this child should be given the equal opportunity of the child whose parent or parents, though under 21 can by will name his or her guardian and arrange for his maintenance after the parents' death.

And at the same time the unmarried infant mother whom we have been discussing should not be deprived of her parental right to arrange for guardianship and care of her child after her death by reason only that she is not nor has been married.

I would urge that our Wills Act be changed to provide that a mother who is not of the full age of 21 years and is not and has not previously been married, but has borne a living child, be permitted to make a valid will.

—ADLYNN MISKEW HEWITT*

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BENEFITS UNDER SECTION 137 (2) OF THE INCOME TAX ACT— *CRADDOCK AND ATKINSON* v. *M.N.R.*

The judgment of Gibson, J. in *W. L. Craddock & S. C. Atkinson* v. *M.N.R.*[1] unless it is reversed by the Supreme Court of Canada, may well prove to be a frontier whose crossing will prompt Parliament and its fiscal planners to review the direction which Canada's approach to legal reduction of taxes should take in the future. In two giant strides, starting with the case of *Conn Smythe et al.* v. *M.N.R.*[2] the Exchequer Court has altered the entire complexion of legal tax avoidance by its revolutionary analysis of the construction of Section 137.[3]

Mrs. Gwyneth McGregor in The Canadian Tax Journal[4] has given a careful analysis of the *Smythe* case. She explains that the purpose of dividend strips is to extract the undistributed income of a corporation and get it into the hands of the shareholders without payment of any tax. Prior to the *Smythe* case, section 137 (2) was not generally thought to apply to dividend strips, particularly after the introduction into the Income Tax Act, in 1963, of section 138A. This view seemed to be confirmed by the fact that no attempt had, up to that time, been made by the Minister of National Revenue to assess shareholders as a result of such strips carried out prior to the enactment of this section. The *Smythe* case was the first of those cases where the taxpayer relied upon the courts to establish that a "strip" was not subject to tax. This procedure was adopted in preference to taking advantage of the right offered by The Hon. E. J. Benson, while he was Minister of National Revenue, to pay tax at an effective rate of 16-2/3% on the surplus stripped (a course that had been available to them under section 105(B)) rather than pay tax at full rates less the applicable dividend credit should the strip be held to be taxable. For those who elected to take his offer, the Minister agreed to refund any tax paid if it were subsequently determined by the courts in a parallel case that the shareholders were not taxable as a result of the strip.

The facts in the *Smythe* case are rather complicated and they are fully set out in Mrs. McGregor's article.[5] They are, however, briefly set out as follows:

The shareholders of Conn Smythe Limited, an Ontario company, (Conn Smythe, his son Conn Stafford Smythe, Clarence H. Day and A. M. Boyd) incorporated

1 [1968] C.T.C. 379; 68 D.T.C. 5254.
2 [1967] C.T.C. 498; 67 D.T.C. 5334.
3 H. H. Stikeman, Canada Tax Service Letter No. 130, October 9, 1968.
4 (1968), 16 Can. Tax J. 16.
5 *Id.*, at 19.

a new company, the shares of which were owned by them in the same proportion as their share ownership in the old company. The shareholders caused the old company to sell to the new company all the assets of the old, taking a promissory note for $2,611,769, which was later redeemed for cash by means of a *daylight* loan from a bank. Conn Smythe and the other shareholder of the old company sold their shares to two Vancouver companies, who were at arm's length to them, for $2,570,335. This sum was also obtained by means of a daylight loan from a bank. The difference between this figure and selling price of the assets was the fee to the Vancouver companies. The Vancouver companies who were then the sole shareholders of Conn Smythe Limited, the old company, then caused the old company to subscribe for preferred shares of the Vancouver companies for $2,611,769. Gibson, J., found that these shares were worthless. The original shareholders (Conn Smythe et al) lent the new company most of the proceeds from the sale of their shares in the old company and carried on the business of the old company under the name of the new company in the form of debentures which could be redeemed without payment of tax.

Mr. Justice Gibson concluded that the result of the whole series of transactions was that the old company had in effect, paid a dividend to the old shareholders and thus had conferred a benefit on the appellant shareholders pursuant to section 137(2).

The assessor had assessed the appellants under section 81(1) of the Act, thus giving them the benefit of the dividend tax credit. Gibson, J., reluctantly agreed to this, taking the view that he thought they should be assessed under 8(1) since no "winding-up, discontinuance, or reorganization" of the business, within the meaning of that section, had taken place. He also invoked the U.S. *business purpose* doctrine first enunciated in the case of *Helvering* v. *Gregory*[6] and concluded that there was no legitimate business purpose for the transactions in that they were entered solely as a means of avoiding the taxation consequences of complying with the provisions of sections 105 or 105B of the Income Tax Act.

In the *Craddock* case similar stripping arrangements were carried out. Gibson, J., in dealing with the matter on an appeal from an assessment of the Minister of National Revenue, propounded a number of propositions which should be taken into account for the purpose of determining the income tax consequences of the transaction and that this strip met the test of those propositions. He found that a result could be ascertained, i.e. that a benefit having value in money's worth had been conferred on a person as a result of the strip; that the sale of shares was part of an interrelated transaction; that all of the parts of the interrelated transactions had no business purpose and had been entered as a means of avoiding the taxation consequences of other sections of the Act; that one or more related parts of the transaction had been entered by persons not dealing at arm's length and that the result of the whole series of transactions was the same as though the Company had paid the money out to its shareholders.

He continued:

When the circumstances of the inter-related transactions are such that it is correct to include such 'benefit' 'in computing the taxpayer's income for the purpose of Part I', then the total of it is included in such taxpayer's income as one of the sources of such taxpayer's income within the meaning of Section 3 of the Act in the same manner as if Section 137(2) was in one of the series of sections in Part I such as Section 6, Section 8(1), Section 16(1) and Section 81(1). But Section 137(2) of the Act in any such case is not dependent upon for its efficacy on or connected with any other section or sections in Part I, such as

[6] 69 Fed. 2d 809 affirmed 293 U.S. 465.

Sections 6, 8(1), 16(1) and 81(1) and therefore none of these latter sections are relevant in the adjudication of any case in which Section 137(2) is applicable."[7]

What is the result of the *Craddock* case? In the first place little help has been given in removing two obscurities referred to by Mrs. McGregor:

> There are two obscurities to be got over in the provision: first, what is a benefit; and second, what is the amount to be assessed as a benefit. . . .
> Then, the value of the benefit must be established for tax purposes. Section 137(2) merely says that the person conferring the benefit shall be deemed to have made a payment equal to the amount of the benefit; but that does not help at all in deciding what that amount is. Nor does the judgment help, for the question was not considered; having ruled that a benefit had been conferred, the Court simply said that its value was the amount of the undistributed surplus. But we have heard suggestions that the value of the benefit could be: (a) the amount of tax saved (since this was the only difference between getting the amounts out by a strip rather than via 105B); (b) the amount paid to Cameron and his associates to achieve the strip (the argument being that that was what the strip was worth to the Smythe group); or (c) both of these.
> The widest field for the taxation of benefits received by a taxpayer is that of employment income, since by virtue of section 5 the value of all benefits of any kind whatsoever must be brought into income. But neither this section nor any other gives any guide as to what that 'value' should be—whether fair market value, the value to the employee (it can be greater for some than for others), or the value to the employer.[8]

Professor Jones in an article *Benefits under the Income Tax Act*[9] has dealt with the question of benefits, particularly as they relate to sections 5 and 16 of the Income Tax Act. This article reveals some of the difficulties inherent in defining benefits, advantage and appropriated as those words are used in sections 8(1), 16(1) and 81(1).

The *Craddock* decision has done little to clarify the meaning of benefits except perhaps to a limited degree in purely dividend stripping cases. But the main point of the decision of Gibson, J., in the *Craddock* case is that section 137(2) is not dependent for its efficacy on any other section or sections in Part I of the Income Tax Act. This finding has, however, created more problems than it has solved.

As H. H. Stikeman says:

> If Section 137(2) is indeed to be regarded as a section standing alone and complete in itself, how is it to be used by the Minister so as to most accord with the structure and philosophy of the Income Tax Act as a whole. . . .
> This means that the Minister would have a number of choices. He must first decide what constitutes the benefit to be assessed. Is it the actual tax saving (the real economic advantage obtained), or the entire receipt tax gross; or should it be treated as a payment to a non-resident or as a gift?[10]

One might well ask what section of the Act will the Minister use in imposing tax. In the *Smythe* case, Gibson, J., had considerable doubt as to whether the tax should be imposed under sections 8(1) or 81(1). In the latter case, the taxpayer would be entitled to the benefit of a dividend credit to which he would not be entitled under section 8(1). In the *Craddock* case he has said that section 137(2) stands independently. On the other hand, in a number of recent cases, the court has decided that the taxpayer had received a benefit under both section 137(2) and under other sections as well. In the case of *Cake-Bread* v. *the Minister of National Revenue*[11] the Chairman (Cecil L. Snyder, Q.C.) held that the taxpayer was liable under both 8(1)(c) and 137(2). Similarly in

[7] [1968] C.T.C. 379, 386.
[8] *Op. cit. supra*, n. 4, at 23.
[9] (1968), 6 Alta. L. Rev. 157.
[10] *Supra*, n. 3, at 5.
[11] [1968] Tax A.B.C. 531; 68 D.T.C. 424.

St. Germain v. *the Minister of National Revenue*,[12] Dumoulin, J., in the Exchequer Court held that the taxpayer was liable either under 8(1)(c) or section 137(2). Either section 137(2) is unnecessary in cases of this kind or further direction is necessary as to when it is to be applied. An appeal in the *Smythe* case should soon be heard before the Supreme Court of Canada. It is doubtful, however, whether judicial interpretation will be able to effect a satisfying solution to a section which appearing, as it does, in Part VI of the Act under the rubric *Tax Evasion* has now become a charging section displacing to some extent those sections such as 8(1) and 81(1) which had been regarded as the applicable charging sections of the Act. It would seem that legislative enactment will be required to effect a suitable solution. Hopefully, the Minister of Finance will consider this in the Bill revising the Income Tax Act, which he has announced will be introduced into the House of Commons early in 1969.

—E. M. BREDIN, Q.C.*

12 [1968] C.T.C. 148; 68 D.T.C. 5105.
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INSURANCE ACT, S.A. 1960, c. 49, s. 263—SURVIVORSHIP ACT, S.A. 1964, c. 91, s. 2(1)—CONFLICT OF STATUTES—*RE CANE AND CANE* (1968), 66 D.L.R. (2d) 741—*RE BILN* (1967), 59 W.W.R. 229.

The Survivorship Act[1] in section 2(1) creates a presumption, where two or more persons die at the same time or in circumstances rendering it uncertain which of them survived the other, that the elder died first. The Insurance Act[2] by section 263 creates a presumption that where the person whose life is insured and a beneficiary die at the same time or in circumstances rendering it uncertain which of them survived the other, the insurance money is payable as if the beneficiary had died first. These presumptions, in a situation where the insured is the elder of the two victims, are at odds with each other and it is therefore necessary to determine which presumption should properly prevail. To properly understand the intendment of the Survivorship Act it is necessary to have an understanding of the reasons for passage of the Act.

Survivorship at Common Law

At common law where two people perished by the same calamity, whether testate or intestate, there was no presumption that one survived the other or that they died at the same moment.[3] The *onus probandi* lay upon the party asserting survival. This was clearly pointed out in *Hickman* v. *Peacey* by Lord Simonds when he said:[4]

> . . . if A and B died in a common calamity it was necessary for the representatives of that one of them who claimed to be interested in the estate of the other under his will or as upon his intestacy, to prove that he was the survivor. If they did not prove it the claim failed. In the not uncommon case when each of them was interested under the will or as upon the intestacy of the other, neither of them could take any interest unless survivorship was

1 S.A. 1964, c. 91, s. 2(1).
2 S.A. 1960, c. 49, s. 263.
3 *Underwood* v. *Wing* (1854), 4 De. G.M. & G. 633; 43 E.R. 655; *aff'd.* on appeal sub-nom. *Wing* v. *Angrave* (1860), 8 H.L. Cas. 183; 11 E.R. 397.
4 [1945] A.C. 304, 341.