

BESSIE L. SHAW .....APPELLANT;

AND

1939  
\* May 24, 25  
\* Oct. 3.

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

ON APPEAL FROM THE EXCHEQUER COURT OF CANADA

*Income tax—"Income" within s. 3 of Income War Tax Act, R.S.C., 1927, c. 97—Clause (b) of said section—Monthly instalments payable under insurance policy.*

By an insurance policy applied for by appellant and dated October 26, 1927, the insurance company agreed that on the death of appellant's husband it would pay to appellant \$700 each month for 120 months and should she survive that period it would continue to pay her \$700 monthly during her life. An option was given to commute all instalments into a single cash payment of \$71,400. The total of the premiums paid during the husband's lifetime, over and beyond dividends aggregating \$6,815.15 which accrued on the policy and were applied against premiums, was \$37,039.85. Appellant's husband died:

(1) (1889) 14 App. Cas. 665.

\* PRESENT:—Duff C.J. and Crocket, Davis, Kerwin and Hudson JJ..

on November 23, 1933. Appellant did not elect to take the single cash payment of \$71,400; and she was paid the monthly instalments. For those received in 1934 (in all, \$8,400) she was assessed for that year for income tax under the *Income War Tax Act*, R.S.C., 1927, c. 97. She appealed against such assessment.

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*Held* (reversing judgment of Maclean J., President of the Exchequer Court of Canada, [1939] Ex. C.R. 35): The assessment should be set aside. The payments sought to be taxed did not fall within the definition of "income" in s. 3 of said Act, reading that section as a whole and on particular examination of clause (b) therein.

APPEAL from the judgment of Maclean J., President of the Exchequer Court of Canada (1), dismissing an appeal from the decision of the Minister of National Revenue affirming the assessment of appellant for income tax under the *Income War Tax Act*, R.S.C., 1927, c. 97, in respect of the sum of \$8,400 received in monthly instalments of \$700 each during the year 1934 under a certain policy of insurance.

The policy was applied for by appellant and was issued by the Sun Life Assurance Company of Canada and was dated October 26, 1927. By it the Company agreed that on the death of appellant's husband (therein called the assured) it would pay to appellant (therein called the owner and therein called the beneficiary) the sum of \$700 and a like monthly instalment in each succeeding month until 120 monthly instalments in all should have been paid; that should appellant still survive after the payment of the 120 monthly instalments it would continue to pay to her the sum of \$700 monthly so long as she survived thereafter. It was agreed that when the first instalment under the policy became due the person or persons legally entitled to receive said first instalment should have the option of commuting all instalments into a single cash payment of \$71,400 ("provided always that this option cannot be exercised by the beneficiary or payee unless the owner shall have filed with the Company a written request to that effect, or shall have so expressed his desire by will").

The annual premiums were paid on the policy, being \$6,265 in each year and amounting in all to \$43,855, but less the dividends accrued on the policy during the husband's life time, amounting in all to \$6,815.15, which were

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applied against the premiums from time to time due; thus the actual premiums paid in cash after crediting such dividends amounted to \$37,039.85.

Appellant's husband died on November 23, 1933. Appellant did not elect to exercise the option of commuting the monthly instalments into a single cash payment of \$71,400, and consequently the monthly instalments stipulated in the contract have been paid to appellant since her husband's death. In the year 1934 she received the sum of \$8,400, in respect of which she was assessed for income tax and she appealed against such assessment. By the judgment now reported the appeal from the judgment of Maclean J. aforesaid dismissing appellant's appeal from the decision of the Minister affirming the assessment, was allowed, and the assessment set aside, with costs throughout.

*I. F. Hellmuth K.C.* and *H. C. F. Mockridge* for the appellant.

*F. P. Varcoe K.C.* and *J. R. Tolmie* for the respondent.

The judgment of the Chief Justice and Crocket and Hudson JJ. was delivered by

THE CHIEF JUSTICE—The charging section is section 9. There is no question that the appellant falls within one or more of the classes of persons to whom this section applies and the appeal really turns upon the question whether the payments which have been held to be taxable fall within the statutory definition of "income."

The defining section is section 3 and that section must be read as a whole. First of all, there is a declaration that, "for the purposes of this Act, 'income' means the annual net profit or gain or gratuity," whether as being a "fixed amount," such as wages or salary, or "unascertained," such as fees or emoluments, profits from a business or calling or from an office or employment, or a "profession or calling," or from a trade, manufacture or business. Then the section proceeds to say that income "shall include the interest, dividends or profits \* \* \*

from money at interest" or "from stocks, or from any other investment"; and finally,

also the annual profit or gain from any other source including

(a) the income from but not the value of property acquired by gift, bequest, devise or descent; and

(b) the income from but not the proceeds of life insurance policies paid upon the death of the person insured, or payments made or credited to the insured on life insurance endowment or annuity contracts upon the maturity of the term mentioned in the contract or upon the surrender of the contract;

and certain other classes of annual payments with which we are not concerned.

It should be observed, first of all, that the annual profit or gain which paragraphs (a) and (b) treat as income is the "income" from a specified source which is treated as not of an income nature. In (a) this source is "property acquired by gift, bequest, devise or descent" and the declaration that such income is "income for the purposes of the Act" is accompanied by a declaration that the value of such property is not included within the classes of annual profit or gain designated by the term "income" for the purposes of the statute.

Going to (b), the income, on the natural reading of the paragraph which is "income for the purposes of the Act" is the income from the proceeds of life insurance policies paid upon the death of the person insured, that is to say, upon the contingency of the death of such person. And here again, this declaration is accompanied by a declaration that such proceeds are not included under the term "income" nor are "payments made or credited on life insurance endowment or annuity contracts" or certain other specified payments.

Paragraphs (a) and (b) both specify sources the income from which is taxable and at the same time declare that these sources of income are not themselves embraced within the designation "income for the purposes of the Act."

The learned trial judge, in the course of his judgment, says it is evident that section 3 (b) contemplates the taxation of income derived from life insurance contracts and annuity contracts. With great respect, this proposition is, I think, stated rather too absolutely. Grammatically, this is the way, I think, in which paragraphs (a) and (b) are related to the second member of section 3:

and shall include \* \* \* and also the annual profit or gain from any other source including (a) the income from \* \* \* property acquired

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in the designated ways; "but not the value of" such "property." That is to say, the value of such property is explicitly excluded from the category of income. Then, coming to (b), "income" includes for the purposes of the Act,

the annual profit or gain from any other source including

(b) the income from \* \* \* the proceeds of life insurance policies paid upon the death of the person insured

but not the proceeds of such policies or,

payments made or credited to the insured on life insurance endowment or annuity contracts upon the maturity of the term mentioned in the contract or upon the surrender of the contract.

"Not \* \* or" has in this context its ordinary meaning "neither \* \* nor."

It is clear enough to me that upon a strict reading of these provisions, the payments sought to be taxed do not fall within them. It is no part of our duty in construing and applying a taxing statute to ask ourselves what might have been in the draughtsman's mind or to accept the impression received from a casual inspection of the enactment to be applied. It is our duty to analyze such enactments with strictness and, in the case of a definition such as this, to apply it only to those cases which plainly and indubitably fall within it when strictly read.

There is an additional consideration which ought not to be overlooked. It will be observed that in paragraphs (a) and (b) the word "income" is repeated. The section is defining "income" and, in defining "income," it says that "income" "includes the annual net profit or gain from any source including the income" from certain specified sources. The legislature, it seems to me, is at pains to emphasize the distinction between income and the source of income. The income derived from the capital source is income for the purposes of the Act. The source is not income for the purposes of the Act. If, therefore, you find something which is the proceeds of a life insurance policy paid upon the death of the insured, or payments made or credited in the circumstances defined in (b), then you have something which is not "income for the purposes of the Act" by the explicit declaration of the statute itself.

Broadly speaking, the statute seems to be emphasizing the intention not to tax anything that is not of an income nature. But defined classes of benefits received—property acquired by gift, testamentary or *inter vivos* and the proceeds paid on the contingency of the death of the insured under an insurance policy as well as defined classes of payments under specified classes of contracts—are explicitly declared not to be income.

As regards the ten annual payments of \$8,400 each, which come to an end at the expiration of ten years from the death of the insured, it seems impossible to escape the conclusion that each of these payments contains a very considerable element of capital. \$71,400 was agreed upon between the parties as the capitalized value of these payments plus any additional payments if the beneficiary should live longer; and I should have said, even apart from the provisions of the statute, that there is at least as much to be urged in favour of the view that these payments are of a capital nature as that they are of an income nature. There has been no attempt to segregate capital from income and the Crown does not put its case on the ground that some part, at least, of these payments are of an income nature.

The appeal should be allowed and the assessment set aside with costs throughout.

DAVIS, J.—The facts in this case are not in dispute; they were set forth in a statement signed by the solicitors for both parties.

The appellant, Mrs. Bessie L. Shaw, of Toronto, in October, 1927, took out a policy of insurance with the Sun Life Assurance Company of Canada on the life of her husband, George Baldwin Shaw, who subsequently died November 23rd, 1933. Mrs. Shaw herself made the application for the insurance and named herself as the sole beneficiary thereof. The annual premium was \$6,265, and the total cash premiums paid upon this policy during the husband's lifetime, over and beyond dividends of \$6,815.15 which accrued upon the policy from time to time and had been applied against premiums, amounted to \$37,039.85. Mrs. Shaw survived her husband and under the terms of the policy she became entitled on her husband's

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death to the sum of \$700 "and a like monthly instalment on the same day in each succeeding month until one hundred and twenty monthly instalments in all shall have been paid." There is no question that under the policy 120 monthly instalments, aggregating \$84,000 were to be paid irrespective of whether Mrs. Shaw survived her husband or not. \$84,000 is a sum, definite and fixed, which is to be paid by instalments. The policy specifically provided that if Mrs. Shaw should die before her husband, the amount of the annual premium would thereafter be reduced from \$6,265 to \$4,522.

The Company further agreed that if Mrs. Shaw was still living "after the payment in full of the 120 monthly instalments mentioned above," it would continue to pay to her the sum of \$700 monthly on the same day in each month as that on which the preceding instalments became due "so long as she may survive thereafter."

The Company further agreed that when the first instalment under the policy became due the person or persons legally entitled to receive the said first instalment should have the option of commuting all instalments into a single cash payment of \$71,400; but it was provided that this option could not be exercised by the payee unless Mrs. Shaw "shall have filed with the Company a written request to that effect, or shall have so expressed (her) desire by will."

Mrs. Shaw did not exercise the option to accept a single cash payment of \$71,400. The monthly payments have been made to her by the company and the sole question for determination in this appeal is whether or not the Minister of National Revenue is entitled to assess the \$8,400 received in the taxation period 1934 as income of the appellant liable to taxation within the provisions of the (Dominion) *Income War Tax Act* and amendments.

Mrs. Shaw was so assessed and appealed to the Minister against the assessment. The Minister affirmed the assessment on the ground that under the provisions of the policy Mrs. Shaw had the option of commuting all payments into a single cash payment of \$71,400 and that, as she refrained from exercising the option and by reason of the nature of the monthly payments received by her, the payments constitute income by virtue of the pro-

visions of sec. 3 and other provisions of the *Income War Tax Act*, and that the provisions of sec. 5 (*k*) of the Act allowing an exemption in respect of income derived from certain annuity contracts there mentioned do not apply to this particular case.

On appeal by Mrs. Shaw from the Minister's decision to the Exchequer Court of Canada, the Minister in his pleading took the position that in effect Mrs. Shaw purchased an annuity contract with the proceeds of the said insurance policy and that in that sense an annuity contract with the company was created when, on the death of her husband, she refrained from exercising her option to take a single cash payment, and that the assessment had been affirmed by the Minister on the ground that

the annuity payments are income under sec. 3 of the Act and are not the proceeds of the insurance policy on the life of the appellant's husband, the proceeds of such policy having been utilized to purchase the said annuity contract and that the annuity contract in question is not within sec. 5 (*k*), being not similar to the type of contract issued by the Dominion or provincial governments.

By an amended pleading the Minister took the position that if sec. 5 (*k*) applies, which was not admitted but denied, then the exemption is \$5,000 rather than \$1,200 as previously alleged by him, the annuity contract alleged by him having been entered into prior to May 26th, 1932, which was the date of an amendment made to sec. 5 (*k*) by sec. 6 of ch. 43 of the Statutes of 1932, reducing the exemption in respect of income derived from annuity contracts with the Dominion Government or like annuity contracts from \$5,000 to \$1,200.

The President of the Exchequer Court held that the instalment payments made by the company to the appellant were not proceeds of a life insurance policy within the meaning of paragraph (*b*) of sec. 3 of the *Income War Tax Act* and accordingly determined that, having regard to the other provisions of said sec. 3, the said instalment payments were income within the meaning of that section. Counsel for the appellant submitted to this Court that the learned President was in error in so holding and that the instalment payments received by the appellant during the period 1934 (aggregating \$8,400) were part of the proceeds of the said policy of life insurance and accordingly exempt from taxation under the provisions of said sec. 3.

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This may be a convenient place to set out the pertinent portions of sections 3 and 5 of the statute.

3. For the purposes of this Act, "income" means the annual net profit or gain \* \* \* ; and shall include \* \* \* and also the annual profit or gain from any other source including

\* \* \*

(b) the income from but not the proceeds of life insurance policies paid upon the death of the person insured, \* \* \*

5. "Income" as hereinbefore defined shall for the purposes of this Act be subject to the following exemptions and deductions:—

\* \* \*

(k) Twelve hundred dollars only, being income derived from annuity contracts with the Dominion Government or like annuity contracts issued by any Provincial Government or any company incorporated or licensed to do business in Canada.

It is income that is being taxed and not capital. The governing words of sec. 3, in so far as life insurance policies are concerned, are "and also the annual profit or gain from any other source including." I am unable to read the provision as bringing into charge something which, when its true nature is looked at, is of a capital nature which otherwise would not have been chargeable. Obviously the whole of the \$8,400 annual payment, with which this appeal is solely concerned, was not "profit or gain." The appellant had paid in premiums during her husband's lifetime \$37,039.85 over and beyond dividends credited in the sum of \$6,815.15. She might die before the annual payments had returned to her an amount equal to what she had paid. It is true that the policy assures annual payments for ten years certain, but in the event of the appellant's death before the expiration of the ten-year period, the subsequent payments could not be regarded as income to her—they would pass under her will or upon an intestacy. It may well be that on a strict actuarial accounting some part of each of the \$8,400 annual payments may be income, but obviously a comparatively small portion. But the Crown does not put forward a claim on that basis. Its contention is that the whole of the annual payment of \$8,400 is an annuity and taxable as income from (rather than the proceeds of) the life insurance policy.

I would allow the appeal with costs throughout and vary the assessment of the appellant for the taxation year in question by deleting the said item of \$8,400.

KERWIN J.—Mrs. Bessie L. Shaw appeals from a judgment of the Exchequer Court confirming the assessment levied upon her under the *Income War Tax Act* for the 1934 taxation period. Mrs. Shaw is the widow of G. B. Shaw, upon whose life a policy of insurance was taken out with the Sun Life Assurance Company of Canada. No importance is to be attached to the fact that the appellant signed the formal application for this policy nor to the fact that the premiums (less the annual dividends declared by the Insurance Company on the policy) were apparently paid out of appellant's funds,—funds to which she became entitled by reason of the transfer to her by her husband of certain shares in the capital stock of an incorporated company. In my opinion the same result would follow if G. B. Shaw had applied for the policy and if he had paid the premiums.

By the policy, the appellant, who is referred to therein as "the owner" and also as "the beneficiary," is to be paid \$700 per month for one hundred and twenty months and, if she should survive after the payment in full of the one hundred and twenty monthly instalments, she was to be paid by the Company \$700 monthly so long as she might survive thereafter. The policy further provides:—

It is further agreed that when the first instalment under this policy becomes due, as above, the person or persons legally entitled to receive said first instalment shall have the option of commuting all instalments into a single cash payment of Seventy-one Thousand Four Hundred Dollars and the payment of this amount shall completely discharge the Company from all liability in connection with this contract; provided always that this option cannot be exercised by the beneficiary or payee unless the owner shall have filed with the Company a written request to that effect, or shall have so expressed his desire by will.

Mr. Shaw died November 23rd, 1933; the appellant did not exercise the option conferred on her by this clause and the Insurance Company has therefore paid her \$700 each month. The question is whether she is assessable to income tax with respect to the sum of \$8,400 so received by her during the year 1934.

This question depends upon the proper construction of section 3 of the *Income War Tax Act*, R.S.C., 1927, chapter 97, the relevant parts of which are as follows:—

For the purposes of this Act, "income" means the annual net profit or gain or gratuity, \* \* \* and also the annual profit or gain from any other source including

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(b) the income from but not the proceeds of life insurance policies paid upon the death of the person insured, or payments made or credited to the insured on life insurance endowment or annuity contracts upon the maturity of the term mentioned in the contract or upon the surrender of the contract.

My view of the meaning of these words is that Parliament intended to exempt from income tax:—

- I. The proceeds of life insurance policies paid upon the death of the person insured.
- II. Payments made or credited to the insured on life insurance endowment or annuity contracts
  - (a) upon the maturity of the term mentioned in the contract, or
  - (b) upon the surrender of the contract.

It is arguable that the payments referred to relate to life insurance contracts or endowment contracts or annuity contracts and not to life insurance endowment contracts or life insurance annuity contracts (whatever that expression may mean), as has been suggested. It is unnecessary to come to any definite conclusion on that question because it is evident that the distinction to be drawn is between "proceeds \* \* \* paid *upon the death of the person insured*" and "payments made or credited *to the insured*." The instalments here in question were not paid to the insured, and the latter part of paragraph (b) may, therefore, be disregarded.

In view of the evident intention to tax the annual profit or gain from any source, the monthly instalments paid to the appellant would, I think, be taxable unless they fall within the first part of paragraph (b) of section 3 as being "the proceeds of life insurance policies paid upon the death of the person insured." The income that is to be included under paragraph (b) is the income from the proceeds of such life insurance and the income from the payments made or credited to the insured. In my opinion the monthly instalments are as much proceeds of life insurance policies as any single cash payment and they are "paid upon the death of the person insured" just as much as the single cash payment of \$71,400 would have been had the appellant exercised the option given her by the policy.

Counsel for the respondent attached considerable importance to paragraph (k) of subsection 1 of section 5 of the Act. It could never have been intended by Parliament, he argued, that twelve hundred dollars only, being income derived from annuity contracts with the Dominion Government, etc., should be exempt, and that the total of the monthly instalments received by Mrs. Shaw under the policy should be exempt. But it is quite clear, from the evidence of Mr. Blackadar given in the Exchequer Court in this case, that this policy is an entirely different thing from the annuity contracts issued by the Dominion Government. Whatever considerations may have moved Parliament to enact clause (k) of subsection 1 of section 5 in 1930 and 1932, with reference to agreements to pay an annuitant certain sums during his lifetime, can have no bearing, it seems to me, upon the question as to what are proceeds of life insurance policies paid upon the death of of the person insured, as mentioned in clause (b) of section 3. It is quite true that any income from these proceeds is taxable and that, therefore, there is more likely to be a large taxable income if a beneficiary under such a policy takes a lump sum in satisfaction of her claim, but all this is *nihil ad rem*.

The appeal should be allowed and the assessment of the monthly instalments for 1934 set aside, with costs throughout.

*Appeal allowed with costs.*

Solicitors for the appellant: *Osler, Hoskin & Harcourt.*

Solicitor for the respondent: *W. S. Fisher.*

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