

Docket: 2008-1658(IT)I

BETWEEN:

RONALD E. JARVIS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on March 26, 2009, at Nanaimo, British Columbia

Before: The Honourable Justice L.M. Little

Appearances:

For the Appellant:	The Appellant himself
Counsel for the Respondent:	Matthew Turnell

JUDGMENT

The appeal from the assessment made under the *Income Tax Act* for the 2006 taxation year is dismissed, without costs.

Signed at Vancouver, British Columbia, this 23rd day of April 2009.

“L.M. Little”

Little J.

Citation: 2009 TCC 224
Date: 20090423
Docket: 2008-1658(IT)I

BETWEEN:

RONALD E. JARVIS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Little J.

A. Facts

[1] In November 1966 the Appellant purchased a life insurance policy (the “Policy”) from the Prudential Assurance Company Limited.

[2] The Policy was described as an Endowment to Age 60 type of policy. The Policy number was 7224220.

[3] The Appellant was required to pay annual premiums of \$260.00 per year commencing in December 1966. All of the premiums were paid by the Appellant for 40 years.

[4] The Policy provided that if the Appellant survived until November 28, 2006 he would receive the Sum Assured (\$10,000.00) increased by any paid up additions.

[5] Mutual Life Insurance Company purchased the shares of Prudential Assurance Company. Sometime later Sun Life Assurance Company of Canada (“Sun Life”)

purchased the shares of Mutual Life Insurance Company. As a result of these transactions the Appellant became a policyholder of Sun Life, under the new policy number LI-8024, 992-5.

[6] By letter dated November 10, 2006, the Appellant was advised by Sun Life that the Policy will mature on November 28, 2006 (Exhibit A-5). The letter stated that the Appellant had the following options:

- Purchase a Payout Annuity with the maturity value as stated in your policy provisions. If this option is elected, the taxable gain would be spread out over the duration of the income period you select. The purchase date for the Payout Annuity must be the same day as the maturity date. Future policy changes or refunds will not be allowed once an income is selected.
- Transfer the funds into one of Clarica's Guaranteed Savings contracts. If this option is elected, the taxable gain would be reported to you in the year of maturity.
- Issue a cheque for the maturity value of \$30,004.50. The approximate taxable maturity gain of \$17,593.12 will be reported to you as the policyholder in the year of maturity.

[7] The Appellant advised Sun Life that he wished to receive the sum of \$30,004.50 and a cheque in this amount was issued to him by Sun Life sometime in November or December 2006.

[8] Sun Life issued a T-5 Statement of Investment Income to the Appellant (Exhibit A-4). In the Statement the amount of \$17,593.12 is referred to as "Interest from Canadian Sources".

[9] The Appellant testified that he did not receive the T-5 Statement issued by Sun Life before he filed his income tax return for the 2006 taxation year and therefore he did not report any portion of the payment received by him from Sun Life in computing his income for the 2006 taxation year. The Appellant said that his mail is delivered by Canada Post to a community post office and during the fall of 2006 some of the mail in the community mail box was taken by vandals.

[10] The Respondent accepts the Appellant's position regarding theft of mail from the community mail box but maintains that the Appellant is required to include the amount of \$17,593.12 in his income for the 2006 taxation year.

B. Issue

[11] The issue is whether the Minister of National Revenue (the “Minister”) properly determined that the Appellant failed to report Investment Income of \$17,593.12 that he received from Sun Life.

C. Analysis and Decision

[12] During the hearing the Appellant agreed that the amount of \$17,593.12 is taxable, and should therefore be included in his income for the 2006 taxation year. However, the Appellant says that the amount of \$17,593.12 should be recognized as dividend income, rather than as “Interest from Canadian Sources”. The Appellant said that he understood he would be taxed at a lower rate if the amount of \$17,593.12 were treated as dividends.

[13] The Respondent maintains that the amount of \$17,593.12 is properly included in the Appellant’s income as investment income, pursuant to subsection 148.(1) of the *Income Tax Act* (the “Act”).

[14] Paragraph 56.(1)(j) of the *Act* reads:

56. (1) Amounts to be included in income for year – Without restricting the generality of section 3, there shall be included in computing the income of a taxpayer for a taxation year,

...

(j) Life insurance policy proceeds – any amount required by subsection 148(1) or 148(1.1) to be included in computing the taxpayer’s income for the year;

...

[15] Subsection 148.(1) reads:

148. (1) Amounts included in computing policyholder’s income – There shall be included in computing the income for a taxation year of a policyholder in respect of the disposition of an interest in a life insurance policy, ...

...

the amount, if any, by which the proceeds of the disposition of the

policyholder's interest in the policy that the policyholder, beneficiary or assignee, as the case may be, became entitled to receive in the year exceeds the adjusted cost basis to the policyholder of that interest immediately before the disposition.

[16] In *Patel v. Canada*, [1999] T.C.J. No. 847, Justice Dussault of the Tax Court of Canada explained the application of these sections of the *Act* as follows:

7. Paragraph 56(1)(j) of the Income Tax Act (the "Act") provides that there shall be included in computing the income of a taxpayer for a taxation year any amount required to be so included by subsection 148(1) or (1.1) of the Act.

8. Basically, and subject to certain exceptions, subsection 148(1) of the Act provides for the inclusion in income of the amount by which the proceeds of the disposition of a policyholder's interest in a life insurance policy exceeds the adjusted cost basis of that interest immediately before the disposition.

[17] Essentially, paragraph 56(1)(j) and section 148 of the *Act* provide that certain proceeds of life insurance policies must be included in a taxpayer's income as "Other Sources of Income". These sections do not provide that the proceeds received from life insurance policies are to be recognized as dividend income.

[18] The Appellant agrees that the amount of \$17,593.12 represents the difference between the proceeds of disposition of the Policy (\$30,004.50) and its adjusted cost basis (\$12,411.38). These amounts were calculated by Sun Life using the prescribed formulas under their respective definitions in subsection 148.(9).

[19] I have carefully reviewed the documents with respect to the Policy held by the Appellant. It appears that certain "dividends" were allotted to the Appellant during each year that he held the Policy (Exhibit A-3). However, those dividends were re-invested by Sun Life or its predecessors into the insurance policy, and were allotted to be "used to purchase additional paid-up insurance" (Exhibit A-3).

[20] The relevant parts of the definition of the "adjusted cost basis" and "proceeds of disposition" under subsection 148.(9) read as follows:

"**adjusted cost basis**" to a policyholder as at a particular time of the policyholder's interest in a life insurance policy means the amount determined by the formula

$$(A + B + C + D + E + F + G + G.1) - (H + I + J + K + L)$$

where

...

B is the total of all amounts each of which is an amount paid before that time by or on behalf of the policyholder in respect of a premium under the policy, other than amounts referred to in clause 148(2)(a)(ii)(B), in subparagraph (iii) of the description of C in paragraph (a) of the definition "proceeds of the disposition" or in subparagraph (b)(i) of that definition, ...

...

"proceeds of the disposition" of an interest in a life insurance policy means the amount of the proceeds that the policyholder, beneficiary or assignee, as the case may be, is entitled to receive on a disposition of an interest in the policy and for greater certainty, ...

[21] Therefore, the dividends that were allotted to the Appellant, which were used to purchase additional paid-up insurance, would be included in the calculation of the Policy's adjusted cost basis, by virtue of item "B" under the definition of that phrase. This provision ensures that when the adjusted cost basis is subtracted from the proceeds of disposition, pursuant to subsection 148(1) and paragraph 56(1)(j), the amounts relating to the "dividends" previously received by the Appellant would not be included in the taxable amount. Therefore, the amount of \$17,593.12 does not include any amounts relating to the dividends that were allotted to purchase additional paid-up insurance. There is no evidence to suggest that a mistake had occurred in the calculation of the amount of \$17,593.12. I have therefore concluded that no portion of the amount of \$17,593.12 can be recognized as dividend income.

[22] The Appellant also maintains that it was incorrect for Sun Life to categorize the amount of \$17,593.12 as "Interest from Canadian Sources", since there is no mention of "interest" or "interest rate" on any of the Policy's documents. I find the facts in *Lalonde v. Canada*, [1997] T.C.J. No. 1268, to be analogous to the current appeal. In that case, the Appellant received interest and dividend payments each year from his life insurance policy, which were both automatically re-invested in the policy. During each of those years, the Appellant properly included the interest income in his taxable income. Upon the disposition by the Appellant of his interest in that policy, the insurance company issued him a T-5 Slip that recognized an amount of \$5,839.87 as "interest income". In paragraph 19 of that Judgment, Justice Lamarre Proulx of the Tax Court of Canada explained:

As regards the amount in dispute, namely \$5,839.87, although it was entered in the “Interest” box on the T5 form, this does not in any way mean that it was the same kind of interest that the appellant had received each year and on which he had already paid tax. In fact, the \$5,839.87 resulted from the subtraction of the adjusted cost basis of the policy from the proceeds of the disposition of the policy, and this is a result I must accept since there was no evidence to the contrary about the amount of the proceeds of the disposition or the adjusted cost basis. In other words, \$5,839.87 is the amount by which the proceeds of the disposition of the appellant’s interest in the insurance policy exceeded the adjusted cost basis of that interest.

[23] Similarly, the amount of \$17,593.12 is not the same in nature as the “dividends” that the Appellant received during each year that he held the Policy. Similarly, it is also not “interest” income in the usual sense of the word. Instead, it is a specific form of investment income, for which the taxable amount is arrived at by application of the formulas under paragraph 56.(1)(j) and section 148 of the *Act*, upon the Appellant’s disposition of his interest in the Policy. Although Sun Life labelled the amount of \$17,593.12 as “Interest from other Canadian Sources” on the Appellant’s T-5 Statement, the end result of including the full amount in the income of the Appellant is correct. In any case, the *Act* does not provide for any dividend tax credits or a lower tax rate for this type of investment income.

[24] Since there is no contrary evidence relating to the “proceeds of disposition” and “adjusted cost basis” of the Appellant’s interest in the Policy, I conclude that the amount of \$17,593.12 is properly included in the Appellant’s income as investment income, pursuant to paragraph 56.(1)(j) and section 148 of the *Act*.

[25] The appeal is dismissed, without costs.

Signed at Vancouver, British Columbia, this 23rd day of April 2009.

“L.M. Little”

Little J.

CITATION: 2009 TCC 224

COURT FILE NO.: 2008-1658(IT)I

STYLE OF CAUSE: Ronald E. Jarvis and
Her Majesty The Queen

PLACE OF HEARING: Nanaimo, British Columbia

DATE OF HEARING: March 26, 2009

REASONS FOR JUDGMENT BY: The Honourable Justice L.M. Little

DATE OF JUDGMENT: April 23, 2009

APPEARANCES:

For the Appellant:	The Appellant himself
Counsel for the Respondent:	Matthew Turnell

COUNSEL OF RECORD:

For the Appellant:

Name:

Firm:

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