme. The benefits under the national insurance scheme depend upon the payment of a requisite number of contributions. If the contribution condition is not met, the benefits are proportionately reduced. As a result of the accident, the plaintiff will avoid making contributions for the period during which he is unable to work but, as a result, the benefits to which he is entitled under the scheme are reduced. It is not legitimate to say that what the plaintiff is entitled to is the loss of the contents of his pay packet. It is necessary to take into account the possible reduction in the benefits to which he is entitled under the national insurance scheme because he is no longer making contributions to it.

It has been suggested that the employee's national health service contributions should also be deducted in calculating an award for loss of earnings. This, unlike national insurance contributions, would be a legitimate deduction to make. The benefits of the health service are not contingent upon contributions. There is no loss of benefit to weigh in the scale against the incidental benefit of not having to pay the national health service contribution. The full benefits of the national health scheme are still available.

Should union dues be deducted in assessing damages for loss of earnings? If the plaintiff were employed in a closed shop, it might be argued that this was a legitimate deduction to make in that he must pay union dues in order to earn that income. However, in a case where you are compensating the plaintiff for a permanent loss of income, deduction of the union dues would ignore the possibility that the plaintiff might otherwise have sought employment where there was no union or where there was not a closed shop.

In Canada, it is submitted that the Gourley principle should not be extended to cover Unemployment Insurance contributions or contributions to the Canada or Quebec Pension Plans. It is only through contributions to these plans that it is possible to obtain any benefit. If a person were negligently injured and re-

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42 Supra, footnote 40 (Editorial note).
43 Unemployment Insurance Act, R.S.C., 1952, c. 273, s. 14; Canada
ceived compensation for loss of earnings, he would be freed from having to make contributions but he would lose the benefits to which his contributions would have entitled him.\textsuperscript{44}

The \textit{Gourley} case was concerned with whether the liability to income tax which the plaintiff would have incurred, if he had received his income in the normal course, should be taken into consideration in assessing damages. No question arose about taking into account the appearance of an asset but rather what significance should be attached to the disappearance of a prospective liability. However, in \textit{Browning v. War Office},\textsuperscript{45} the English Court of Appeal said that \textit{Gourley} settled the proposition that damages are intended to compensate the plaintiff and not to punish the wrongdoer. It was derived from this proposition that, in assessing the damages for tortious conduct, account should be taken of the disability pension to which the plaintiff, a United States Air Force sergeant, became entitled under United States law. The \textit{Gourley} case has thus been expanded into a two pronged weapon by which the defendant can hope to reduce the assessment of damages for which he is liable. The \textit{Gourley} case pushed back the frontier between what was relevant and what was regarded as too remote with regard to a liability. The prospective liability of the plaintiff to income tax became relevant. In \textit{Browning v. War Office}, the frontier between what was relevant and what was regarded as too remote with regard to an asset was rolled back. That the frontier has shifted with regard to the relevance of a collateral benefit is clear. What is less clear is the precise demarcation between a collateral benefit which is relevant and one which is irrelevant in assessing damages. What is even more obscure is the logic of the distinctions which are made.

In \textit{Payne v. Railway Executive},\textsuperscript{46} the English Court of Appeal held that in assessing damages for negligence, a disability pension awarded by the Royal Navy was not to be taken into account. Cohen L. J. said: "It seems to me that the accident in this case was not the \textit{causa causans} of the receipt by the first plaintiff of the disability pension, but the \textit{causa sine qua non}. The \textit{causa causans}

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\item A strong case could be made for the contention that the negligently injured plaintiff should be entitled to not merely his income after deduction of tax, but also to compensation for the fact that his former employer is no longer obliged to make a contribution to the Canada Pension Plan on his behalf.
\item \textsuperscript{45} [1963] 1 Q.B. 750, [1962] 3 All E.R. 1089 (C.A.).
\item \textsuperscript{46} [1952] 1 K.B. 26, [1951] 2 All E.R. 910 (C.A.).
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was his service in the Royal Navy."

The analogy was drawn between the proceeds of an accident insurance policy, taken out by the plaintiff, which in Bradburn v. Great Western Railway Co. was held not to be deductible in assessing damages, and a pension for which the plaintiff has qualified by reason of his service. In Browning v. War Office, Payne v. Railway Executive was not followed.

Lord Denning said that the injured person must give credit for any sums which he receives as of right in consequence of his injury except in so far as it would be unfair to require him to do so. He admitted that it is difficult to say what is or is not unfair. The chief exceptions which he mentions are charitable donations and insurance benefits purchased with his own money. Where a pension is discretionary and particularly where it may be reduced as a result of damages awarded to the plaintiff, it may be reasonable to treat the pension as analogous to a charitable donation which should not be brought into account.

Browning v. War Office established that a pension which one receives as of right should be deducted in assessing damages. Was it unfair to the plaintiff to require it to be brought into account? Donovan L. J., dissenting in Browning v. War Office, indicated that recognition of the truth that damages are intended to compensate the plaintiff and not to punish the defendant does not get one very far. "Is it, for example, punishment if one asks the defendant to make good the loss he had inflicted without taking into account receipts which the labour, or the thrift and foresight of the plaintiff alone has secured?"

In the Browning case, it was a non-contributory pension. Can any meaningful distinction be drawn between contributory and a non-contributory pension that a plaintiff is entitled to as of right? I think not. Why

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47 Ibid., at pp. 36 (K.B.), 912 (All E.R.).
48 (1874), L.R. 10 Ex. 1, 44 L.J. Ex. 9.
49 Diplock L.J. considered that the Payne case was no longer binding on the court because of the Gourley case. Lord Denning escaped from the Payne case by another route. He indicated that there were two grounds to the decision in the Payne case. Using his interesting approach to precedent, he rejected the ground advanced by Cohen L.J. Lord Denning preferred that of Singleton L.J. who had arrived at the conclusion that the pension should not be taken into account in that the Minister of Pensions had the right to withhold or reduce the pension. Sargent Browning, on the other hand, had an absolute right to his pension.
50 Supra, footnote 45, at pp. 759 (Q.B.), 1091 (All E.R.).
52 Supra, footnote 45, at pp. 763 (Q.B.), 1093 (All E.R.).
should a distinction be made between a pension which comes into existence because of past services and one which results from past contributions? It must be recognized that the type of pension is going to have a direct effect on wages. An employee who receives a pension as of right without having made any direct contribution will have paid for this right indirectly in that he will have received a lower remuneration than if he had been required to contribute to the pension. It is submitted that it is unfair to the plaintiff to require a pension which he receives as of right to be brought into account whether it is a contributory or a non-contributory plan. The person who has pension rights will have received, other things being equal, a lower net wage than the person with no pension rights.

In Canada, Browning v. War Office has been agreed with in Smith v. C.P.R. Bence C. J. Q. B. of Saskatchewan held that in assessing damages that part of the value of a pension that is received by the plaintiff as of right and which is attributable to the employer's contribution should be deducted. However, that portion of the pension which is attributable to the plaintiff's contribution, even though these payments are compulsory, should not be taken into account in assessing the damages. The view taken by Maybank J. in Workmen's Compensation Board v. Spence which was decided after the Browning case, but before that case could have come to his attention, appears preferable and more realistic. He stated:

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53 A different point of view is expressed by Ganz, Mitigation of Damages by Benefits Received (1962), 25 Mod. L. Rev. 559.

54 Supra, footnote 35. It has also been applied by Bissett J. in Parsons v. Saunders and Snair (1963), 39 D.L.R. (2d) 190 (N.S.S.C.), where it was held that salary paid under a contractual obligation during the period of disability cannot be recovered. The same conclusion was reached in Woodworth v. Farmer (1963), 39 D.L.R. (2d) 179 (N.S.S.C.). However, in Wyne v. Smith Bros. (1963), 43 W.W.R. 254 (B.C.S.C.), it was held by McInnes J., at p. 256 that: "The defendant is not entitled to credit against the amount he is required to pay for loss of wages of any amount received by the plaintiff from another source whether such payment was ex gratia or otherwise." Whereas in Dell v. Vermette, [1963] 1 O.R. 333, (1963), 37 D.L.R. (2d) 101 (H.C.), Ferguson J. held that even in the case of a voluntary payment of wages by his employer an injured plaintiff may not recover for loss of wages. The Court of Appeal dismissed an appeal on this point without reasons [1964] 1 O.R. 372.

55 In Judd v. Board of Governors of the Hammersmith, West London and St. Marks Hospitals, supra, footnote 53, no attempt was made to apportion that part of the pension referable to the employer's contribution and to deduct that in assessing damages. It was held that no part of the contribution could be deducted. This case was decided prior to the Browning case but it has not as yet been expressly overruled.

In my view of employer-employee relations the employee had paid for the right to receive these eight weeks of pay, just as truly as if he had paid such a premium on such an insurance contract or scheme. The wages and working conditions of policemen in Winnipeg result from collective bargaining; but this is only a statement of incidental intelligence. I start, in reasoning, with what I believe to be truth, namely, that no employer ever pays any more in wages, nor grants any more in working conditions than he has to pay or grant. There must always be *quid pro quo*.

It is submitted that no valid distinction can be drawn between an employee who pays for his pension rights or for his right to receive wages for a certain period after being disabled through service to his employer and an employee who contributes part of his wage to a fund set up for that purpose or purchases insurance to provide such benefits in case of disability. If this is so, it is unfair to the plaintiff to permit the defendant to take advantage of the rights which the plaintiff has himself secured.

4. **Foreign tax law becomes relevant.**

The *Gourley* principle not only results in a court having to delve into the intricacies of its own tax law in order to assess damages, but foreign tax law may also become relevant. In *The Telemachus*, unspecified European taxation was taken into account to increase the salvage award. Willmer J. stated that he was applying the *Gourley* principle. He started with the proposition that the purpose of awarding salvage was to encourage mariners to perform such services. This incentive would be reduced if the award were subject to income tax and if no allowance were made for this fact. He consequently increased the award. This case represents a very doubtful application of the *Gourley* principle. The principal has in every other case resulted in a reduction in the award and not an increase. The two conditions precedent to an application of the *Gourley* principle were not satisfied. In another English case, Canadian income tax law would have become relevant if *The Telemachus* had been followed. In a later English case, *Winkworth v. Hubbard*, a Canadian stockbroker, who was injured as a member of a water skiing party in Monaco, brought an action against the owner and driver of the boat. Streathfield J. awarded damages for loss of salary and made the *Gourley* deduction on the basis of Canadian income tax to which

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the plaintiff would have become subject if he had not been injured. In *Julien Praet et Cie., S/A v. H. G. Poland Ltd.*,61 Belgium insurance agents were held liable to a Lloyd's syndicate for a breach of contract. As a result of the *Gourley* principle, Belgium tax law had to be considered. Mocatta J. found that the award itself would be subject to Belgian tax and for that reason the *Gourley* principle was not relevant. In *Smith v. C.P.R.*,62 an Ohio school teacher was negligently injured. Bence C. J. Q. B. of Saskatchewan awarded damages for loss of income after making the *Gourley* deduction on the basis of the United States taxes which would have been paid.

5. **Burden of proof.**

Also arising out of the *Gourley* case is the problem about where the onus of proof rests. Three separate questions must be clearly distinguished. First, who bears the onus of proving that what is being compensated for would or would not have been taxable if it had been received in the ordinary course of events. Second, who bears the onus of proving that the award for damages will or will not itself be subject to tax. Third, assuming that the *Gourley* principle is applicable, who bears the onus of proving the quantum of taxation (that is who must adduce the evidence about the plaintiff's tax situation in order that the *Gourley* deduction may be computed). It has been suggested that the defendant should bear the burden of proving that what is being compensated for would have been taxable in the hands of the plaintiff and also the quantum of taxation. Whereas the plaintiff, if he is to avoid the *Gourley* deduction, must prove that the award of damages would itself be taxable.63 This suggestion involves splitting the burden of proof in regard to the two conditions precedent to an application of the *Gourley* principle. The defendant has the burden of proving the first condition precedent. The plaintiff has the burden of proving the second condition precedent. It is submitted that this is not satisfactory. It is my opinion that the burden of proving both conditions precedent to an application of the *Gourley* principle should rest with the defendant.

If there is doubt about whether the award of damages will itself be subject to tax, it would seem that the doubt should be resolved in favour of the injured party or otherwise that party may suffer a deduction of tax twice over. On the other hand, it

62 Supra, footnote 35.
63 Stevenson and Orr, *loc. cit.*, footnote 3.
could be contended that the defendant might in such a situation be prejudicially affected. If the award is not in fact subject to taxation, he will be compelled to pay more in damages than the plaintiff has lost after taxation has been taken into account. This is just what the Gourley principle was intended to eliminate. Nevertheless, it should be remembered that the defendant is the person who is in breach of a duty. If he wishes to avail himself of the Gourley deduction and thereby reduce the damages which he must pay, it should be incumbent upon him to prove both conditions precedent to the application of the Gourley principle.

It is also my opinion that the burden of proving the quantum of taxation should not rest with the defendant but with the plaintiff. The facts relevant to determining the amount of tax which the plaintiff would have paid, if what is being compensated for had been received in the ordinary course, are within the plaintiff’s knowledge. The plaintiff is better able to adduce evidence about his tax position. The best evidence of his tax position would be recorded on the tax returns filed by the plaintiff. It is the practice of the Department of National Revenue to produce copies of the income tax returns of a taxpayer upon his request where there is good reason. However, it appears that the defendant could not compel the Department to produce a copy of the plaintiff’s tax return in view of Weber v. Pawlik, M.N.R. v. Die-Plast Co., Clemens v. Crown Trust Company, and Miles v. Miles where the Minister’s objection to producing such returns on the ground that it was contrary to the public interest was upheld. Nevertheless, the conclusiveness of a ministerial objection as set out in Duncan v. Cammell Laird & Co. Ltd is receiving judicial reconsideration. Lord Denning, M.R. in Re Grosvenor Hotel, London (No. 2) states that observations made by Viscount Simon in Cammell Laird “have been shown to rest on an insecure foundation”. At the present time, the defendant probably will be

unable to compel the production of the tax returns of the plaintiff. He is thus barred from adducing the best evidence. This is one factor which indicates that the onus should rest on the plaintiff. However, if the onus does rest on the defendant, he could obtain information as to the plaintiff’s tax situation at the examination for discovery and adduce evidence on cross-examination at trial. If the plaintiff has retained a copy of his income tax return, the defendant will be able to obtain it on production of documents.

The basic reason for stating that the plaintiff should bear the burden of proving the quantum of taxation is that, once it has been established that the Gourley principle is applicable, the damages are to be assessed on after tax basis. It is fundamental that it is the plaintiff who must prove his damages. If the Gourley conditions have both been established, the plaintiff can only prove his after tax loss by adducing evidence about his tax position.

The question of the burden of proof did not arise in the Gourley case. There was no doubt that Gourley’s professional income would have been taxable if it had been received. It was agreed by counsel that the award of damages would not itself be taxable. The figures representing the before and after tax loss were also agreed upon. There is little authority about where the burden of proof rests. In Spencer v. MacMillan’s Trustees, the dispute was with reference primarily to the first condition precedent to the application of the Gourley principle. It was an action for breach of contract for the sale of shares. The party alleged to have committed the breach of contract maintained that the persons suing was a dealer in securities and that a deduction of tax should be made in awarding damages. Lord Mackintosh stated:

I do not think that the averments which the defenders have made . . . are sufficient to make a relevant case for the application of the Gourley principle to such damages as may be awarded in this case. In order to lay a sufficient foundation for the application of that principle the averments must, in my opinion, be such that if proved they will establish both (a) that the damages were being awarded as reparation or compensation for the loss of something which would, like earnings or profits, undoubtedly have been subject to income tax if they had been received, and (b) that the damages actually awarded would not attract income tax or surtax in the hands of the recipient.

This case indicates that the burden of proving both conditions precedent to an application of the Gourley principle rests with

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71 Supra, footnote 1, at pp. 197 (A.C.), 799 (All E.R.).
72 Ibid., at pp. 204 (A.C.), 803 (All E.R.).
73 Supra, footnote 12.
74 Ibid., at p. 322.
the defendant. In *Jennings v. Cronberry*, the Ontario Court of Appeal dealt with the second condition precedent and concluded that a proper foundation was not laid for making the *Gourley* deduction. Kelly J. A. stated that: "A defendant who seeks reduction in damages otherwise payable to him on the basis that, despite the fact that the award is in part in lieu of future earnings, that part in the hands of the plaintiff will not attract income tax, must first satisfy the court that the Minister of National Revenue will not be able to impose such a tax..." MacKay J. A. stated: "While there are strong arguments on principle that if no income tax is payable in respect of such damages that the amount should be reduced by the estimated tax that would have otherwise been payable in respect of such wages or salary, there is, in my view, no certainty that such an award may not be taxable under the Canadian Income Tax Act." As there was some doubt about whether the second condition precedent was satisfied, MacKay J. A. held that the *Gourley* deduction should not be made. This clearly indicates that the burden of proving the second condition rests upon the defendant. McGillivary J. A. dissented but not with reference to the burden of proof. He found that the award was capital in nature and non-taxable and that accordingly the *Gourley* deduction was appropriate.

To the same effect is the decision in *Morahan v. Archer and Belfast Corporation*. Curran L. J. said: "In my opinion, in order to bring themselves within the case [*Gourley*], the defendants have to show that the plaintiff would not be liable for tax on the damages actually recovered." Gregory J. in *Buck v. Rostill* made it clear that the burden of proving the existence of the second condition precedent to an application of the *Gourley* principle rests with the defendant. He stated: "In any event, there was no evidence or argument to indicate that the plaintiff might not be assessed income tax on that part of the damages awarded to her to compensate her for loss of income, and I assess her general damages at $4,000 with no deduction for income tax." It thus appears that the burden of proof with respect to both conditions precedent lies with the defendant.

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75 *Supra*, footnote 14.
78 *Supra*, footnote 38, at p. 62.
80 Stevenson and Orr, *loc. cit.*, footnote 3, at p. 15, state that the Official Referee in *Hall & Co. Ltd. v. Pearlberg*, [1956] 1 All E.R. 297, [1956] 1 W.L.R. 244 (Q.B.D.), concluded that proof that the necessary condi-
As to the burden of proving the quantum of taxation, the English position appears to be clear. The burden rests upon the plaintiff. In *West Suffolk County Council v. W. Rought Ltd.*, Lord Morton of Henryton said: 81

"It is for the respondents to prove the loss which they have suffered. Their trading year ends on August 31. They have proved to the satisfaction of the tribunal that they have lost £11,600 profits which they would have made during the trading year ending August 31, 1953, but it is still incumbent upon them to prove their loss after taking into account the incidence of taxation. This they could do by submitting to the tribunal (a) a statement of the tax liability which they actually incurred in respect of their trading during the year in question and (b) an estimate of the tax liability which they would have incurred in respect of their trading during the same year if they had made this profit of £11,600.

To the same effect is the decision in *Stewart v. Glentaggart Limited*. Lord Hunter stated that: 82 "The conclusion which I have reached in principle involves, as a necessary consequence, that the pursuer's averments on damages are not relevant as they stand, since they take no account of the pursuer's tax position. . . . The onus of proving his actual loss in such a case, as indeed in all cases where damages are claimed, lies upon the pursuer. . . ."

The only Canadian decision to consider the burden of adducing evidence about the quantum of taxation is *Jennings v. Cronsberry*. In this case, the Ontario Court of Appeal took the position that the burden rests with the defendant. There was neither discussion nor the citation of any authority for this position. 83 Kelly J. A. stated that: 84 "A defendant who seeks reduction in damages otherwise payable by him. . . must adduce evidence as to the probable taxable income of the plaintiff and other necessary facts which will enable the court with some degree of accuracy to

81 Supra, footnote 32, at pp. 413-414 (A.C.), 221 (All E.R.).
83 The court may have been influenced by what Brendan O’Brien, O.C., said in the Law Society of Upper Canada, Special Lectures (1958), Damages for Personal Injuries, upon being referred to it. He stated, p. 47 that: "It will be appreciated that in cases of this kind it is, of course, incumbent upon the defendant to bring before the court the necessary evidence to permit of a calculation of what the tax would have been. If such evidence cannot be adduced, then obviously there can be no deduction representing the tax." This statement fails to take into consideration the fact that once the conditions precedent to an application of the Gourley principle have been established by the defendant, the only loss which the plaintiff may recover is his after tax loss. To prove his after tax loss, the plaintiff must adduce evidence about the quantum of taxation.
84 Supra, footnote 14, at pp. 319 (O.R.), 419 (D.L.R.).
equate that part of the award representing loss of earnings to the net amount which would have remained in the plaintiff’s hands had the plaintiff continued to receive his usual earnings and had income tax been assessed against him in respect of these earnings.” MacKay J. A. seemed to take the same view when he said:85 “There is no evidence as to the plaintiff’s investment income, if any, so that in this case no proper foundation was laid for making such a deduction.” It might be contended that these statements are obiter dicta in having found that the conditions precedent to an application of the Gourley principle had not been satisfied, it was unnecessary to decide who had the burden of adducing evidence about the plaintiff’s tax position. It is submitted that the English approach as enunciated by the House of Lords in West Suffolk County Council v. W. Rought Ltd.86 is preferable to that of the Ontario Court of Appeal.

6. Quantum of taxation.

In order to determine the Gourley deduction, it is necessary to determine the personal tax exemptions to which the plaintiff is entitled. It is a simple matter to determine the personal exemptions to which he is presently entitled. In applying the Gourley principle to determine the award for loss of earnings in case of a permanent incapacity, it is necessary to know what his future exemptions will be. This did not create any difficulty in the Gourley case as Gourley was sixty-five years of age.87 If he had been twenty-five years of age and a bachelor, it would have been more difficult to determine whether and when he should have been given credit for a marriage exemption and the number of dependent children exemptions in calculating the tax which he would otherwise have paid on future earnings.

Another practical difficulty involved in applying the Gourley principle is the uncertainty involved in estimating the future rates of taxation. In cases where the principle is applicable, it is necessary to estimate the amount of tax which the plaintiff would have paid but for the defendant’s breach of duty and to deduct this from the gross income he would have received. If a man is permanently injured at any early age, in awarding damages for loss of earnings it is necessary to estimate the level of income tax for thirty or forty years. Lord Goddard in the Gourley case, when he was setting out

85 Ibid., at pp. 296-297 (O.R.), 396-397 (D.L.R.).
86 Supra, footnote 81.
87 Supra, footnote 1, at pp. 210 (A.C.), 807 (All E.R.).
how a jury should be directed, said: 88 "No one can foresee whether
tax will go up or down, and I advise you not to speculate on the
subject but to deal with it as matters are at the present." In the
Gourley case, this may have been a reasonable assumption to
make as Gourley was sixty-five years of age when he was injured. 89
The tax structure is not likely to change very much during the re-
mainder of his working life. If Gourley had been twenty-five,
would it have been reasonable?

There can be little doubt that government spending will con-
tinue to grow at a rate at least equal to the rate of growth of gross
national product. This means that total tax revenue of the govern-
ment must at least remain at the same percentage of gross national
product. This does not mean that the income tax will remain at
the same level. It is quite possible for income taxation to be re-
duced while such taxes as sales and excise are increased so that
government revenue continues to represent the same percentage
of gross national product.

To take the extreme case, let us suppose that individual income
taxes are reduced to zero and sales and excise taxes increased in
order to maintain government receipts. What effect does this have
upon the plaintiff who has been awarded damages where the
Gourley principle was applied before income taxes were reduced?
He will suffer the effect of taxation twice over. Income tax will
have been deducted from his award on a prospective basis and
yet what he buys will be subject to higher sales and excise taxes.
The person in a comparable job who has not been injured will be
better off financially than the person who has been awarded
damages for loss of earnings under the Gourley principle. He will
have a greater take home pay because of the reduction of income
tax which will compensate for higher sales and excise taxes. It
should, of course, be noted that if the level of income taxes were
raised and sales and excise taxes lowered, the injured plaintiff will
be relatively better off than a person in a comparable job who
continues working.

The level of income tax is no longer constant across Canada.
Manitoba and Saskatchewan for instance, levy a provincial income
tax which is twenty-six per cent and twenty-seven per cent re-

88 Ibid., at pp. 209 (A.C.), 806 (All E.R.).
89 However, Street, op. cit., footnote 19, p. 102, notes that the down-
ward changes in the rate of income tax and the additional earned income
reliefs which were introduced shortly after the case was decided would
have resulted in Gourley receiving several thousand pounds more by way
of damages.
respectively of the basic federal income tax in the taxation year 1965 as compared with provinces other than Quebec which levy tax at twenty-one per cent. If a person resident in Manitoba is incapacitated through negligent conduct, the Gourley deduction made on the basis of income tax applicable to residents of Manitoba, tacitly assumes that he will continue to reside in Manitoba. Such an assumption may be prejudicial to the plaintiff. If he moves from Manitoba which levies no sales tax and a higher provincial income tax to British Columbia which levies a five per cent sales tax and a lower provincial income tax, he will be detrimentally affected. He will have in effect prepaid the higher Manitoba provincial income tax. He will no longer benefit from the absence of sales tax in Manitoba but will be paying the five per cent sales tax of British Columbia. If he has been permanently incapacitated, he may have little or no income which would benefit from the lower rate of provincial income tax in British Columbia.

A plaintiff who has been compensated for loss of earnings subject to the Gourley principle would find it far more difficult to move to a jurisdiction such as Bermuda or Nassau where instead of levying income tax the government relies on tariff or sales and excise taxes for its revenue. Unless the plaintiff is independently wealthy, the Gourley deduction may compel him to continue to live in the same jurisdiction or at least one in which income tax yields about the same percentage of total government revenue as that jurisdiction.

Even if you assume that tax rates will remain constant and that the plaintiff will remain resident in the same jurisdiction, there are many difficulties in determining the Gourley deduction. For example, the plaintiff may be engaged in business and have a

90 An Act to Amend the Income Tax Act, S.C., 1960-61, c. 49, s. 13(1) provided for a tax abatement of 16, 17, 18, 19 and 20 per cent of the basic federal tax for the taxation years 1962, 1963, 1964, 1965, and 1966 respectively. This was amended by S.C., 1964-65, c. 54, s. 19(1) and increased to 21 and 24 percent for the taxation years 1965 and 1966 respectively. All provinces except Quebec, Manitoba and Saskatchewan levy provincial income taxes equal to the federal tax abatement. Manitoba levied a provincial income tax at a rate of 22, 23 and 24 percent for the taxation years 1962 to 1964 respectively of the basic federal tax under The Income Tax Act (Manitoba) 1962, S.M., 1961 (2nd Sess.), c. 1, s. 6(2). For the years 1965 and 1966, it is 26 and 29 per cent respectively (S.M., 1964 (2nd Sess.), c. 10, s. 51). Saskatchewan under the Income Tax Act, 1961, S.S., 1961 (2nd Sess.), c. 2, s. 3(3), levied an income tax of 22, 23, and 24 per cent for the taxation years 1962 to 1964 respectively and for 1965 and 1966, 27 and 30 per cent of the basic federal tax (S.S., 1965, c. 22, s. 2). Quebec levies and collects its own income tax under the Provincial Income Tax Act, S.Q., 1953-54, c. 17, as am.

91 Social Services Tax Act, R.S.B.C., 1960, c. 361, s. 3(1).
If the award of damages is itself non-taxable but what is being compensated for would have been subject to tax, do you take into account the plaintiff's loss-carry-forward? If the loss of income before tax flowing from the breach of duty was equal to the loss-carry-forward and it would have been the first income to be received, no tax would have been payable in that it would have been used to wipe out the loss-carry-forward. If for this reason no Gourley deduction is made in assessing damages, the plaintiff is placed in an advantageous position. He will have received the award of damages without deductions of tax and yet he will still have a loss-carry-forward which can be used to off-set subsequent income. However, it is submitted that it would be unfair to the plaintiff not to take some account of his loss-carry-forward. The extent of the account to be taken poses a difficult problem.

7. A defect in the application of the Gourley principle.

There is a very serious defect in the way in which the Gourley principle has been applied. No consideration has been given to the fact that if the award is used to purchase an annuity, the income content of each payment is taxable. Professor Street says that: "The principle which the law recognizes is that the damages awarded under the head of loss of earnings should be sufficient to provide by way of capital and interest combined for the earnings lost; as if the defendant were buying the plaintiff an annuity for the calculated period for which the income has been lost."

In order to arrive at a capital sum, the loss of income after deduction of tax is discounted to the present at a rate equal to the rate of interest that can be obtained on a safe security. This gives you the present value of the income stream of which the plaintiff has been deprived on an after tax basis. With this capital sum, an annuity could be purchased which would produce the exact income flow which the plaintiff has lost. The problem is that the income content of each payment would be taxable, although the capital content would be tax free. The technique results in equating two flows, one of which is partially taxable while the other has been calculated on an after tax basis. This is not a legitimate equation. Allowance must be made for the tax

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92 Canadian Tax Foundation, op. cit., footnote 64, p. 368.
93 Street, op. cit., footnote 19, p. 115. This principle has been approved by the Supreme Court of Canada in C.P.R. v. Jackson (1916), 52 S.C.R. 281, at pp. 286-287, (1916), 27 D.L.R. 86, at p. 90.
94 Income Tax Act, supra, footnote 11, s. 6(1)(a) and s. 11(1)(k).
which will be payable on the income content of the annuity. What should be equated is the capital content of the annuity plus the income content of the annuity on an after tax basis with the loss of income on an after tax basis.

The cost of such an annuity will be considerably greater than the present value of the lost income calculated on an after tax basis. The difference will become greater as the income content of the annuity increases because the amount of tax which will be payable increases. The income content of an annuity increases in accordance with the number of years for which the loss of income is being compensated. In the Gourley case, Mr. Gourley was sixty-five years of age at the time of the accident and therefore he was being compensated for the loss of earnings for only a very few years. In such a case, the income content of the annuity would be very small and thus the fact that the liability to income tax was ignored on the income content of the annuity did not cause a great loss. However, because of Mr. Gourley’s very high tax rate, the loss would be substantial in spite of the small income content of the annuity. If a person is permanently incapacitated and is being compensated for the loss of income for a thirty or forty year period, harm will be done to the plaintiff by ignoring the income tax that he will have to pay on the income content of such an annuity.95

8. Encouragement to breach of contracts of employment.

An unfortunate aspect of the Gourley principle is that it offers some encouragement to employers to breach contracts of employment where they have become dissatisfied with the bargain they have made. The Gourley principle has made it less costly to break a contract of employment than to perform it. If the employer breaks the contract, he pays only the gross wage less income tax. If he performs the contract, he will have to pay the gross wage. The benefit of the tax is diverted to the person who has deliber-

95 It does not matter whether in fact the plaintiff purchases an annuity. What is important is that when compensation is awarded for the loss of a stream of income, the plaintiff is not awarded the arithmetic sum of the stream but the discounted value of the stream. This is due to the fact that money is capable of earning interest and thus a sum of money today is worth more than the same sum in the future. However, when money earns interest, liability to income tax arises. For this reason the rate of interest used to discount the flow of income should be sufficiently below the current market rate of interest on a safe security in order that the plaintiff’s liability to income tax on the interest may be met. If, for instance, the current market rate of interest were 5 per cent and if the plaintiff’s effective rate of tax on the interest earned on the damage award would be 50 per cent, the rate of discount should be only 2 1/2 per cent.
ately broken his contract. It was basically for this reason that Sellers L. J. in his dissenting judgment in Parsons v. B.N.M. Laboratories Ltd. attempted to restrict the Gourley principle to the assessment of damages in tort and to exclude it in matters of contract.

This matter was considered by Lord Reid in the Gourley case. He said: "The real answer is, I think, that before the wrong the employer was paying for the plaintiff’s services, whereas now he is paying the plaintiff’s loss and he will have to pay someone else to perform the services." Nevertheless, in many cases employees are dismissed when the particular industry contracts or there is a general economic recession and no one is hired in their stead. In such a case, it is the Revenue that loses which means in effect the general body of taxpayers. It is they who are subsidizing and thereby encouraging employers to breach contracts of employment.


In the Gourley case and in all cases prior to Parsons v. B.N.M. Laboratories Ltd., no problem arose as a result of differential taxation. The award of damages either was or was not taxable. If it was taxable, it was taxed in the same way as other income and consequently no Gourley deduction was made. As a result of the United Kingdom Finance Act 1960, sections 37 and 38, sums paid in connection with the termination of the holding of an office or employment or a payment in commutation of pension rights were made subject to tax but tax was levied only where the payment exceeded £5,000. Parsons v. B.N.M. Laboratories Ltd. was an action for wrongful dismissal in which the loss of salary and commissions amounted to £1,200. The problem which this case presented was whether the Gourley principle was applicable in that the damages were subject to tax but in fact no tax would be levied as the sum was less than £5,000. Master Jacob held that the loss of income should be awarded without deduction of income tax in that Parliament had expressly imposed some measure of taxation on such damages even though the damages in this instance escaped actual taxation because of the relief given. The Court of Appeal reversed this decision, with Sellers L. J. dissenting, and

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98 Supra, footnote 1, at pp. 213-214 (A.C.), 809 (All E.R.).
99 For an excellent discussion of problems arising from differential taxation and for the various possible solutions see Wheatcroft, op. cit., footnote 23, pp. 1487-1489 and 1st Supplement (1964), pp. 32-34.
100 Supra, footnote 97.
held that when the damages were not sufficiently large to attract tax, the Gourley deduction should be made.

A more fascinating problem arose in *Stewart v. Glentaggart Limited* where through a breach of contract of employment, a managing director suffered loss of salary and a share of profits amounting to more than £12,000 before deduction of tax. If there had been no breach of the contract of employment, the full amount would have been subject to tax. However, the damage award for the breach would only be taxed to the extent that it exceeded £5,000 and on a different basis called topslicing. Lord Hunter held that the loss should be calculated by applying the ordinary Gourley deduction and an amount should be awarded which would, after deduction of the tax provided by the Act of 1960, equal the loss calculated after making the Gourley deduction.

This method is a logical extension of the Gourley principle and would exactly compensate the plaintiff for his loss of earnings on an after tax basis. It does, however, mean that the second condition precedent to an application of the Gourley principle is violated. However, this condition precedent, that the award itself should not be taxed, was derived from the Gourley case when no consideration was given to the possibility that an award for damages might be taxed in a different way from what it replaced. If the award of damages is taxed in a different way, the second condition precedent should not be applicable. It is then necessary to make the two tax calculations indicated by Lord Hunter in order that the plaintiff may be exactly compensated on an after tax basis. Such a technique would in the odd case, where the tax, provided by the Act of 1960, was higher than that which would have been paid on the earnings, result in an award of damages greater than the gross loss of earnings before tax. Lord Hunter said:

> I see nothing anomalous, however, in such a result once it is assumed that the tax position of the injured party is not a factor too remote for consideration when reaching an estimate of his actual loss. If an employer by breach of contract of employment, not only deprives the injured party of earnings, but in addition subjects him to a higher tax liability than would have been incurred if the contract of employment had not been broken, I see no reason why the fact that the injured party now has to pay more tax than he would have done should be a factor too remote to be taken into consideration.

However, in *Parsons v. B.N.M. Laboratories Ltd.*, Harman L. J. considered that Lord Hunter’s decision was a counsel of perfection

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101 *Supra*, footnote 82.

and impractical. He would in a case where the damages were taxable have assessed them gross. Pearson L. J. also disapproved of the method adopted by Lord Hunter. Most of the arguments which he utilizes might with more effect be directed against the Gourley principle itself. The disapproval in the Court of Appeal of Lord Hunter's method was, however, obiter dicta. The damages in that case were not sufficiently large to attract taxation under the 1960 Act. If you accept the Gourley principle, it is logically indefensible to fail to adopt the approach of Lord Hunter. In addition, arguments about the impracticality of the second tax calculation are no more compelling than those rejected by the House of Lords in the Gourley case. It is submitted that Lord Hunter's approach is right in theory. It is no more impractical than the Gourley principle itself and should be followed if the Gourley principle is accepted. In Canada, this problem has not yet arisen in that damages have been held either taxable as ordinary income or non-taxable.

10. Tax planning.

In these days of high tax rates, much effort is being devoted to arranging one's affairs in ways so as to minimize tax. The Gourley case has a direct effect upon tax planning. It is very difficult to determine the significance which should be accorded to future tax planning which the plaintiff may undertake. However, to estimate future taxation solely on the basis of his present tax position may be very unfair to the plaintiff. Lord Goddard in the Gourley case briefly considered what effect should be given to outside income. He stated: "If it is a life annuity under a will or a settlement it may well be expected to continue. If it is disposable investments which might be sold at any time or transferred to a child, less, perhaps little, regard should be had to it."

In the Gourley case, damages were assessed on an after tax basis solely on a consideration of the tax applicable to his earned income. Either Gourley had no investment income or his in-

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103 Supra, footnote 97, at pp. 129-130 (Q.B.), 675 (All E.R.).
105 It might, however, arise with respect to s. 36 of the Income Tax Act, supra, footnote 11. See Canadian Tax Foundation, op cit., footnote 64, p. 368.
106 Supra, footnote 1, pp. 209 (A.C.), 806 (All E.R.). In Re Houghton Main Colliery Co. Ltd., supra, footnote 31, at pp. 303 (All E.R.), 1223 (W.L.R.), Wynn Parry J. stated that full effect must be given to this statement.
107 Beach v. Reed Corrugated Cases, Ltd., supra, footnote 26, at pp. 657 (All E.R.), 813 (W.L.R.).
vestment income was ignored in computing tax deductions to be made from his earnings. Even if the investment income were ignored, the Gourley case would be very weak authority for this approach in that the figures were agreed to by both parties in the appellate courts. The only issue facing the House of Lords was whether the incidence of taxation should be taken into account in assessing damages for loss of earnings. Earl Jowitt said:108 "We were, therefore, in no way concerned to consider the precise method which the trial judge employed in arriving at these figures."

In Beach v. Reed Corrugated Cases, Ltd.,109 which was an action for damages for breach of a contract of service, Pilcher J. virtually ignored the effect of investment income of £20,000 per year on the plaintiff's tax, relying upon the obiter dictum of Lord Goddard quoted above. He stated:110 "It is common knowledge that, with the present high incidence of taxation of income, those who are fortunate enough to enjoy a large income which is primarily unearned can legitimately and do, in fact, reduce their taxable income substantially by covenanting, sometimes for life, and sometimes for a period in excess of six years, large yearly sums to relatives and sometimes to old friends. They are thus legitimately generous at the expense of the Exchequer. Similarly it is common knowledge that men of the plaintiff's age with large disposable investments are more prone, owing to high death duties, to transfer during their life capital sums to their children or dependants which, in the past would have been disposed of by will.

The plaintiff had adduced evidence that he had entered into deeds of convenant for periods of more than six years in order to reduce the incidence of tax. He also convinced the judge that he intended to dispose of a substantial amount of his capital in favour of his family. This case indicated a very receptive attitude towards tax planning. Pilcher J. was unwilling to freeze the tax position of the plaintiff at the date at which the breach occurred and to apply the Gourley deduction solely in accordance with that position. He stated:111 "... there is nothing to prevent the plaintiff, after making the proposed capital gift, from setting aside sufficient income-producing investments to pay the sums due under the covenants from time to time and from investing the remainder of his capital in some non-income bearing investment which possesses the prospects of capital appreciation, provided he keeps in the bank a sum of ready money sufficient to provide for his immediate

108 Supra, footnote 1, at pp. 204 (A.C.), 803 (All E.R.).
109 Supra, footnote 26.
110 Ibid., at pp. 658 (All E.R.), 814 (W.L.R.).
111 Ibid., at pp. 658-659 (All E.R.), 815-816 (W.L.R.).
requirements or, alternatively, to buy himself a substantial annuity." Accordingly, in calculating the Gourley deduction, little attention was paid to his investment income and the appropriate rate of tax was determined by looking almost exclusively to the income which he would have received as managing director but for the breach of this contract of employment by the company.

Undoubtedly, the onus of proving what tax planning measures the plaintiff will take rests with the plaintiff. A record of having ordered his affairs in order to minimize tax was considered to be significant in *Beach v. Reed Corrugated Cases, Ltd.* The case indicates that the onus resting upon the plaintiff is not great. A significant question is whether Canadian judges will be as receptive to tax planning. The very significant difference between the Canadian and British tax structure, militates against such a receptive attitude on the part of the Canadian judiciary.

Two factors which make tax planning in Britain much easier than in Canada are first, the existence of the seven year deed of covenant; and second, the absence of any gift tax in the United Kingdom. In Canada, there is nothing remotely comparable to the seven year deed of covenant. Annual payments, voluntarily and irrevocably agreed to made to a person who is not an infant child of the covenator or the spouse of the covenator for a period which must be capable of exceeding six years, cease to be the income of the covenator and become that of the covenatee for standard rate income tax. Until the United Kingdom budget of 1965, this applied to surtax as well, so long as the covenantee was an individual and was not an employee or solicitor of the covenator. As a result of the 1965 budget, the tax minimizing potential of the seven year covenant has been drastically reduced and its popularity is likely to diminish accordingly. The lack of a gift tax in the United Kingdom coupled with the high rates of estate tax means that wealthy persons have a strong incentive to transmit much of their wealth to the next generation at least five years before their death.

In Canada, the estate tax and where applicable, provincial succession duties are substantial but not nearly as high as the United Kingdom level. The incentive to dispose of one's wealth
before death is therefore not as great and it is greatly diminished by a gift tax, except for gifts within the gift tax exemption. For wealthy persons, the gift tax rates on inter vivos gifts are considerably lower than comparable testamentary gifts. Nevertheless, the gift tax is undoubtedly a deterrent to inter vivos transfer of wealth as its incidence is certain and immediate while the incidence of the estate tax is prospective. For these reasons, it would appear that a Canadian court might feel that considerable regard should be had to investment income unless there was cogent evidence that he had formulated a gift programme as part of his tax plan. However, there is always the possibility that he might invest his capital in some non-income bearing investment in the hope of realizing a capital gain which is non-taxable.

To determine the appropriate tax rate for the Gourley deduction on the basis of his outside income at the date of the breach would greatly diminish the effectiveness of any future tax planning in which he might engage. The Gourley deduction should be applied to the lost income as though the lost income were the top slice of his income after the breach and at the rate applicable to the top slice. If, in the future, he makes investments solely for

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Schedule to the Finance Act, 1949, 12 & 13 Geo. 6, c. 47, as am. by s. 32(1) of the Finance Act, 1954, 2 & 3 Eliz. 2, c. 44, by s. 27(1) of the Finance Act, 1962, 10 & 11 Eliz. 2, c. 44, and by s. 52 of the Finance Act, 1963, 11 & 12 Eliz. 2, c. 25.

116 Income Tax Act, supra, footnote 11, ss. 111 & 112.

117 Ibid., s. 113 and Estate Tax Act, supra, footnote 115, s. 8. The maximum rate of gift tax is 28 per cent while the maximum rate of estate tax is 54 per cent. It should be noted that the gift tax rates are expressed as an average rate whereas the estate tax rates are expressed as marginal rates. Thus the gift tax is not as low compared with the estate tax as it first appears.

118 In the United Kingdom, short-term capital gains were made taxable by the Finance Act, 1962, supra, footnote 115 and a more comprehensive capital gains tax was imposed by the Finance Act, 1965, 13-14 Eliz. 2, c. 25.

119 However, Wynn-Parry J. in Re Houghton Main Colliery Co. Ltd., supra, footnote 31, at pp. 304 (All E.R.), 1225 (W.W.R.), said that in making the Gourley deduction the lost income cannot be said to constitute the top slice or bottom slice of his income. This statement has been criticized by Hall, loc. cit., footnote 3, at p. 217. Kemp and Kemp, The Quantum of Damages Vol. 1 (2nd ed., 1961), p. 50 submit that the decision was wrong on this point. An example will help to illustrate that the lost income for which damages are awarded on the Gourley principle must be considered to be the top slice of his income in order that the plaintiff will just be compensated on an after tax basis. Let us assume that the person has been incapacitated for a year, and consequently loses a salary of $10,000.00. It will also be assumed that he has interest income of $11,100.00 a year and that he is single with a personal exemption of $1,000.00 and claims the standard deduction of $100.00. The rates used in this example are the rates for the taxation year 1964 and include the Old Age Security Tax. Before the accident, he had a taxable income of $20,000.00 and would pay federal income tax of $6,440.00. This left an income after federal in-
capital gain rather than income, he will reduce his income tax but this will not alter the fact that a higher marginal rate of tax, than is now appropriate because of his smaller outside income, has already been deducted from his lost income for which he was compensated. No matter how successful his future tax planning may be, its effectiveness will be reduced if it is not in some way anticipated at the time of the making of the award subject to the Gourley deduction.  

The Gourley principle thus imposes a difficult practical problem about the extent to which tax planning should be taken into account in arriving at the appropriate deduction to be made on account of tax. It also focuses attention upon the fact that the Gourley principle may result in a significant invasion of the privacy of the plaintiff. In order to prove his after tax loss, he must adduce evidence about his other income. It may be that he has a casual business and he might be very reluctant to disclose the profit which he derives from it for fear of encouraging competition. If his private income is substantial, he may also be reticent about disclosing it in that he may wish to avoid being the subject of solicitation from relatives and the public. Even his wife's income is relevant (that is if it is less than $1,250) in determining whether he is entitled to a married exemption. These come tax of ($21,100.00 - $6,440.00) $14,660.00. After the accident he will have only interest income of $11,100.00 or a taxable income of $10,000.00 on which he would pay $2,290.00 federal income tax, leaving an income of ($11,100.00 - $2,290.00) $8,810.00. His after tax loss would be ($14,660.00 - $8,810.00) $5,850.00 per year. If his loss of salary of $10,000.00 is regarded as the top slice of his income it represents taxable income between $10,000.00 and $20,000.00. On the first $2,000.00, taxable income between $10,000.00 and $12,000.00, the rate of federal tax is 35 per cent making a tax of $700.00. On the next $3,000.00, the rate is 40 per cent making a tax of $1,200.00. On the last $5,000.00, the rate is 45 per cent making a tax of $2,250.00. The Gourley deduction is ($700.00 + $1,200.00 + $2,250.00) $4,150.00 if his salary income is regarded as the top slice of his income. He would thus be awarded ($10,000.00 - $4,150.00) $5,850.00 which is his after tax loss. The Gourley deduction must be made on the basis that what is being compensated for represents the top slice of his income. Otherwise, the award will be greater than his after tax loss. This was exactly what the Gourley principle was intended to avoid.

On the other hand, what consideration should be given a spes successionis? If he does inherit a substantial legacy, the rate of tax on the top slice of his income will be increased and also the Gourley deduction.

This matter was considered by Sellers, L.J. in his dissenting opinion in Parsons v. B.N.M. Laboratories Ltd., supra, footnote 97, at pp. 113 (Q.B.), 665 (All E.R.).

Income Tax Act, supra, footnote 11, s. 26(1)(a) & (2) as a.m. by S.C., 1958, c. 32, s. 9(1).

In the United Kingdom, the wife's income is relevant without limit in that the income of a married woman living with her husband is deemed to be the husband's income by virtue of the Income Tax Act, 1952, supra, footnote 114, s. 354(1), for purposes of tax.
are matters which the plaintiff may legitimately feel are of a personal and private nature and not matters which he should have to reveal in open court. Before Gourley, these matters would have been irrelevant, but Gourley has made such evidence indispensable in determining the quantum of damage.124

II The Status of British Transport Commission v. Gourley in Canada.

What is the status of British Transport Commission v. Gourley in Canada? As a House of Lords decision, it is, of course, not binding in Canada: nevertheless, it is highly persuasive. It was considered so highly persuasive by many Canadian judges that it has been followed without discussion and without reference to earlier Canadian decisions which adopted the opposite view with respect to income tax liability. This was the situation in Power v. Stoyles,125 a decision of Winter J. of the Newfoundland Supreme Court, in Walker v. Copp Clark Publishing Co. Ltd.,126 a decision of Spence J. of the Ontario High Court, in Widrig v. Straser,127 a decision of Johnson J. A. of the Appellate Division of the Alberta Supreme Court, and in Smith v. C.P.R.,128 a decision of Bence C. J. Q. B. of Saskatchewan. The only Canadian decision which has followed the Gourley case and in which there has been a discussion of the issues is Posluns v. Toronto Stock Exchange,129 a decision of Gale J. of the Ontario High Court. Even in this case, the Canadian decisions prior to the Gourley case were not discussed, but the remarks about Gourley were obiter dicta in that no damages were awarded as it was held that inducing the breach of the employment contract was justified.

Until recently, the tide has been running strongly towards an uncritical acceptance of the Gourley principle. The first case in opposition to this trend was Soltys v. Middup Moving and Storage Ltd.130 In this case, Nitikman J. of the Manitoba Queen’s Bench discussed the issue and concluded that the amount awarded for loss of wages was not to be reduced by the income tax which would have been payable on it. He quoted approvingly from the dissenting judgment of Lord Keith of Avonholm. in the Gourley case. He approved of remarks of Stewart J. in the Law Society

124 It was held in Phipps v. Orthodox Unit Trusts Ltd., [1958] 1 Q.B. 314, [1957] 3 All E.R. 305 (C.A.) that in an action for wrongful dismissal particulars of the plaintiff’s tax position should be ordered if it is not set out in the statement of claim.
125 Supra, footnote 35.
126 Supra, footnote 28.
127 Supra, footnote 29.
128 Supra, footnote 35.
129 Supra, footnote 24.
of Upper Canada, *Special Lectures*, 1958 in which Stewart J. indicated that he strongly disapproved of the *Gourley* case and would not follow it. Reliance was also placed on *Bowers v. J. Hollinger & Co. Ltd.*, an Ontario High Court decision, which was rendered prior to the *Gourley* case.

In *Deschamps v. Levesque*, Associate Chief Justice Challies of the Superior Court of Quebec refused to follow the *Gourley* case. He is reported to have said: "The obligations of the injured person in connection with his salary concern the defendant and the court in no way. His responsibility for income tax concerns only the injured person and the state. If the state decides not to demand income tax that is no reason for reducing the amount granted, any more than if he had promised to pay one-half of his salary to a third party for his whole life."

In *Buck v. Rostill*, Gregory J. of the Supreme Court of British Columbia refused to follow the *Gourley* case. He stated: The practice among the judges of this court is not uniform. In my experience at the bar in an active litigious practice I never had a damage award reduced by reason of income tax which would have been payable had the amount awarded as compensation for loss of income been earned. There have, I am aware, been occasions where judges of this court have made such a reduction, but it seems to me that the practice of this court (approved, albeit perhaps without specific reference to the problem, by the court of appeal) which existed prior to *Br. Transport Commn. v. Gourley* should not be disturbed until the court of appeal has given the matter consideration or at least until the judges of this court agree upon a uniform practice.

Verchere J. also of the Supreme Court of British Columbia, in *Heltman v. Western Canada Greyhound Lines Ltd.*, refused to follow the *Gourley* case and awarded damages for personal injuries including the loss of wages for one year with no deduction for income tax.

The Court of Appeal of Ontario has also recently considered the *Gourley* case. The *ratio decidendi* of *Jennings v. Cronisberry* appears to be that the burden of proving the second condition precedent to an application of the *Gourley* principle rests with the defendant and this burden is not satisfied merely by indicating that it is the practice of the Revenue not to levy income tax on awards of

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131 *Supra*, footnote 83, pp. 120, 128-129.
132 *Supra*, footnote 4.
133 *Supra*, footnote 4.
134 *Supra*, footnote 79, at p. 320.
135 A digest of this case appears in (1965), 23 The Advocate 78 (published by the Vancouver Bar Association).
136 *Supra*, footnote 14.
damages for loss of earnings in tort actions. Unless counsel agree as in the Gourley case that the award would not attract tax, Kelly J. A. said: \(^{137}\) "... the court should be satisfied that the question has been the subject of an authoritative decision which would be binding upon the Minister of National Revenue in any proceedings by him aimed at collecting income tax from the plaintiff to whom had been awarded such damages." Thus, in Ontario, where the plaintiff does not agree that the award of damages for loss of income in a tort case is not taxable, the Gourley deduction would not be made in that the defendant cannot point to a case which decides that such an award is not taxable. As it is apparently the practice of the Revenue not to tax damage awards of tort actions, there is little prospect that there will be a decision holding that such awards are non-taxable. The Ontario Court of Appeal decision thus restricts the scope of the Gourley case. In Ontario, it no longer applies to a claim for loss of income in a tort action unless the plaintiff admits that the award will not be taxed. However, the Gourley principle would apparently still be applicable in an action for damages for breach of a contract of employment. This is due to the fact that it has been held in John H. Millman v. M.N.R.,\(^ {138}\) in G. M. Brown v. M.N.R.,\(^ {139}\) in No. 45 v. M.N.R.\(^ {140}\) and in Hafezi v. M.N.R.\(^ {141}\) that damages received in an action for wrongful dismissal should be classed as capital and not subject to income tax.

The practical effect of Jennings v. Cronberry\(^ {142}\) is to exclude the Gourley principle in the assessment of damages for tort but the principle would appear to be still operative in the assessment of damages for wrongful dismissal. This is just the opposite result from what Sellers L. J. attempted to achieve in Parsons v. B.N.M. Laboratories Ltd.\(^ {143}\) If the Gourley principle is to be applied, there can be little doubt that it is less objectionable in the field of tort than in the field of contract. It would be difficult to contend that a person would receive much encouragement to go out and commit a tort through the knowledge that in the assessment of damages for loss of earnings, tax would be deducted. Whereas such a consideration might very easily influence an employer to breach a contract of employment, particularly if the employee were no longer necessary. In Ontario, Jennings v. Cronberry has restricted

\(^{137}\) Ibid., at pp. 320 (O.R.), 420 (D.L.R.).
\(^{138}\) (1951), 51 D.T.C. 305, 4 Tax A.B.C. 373.
\(^{139}\) (1952), 52 D.T.C. 9, 5 Tax A.B.C. 279.
\(^{140}\) (1952), 52 D.T.C. 72, 5 Tax A.B.C. 417.
\(^{141}\) (1961), 61 D.T.C. 357.
\(^{142}\) Supra, footnote 14.
\(^{143}\) Supra, footnote 97.
the Gourley principle but it has restricted it to a field in which the objections to its application are more cogent than in the field of tort.

This case cannot be taken as endorsing or denouncing the Gourley principle. MacKay J.A. said: 144 "In view of my conclusion that a proper foundation on which to base a deduction for income tax was not laid in this case, I do not propose to discuss these commentaries and authorities except to say that while the matter is not free from doubt, I prefer the views expressed in the dissenting judgment of Lord Keith of Avonholm in the Gourley case and adopted by Justice Nitikman in Soltys case.” McGillivary J.A., who dissented on this matter, held the Gourley deduction should be made. He said that he was in full accord with both reasons and result in the Gourley case. The third member of the court, Kelly J. A. expressed no opinion about the Gourley case. He disposed of the matter solely on the basis that the defendant had not laid the foundation for an application of the Gourley principle.

It is, therefore, impossible to say what is the exact status of the Gourley principle in Canada. It is, however, clear that the Gourley case will not be applied in the mechanical and uncritical way that it was in the past. Whether the Gourley principle will prevail is still uncertain; that the courts will now discuss its merits and difficulties is certain.

Conclusion

The difficulties involved in applying the Gourley principle have been considered. It remains to discuss the effect of the Gourley principle. If Billingham v. Hughes 146 had not been overruled, Mr. Gourley would have been awarded £37,720 for loss of earnings. This would have represented over-generous compensation to Mr. Gourley. If he had earned this sum, he would have paid £31,025 to the Revenue and he would have retained only £6,695 after tax. 146 However, it cannot be said that it would be unfair to the defendant to require him to pay £37,720. This was the gross loss which his breach of duty caused. As a result of steeply progressive income taxation, only seventeen point seven per cent of this sum would have accrued to Mr. Gourley. The largest part, eighty-two point three per cent would have accrued to the Revenue. The law as it was before the Gourley case was over-generous to the plaintiff, fair to the defendant and unfair to the Revenue and general body

144 Supra, footnote 14, at pp. 298 (O.R.), 398 (D.L.R.).
145 Supra, footnote 4.
146 Supra, footnote 1.
of taxpayers. The House of Lords held that Mr. Gourley should be awarded only his after tax loss. The law after the Gourley case was fair to the plaintiff, over-generous to the defendant and unfair to the Revenue and the general body of taxpayers.

When income tax liability was classified as a matter which was res inter alias acta or too remote to be taken into account in the assessment of damages, the result was that the general body of taxpayers gave a subsidy to the injured party. The Gourley decision resulted in the general body of taxpayers giving a subsidy to the person in breach of duty. The Gourley principle has the effect of spreading the risk of some breaches of duty among a very large class, the general body of taxpayers. But why should they bear this burden? If all damages for loss of income were made taxable as ordinary income, in the years in which it would have been earned, damages would then be assessed on a gross basis and taxed in the plaintiff’s hands. This would be equitable to the plaintiff, the defendant and the Revenue. It would not matter whether the Gourley principle was accepted or finally rejected in Canada. If the principle were accepted, it would be rendered inapplicable in that the damage award itself would be taxable and consequently would be assessed on a gross basis.

This would appear to be the most equitable solution to the dilemma which income taxation poses in the assessment of damages. Is it feasible to expect the federal Parliament to adopt such a solution? I think that the answer is probably no. The amount of additional revenue would be small and the tax would undoubtedly produce unfavourable comment. In provinces where the Gour-
ley principle has not been accepted, making all damages for loss of income taxable would have the effect of depriving plaintiffs of a subsidy which they had formerly received from the Revenue. This would be unpopular with the average citizen. In provinces where the Gourley principle has been accepted, making all damages for loss of income taxable would have the effect of depriving defendants of a subsidy which they had formerly received from the Revenue. This would be most unpopular with insurance companies.

The prospect for a change in the Income Tax Act or simply in the way it is administered resulting in the taxation of all damages for loss of income is not great. It would appear that the courts will have to decide whether it is the plaintiff or the defendant who will receive a subsidy from the general body of taxpayers. The plaintiff will receive the subsidy if the courts reject the Gourley principle. The defendant will receive the subsidy if the Gourley principle is accepted.

It has been argued that since damages are not explicitly referred to in the Canadian Income Tax Act it can be inferred that Parliament intended that the subsidy should accrue to the plaintiff. When the Income Tax Act was passed, damages for loss of earnings were awarded gross. It would appear that either as a result of a legislative concession or an administrative concession, a subsidy was being directed to the injured party. Adoption of the Gourley principle has the effect of negating this concession and diverting the subsidy to the person who is in breach of his duty. This is a factor which the courts have not yet taken into consideration.

The reasoning in the Gourley case is cogent. It is difficult to contend that taxation is too remote to be taken into consideration in the assessing of damages. However, as Lord Wright observed in Leisbosch Dredger v. S. S. Edison: "In the varied web of affairs, the law must abstract some consequences as relevant, not perhaps on grounds of pure logic but simply for practical reasons.” The difficulties inherent in the application of the Gourley principle would constitute sound practical reasons for Canadian judges refusing to follow the Gourley case. This is so particularly in view of the fact that the assessment of damages may still be entrusted

149 British Columbia, Manitoba and Quebec.
150 Alberta, Newfoundland, Ontario and Saskatchewan.
to a jury. Lord Keith of Avonholm has said that compensation on the basis of gross earnings “provides a simple rule which has been adopted for generations and creates the minimum of trouble”.\textsuperscript{153} It is submitted that the Canadian judiciary should maintain or restore this simple rule.

\textsuperscript{153} \textit{Supra}, footnote 1, at pp. 217 (A.C.), 811 (All E.R.).