

58, 1933

In the Privy Council.

No. 72 of 1932.

ON APPEAL FROM THE SUPREME COURT OF
CANADA.

BETWEEN

THE MINISTER OF NATIONAL REVENUE - -
(Respondent) Appellant

AND

MRS. CATHERINE SPOONER - - (Appellant) Respondent.

RECORD OF PROCEEDINGS.

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In the Privy Council.

No. 72 of 1932.

ON APPEAL FROM THE SUPREME COURT OF
CANADA.

BETWEEN
THE MINISTER OF NATIONAL REVENUE - - -
(Respondent) Appellant
AND
MRS. CATHERINE SPOONER - - - *(Appellant) Respondent.*

RECORD OF PROCEEDINGS.

No. 1.

Agreement between Catherine Spooner and Vulcan Oils Limited.

AGREEMENT made in duplicate this Fifteenth day of April, 1925.

BETWEEN: CATHERINE SPOONER, of Vulcan, Alberta, hereinafter
~~called~~ the "Vendor," OF THE FIRST PART; AND VULCAN OILS
LIMITED, of Vulcan, Alberta, hereinafter called the "Company,"
OF THE SECOND PART.

No. 1.
Agreement
between
Catherine
Spooner and
Vulcan Oils
Limited,
15th April
1925.

WHEREAS the Vendor herein is the owner of the North West Quarter
of Section Thirteen (13) Township Twenty (20) Range Three (3) West of
10 the Fifth Meridian, including all mines and minerals thereon or under
the said lands.

WHEREAS the said Catherine Spooner has agreed to sell to the
Company herein the South twenty acres of the said Section Thirteen (13)
Township Twenty (20) Range Three (3) West of the Fifth Meridian. Subject
to the provisos, conditions, restrictions.

NOW THEREFORE THIS INDENTURE WITNESSETH

1. That the Vendor hereby sells, assigns, transfers and sets over unto
the Company, its successors and assigns, all her right, title and interest, in

No. 1.
 Agreement
 between
 Catherine
 Spooner and
 Vulcan Oils
 Limited,
 15th April
 1925—con-
 tinued.

and to the following property; namely, the South twenty acres of the North West quarter of Section Thirteen (13) Township Twenty (20) Range Three (3) West of the Fifth Meridian, which includes all mines and minerals, on, in or under the said lands. Subject to the provisos, conditions and royalties hereinafter reserved.

2. The Company hereby agrees in consideration of the said sale to it, to pay to the said Vendor the sum of Five Thousand (\$5,000.00) dollars in cash upon the execution of this Agreement by the Company, and to issue to the Vendor or her nominee certificates of stock of the company to the aggregate amount of twenty-five thousand shares of the par value of One Dollar each and the said shares shall be deemed to be and are hereby declared to be fully paid shares and not liable to any call thereon, and the holders of such stock shall not be liable to any further payment thereon. 10

3. The Company hereby further agrees in consideration of the said sale to deliver to the order of the said Vendor the royalty hereby reserved to the Vendor, namely: ten per cent. of all the petroleum, natural gas, and oil, produced and saved from the said lands free of costs to the said Vendor on the said premises. And the said petroleum, natural gas and oil shall be delivered under the instructions and upon the method decided by the Vendor, and the Company further covenants and agrees that it will deliver to the said Vendor the beforementioned percentage of petroleum, natural gas and oil saved on the said land at least once in every thirty days and will not sell or remove any petroleum, natural gas or oil from the said premises until the said percentage or share thereof belonging to the Vendor shall have been delivered as aforesaid. 20

4. The Company shall keep or cause to be kept proper books of account at its registered office showing correctly the quantity of petroleum, natural gas, and oil produced from the said lands, and of all oil and gas taken away or removed therefrom and will from time to time on demand produce the said books of account and permit the said Vendor or her attorney or agent to inspect them and take extracts therefrom or copies thereof, and the Company will permit and suffer the Vendor, her attorney or agent at all times to enter upon the said premises for the purposes of inspecting the operations of drilling or pumping and working in any well or wells finished or in the course of construction on the said premises. 30

5. The Company covenants and agrees with the Vendor that it will proceed forthwith to obtain standard drilling machinery fully equipped and will commence drilling operations upon the said lands as expeditiously as possible and to continue such drilling operations without interruption, except as may be unavoidable until oil and/or gas in commercial quantities is struck or to a minimum depth of 4,500 feet. 40

6. Upon oil or petroleum being discovered the said Company hereby covenants and agrees to install and properly maintain the necessary

machinery for pumping or procuring said oil or petroleum from the well or wells and delivering it in pipes, reservoirs or tanks and the said Company hereby agrees to carry on the operations of pumping or otherwise procuring the said oil or petroleum or gas from the said lands.

No. 1.
Agreement
between
Catherine
Spooner and
Vulcan Oils
Limited,
15th April
1925—con-
tinued.

7. In the event of oil or gas being discovered in commercial quantities on the said lands the Vendor as part of the consideration for this Agreement, covenants to transfer to the said Company by good and sufficient transfer in fee simple the said twenty acres of land freed and discharged from all encumbrances and also shall transfer to the said Company by good and sufficient transfer in fee simple freed and discharged from all encumbrances the South twenty acres of the North West Quarter of Section twenty-four (24) Township twenty (20) Range three (3) West of the 5th Meridian and such transfers shall be completed and delivered forthwith after oil or gas is discovered in commercial quantities by the said Company, reserving always however to the Vendor the said royalty of ten per cent. of all petroleum, natural gas and oil in respect to the said South twenty acres of the N.W. $\frac{1}{4}$ of Section 13, Township 20, Range 3, West of the 5th Meridian and also free access on and over all said lands described in this paragraph to an extent not exceeding three trails and the location of the said trails shall be selected by the Vendor.

8. The Vendor further covenants and agrees with the Company upon the request and at the cost of the Company to execute and do all such further assurances and things as shall reasonably be required by the Company, for vesting in it the property and rights agreed to be hereby sold and giving to it the full benefit of this Agreement.

9. It is further declared and agreed that these presents and everything herein contained shall enure to the benefit of and be binding upon the parties hereto and each of their heirs, executors and administrators and successors and assigns respectively.

30 IN WITNESS WHEREOF the Party of the First Part has hereunto set her hand and seal and the Vulcan Oils, Limited, has hereunto affixed its corporate seal, attested by the signatures of its proper officers.

WITNESS :
D. C. JONES,
Druggist
Vulcan, Alta.

}
CATHERINE SPOONER.
VULCAN OILS, LIMITED.
A. G. SPOONER.
A. J. FLOOD.



No. 1.
Agreement
between
Catherine
Spooner and
Vulcan Oils
Limited,
15th April
1925—*con-
tinued.*

CANADA.
PROVINCE OF ALBERTA
TO WIT: }

I, D. C. JONES, of Vulcan, in
the Province of Alberta, Druggist,
make oath and say:—

1. That I was personally present and did see Catherine Spooner,
named in the within instrument, who is personally known to me to be
the person named therein, duly sign, seal and execute the same for the
purposes made therein. 10

2. That the same was executed at Vulcan, in the Province of Alberta,
Canada, and that I am the subscribing witness thereto.

3. That I know the said Catherine Spooner and she is in my belief of
the full age of twenty-one years.

SWORN before me at the Town of }
Vulcan, in the Province of Alberta, }
this 15th day of April, 1925. }

D. C. JONES.

L. H. STACK,
A Commissioner for Oaths in and
for the Province of Alberta. 20

No. 2.
Notice of
Appeal from
Assessment,
21st Octo-
ber 1929.

No. 2.

Notice of Appeal from Assessment.

Notice of Appeal is hereby given from the assessment bearing date the
24th day of September, 1929, wherein a tax in the sum of \$301.07 is levied
in respect of income for the taxation year 1927.

Prior to 15th April, 1925, the Appellant was the owner of the North
West Quarter of Section Thirteen (13) Township Twenty (20) Range Three
(3) West of the Fifth Meridian including all mines and minerals thereon
or under the said lands.

By agreement dated 15th April, 1925, the Appellant sold to Vulcan 30
Oils Limited the south twenty (20) acres of the said North West Quarter
of Section Thirteen. The agreement contained the following clauses:

1. That the Vendor hereby sells, assigns, transfers, and sets
over unto the Company, its successors and assigns, all her rights,
title and interest, in and to the following property; namely, the
South twenty acres of the North West quarter of Section thirteen
(13) Township twenty (20) Range three (3) West of the 5th
Meridian, which includes all mines and minerals on, in or under
the said lands, subject to the provisos, conditions and royalties
hereinafter reserved. 40

2. The Company hereby agrees in consideration of the said sale to it to pay to the said Vendor the sum of Five Thousand (\$5,000.00) Dollars in cash upon the execution of this Agreement by the Company, and to issue to the Vendor or her nominee certificates of stock of the company to the aggregate amount of twenty-five thousand shares of the par value of one dollar each and the said shares shall be deemed to be and are hereby declared to be fully paid shares and not liable to any call thereon, and the holders of such stock shall not be liable to any further payment thereon.

No. 2.
Notice of
Appeal from
Assessment,
21st Octo-
ber 1929—
continued.

10

3. The Company hereby further agrees in consideration of the said sale to DELIVER to the order of the said Vendor the royalty HEREBY RESERVED by the Vendor, namely; Ten per cent. of all the petroleum, natural gas, and oil, produced and saved from the said lands free of cost to the said Vendor on the said premises, and the said petroleum, natural gas and oil shall be delivered under the instructions and upon the method decided by the Vendor, and the Company further covenants and agrees that it will deliver to the said Vendor the before mentioned percentage of petroleum, natural gas and oil saved on the said land at least once in every thirty days and will not sell or remove any petroleum, natural gas or oil from the said premises until the said percentage or share THEREOF BELONGING TO THE VENDOR shall have been delivered as aforesaid.

20

Under Paragraph 1 the royalty is reserved to the Appellant. The covenant in paragraph 3 is not a covenant to pay a royalty but one to deliver the royalty reserved by the Vendor. This paragraph states that a certain percentage of the petroleum, natural gas and oil belongs to the Appellant. It is submitted that the clause contemplates the reservation by the Vendor of ten per cent. of all the petroleum, natural gas and oil produced on the lands. This ten per cent. being of necessity included in the production obtained by the Company the latter receives it not as its own property but as the property of the Appellant and the covenant consequently is merely one for delivery only of the portion belonging to the Appellant.

30

That this is the meaning of the agreement is also clear from paragraph 7 which reads as follows :—

In the event of oil or gas being discovered in commercial quantities on the said lands the Vendor as part of the consideration for this Agreement, covenants to transfer to the said Company by good and sufficient transfer in fee simple the said twenty acres of land freed and discharged from all encumbrances and also shall transfer to the said Company by good and sufficient transfer in fee simple, freed and discharged from all encumbrances the South Twenty acres of the North West quarter of Section twenty-four (24) Township twenty (20) Range three (3) West of

40

No. 2.
Notice of
Appeal from
Assessment,
21st Octo-
ber 1929—
continued.

the 5th Meridian, and such transfers shall be completed and delivered forthwith after oil or gas is discovered in commercial quantities by the said Company, reserving always however to THE VENDOR THE SAID ROYALTY OF TEN PER CENT. OF ALL PETROLEUM, natural gas and oil in respect to the said twenty acres of the N.W. $\frac{1}{4}$ of Section 13, Township 20, Range 3, West of the 5th Meridian, and also free access on and over all said lands described in this paragraph to an extent not exceeding three trails and the location of the said trails shall be selected by the Vendor.

10

This clause provides that on the conditions entitling the Company to transfer being fulfilled the Appellant will transfer the property to the Company reserving to herself the royalty of ten per cent. of the petroleum and natural gas.

The only obligation on the Company is that of delivery and this obligation is clearly stated to be the delivery of the royalty actually reserved by the Vendor, or the percentage belonging to her.

If however this interpretation is not acceptable and the royalty is held not to be reserved but to be payable by the Company it is submitted that in such case it should be held to be part of the purchase price, the clause covering it being in exactly the same terms as the previous clause providing for the payment of cash and allotment of shares.

20

Generally in regard to the agreement it is submitted that the word "royalty" is used in a slightly incorrect sense. The word is defined as follows :

A payment made to a land owner by the lessee of a mine in return for the privilege of working it.

Murray's New English Dictionary 1914 Edition, Vol. VIII. page 852.

A share of proceeds paid to a proprietor by those who are allowed to develop or use property or operate under some right belonging to him as to the owner of mining lands for ore taken out.

30

Funk & Wagnall's Dictionary 1913, page 2140.

The proper use of the word royalty would imply that the Appellant was the proprietor or owner of the property. The word actually refers to that portion of the petroleum and natural gas which in the terms of the agreement is reserved to the Appellant or belongs to the Appellant. The share actually receivable by the Appellant under the Agreement represents either the property reserved to herself or an instalment of the purchase price and is therefore a return of capital only.

40

The Appellant does not deny that she received from Vulcan Oils Limited the sum of \$9,570.41 representing her one-tenth of the oil recovered from the property but she denies that this was a royalty received for the permission to use or develop the property in question as the property belonged to Vulcan Oils Limited subject to the reservation to her of one-tenth of the petroleum and natural gas.

The Appellant claims that the transaction constituted a sale by her of the surface rights and ninety per cent. of the petroleum, natural gas and oil for the cash and share consideration above mentioned and that she never parted with the property in the said ten per cent. and that as she owned the same before 1917 it becomes a return of capital when she recovers it from the ground and realizes on it in cash.

If it is held that the Appellant's contentions as above set out are invalid then the Appellant would be entitled under Section 3 (1.A) to an allowance for the exhaustion of the minerals.

10 DATED at Calgary, Alberta, this 21st day of October, 1929.

(Sgd.) CATHERINE SPOONER,
by her Solicitor.

H. S. PATTERSON,
220, 8th Ave. W.,
Calgary, Alberta.

No. 2.
Notice of
Appeal from
Assessment,
21st Octo-
ber 1929—
continued.

No. 3.

Decision of the Minister.

IN THE MATTER OF The Income War Tax Act,

AND

20 IN THE MATTER OF The Appeal of Mrs. Catherine Spooner,
of the City of Calgary, in the Province of Alberta,
hereinafter called the taxpayer - - - - - *Appellant.*

DECISION OF THE MINISTER.

WHEREAS the taxpayer filed an Income Tax Return on the 28th April, 1928, for and in respect of the year 1927, in which no income was reported.

AND WHEREAS by Notice of Assessment dated the 24th September, 1929, the taxpayer was assessed in respect of the sum of \$9,570.41 received by her from Vulcan Oils, Limited.

30 AND WHEREAS the taxpayer appealed from the said Assessment,
by Notice of Appeal dated the 21st October, 1929, on the ground that the amount received from Vulcan Oils Limited was Royalty and was not taxable income.

The Minister of National Revenue, having duly considered the facts set forth in the said Notice of Appeal and other facts relative thereto, hereby affirms the said assessment on the ground that under and by virtue of the agreement of the 15th April, 1925, between the taxpayer and the Vulcan Oils Limited the taxpayer secured unto herself an income, fluctuating

No. 3.
Decision of
the Minister,
30th Nov-
ember 1929.

No. 3.
Decision of
the Minister,
30th Nov-
ember 1929
—continued.

annually in accordance with the production of oil and that the monies realized from the sale of such oil either by herself or through her agent or by contract or otherwise, such monies coming to her constitute taxable income and she is taxable in respect thereof, subject however, to adjustment as to depletion in accordance with Section 4, of Chapter 12 of the Statutes of 1928, reading—

“ And in the case of leases of mines, oil and gas wells and timber limits, the lessor and the lessee shall each be entitled to deduct a part of the allowance for exhaustion as they agree and in case the lessor and the lessee do not agree, the Minister shall have full power to apportion the deduction between them and his determination shall be conclusive.”

Notice of such decision is hereby given in accordance with Section 59 of Chapter 97 of the Revised Statutes of Canada, 1927.

DATED at Ottawa this 30th day of November, A.D. 1929.

W. D. EULER,
Minister of National Revenue.

C. S. WALTERS,
Commissioner of Income Tax.

To :
MRS. CATHERINE SPOONER,
c/o A. G. Spooner, Esq.,
311 Lancaster Bldg., Calgary, Alta.

AND TO :
H. S. PATTERSON, Esq.,
Barrister, etc.
220 A. 8th Avenue W.,
Calgary, Alta.
Her solicitor herein.

20

No. 4.
Notice of
Dissatis-
faction,
30th Dec-
ember 1929.

No. 4.

Notice of Dissatisfaction.

In Re The Appeal of Catherine Spooner, of the City of Calgary, in the Province of Alberta.

The Appellant herein desires that her appeal be set down for trial. 30

DATED, at the City of Calgary, in the Province of Alberta, this 30th day of December, 1929.

(Sgd.) CATHERINE SPOONER,
Appellant.

No. 5.

Reply of the Minister.

No. 5.
Reply of the
Minister,
24th April
1930.

A Notice of Dissatisfaction having been received from the taxpayer with respect to her assessment for the year 1927 and security for costs having been duly furnished, the Honourable the Minister of National Revenue replies to the said Notice of Dissatisfaction as follows :

(1) Denies the contentions and allegations set forth in the said Notice of Dissatisfaction ;

10 (2) Confirms the taxpayer's assessment for the year 1927 appealed against for the reasons set forth in the Decision of the Minister herein dated the 30th November, 1929.

Notice of such confirmation is hereby given in accordance with Section 62 of the Act.

DATED at Ottawa this 24th day of April, A.D. 1930

W. D. EULER,
Minister of National Revenue.

Per C. S. WALTERS,
Commissioner of Income Tax.

To :
20 MRS. CATHERINE SPOONER,
c/o A. G. Spooner, Esq.,
311 Lancaster Bldg.,
Calgary, Alta.

AND TO :
H. S. PATTERSON, Esq.,
Barrister, etc.,
220, 8th Avenue W.,
Calgary, Alta.
Her Solicitor herein.

No. 6.

Order for Pleadings to be filed.

IN THE EXCHEQUER COURT OF CANADA.

BEFORE THE DEPUTY REGISTRAR IN CHAMBERS.

30 IN THE MATTER OF The Income War Tax Act,
AND
IN THE MATTER OF The Appeal of Mrs. Catherine Spooner,
of the City of Calgary, in the Province of Alberta, herein-
after called the taxpayer - - - - - *Appellant* ;
AND
THE MINISTER OF NATIONAL REVENUE - - - - - *Respondent*.

*In the
Exchequer
Court of
Canada.*

No. 6.
Order for
Pleadings to
be filed,
10th May
1930.

Upon the application of the Solicitor for the respondent and upon hearing read the consent of counsel of the appellant and respondent.

1. IT IS ORDERED that formal pleadings be filed in this cause.

*In the
Exchequer
Court of
Canada.*

No. 6.

Order for
Pleadings to
be filed,
10th May
1930—con-
tinued.

2. IT IS FURTHER ORDERED that the Statement of Claim of the Appellant be filed within thirty days from the date hereof and that within the said period copy be served upon the Commissioner of Income Tax or other responsible officer of the Income Tax Division of the Department of National Revenue.

3. IT IS FURTHER ORDERED that the Statement in Defence on behalf of the Minister of National Revenue shall be filed and serve within twenty days from the date of service of the Appellant's Statement of Claim.

4. IT IS FURTHER ORDERED that the reply, if any, of the Appellant be filed and served within fourteen days after the service of the Statement in Defence on the said Appellant. 10

5. IT IS FURTHER ORDERED that no further pleadings shall be filed thereafter without the consent of the Court or Judge thereof.

6. IT IS FURTHER ORDERED that the printing of the pleadings be dispensed with.

DATED at Ottawa this 10th day of May, A.D. 1930.

(Sgd.) ARNOLD W. DUCLOS,
Deputy Registrar.

No. 7.
Statement
of Claim,
17th May
1930.

No. 7.

Statement of Claim.

Filed May 21st, 1930.

20

1. The Appellant is a widow and resides at the City of Calgary, in the Province of Alberta.

2. The Appellant was prior to the year 1917 and has been at all times since the said year the owner of all petroleum, natural gas and oil in and under the Southerly 20 acres of the North West Quarter of Section 13, Township 20 Range 3, West of the Fifth Meridian in the Province of Alberta.

3. By agreement dated the 15th day of April, 1925, and made between the Appellant of the First Part and Vulcan Oils Limited of the Second Part the Appellant agreed to sell to the said Vulcan Oils Limited the said land subject to the provisos, conditions and royalties expressed in the said agreement. 30

4. The Appellant in the year 1927 received from Vulcan Oils Limited certain petroleum, natural gas and oil of the value of \$9,570.41, said petroleum, natural gas and oil having been delivered to the Appellant pursuant to the terms of the said agreement. The Respondent alleges that the Appellant is liable under the provisions of the Income War Tax Act for the payment of a tax on the monies received from the sale of the said petroleum, natural gas and oil and the Appellant denies that she is so liable. 40

5. In and by the said agreement the Vendor covenanted with the said Vulcan Oils Limited that in the event of oil or gas being discovered in commercial quantities on the said lands the Vendor would by good and sufficient transfer in fee simple, transfer the said lands to the said Vulcan Oils Limited reserving always, however, unto the Vendor the royalty of 10 % of all petroleum, natural gas and oil produced thereon or therefrom and also reserving free access in and over the said lands to an extent not exceeding three trails the location of the said trails to be selected by the Appellant. The Appellant says that on the true interpretation of the said
 10 agreement the Appellant covenanted to transfer to the said Vulcan Oils Limited 90 % of all petroleum, natural gas and oil in or under the said lands.

6. In the alternative the Appellant says that in and by the said agreement the Appellant sold the said lands to Vulcan Oils Limited and received in consideration of the said sale the sum of \$5,000.00 and the covenant of the Vulcan Oils Limited to deliver to the Appellant 10 per cent. of all petroleum, natural gas and oil recovered from the said lands.

7. The Appellant says that the said 10 % of petroleum, natural gas and oil which under the terms of the said agreement was to be reserved or delivered to the Appellant constituted either a reservation to the
 20 Appellant of said petroleum, natural gas and oil or a portion of the purchase price of the said lands and was in either case a return of capital and not taxable under the provisions of the Income Tax Act.

DATED at the City of Calgary, in the Province of Alberta, this 17th day of May, A.D. 1930, and DELIVERED by H. S. Patterson, K.C., solicitor for the Appellant.

(Sgd.) H. S. PATTERSON,
 Counsel for Appellant.

*In the
 Exchequer
 Court of
 Canada.*

No. 7.
 Statement
 of Claim,
 17th May
 1930—con-
 tinued.

No. 8.

Statement of Defence.

30 Filed on the 28th day of June, 1930.

In reply to the statement of claim herein the Respondent,

(1) Admits paragraphs (1) and (3), but denies all other paragraphs.

AND THE RESPONDENT FURTHER STATES:

(1) That the Appellant was in 1927, and is now a person resident in Canada and liable to tax under the provisions of the said Act.

(2) That the Appellant did on the 28th April, 1928, file an income tax return.

No. 8.
 Statement
 of Defence,
 28th June
 1930.

*In the
Exchequer
Court of
Canada.*

No. 8.
Statement
of Defence,
28th June
1930—*con-
tinued.*

- (3) That the income of the Appellant was duly determined to be in the sum of \$9,570.41, for the taxation period 1927.
- (4) That Notice of Assessment was issued on the 24th September, 1929, assessing the Appellant in respect of the said income in the sum of \$301.07.
- (5) That the income of the Appellant consists of payments made to her by the Vulcan Oil Company Limited arising out of an agreement between the Appellant and the said Company, bearing date of the 15th of April, 1925 (a copy of which now forms part of the record herein).
- (6) That the monies so received in the said year 1927 were not received as capital but as income within the meaning of the said Act and liable for assessment to income tax.

10

THE RESPONDENT THEREFORE CLAIMS :

- (a) That appeal of the Appellant be dismissed;
- (b) That the said assessment should be confirmed;
- (c) Payment of the said sum of \$301.07;
- (d) Interest as provided in the said Act and Amendments;
- (e) The Costs of this appeal;
- (f) Such further and other relief as the nature of the case may require.

DATED at Ottawa the 28th day of June, A.D. 1930.

C. F. ELLIOTT,
Solicitor for Respondent.

No. 9.
Joinder of
Issue,
16th July
1930.

**No. 9.
Joinder of Issue.**

The Appellant joins issue upon the Defendant's Statement of Claim.
DELIVERED the 16th day of July, A.D. 1930.

ALLAN J. FRASER,
31 Citizen Building,
Ottawa, Ont.
Agent for H. S. Patterson, K.C.

H. S. PATTERSON,
Calgary, Alta.
Solicitor for the Appellant.

30

No. 10.

Agreement as to facts agreed upon by Counsel for the parties.

*In the
Exchequer
Court of
Canada.*

1. The Appellant in 1902 purchased from the Canadian Pacific Railway the lands referred to in the hereinafter referred to Agreement along with other lands, the whole for the purpose of conducting ranching operations thereon. The Appellant was not and is not a dealer in or in the business of buying and selling oil lands or leases.
2. The Appellant was in 1927 and is now a resident in Canada.
3. The Respondent determined the income of the Appellant to be in the sum of \$9,570.41, being monies received as "Royalties" under the Agreement hereinafter referred to.
4. Vulcan Oils Limited was and is a Company incorporated on the 13th day of April, 1925, under the laws of the Province of Alberta, organized and operated for the purpose of drilling for and procuring the production and vending of oil.
5. That Vulcan Oils Limited and the Appellant entered into an Agreement dated the 15th day of April, 1925, a true copy of which has been filed with and forms part of the records of this Court.
6. That of the property referred to in the said Agreement the Appellant was the owner in fee simple except as to the coal therein and thereunder.
7. That in accordance with the said Agreement Vulcan Oils Limited entered upon the property as in the Agreement described and commenced the operations of drilling for oil with equipment and in a manner satisfactory to the Appellant.
8. That during the fall of 1926 Vulcan Oils Limited struck oil (as referred to in the contract) "in Commercial quantities on the said lands."
9. A transfer of the petroleum, natural gas or oil has not been effected and the Appellant is still the owner in fee simple of the said lands except as to coal.
10. That due to the mining operations the whole of the oil produced in the year 1927, the year in question, was sold by Vulcan Oils Limited and out of the monies received from the sale of the oil (before the Company deducted expenses or made any reduction therefrom) 1-10th of the gross proceeds were paid over to the Appellant.
11. That the oil produced by Vulcan Oils Limited is not in fact physically divided by the Company nor is it sold in two distinct portions of 90 % and 10 %, but the whole is handled in bulk. Vulcan Oils Limited never in fact delivered any of the actual oil to the Appellant, but has in fact delivered (as per the Agreement), "to the order of the said Vendor the royalties hereby reserved to the Vendor" (the Appellant), the delivery in fact being effected by payment in cash.
12. That the Appellant, or her Agent, has in fact from time to time entered upon and viewed the operations and workings of Vulcan Oils Limited as to the operations of the mining of oil on the property.

No. 10.
Agreement
as to facts
agreed upon
by Counsel
for the
parties.

13. The Appellant upon entering into the said Agreement received the sum of \$5,000.00 in cash and 25,000 shares of Vulcan Oils Limited at a par value of one dollar each, as fully paid up and since the production of oil and the sale thereof has been receiving "royalties" under the contract.

No. 10.
Agreement
as to facts
agreed upon
by Counsel
for the
parties—
continued.

C. F. ELLIOTT.
H. S. PATTERSON.

No. 11.
Formal
Judgment,
23rd Octo-
ber 1930.

**No. 11.
Formal Judgment.**

IN THE EXCHEQUER COURT OF CANADA.

Thursday, the Twenty-third day
of October, A.D. 1930.

PRESENT:

The Honourable Mr. Justice
Audette.

10

IN THE MATTER OF The Income War Tax Act,

AND

IN THE MATTER OF The Appeal of Mrs. Catherine
Spooner, of the City of Calgary, in the Province of
Alberta

- - - - - *Appellant ;*

AND

THE MINISTER OF NATIONAL REVENUE -

- - - - - *Respondent.*

The appeal under the provisions of the Income War Tax Act of the Appellant herein from the decision of the Minister of National Revenue dated the 30th day of November, 1929, confirming the assessment levied on certain moneys received by the Appellant under and by virtue of a certain agreement with Vulcan Oils Limited, for the year ending the 31st of December, 1927, having come on for hearing before this court at the City of Calgary, on the 17th day of September, A.D. 1930, in the presence of counsel both for the Appellant and the Respondent: upon hearing read the statement of facts admitted and upon reading the papers and documents filed with this Court, as required by the said Act, and the pleadings filed, and upon hearing what was alleged by counsel aforesaid:

30

THIS COURT WAS PLEASED TO DIRECT that the said appeal should stand over for judgment, and the same coming on this day for judgment:

THIS COURT DOTH ORDER AND ADJUDGE that the appeal of the Appellant be and the same is hereby dismissed.

AND THIS COURT DOTH FURTHER ORDER AND ADJUDGE that there be no costs of this appeal to either party.

(Sgd.) ARNOLD W. DUCLOS,
Deputy Registrar.

No. 12.

Reasons for Judgment.

*In the
Exchequer
Court of
Canada.*

AUDETTE, J.

Judgment rendered 23rd October, 1930.

This is an appeal, under the provisions of the Income War Tax Act, 1917, and Amendments thereto, from the assessment of the Appellant, for the year 1927, on her income received from the Vulcan Oils Limited, in the nature of ten per cent. royalty of all petroleum, natural gas and oil, under the reservation mentioned in the deed of agreement hereinafter recited.

No. 12.
Reasons for
Judgment.
Audette J.,
23rd Octo-
ber 1930.

10 The question to be determined is whether such royalties are capital or income.

At the opening of the trial the parties filed the following admission of facts which reads as follows :

“ AGREED UPON BY COUNSEL FOR THE PARTIES HERETO.

20 “ 1. The Appellant in 1902 purchased from the Canadian Pacific Railway the lands referred to in the hereinafter referred to Agreement along with other lands, the whole for the purpose of conducting ranching operations thereon. The Appellant was not and is not a dealer in or in the business of buying and selling oil lands or leases.

“ 2. The Appellant was in 1927 and is now a resident in Canada.

“ 3. The Respondent determined the income of the Appellant to be in the sum of \$9,570.41, being monies received as “ Royalties ” under the Agreement hereinafter referred to.

“ 4. Vulcan Oils Limited was and is a Company incorporated on the 13th day of April, 1925, under the laws of the Province of Alberta, organized and operated for the purpose of drilling for and procuring the production and vending of oil.

30 “ 5. That Vulcan Oils Limited and the Appellant entered into an Agreement dated the 15th day of April, 1925, a true copy of which has been filed with and forms part of the records of this Court.

“ 6. That of the property referred to in the said Agreement the Appellant was the owner in fee simple except as to the coal therein and thereunder.

“ 7. That in accordance with the said Agreement Vulcan Oils Limited entered upon the property as in the Agreement described and commenced the operations of drilling for oil with equipment and in a manner satisfactory to the Appellant.

40 “ 8. That during the fall of 1926 Vulcan Oils Limited struck oil (as referred to in the contract) “ in commercial quantities on the said lands.”

“ 9. A transfer of the petroleum, natural gas or oil has not been effected and the Appellant is still the owner in fee simple of the said lands except as to coal.

*In the
Exchequer
Court of
Canada.*

No. 12.
Reasons for
Judgment.
Audette, J.,
23rd Octo-
ber 1930—
continued.

“ 10. That due to the mining operations the whole of the oil produced in the year 1927, the year in question, was sold by Vulcan Oils Limited and out of the monies received from the sale of the oil (before the Company deducted expenses or made any reduction therefrom) 1-10th of the gross proceeds were paid over to the Appellant.

“ 11. That the oil produced by Vulcan Oils Limited is not in fact physically divided by the Company, nor is it sold in two distinct portions of 90% and 10%, but the whole is handled in bulk. Vulcan Oils Limited never in fact delivered any of the actual oil to the Appellant, but has in fact delivered (as per Agreement), “ to the order of the said Vendor the royalties hereby reserved to the Vendor ” (the Appellant), the delivery in fact being effected by payment in cash. 10

“ 12. That the Appellant, or her Agent, has in fact from time to time entered upon and viewed the operations and workings of Vulcan Oils Limited as to the operations of the mining of oil on the property.

“ 13. The Appellant upon entering into the said Agreement received the sum of \$5,000.00 in cash and 25,000 shares of Vulcan Oils Limited at a par value of one dollar each, as fully paid up and since the production of oil and the sale thereof has been receiving “ royalties ” under the contract. 20

This admission is a corrected one substituted for a former one to which was attached an exhibit called transfer of land, and withdrawn from the record.

The deed of agreement (exhibit A) upon which these royalties are paid, reads as follows, viz. :

“ AGREEMENT made in duplicate this Fifteenth day of April, 1925.

BETWEEN :

CATHERINE SPOONER of Vulcan, Alberta,
hereinafter called the “ Vendor,”

OF THE FIRST PART;

AND

VULCAN OILS LIMITED of Vulcan, Alberta,
hereinafter called the “ Company,”

OF THE SECOND PART.

“ WHEREAS the Vendor herein is the owner of the North West Quarter of Section Thirteen (13) Township Twenty (20) Range Three (3) West of the Fifth Meridian, including all mines and minerals thereon or under the said lands. 40

“ WHEREAS the said Catherine Spooner has agreed to sell to the Company herein the South twenty acres of the said Section Thirteen (13) Township twenty (20) Range three (3) West of the

5th Meridian. Subject to the provisos, conditions, restrictions, stipulations and royalties hereinafter reserved.

“NOW THEREFORE THIS INDENTURE WITNESSETH :

“1. That the Vendor hereby sells, assigns, transfers, and sets over unto the Company, its successors and assigns, all her right, title and interest, in and to the following property; namely, the South twenty acres of the North West quarter of Section thirteen (13) Township twenty (20) Range three (3) West of the 5th Meridian, which includes all mines and minerals, on, in or under the said lands. Subject to the provisos, conditions and royalties hereinafter reserved.

10

“2. The Company hereby agrees in consideration of the said sale to it, to pay to the said vendor the sum of Five Thousand (\$5,000.00) dollars in cash upon the execution of this Agreement by the Company, and to issue to the Vendor or her nominee certificates of stock of the Company to the aggregate amount of twenty five thousand shares of the par value of One Dollar each and the said shares shall be deemed to be and are hereby declared to be fully paid shares and not liable to any call thereon, and the holders of such stock shall not be liable to any further payment thereon.

20

“3. The Company hereby further agrees in consideration of the said sale to deliver to the Order of the said Vendor the royalty hereby reserved to the Vendor, namely; ten per cent. of all petroleum, natural gas, and oil, produced and saved from the said lands free of costs to the said Vendor on the said premises. And the said petroleum, natural gas and oil shall be delivered under the instructions and upon the method decided by the Vendor, and the Company further covenants and agrees that it will deliver to the said Vendor the before-mentioned percentage of petroleum, natural gas and oil saved on the said land at least once in every thirty days and will not sell or remove any petroleum, natural gas or oil from the said premises until the said percentage or share thereof belonging to the Vendor shall have been delivered as aforesaid.

30

“4. The Company shall keep or cause to be kept proper books of account at its registered office showing correctly the quantity of petroleum, natural gas, and oil produced from the said lands, and of all oil and gas taken away or removed therefrom and will from time to time on demand produce the said books of account and permit the said Vendor or her attorney or agent to inspect them and take extracts therefrom or copies thereof, and the Company will permit and suffer the Vendor, her attorney or agent at all times to enter upon the said premises for the purposes of inspecting the operations of drilling or pumping and working in any well or wells finished or in the course of construction on the said premises.

40

“5. The Company covenants and agrees with the Vendor that it will proceed forthwith to obtain standard drilling machinery fully

*In the
Exchequer
Court of
Canada.*

—
No. 12.
Reasons for
Judgment.
Audette J.,
23rd October 1930—
continued.

*In the
Exchequer
Court of
Canada.*

No. 12.

Reasons for
Judgment.
Audette J.,
23rd Octo-
ber 1930—
continued.

equipped and will commence drilling operations upon the said lands as expeditiously as possible, and to continue such drilling operations without interruption, except as may be unavoidable until oil and/or gas in commercial quantities is struck or to a minimum depth of 4,500 feet.

“ 6. Upon oil or petroleum being discovered the said Company hereby covenants and agrees to install and properly maintain the necessary machinery for pumping or procuring said oil or petroleum from the well or wells and delivering it in pipes, reservoirs or tanks and the said Company hereby agrees to carry on the operations of pumping or otherwise procuring the said oil or petroleum or gas from the said lands. 10

“ 7. In the event of oil or gas being discovered in commercial quantities on the said lands the Vendor as part of the consideration for this Agreement, covenants to transfer to the said Company by good and sufficient transfer in fee simple the said twenty acres of land freed and discharged from all encumbrances and also shall transfer to the said Company by good and sufficient transfer in fee simple freed and discharged from all encumbrances the South twenty acres of the North West Quarter of Section twenty four (24) Township twenty (20) Range three (3) West of the 5th Meridian, and such transfers shall be completed and delivered forthwith after oil or gas is discovered in commercial quantities by the said Company, reserving always however to the Vendor the said royalty of ten per cent. of all petroleum, natural gas and oil in respect to the said South twenty acres of the N.W. $\frac{1}{4}$ of Section 13, Township 20, Range 3, West of the 5th Meridian, and also free access on and over all said lands described in this paragraph to an extent not exceeding three trails and the location of the said trails shall be selected by the Vendor. 20

“ 8. The Vendor further covenants and agrees with the Company upon the request and at the cost of the Company to execute and do all such further assurances and things as shall reasonably be required by the Company, for vesting in it the property and rights agreed to be hereby sold and giving to it the full benefit of this Agreement. 30

“ 9. It is further declared and agreed that these presents and everything herein contained shall enure to the benefit of and be binding upon the parties hereto, and each of their heirs, executors and administrators and successors and assigns, respectively. 40

IN WITNESS WHEREOF the Party of the First Part has hereunto set her hand and seal, and the Vulcan Oils, Limited has hereunto affixed its corporate seal, attested by the signatures of its proper officers.”

This grant of express liberty to work such property, upon the payment of a fixed sum of money, with the reservation that if oil or petroleum are

discovered in commercial quantities to pay a certain share of the profits derived therefrom, seems to present no ambiguity or difficulty. It is the usual reservation provided in such circumstances.

Reservations of royalties are found in almost all Crown grants; they are also found in most of the C.P.R. land sales. The rights or superiorities of the King thereunder are called royalties. The word royalty reserved to the landlord of mines is also thus called apparently in analogy to such superiorities of the Crown. Brown's Law Dictionary, 470.

10 And this secondary sense or meaning of the word "royalty" signifies in mining leases, that part of the Reddendum clause, whereby certain profit is reserved and which is variable and depends upon the quantity of mineral gotten. Stroud, Judicial Dictionary, 2nd Edition, pp. 1772, 1688.

The word "royalty", as used in a gas lease, generally refers to "a share of the product or profit reserved by the owner for permitting another to use the property". *Indiana Natural Gas & Oil Co. vs. Stewart*.¹ The word "royalty" as employed in coal mining leases means the share of the profit reserved by the owner for permitting the removal of the coal and is in the nature of a rent. *Kissick vs. Bolton*.²

20 The royalty payable under the agreement in question in this case is in the nature of a reservation operating as an exception out of the demise. *The King vs. The Inhabitants of St. Auslett*.³

This royalty, mentioned in the agreement, is a reservation, operating as an exception out of the demise, in favour of the appellant, of the profits derived from the working and development of this land and is in its very nature income and could not amount, in any sense, to capital. It is quite variable in quantities and is taxable as income under the Act. See 11 Hals. 219. See also 20 Hals. 559, 560.

30 *Edmonds vs. Eastwood*;⁴ *Commissioner of Inland Revenue vs. Marine Turbine Co.*;⁵ *Commissioner of Inland Revenue vs. Sangster*;⁶ The reservation of ten per cent. in the agreement was never sold and never passed out of the hands of the appellant.

The oil and gas having been discovered in commercial quantities the \$5,000·00 and the \$25,000·00 of paid up shares having been duly satisfied and moreover the royalties having already been paid the appellant is now bound by clause 8 of the agreement, exhibit A, which says: "8. The Vendor further covenants and agrees with the Company upon the request and at the cost of the Company to execute and do all such further assurances and things as shall reasonably be required by the Company, for vesting in it the property and rights agreed to be hereby
40 sold and giving to it the full benefit of this Agreement."

The facts and circumstances of the case having brought us to the time when oil and gas have been found in Commercial quantities and when the royalties became payable, we have gone beyond the speculative questions

*In the
Exchequer
Court of
Canada.*

No. 12.
Reasons for
Judgment.
Audette J.,
23rd Octo-
ber 1930—
continued.

¹ 90 N.E. 384, 386; 45 Ind. App. 554.

² 112 N.W., 95, 96, 134, Iowa, 652.

³ 5 Barnewall & Alderson, 693 (1821-22).

⁴ 2 Hurlston & Normand 811.

⁵ (1920) 1 K. B. 193.

⁶ (1920) 1 K. B. 587.

*In the
Exchequer
Court of
Canada.*

No. 12.
Reasons for
Judgment.
Audette J.,
23rd Octo-
ber 1930—
continued.

and conjectures discussed at trial as to what would be the effect of the agreement before that time.

I, therefore, find the appellant is liable for income tax on the royalty; but before rendering account for the amount of the tax collectible, the statutory allowance for depletion or depreciation (section 5) must be ascertained and deducted. By doing so the amount of the claim by the Crown in the case will be reduced by crediting that amount to the appellant and under such circumstances there will be no costs to either party.

There will be judgment dismissing the appeal, each party paying his own costs. 10

*In the
Supreme
Court of
Canada.*

No. 13.
Order
granting
leave to
appeal to
Supreme
Court of
Canada,
14th Nov-
ember 1930.

No. 13.

Order granting leave to appeal to Supreme Court of Canada.

IN THE SUPREME COURT OF CANADA.

Before the Honourable Mr. Justice
Lamont in Chambers.

Friday, the 14th day of
November, A.D. 1930.

IN THE MATTER OF The Income War Tax Act.

BETWEEN :

MRS. CATHERINE SPOONER - - - (*Appellant*) *Appellant* ;

AND

THE MINISTER OF NATIONAL REVENUE

(*Respondent*) *Respondent*.

20

Upon the application of the above-named Appellant, upon reading the Affidavit of the Appellant filed and upon hearing what was alleged by Counsel for the Appellant and the Respondent.

IT IS ORDERED that Catherine Spooner, the above-named Appellant be allowed to appeal to the Supreme Court of Canada from the judgment in this cause delivered by the Honourable Mr. Justice Audette in the Exchequer Court of Canada, on the 23rd day of October, A.D. 1930.

30

AND IT IS FURTHER ORDERED that the costs of this application be costs in the cause.

J. H. LAMONT, J.

No. 14.
Notice of Appeal.

*In the
Supreme
Court of
Canada.*

TAKE NOTICE that the above-named Appellant intends to appeal and does hereby appeal to the Supreme Court of Canada from the judgment in this cause delivered by the Honourable Mr. Justice Audette, on the 23rd day of October, A.D. 1930, dismissing the Appeal of the above-named Appellant from the decision of the Minister of National Revenue, dated the 30th day of November, A.D. 1929.

No. 14.
Notice of
Appeal,
15th Nov-
ember 1930.

DATED at Ottawa this 15th day of November, A.D. 1930.

10

ALLAN J. FRASER,
Solicitor for the Appellant.

No. 15.

Order dispensing with printing of certain documents.

No. 15.
Order
dispensing
with
printing of
certain
documents,
5th January
1931.

IN THE SUPREME COURT OF CANADA.

Before the Registrar }
in Chambers. }

Monday, the Fifth day of January,
1931.

BETWEEN :

CATHERINE SPOONER - - - - (*Appellant*) *Appellant* ;
AND

20

THE MINISTER OF NATIONAL REVENUE
(*Respondent*) *Respondent*.

Upon the application of the Appellant, upon hearing read the affidavit of Allan Joseph Fraser filed, and upon hearing Counsel for the Appellant and the Respondent.

It is ordered that the printing of documents (a) and (b) being the Income Tax Return of the taxpayer for the year 1927 and The Notice of Assessment appealed from respectively, and that portion of document (e) being the portion entitled Recapitulation of Facts and a copy of an agreement entered into between the Appellant and Vulcan Oils Limited attached thereto all of which documents are included in the Certificate filed by the Minister of National Revenue, be and the same is hereby dispensed with.

30

And It Is Further Ordered that ten copies of the said documents (a) and (b) be filed for the use of the Court.

And It is Further Ordered that the costs of and incidental to this application be costs in the appeal.

J. F. SMELLIE,
Registrar.

*In the
Supreme
Court of
Canada.*

No. 16.

Agreement as to contents of Appeal Book.

No. 16.
Agreement
as to con-
tents of
Appeal
Book,
5th January
1931.

1. Statement of Case.
2. Certificate and the following documents filed by the Minister of National Revenue :—
 - (a) The Income Tax Return of the taxpayer for the year 1927.
 - (b) The Notice of Assessment appealed from.
 - (c) The Notice of Appeal.
 - (d) The Decision of the Minister.
 - (e) The Notice of Dissatisfaction. 10
 - (f) The Reply of the Minister.
3. Order that Pleadings be filed.
4. Pleadings.
5. Statement of Facts agreed upon by Counsel for the parties hereto.
6. Exhibits.
7. Notice of Appeal.
8. Judgment.
9. Reasons for Judgment.
10. Order granting leave to appeal.
11. Order dispensing with printing of certain Exhibits. 20
12. Agreement as to contents of case.
13. Certificate of the Registrar.

DATED the 5th day of January, A.D. 1931.

ALLAN J. FRASER,
Agent for Appellant's Solicitor.
C. F. ELLIOTT,
Solicitor for Respondent.

No. 17.

No. 17.

Certificate as to Correctness of Case, 12th January, 1931.

(Not printed.)

30

No. 18.

No. 18.

Certificate of Registrar verifying Case, 13th January, 1931.

(Not printed.)

No. 19.

Factum of the Minister of National Revenue.

*In the
Supreme
Court of
Canada.*

No. 19.
Factum of
the Minister
of National
Revenue.

This is an appeal instituted by the appellant from the judgment of the Honourable Mr. Justice Audette. The judgment affirmed the assessment made against the appellant upon monies received by her as "royalties" arising out of a certain agreement made by her with Vulcan Oils Limited.

The pertinent facts of this agreement are as follows:—

10 " 1. That the vendor hereby sells . . . to the company . . . all her right, title and interest, in and to the following property (property described) which includes all mines and minerals, on, in or under the said lands. Subject to the provisos, conditions and royalties hereinafter reserved.

" 3. The company hereby further agrees in consideration of the said sale to deliver to the order of the said vendor the royalty hereby reserved to the vendor, namely: ten per cent. of all the petroleum, natural gas and oil, produced and saved from the said lands free of costs to the said vendor on the said premises. . . .

20 " 7. In the event of oil or gas being discovered in commercial quantities on the said lands the vendor . . . covenants to transfer to the said company by good and sufficient transfer in fee simple the said . . . land freed and discharged from all encumbrances . . . and such transfers shall be completed and delivered forthwith after oil or gas is discovered in commercial quantities by the said company, reserving always however to the vendor the said royalty of ten per cent. of all petroleum, natural gas and oil . . ."

At the trial Counsel for both parties agreed on certain facts (Record p. 15), the most important of which are as follows:—

That the appellant was in 1927 and is now a resident of Canada;

30 That the property referred to in the agreement was and still is owned in fee simple by the appellant;

That the Vulcan Oils Limited carried on operations for the drilling of oil with equipment and in a manner satisfactory to the appellant (Agreement, paragraphs 3, 4, 5 and 6—Record p. 15) and in 1926 struck oil in commercial quantities on the said land and continued like operations and production during 1927;

40 That the oil produced by Vulcan Oils Limited was sold in bulk for cash and ten per cent. thereof was paid, as per the agreement, "to the order of the said vendor (the appellant) the royalties hereby reserved to the vendor" (Record p. 4, line 10).

The Appellant received "royalties" of \$9,570.41 in cash. (See agreement as to facts, Record p. 15, line 10.)

*In the
Supreme
Court of
Canada.*

STATUTE LAW APPLICABLE.

No. 19.
Factum of
the Minister
of National
Revenue—
continued.

In view of the fact that the Revised Statutes of Canada in which the Income Tax Act is consolidated as Chapter 97 did not come into force until February of 1928, the law dealing with the facts herein is that of the Act as originally enacted (Statutes of 1917, Chapter 28) and subsequent amendments. The subsequent amendments are not of importance to the decision of this case, with the exception of the amendment of 1924, Chapter 46, Section 3, inasmuch as in Section 3 the word "royalty" is there directly mentioned, showing that non-residents who receive "royalty" are receiving "income" within the meaning of the Act and are to pay tax thereon even though non-resident. In *Pope Appliances Corporation Limited v. Minister of Customs and Excise*¹ Maclean, J. stated :— 10

"These payments are clearly income within the statute."
They are "not a capital sum but a sum dependent on the volume of paper produced and which would vary according to market demand and other factors."

POINTS AT ISSUE.

The Appellant upon this appeal contends that the monies received as "royalties" under the agreement do not constitute "income" within the meaning of the Income War Tax Act, but rather, that the monies are part of the purchase price of the land and are therefore in the nature of a return of capital and consequently not liable to taxation under the provisions of the said Act. 20

The respondent contends that the \$9,570.41 received under the terms of the contract is "income" within the meaning of the Act, received either as "royalties" or as a share of oil produced and sold by mining, drilling and marketing operations and fluctuates according to the mining and drilling operations and the quantities and qualities of oil produced from the ground with the combined use of skill, labour, material and capital.

ARGUMENT.

"Income" is defined as follows: (Section 3, Chapter 28, Statutes of 1917) 30

"3. (1) For the purposes of this Act, 'income' means the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling,

¹ 1927 Ex. Ct. Rpts. p. 17, at p. 20.

directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be; . . . and also the annual profit or gain from any other source; . . .

*In the
Supreme
Court of
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(a) . . . and the Minister, when determining the income derived from mining and from oil and gas wells, shall make an allowance for the exhaustion of the mines and wells."

No. 19.
Factum of
the Minister
of National
Revenue—
continued.

10 These "royalties" or percentage of profits contingent upon mining operations are "annual net profit or gain" within the definition—a profit "from any other source."

ENGLISH CASES.

In the English case of *Jones v. Commissioners of Inland Revenue*¹ (referred to by Maclean, J. in his judgment, supra p. 3, line 32) the appellant Jones sold his interest in certain inventions and letters patent for a sum in cash and a percentage, called a royalty, payable for ten years on the sale of all machinery constructed under the patent. At p. 714 Rowlatt, J. says:—

20 "In each case regard must be had to what the sum is. A man may sell his property for a sum which is to be paid in instalments, and when that is the case the payments to him are not income: *Foley v. Fletcher*.² Or a man may sell his property for an annuity. In that case the Income Tax Act applies. Again, a man may sell his property for what looks like an annuity, but which can be seen to be not a transmutation of a principal sum into an annuity but is in fact a principal sum, payment of which is being spread over a period and is being paid with interest calculated in a way familiar to actuaries—in such a case income tax is not payable on what is really capital: *Secretary of State for India v. Scoble*.³ On the other
30 hand, a man may sell his property nakedly for a share of the profits of the business. In that case the share of the profits of the business would be the price, but it would bear the character of income in the vendor's hands. *Chadwick v. Pearl Life Assurance Co.*⁴ was a case of that kind. In such a case the man bargains to have, not a capital sum but an income secured to him, namely, an income corresponding to the rent which he had before. I think therefore that what I have to do is to see what the sum payable in this case really is. The ascertainment of an antecedent debt is not the only thing that governs, although in many cases it is a very valuable
40 guide. In this case there is no difficulty in seeing what was intended. The property was sold for a certain sum, and in addition the vendor took an annual sum which was dependent upon the volume of

¹ (1920) 1 K.B. 711 @ 714; 7 T.C. 310 @ 314.

² (1858) 3 H. & N. 769.

³ (1903) A.C. 299.

⁴ (1905) 2 K.B. 507-514.

*In the
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Court of
Canada.*

business done, that is to say, he took something which rose or fell with the chances of the business. When a man does that he takes an income; it is in the nature of income, and on that ground I decide this case."

No. 19.
Factum of
the Minister
of National
Revenue—
continued.

In the present case the appellant received a certain consideration upon signing the agreement, that is \$5,000 in cash and 25,000 shares in the Vulcan Oils Limited (Record p. 4, line 6). In addition thereto she secured to herself an income from the lands, variable in proportion to the amount of oil produced and sold. In other words, she secured to herself an annual net profit or gain which fluctuates according to the quantity and quality of oil gained from the soil by the operations of the company, *i.e.*, she has secured to herself an income out of the gross profits of the business of the company. 10

It is submitted that the principle involved in the present case is identical with the decision given by Rowlatt, J. in the case of *Jones v. Commissioners of Inland Revenue (supra)* and the decision in *Constantinesio v. Rex*¹ which went to the House of Lords.

Royalties on output of mines, oil and gas wells are really in the nature of true rent and may be distrained for, which is a characteristic of rent subject to agreement. (See *Daniel v. Gracie*;² *Black v. F. C. of T.*;³ *Apperley v. F. C. of T.*;⁴ *Attorney-General of Ontario v. Mercer*⁵) and consequently would be income derived from such property. 20

In *Akers v. Commissioner of Taxes*⁶ the appellant granted a right to cut flax on his land in consideration of a royalty of 10/ per ton. The contract was oral and there were no special terms. The appellant endeavoured to bring himself under an exemption clause of the Income Tax Act as being profits "derived from the direct use or cultivation of land." It was held that he was not entitled to the exemption but that the royalty was taxable. The decision of the Court in the first instance was confirmed by the Supreme Court. 30

UNITED STATES CASES.

The Supreme Court of the United States has construed similar agreements on cases arising under the Federal Corporation Tax Act.⁷ The Supreme Court of the United States has steadfastly declined to consider "royalties" as a conversion of capital assets. The Court holds they are "income."

In *Stratton's Independence v. Howbert*⁸ the taxpayer sought to recover a tax paid, claiming that its gold mining operations simply converted

¹ 11 T.C. 730 @ 739.

² 6 Q.B.D. 145.

³ (1920) 27 C.L.R. 483 (Australia).

⁴ (1914) 17 C.L.R. 535 @ 546.

⁵ 8 A.C. 767 c. 777-778.

⁶ (1926) Gaz. L.R. 259 (N.Z.).

⁷ 36 U.S. Stat. 1, c. 6, p. 112.

⁸ 231 U.S. 399.

capital represented by real estate into capital represented by cash. That the ore mined resulted in a waste of the estate, but the Court said (p. 417).

“ We have no difficulty in concluding that the proceeds of ores mined by a corporation from its own premises are to be taken as a part of the gross income of such corporation.”

In *Von Baumbach v. Sargent Land Company*¹ a taxpayer leased to others large tracts of land for mining purposes, reserving to himself “ royalties.” In the lower Courts these “ royalties ” were held to be mere conversions of capital. The Supreme Court of the United States in reversing
10 the decision of the lower Courts said :—

“ We think that the payments made by the lessees to the corporations now before the court were not in substance the proceeds of an outright sale of a mining property, but, in view of the terms of these instruments were in fact rents or royalties to be paid upon entering into the premises and discovering, developing and removing the mineral resources thereof, and as such must be held now as then, to come fairly within the term income as intended to be reached and taxed under the terms of the Corporation Tax Act.”

In the present case Vulcan Oils Limited entered upon the land for the
20 purpose of discovering, developing and removing the mineral resources thereof and if mineral in commercial quantities were discovered they might call for a transfer in fee and if in equity this were presumed to have been done then the situation might be likened to a partnership where the appellant supplies one portion of the capital and the Vulcan Oils Limited supplies the skill, and machinery, the combination producing oil and the division of profits concluded on the terms of the agreement. On the other
30 hand the fee not having been transferred the appellant is still the owner and she merely grants a right to Vulcan Oils Limited to enter upon the property with machinery and skilled workmen and drill for oil under the terms of the agreement whereby she is to receive one-tenth of the proceeds. This latter appears to be on the facts the more accurate interpretation inasmuch as there is reserved to the appellant the right to inspect “ the operations of drilling or pumping in any well or wells finished or in the course of construction on the said premises,” that the company are to obtain standard drilling machinery fully equipped and will “ commence drilling operations upon the said lands as expeditiously as possible ” and upon oil being discovered the company “ covenants to install and maintain the necessary machinery for pumping and procuring oil from the wells and delivering it in pipes, reservoirs or tanks ” and the company shall keep
40 proper books of account showing correctly the quantity of oil produced and will permit the appellant or her agent to inspect them and take extracts therefrom and will permit the appellant “ at all times to enter upon the said premises for the purpose of inspecting the operations of drilling and pumping and working in any well finished or in the course of construction.”

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Court of
Canada.*

—
No. 19.
Factum of
the Minister
of National
Revenue—
continued.

¹ 242 U.S. 503.

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Factum of
the Minister
of National
Revenue—
continued.

Whichever way the matter is regarded it is obviously the result of a combined use of skill, capital and labour that produces the very thing that is sold as a recognized commercial commodity and thereby creates an income to the parties concerned.

Decisions of the Supreme Court of the United States carrying out the foregoing are as follows: *U.S. v. Biwabik Mining Company*;¹ *Stanton v. Baltic Mining Company*;² the interesting and important case of *Kate W. Rosenberger v. Blakely D. McCaughn*³ where notwithstanding the State law held the lease to be a sale of ore in place, under the Federal law the royalty payments were held to constitute income.

For a comprehensive summing up of the law, both State and Federal, the recent case of *A. C. Alexander, Collector of Internal Revenue v. Helene Walker King*, decided by the United States Circuit Court of Appeals, 10th Circuit, on the 2nd January, 1931 (not yet reported), should be read. It is submitted that it is exactly in point, and conforms not only to the decisions of the Supreme Court of the United States and relies upon them, some of which are referred to above, but shows that other States of the United States are likewise concluding that royalties under conditions similar to the royalties arising in the present case under consideration are always treated as income.

As to the right of landowners to oil and gas underneath the land they own, on account of the vagrant and fugitive nature of the substances, constituting a sort of subterranean *ferae naturae*, they have no absolute right of title to the oil or gas which might permeate the strata underlying their land, as in the case of coal or other solid minerals fixed in, and forming a part of the soil itself, but with respect to such oil and gas they have certain rights which might be designated as a qualified ownership thereof but which may be more accurately stated as an exclusive right to erect structures on the surface of their land and explore therefor by drilling wells through the underlying strata and to take therefrom and reduce to possession, and thus acquire absolute title as personal property to such as might be found and obtained thereby. This right is the proper subject of sale and may be granted or reserved. The right so granted or reserved, and held separate and apart from the possession of the land itself, is an incorporeal hereditament, or more specifically, a *profit a prendre*.

Turning then to the rights granted under the contract under consideration, it seems that there was granted the exclusive right to take all the oil and gas that could be found by drilling wells upon the particular tract of land and for the enjoyment of the principal right to extract oil and gas therefrom. No more nor greater right, except perhaps as to duration, with respect to oil and gas could be granted and even though there had been a purported conveyance of all the oil and gas in place, yet by reason of the nature of these substances, no title thereto or estate therein would have vested but only the right to search for and reduce to possession such as

¹ 247 U.S. 116; 38 S.C.T. 462.

² 240 U.S. 103; 36 S.C. 278.

³ 25 Fed. (2d) 699.

might be found; and when reduced to possession, not merely discovered, title thereto and an estate therein as corporeal property would vest.

The ordinary and legal meaning of the word "royalty" as applied to an existing oil and gas lease is the compensation provided in the lease for the privilege of drilling and producing oil and gas, and consists of a share in the oil and gas produced. It does not include a perpetual interest in the oil and gas in the ground.

In the result, therefore, it is clear that both the British Courts and Supreme Court of the United States have established a rule that the royalties derived from mining operations do not arise from a conversion of capital assets but are "income."

Under the instrument here in question in the present case the monies derived from oil mining and paid to the appellant herein were not converted capital but were royalties or rents and as such income properly included in measuring the tax payable under the Dominion Income Tax Act and the judgment of the Court below should accordingly be sustained.

C. F. ELLIOTT,
Counsel for the Respondent.

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Supreme
Court of
Canada.*

No. 19.
Factum of
the Minister
of National
Revenue—
continued.

No. 20.

Factum of Catherine Spooner.

This is an appeal from a Judgment of the Exchequer Court (reported in 1930 Ex. C. R. page 229) dismissing an appeal from the assessment under the Income War Tax Act 1917 of the Appellant for the year 1927 on certain moneys received from Vulcan Oils Limited under the reservation in the agreement printed at pp. 3 to 6. The question at issue is whether said moneys are taxable under the Act.

The appeal was heard at Calgary on the 17th day of September 1930, by Mr. Justice Audette. The learned Judge took time to consider and on the 23rd day of October, 1930, gave Judgment dismissing the appeal. The reasons for Judgment are given at pp. 17 to 22. The Formal Judgment as entered on the 20th day of November, 1930, is printed at page 16.

No. 20.
Factum of
Catherine
Spooner.

PART I.—STATEMENT OF FACTS.

The Appellant in 1902 purchased certain lands from the Canadian Pacific Railway for ranching purposes. In 1927, she sold twenty acres of these lands to Vulcan Oils Limited (hereinafter referred to as the Company), for the purpose of drilling thereon for oil the sale being "subject to the provisos, conditions and royalties hereinafter reserved." (Page 4, lines 4 and 5).

The Company agreed in consideration of the sale "to deliver to the order of the Vendor the royalty hereby reserved to the Vendor, namely;

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ten per cent. of all the petroleum, natural gas and oil produced and saved from the said lands free of costs to the said Vendor on the said premises.” (Page 4, line 15) such delivery to be made “under the instructions and upon the method decided by the Vendor.” (Page 4, line 19) “at least once in every thirty days.” (Page 4, line 23).

The Company covenanted not to “sell or remove any petroleum, natural gas or oil from the said premises until the said percentage or share thereof belonging to the Vendor shall have been delivered as aforesaid.” (Page 4, lines 23 to 26).

The covenant for transfer contained the following expression : “Reserving always however to the Vendor the said Royalty of ten per cent of all petroleum, natural gas and oil in respect of the said south twenty acres of the North West Quarter of Section 13 Township 20 Range 3 West of the Fifth Meridian and also full access on and over all said lands described in this paragraph to an extent not exceeding three trails.” (Page 5, lines 14 to 19). 10

The Company struck oil in commercial quantities and has made deliveries of ten per cent. of the gross production, said deliveries being effected by payment in cash.

It is admitted that the appellant is not a dealer in, or in the business of buying and selling, oil lands and leases. (Page 15, lines 6 and 7). See Par. 1 of Admission of Facts. 20

PART II.—JUDGMENT.

The learned Judge states that the Company is to pay a certain share of the profits derived from the lands. (Page 21, lines 1 to 3).

It is submitted that the Appellant receives not profits but a portion of the petroleum, natural gas and oil which has been her property since 1902.

Again on page 21, lines 22 to 25 the learned Judge says “This royalty, mentioned in the agreement, is a reservation, operating as an exception out of the demise, in favour of the appellant, of the profits derived from the working and development of this land and is in its very nature income and could not amount, in any sense, to capital.” 30

It is submitted that the appellant is in no sense sharing with the Company the profits made from the operations. Her portion is a fixed one and is deliverable whether profits are made or otherwise.

2. The distinction between a lease and a sale must be kept in mind. Under a lease the lessor at the end of the term receives the reversion and is entitled to allowance for depletion. When production is exhausted the lessor will have been allowed exemption to the amount of the original value of the property or in other words to the capital value; no tax being payable on capital. On a sale there is no reversion and whatever the vendor receives is a return of capital and is not taxable. Under a lease the Lessor may ultimately receive capital plus profits. Under a sale the Vendor receives capital only. 40

PART III.—ARGUMENT.

1. The Appellant not being in the business of buying and selling oil lands is not liable to taxation on a profit realized from the sale of a capital asset. She sold the land as land owner not as trader. This principle was laid down by Lord Dunedin in *Commissioner of Taxes vs. Melbourne Trust, Limited*, 1914 A. C. 1001 as follows :

10 “ It is quite a well settled principle, in dealing with questions of income tax, that where the owner of an ordinary investment chooses to realize it and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D. of the Income Tax Act of 1842 assessable to income tax, but it is equally well established that enhanced values obtained from realization or conversion of securities may be so assessable where what has happened is not merely a realization or change of investments but an act done in what is truly the carrying on or carrying out of a business.”

See also *Anderson Logging Company vs. the King* 1925 S. C. R. 45; 1926 A. C. 140.

20 *California Copper Syndicate vs. Harris* 47 Sc. L. R. 86; 5 Tax Cas. 159. *Collins v. Firth-Brearley Stainless Steel Syndicate Limited*, 9 Tax Cas. 520, 654.

The Rees Roturbo Development Syndicate Limited v. Ducker, 1928, 1 K. B. 506; 13 Tax Cas. 366; 1928 A. C. 132.

Roberts v. Lord Belhaven's Executors 1925 Sc. L. T. 466; 9 Tax Cas. 501. *U. S. v. Nipissing Mines Limited*, 206 Fed. 431.

Von Baumach v. Sargent Land Company, 242 U. S. 503, 516.

An interesting application of the principle is found in *Stevens vs. Hudson's Bay Company* (1909) 101 L. T. 96; 5 Tax Cas. 402.

2. The agreement in question may be interpreted as being :

- 30 (a) A sale of twenty acres of oil lands for a consideration of \$5,000.00, 25,000 shares and one-tenth of production or,
 (b) A sale of twenty acres of oil lands for \$5,000.00 in cash and 25,000 shares with a reservation to the Vendor of one-tenth of the production.

3. If the first alternative is the correct interpretation the following submissions are made :

40 (a) The one-tenth of production which the company is to deliver is a part of the consideration for the sale and is not distinguishable in principle from the money and the shares which it is admitted are not taxable.

(b) Whatever passes from a purchaser to a vendor must irrespective of form be the consideration the purchaser gives for the

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continued.

land and from the standpoint of the vendor a conversion of the capital from one form to another.

(c) "Royalties" may be construed as being a part of purchase price.

Commissioners of Inland Revenue vs. Marine Steam Turbine Company 1920, 1 K. B. 193; 12 Tax Cas. 174;

Commissioners of Inland Revenue vs. Sangster 1920, 1 K. B. 587; 12 Tax Cas. 208.

(d) A consideration of the difficulty of arriving at the value of oil lands indicates the desirability of some method similar to that adopted in the present case. The actual value can only be determined by drilling and both vendor and purchaser desire that the price paid shall bear some relation to the actual production. 10

4. If on the other hand the agreement should be interpreted as a sale of twenty acres of land for \$5,000.00 and 25,000 shares with a reservation to the Vendor of one tenth of production the following submissions are made:

(a) The portion reserved is a part of the capital which the Appellant has owned since 1902.

(b) If the reservation had not been made the purchase price would have been increased and the reservation may therefore be regarded as a substitution for a portion of the purchase price, and it is admitted on this alternative that the purchase price (\$5,000.00 and 25,000 shares) is not taxable. 20

H. S. PATTERSON,
Solicitor for the Appellant.

January 8th, 1931.
Calgary, Alberta.

No. 21.

Formal Judgment.

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IN THE SUPREME COURT OF CANADA.

Tuesday, the twenty-eighth day of April, A.D. 1931.

Present :

The Honourable Mr. Justice NEWCOMBE, C.M.G.,
The Honourable Mr. Justice RINFRET,
The Honourable Mr. Justice LAMONT,
The Honourable Mr. Justice CANNON.

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- 10 The Right Honourable Mr. Justice DUFF being absent, his Judgment was announced by The Right Honourable THE CHIEF JUSTICE, pursuant to the statute in that behalf.

IN THE MATTER of The Income War Tax Act,

AND

IN THE MATTER of the Appeal of Mrs. Catherine Spooner,
of the City of Calgary, in the Province of Alberta.

BETWEEN :

MRS. CATHERINE SPOONER - - - (*Appellant*) *Appellant*

AND

- 20 THE MINISTER OF NATIONAL REVENUE (*Respondent*) *Respondent*.

The appeal of the above-named appellant from the judgment of the Exchequer Court of Canada, pronounced in the above cause on the 23rd day of October, in the year of our Lord one thousand nine hundred and thirty, confirming the assessment levied by the respondent on certain moneys received for the year ending the 31st day of December, A.D. 1927, from Vulcan Oils Limited, under and by virtue of a certain agreement dated the 15th day of April, A.D. 1925, entered into between the said appellant and the said Vulcan Oils Limited, having come on to be heard before this Court on the 5th and 6th days of February, in the year of our Lord one
30 thousand nine hundred and thirty-one, in the presence of Counsel as well for the Appellant as the Respondent, whereupon and upon hearing what was alleged by Counsel aforesaid, this Court was pleased to direct that the said appeal should stand over for judgment, and the same coming on this day for judgment this Court did order and adjudge that the said appeal should be and the same was allowed; that the said judgment of the Exchequer Court of Canada should be and the same was reversed and set aside; and that the assessment levied by the Respondent on certain moneys received by the

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Appellant for the year ending the 31st day of December, A.D. 1927, from Vulcan Oils Limited, under and by virtue of a certain agreement dated the 15th day of April, A.D. 1925, entered into between the said Appellant and the said Vulcan Oils Limited, should be and the same was set aside.

And this Court did further order and adjudge that the said Respondent should and do pay to the said Appellant the costs incurred by the said Appellant as well in the said Exchequer Court of Canada as in this Court.

(Signed) J. F. SMELLIE,

Registrar.

No. 22.
Reasons for
Judgment,
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J. (con-
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by Duff,
Rinfret,
Lamont and
Cannon
JJ.).

No. 22.

10

Reasons for Judgment.

NEWCOMBE, J. (concurrent in by DUFF, RINFRET, LAMONT and CANNON, JJ).

This is a tax appeal, depending upon the meaning and application of the Income War Tax Act, c. 28 of 1917, as amended.

The case came before Audette, J., of the Exchequer Court of Canada, upon appeal from the decision of the Minister of National Revenue, and was heard upon admissions.

By agreement under seal of 15th April, 1925, the appellant, therein called the vendor, of the first part, who was then the owner in fee simple of the lands to which the agreement relates, agreed with Vulcan Oils, Limited, therein called the company of the second part, upon the recital that the appellant had agreed to sell to the company the land described as follows, that 20

“The Vendor hereby sells, assigns, transfers and sets over unto the Company, its successors and assigns, all her right, title and interest, in and to the following property; namely, the South twenty acres of the North West quarter of Section Thirteen (13) Township Twenty (20) Range Three (3) West of the Fifth Meridian, which includes all mines and minerals, on, in or under the said lands. Subject to the provisos, conditions and royalties hereinafter reserved.” 30

The company, in consideration of the sale, agreed to pay to the vendor the sum of \$5,000.00 in cash, upon the execution of the agreement by the company, and to issue to the vendor, or her nominee, 25,000 shares of the company's capital stock of the par value of \$1.00 each, fully paid up.

And, by clause 3, it is stipulated that

“The Company hereby further agrees in consideration of the said sale to deliver to the order of the said Vendor the royalty hereby reserved to the Vendor, namely: ten per cent. of all the petroleum, natural gas, and oil, produced and saved from the said lands free 40

of costs to the said Vendor on the said premises. And the said petroleum, natural gas and oil shall be delivered under the instructions and upon the method decided by the Vendor, and the Company further covenants and agrees that it will deliver to the said Vendor the before-mentioned percentage of petroleum, natural gas and oil saved on the said land at least once in every thirty days and will not sell or remove any petroleum, natural gas or oil from the said premises until the said percentage or share thereof belonging to the Vendor shall have been delivered as aforesaid."

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10 By clause 5, the company covenanted to proceed forthwith to obtain standard drilling machinery, fully equipped; to commence drilling operations upon the lands as expeditiously as possible, "and to continue such drilling operations without interruption, except as may be unavoidable, until oil and/or gas in commercial quantities is struck, or to a minimum depth of 4,500 feet."

By clause 6, the company covenanted, upon oil or petroleum being discovered, to instal and maintain the necessary machinery for pumping or procuring and delivering the oil or petroleum in pipes, reservoirs or tanks, and to carry on the operations.

20 Clause 7 reads as follows :

"In the event of oil or gas being discovered in commercial quantities on the said lands the Vendor, as part of the consideration for this Agreement, covenants to transfer to the said Company by good and sufficient transfer in fee simple the said twenty acres of land freed and discharged from all encumbrances and also shall transfer to the said Company by good and sufficient transfer in fee simple freed and discharged from all encumbrances the South twenty acres of the North West Quarter of Section twenty-four (24) Township twenty (20) Range three (3) West of the 5th Meridian and such transfers shall be completed and delivered forthwith after
30 oil or gas is discovered in commercial quantities by the said Company, reserving always however to the Vendor the said royalty of ten per cent. of all petroleum, natural gas and oil in respect to the said South twenty acres of the N.W. $\frac{1}{4}$ of Section 13, Township 20, Range 3, West of the 5th Meridian and also free access on and over all said lands described in this paragraph to an extent not exceeding three trails and the location of the said trails shall be selected by the Vendor."

40 It will be observed that clause 3, quoted above, by which, as well as by clause 7, the royalty is said to be reserved, introduces a covenant, on the part of the company, by way of further consideration for the sale; and that the company thereby agrees to deliver to the vendor, on the premises, ten per cent. of the petroleum, natural gas and oil produced and saved from the lands sold, free of cost to the vendor; the delivery to be made at least once in every thirty days; and this suggests a question as to whether the

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consideration or so-called royalty, which consists of ten per cent. of the minerals recovered, is validly reserved; for, it is said in Sheppard's *Touchstone*, (80), para. 10 :

“ If a man grant land, yielding or paying money or some such like thing (as a rose, a pound of cummin, &c.) yearly, (or at any other period), this is a good reservation. But if the grantee covenant to pay such a sum of money, or to do such a thing yearly, this is no good reservation, but a covenant to pay a sum of money in gross, and not as a rent, (but whether a clause shall amount to a reservation, or to a covenant, is frequently a question of construction).”

10

One is concerned to know whether the appellant has acquired that which is taxable as income; and, for the purposes of the Act, “ income,” as defined by the relevant provisions of Section 3 (1), means

“ The annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary, or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be; and shall include the interest, dividends or profits directly or indirectly received from money at interest upon any security or without security, or from stocks, or from any other investment, and, whether such gains or profits are divided or distributed or not, and also the annual profit or gain from any other source, with the following exemptions and deductions :—

20

(a) such reasonable allowances as may be allowed by the Minister for depreciation, or for any expenditure of a capital nature for renewals, or for the development of a business, and the Minister, when determining the income derived from mining and from oil and gas wells, shall make an allowance for the exhaustion of the mines and wells;”

30

* * * * *

Now it is clear that one-tenth of the petroleum, gas and natural oil produced from the lands sold is not profit in the hands of the company, which is at the expense of producing it and is bound to give it to the appellant, and, so far as we know, the company did not otherwise make any profit or gain. Also as the appellant has no reversion, and receives one-tenth of the specified minerals as part of the consideration of the sale of the inheritance, it is most unlikely that Parliament intended to include the appellant's tenth as income, within the meaning of paragraph (a) of section 3, above quoted. Why should a vendor have an allowance for the exhaustion of that which he has sold and been paid for? The definition clause must be interpreted in the light of section 36 of the General

40

Interpretation Act, R.S.C., 1927, c. 1, which was in force long before the enactment of the Income War Tax Act, 1917, and it provides that—

“Definitions or rules of interpretation contained in any Act unless the contrary intention appears, apply to the construction of the sections of the Act which contain those definitions or rules of interpretation, as well as to the other provisions of the Act.”

10 And thus, it follows that the word “income” in the first line of section 3 (1) of the Income War Tax Act, 1917, and the same word in clause (a) of that subsection are controlled by the same statutory definition. The stipulated tenth is not rendered annually, but at least every thirty days after production, and that irrespective of whether the operation results in profit or loss. It is by the agreement, for the lack of an apt definition, termed a “royalty”; but, whether or not it may appropriately be named a royalty or an annuity, the statute does not, in terms, charge either royalties or annuities, as such; and here the appellant has converted the land, which is capital, into money, shares and ten per cent. of the stipulated minerals which the company may win. What the appellant will realize, under the covenant is, of course, uncertain; although it may be ascertained in the event.

20 On the other hand, it may be assumed that if the project prove unprofitable, the minerals will not be raised and that circumstance, as well as the uncertainty of the extent of minerals available, contributes to the speculative character of the appellant’s interest; but, nevertheless, the appellant’s receipts come from a potential source of capital. The taxable commodity is “income,” which means, by the definition, annual profit or gain; and for the appellant, there is no question of profit or gain, unless it be as to whether she has made an advantageous sale of her property.

30 In *Jones v. Commissioners of Inland Revenue*, 1920, 1 K.B., 711, a case upon which the Crown relies, the appellant sold his interest in certain patents for a sum in money and percentage, called a royalty, payable for ten years, upon the sale of all machines constructed under the patent; and it was held that the sums received by the appellant in respect of the royalty were income and properly so computed for the purpose of the super-tax. Rowlatt, J., who pronounced the judgment, said, at pp. 714–715, as to the contention that the ten per cent. upon sales was part of the consideration for the transfer:

40 “There is no law of nature or any invariable principle that because it can be said that a certain payment is consideration for the transfer of property it must be looked upon as price in the character of principal. In each case regard must be had to what the sum is. A man may sell his property for a sum which is to be paid in instalments, and when that is the case the payments to him are not income. *Foley v. Fletcher*, 1858, 3 H. & N. 769. Or a man may sell his property for an annuity. In that case the Income Tax Act applies. Again, a man may sell his property for what looks like an annuity,

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but which can be seen to be not a transmutation of a principal sum into an annuity but is in fact a principal sum payment of which is being spread over a period and is being paid with interest calculated in a way familiar to actuaries—in such a case income tax is not payable on what is really capital: *Secretary of State for India v. Scoble*, 1903 A.C., 299. On the other hand, a man may sell his property nakedly for a share of the profits of the business. In that case the share of the profits of the business would be the price, but it would bear the character of income in the vendor's hands. *Chadwick v. Pearl Life Assurance Co.*, 1905 2 K.B., 507, 514, was a case of that kind. In such a case the man bargains to have, not a capital sum but an income secured to him, namely, an income corresponding to the rent which he had before. I think therefore that what I have to do is to see what the sum payable in this case really is. The ascertainment of an antecedent debt is not the only thing that governs, although in many cases it is a very valuable guide. In this case there is no difficulty in seeing what was intended. The property was sold for a certain sum, and in addition the vendor took an annual sum which was dependent upon the volume of business done; that is to say, he took something which rose or fell with the chances of the business. When a man does that he takes an income; it is in the nature of income, and on that ground I decide this case.”

These observations of the learned Judge have their application to the statutes which were under consideration in that case; but the question here is, does a man take an income within the meaning of the Canadian Act when he sells his land in consideration of a part of the oil and gas to be extracted from it by the purchaser, if, as is stated in the present admissions, “the appellant was not and is not a dealer in or in the business of buying and selling oil lands or leases”; and when there is no provision for taxing the property delivered by the purchaser to the appellant, either as annuity or royalty; neither of these words having been used in the statute to describe any right such as that which the vendor acquired under the agreement.

It is the duty of the Court to ascertain the real nature of the transaction. It was argued for the respondent that the appellant sold her land and joined with the purchaser in the business of recovering the minerals, but she clearly was not engaged in the business; that suggestion is excluded by the facts and admissions.

The case is not without its difficulties, but I am not satisfied that the Crown has made out its claim. And, “inasmuch as it is the duty of those who assert and not of those who deny, to establish the proposition sought to be established, I think the Crown must fail.”—*Secretary of State in Council of India v. Scoble*, 1903 A.C., 299.

No. 23.

Order in Council granting special leave to appeal to His Majesty in Council.

AT THE COURT AT BUCKINGHAM PALACE

The 8th day of August, 1932.

PRESENT,

THE KING'S MOST EXCELLENT MAJESTY

EARL OF ATHLONE
LORD SOUTHBOROUGH

SECRETARY SIR HERBERT SAMUEL
SIR HOWARD KINGSLEY WOOD.

*In the
Privy
Council.*

No. 23.
Order in
Council
granting
special leave
to appeal to
His Majesty
in Council.
8th August
1932.

10 WHEREAS there was this day read at the Board a Report from
the Judicial Committee of the Privy Council dated the 26th day of July
1932 in the words following, viz. :—

20 “ WHEREAS by virtue of His late Majesty King Edward
the Seventh's Order in Council of the 18th day of October 1909
there was referred unto this Committee a humble Petition of the
Minister of National Revenue in the matter of an Appeal from
the Supreme Court of Canada between the Petitioner Appellant
and Mrs. Catherine Spooner Respondent setting forth (amongst
other matters) that the Petitioner desires to obtain special leave
to appeal to Your Majesty in Council from a Judgment of the
Supreme Court of Canada dated the 28th day of April 1931
reversing a Judgment of the Exchequer Court of Canada dated
the 23rd day of October 1930 upon a question of general and public
importance affecting the interpretation of the Canadian Income
War Tax Act and in which rights in future will be bound : and
reciting the facts out of which the Petition arose : that the
Petitioner submits that the Judgment of the Supreme Court is
30 wrong in that it is not in accord with the correct interpretation
of the definition of “ Income ” as contained in Section 3 of Chapter
97 R.S.C. 1927 : that “ Income ” as there defined is not exclusive
of “ incomes ” not specifically referred to but inclusive, *i.e.*,
includes not only the “ incomes ” contained in the definition
but “ also the annual profit or gain from any other source ” :
that the Judgment of the Exchequer Court is right and should
be restored and further that the question involved is of general
and public importance and one in which rights in future will be
bound affecting as it does not only this individual taxpayer but
also many other taxpayers in the Dominion who have sold mineral
rights in the land owned by them under similar agreements to
that in question in this case and are receiving royalties from
40 companies in proportion to the volume of the oil or minerals
gained from the soil by the operating company and further that
the decision of the Supreme Court is not in accord with the statement

*In the
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Council.*

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Order in
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tinued.

of the law as given by Rowlatt, J. in the case of *Jones vs. Commissioners of Inland Revenue* (1920) 1 K.B. 711 and particularly the case of *Chadwick vs. Pearl Life Assurance Company* (1905) 2 K.B. 507 referred to by Rowlatt, J.: And humbly praying Your Majesty in Council to order that the Petitioner shall have special leave to appeal from the Judgment of the Supreme Court of the 28th April 1931 or for such further or other Order as to Your Majesty in Council may appear fit :

“THE LORDS OF THE COMMITTEE in obedience to His late Majesty’s said Order in Council have taken the humble Petition into consideration and having heard Counsel in support thereof and for the Respondent and the Petitioner by his Counsel undertaking to pay the Respondent’s costs of the Appeal as between Solicitor and Client whatever may be its result Their Lordships do this day agree humbly to report to Your Majesty as their opinion that leave ought to be granted to the Petitioner to enter and prosecute his Appeal against the Judgment of the Supreme Court of Canada dated the 28th day of April 1931. 10

“And Their Lordships do further report to Your Majesty that the authenticated copy under the seal of the Record produced by the Petitioner upon the hearing of the Petition ought to be accepted (subject to any objection that may be taken thereto by the Respondent) as the Record proper to be laid before Your Majesty on the hearing of the Appeal.” 20

HIS MAJESTY having taken the said Report into consideration was pleased by and with the advice of His Privy Council to approve thereof and to order as it is hereby ordered that the same be punctually observed obeyed and carried into execution.

Whereof the Governor-General or Officer Administering the Government of the Dominion of Canada for the time being and all other persons whom it may concern are to take notice and govern themselves accordingly. 30

M. P. A. HANKEY.

In the Privy Council.

No. 72 of 1932.

On Appeal from the Supreme Court of Canada.

BETWEEN

THE MINISTER OF NATIONAL REVENUE
(Respondent) Appellant

AND

MRS. CATHERINE SPOONER
(Appellant) Respondent.

RECORD OF PROCEEDINGS.

CHARLES RUSSELL & CO.,
37, Norfolk Street,
Strand, W.C.2,
Solicitors for the Appellant.

LAWRENCE JONES & CO.,
Lloyd's Building,
Leadenhall Street, E.C.3,
Solicitors for the Respondent.

EYRE AND SPOTTISWOODE LIMITED, EAST HARDING STREET, E.C. 4.