THE MINISTER OF NATIONAL REVENUE .... APPELLANT;

1960
*Mar. 25, 28, 29
Oct. 4

AND

IMPERIAL OIL LIMITED .... RESPONDENT.

ON APPEAL FROM THE EXCHEQUER COURT OF CANADA

Taxation—Income tax—Determination of base on which depletion allowance calculated—Whether profits should be treated on an individual well basis—Whether losses of loss producing wells must be deducted from profits of profitable producing wells—Whether unrelated drilling, exploration and other costs deductible—Whether deduction of "unrealized profits" should be allowed—Income Tax Act, 1948 (Can.), c. 52, s. 11 (1) (b)—Income Tax Regulations, s. 1201 as amended by Order in Council 4443, August 29, 1951—Income Tax Amendment Act, 1949 2nd Sess. (Can.), c. 25, s. 53 (1).

In computing its income for 1951, the respondent oil company claimed that the depletion allowance to which it was entitled under s. 11(1)(*b*) of the *Income Tax Act* and s. 1201 of the Income Tax Regulations was $13,023,666.59. The company contended that, under the decision of this Court in *Home Oil Ltd. v. Minister of National Revenue*, [1955] S.C.R. 733, for the purpose of computing the profits to establish the base on which the allowance is to be calculated, the profits from each of its wells should be treated individually.

The Minister set the allowance at $790,067.36, and arrived at the base on which this amount was calculated by deducting from the profits of profitable wells (1) losses of loss wells, (2) unrelated drilling, exploration and other costs, and (3) unrealized profits in supply, manufacturing and marketing inventories.

The Exchequer Court allowed a deduction only for losses of loss wells. The Minister, in appealing this decision, sought to have his assessment confirmed in full, and the respondent cross-appealed, claiming that a deduction of losses on loss wells should not have been allowed.

*PRESENT: Kerwin, C.J., Taschereau, Locke, Cartwright, Martland, Judson and Ritchie JJ.

1960

MINISTER OF NATIONAL REVENUE *v.* IMPERIAL OIL LTD.

Held (Cartwright, Martland and Ritchie JJ. *dissenting in part*): The appeal should be allowed, and the cross-appeal should be dismissed. The Minister's notice of re-assessment should be affirmed.

Per Kerwin C.J. and Taschereau, Locke and Judson JJ.: Subsections 1 and 4 of s. 1201 of the Regulations, when read together, make it plain that the losses of the company's loss producing wells must be deducted from the profits of its profitable producing wells in computing the allowance to which it is entitled. Subsection 4, which defines what are the profits referred to in subs. 1 in cases where the taxpayer operates more than one well, is within the authority of s. 11(1)(*b*) of the Act.

Regulation 1201, as redrafted in 1951, legislated away not only the well by well basis for the determination of profits, but also the limitation on the application of the old subs. 4, now subs. 5, to the deduction of items, referred to in s. 53 of the Act, in relation only to the profitable wells. Section 53 items, required to be deducted from reasonably attributable profits, are not now required to be related to the profitable wells mentioned in subs. 1. If they have been deducted in computing the taxpayer's taxable income, they must be deducted in computing the allowance, whether related or unrelated to the aforementioned wells. *Home Oil Ltd. v. Minister of National Revenue*, [1955] S.C.R. 733, distinguished.

The respondent's argument that s. 11(3) of the Act supported its submission that Regulation 1201 still required the application of the Home Oil judgment on unrelated costs was rejected.

As the producing department of the company was not, in fact, a separate entity for tax purposes, the respondent was not entitled to so consider it, nor to include the "unrealized profit" in supply, manufacturing and marketing inventories as part of the "profits" of that department.

Per Cartwright and Ritchie JJ., *dissenting in part*: The aggregate of the profits from all wells operated by the taxpayer cannot be determined for the purpose of subs. 4 until the profits of each have been computed, and as subs. 5 requires a deduction to be made in computing these profits, it follows that s. 53 costs, specified in subs. 5, must be deducted in respect of each well.

It would make the provisions of subs. 4 quite purposeless if *all* the s. 53 costs were required to be deducted in computing the profits of *each* of a number of wells, and as subs. 5 requires the deduction to be made both "in computing the profits . . ." and "for the purpose of this section" it can only be complied with by deducting, in computing the profits of each well, such of the s. 53 costs as can be related thereto.

Per Martland J., *dissenting in part*: The computation of profits for the purpose of s. 1201 has to be made on an individual well basis. Subsection 5 requires that in computing the profits attributable to the production of oil or gas from operating wells, account must be taken of any amounts expended for exploration and drilling in relation to such wells, which have been included in the aggregate of costs deducted by the taxpayer in computing income under the authority of s. 53.

APPEAL from a judgment of Thorson P., of the Exchequer Court of Canada[1], allowing the respondent's appeal from its 1951 income tax assessment. Appeal allowed in toto and cross-appeal dismissed, Cartwright, Martland and Ritchie JJ. dissenting in part.

C. F. H. Carson, Q.C., T. Sheard, Q.C., A. Findlay, Q.C., T. Z. Boles and *G. W. Ainslie,* for the appellant.

A. S. Pattillo, Q.C., A. J. Macintosh, J. G. MacDonell, for the respondent.

THE CHIEF JUSTICE:—This appeal by the Minister of National Revenue and cross-appeal by Imperial Oil Limited from the judgment of the Exchequer Court[1] raise a question as to the proper deductions to be made by the company in computing its income for the 1951 taxation year under no. 1201 of the Regulations passed pursuant to s. 11(1)(*b*) of the *Income Tax Act,* 1948 (Can.), c. 52, as amended.

Because of the nature of some of the arguments advanced on behalf of the parties, it might be recalled that s. 3 of the Act provides that the income of a "taxpayer" for a taxation year is his income for the year from all sources. Section 12(1) enacts that in computing income no deductions shall be made in respect of (*b*):

(*b*) an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part

Section 11(1)(*b*), as enacted by c. 25 of the Statutes of 1949, provides:

11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year

* * *

(*b*) such amount as an allowance in respect of an oil or gas well, mine or timber limit, if any, as is allowed to the taxpayer by regulation

Subsection (3) of s. 11, as enacted by s. 4 of c. 25 of the Statutes of 1949, provides:

11. (3) Where a deduction is allowed under paragraph (*b*) of subsection (1) in respect of an oil or gas well, mine or timber limit operated by a lessee, the lessor and lessee may agree as to what portion of the allowance each may deduct and, in the event that they cannot agree, the Minister may fix the portions.

[1] [1959] C.T.C. 29, 59 D.T.C. 1034.

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Kerwin C.J.

The power to make the relevant regulations is conferred by s. 106(1)(*a*) of the Act:

> 106. (1) The Governor in Council may make regulations
> (*a*) prescribing anything that, by this Act, is to be prescribed or is to be determined or regulated by regulation

Section 1200 of the Regulations, which is in Part XII, headed "Deduction in Respect of Oil Wells, Gas Wells and Certain Mines", reads:

> 1200. For the purposes of paragraph (*b*) of subsection (1) of section 11 of the Act there may be deducted in computing the income of a taxpayer for a taxation year amounts determined as hereinafter set forth in this Part.

This section of the Regulations is the same for the taxation year 1951 as for the years 1949-50. Some of the problems now arising were considered by this Court in *Home Oil Limited v. Minister of National Revenue*[1] with reference to the taxation years 1949-50, but, as s. 1201 of the Regulations, which was there under discussion, is different from the section as it is to be applied to the 1951 taxation year, the two versions should be considered together and they appear conveniently opposite each other in the reasons of Mr. Justice Judson.

I agree with his conclusions and reasons and merely add these remarks to emphasize

(*a*) The new Regulation 1201 has the effect of making the decision of this Court in the Home Oil case inapplicable;

(*b*) In view of s. 3 of the Act, referred to above, and generally because a company cannot sell to itself, the practice of Imperial Oil Limited, even if warranted by sound accounting principles, cannot prevail against the rule;

(*c*) In connection with the item of $19,992,588.33 "Unrelated drilling, exploration and other costs", while one witness for the company was not certain, I am satisfied that under s. 53 of the Act the company deducted this item in computing its taxable income.

I have considered the decision of the House of Lords in *Sharkey v. Wernher*[2], relied upon by counsel for the company, but I am unable to see that it is of any assistance in the present matter.

[1] [1955] S.C.R. 733, [1955] 4 D.L.R. 796.

[2] [1955] 3 All E.R. 493, 36 T.C. 275

While the reasons of the learned President indicated that he disallowed the appeal of the company as to losses of loss wells, the formal order merely states "that the said appeal be and the same is hereby allowed." The judgment of the Exchequer Court should be set aside, the appeal of the Minister allowed, the cross-appeal of the company dismissed and the Minister's notice of re-assessment affirmed. The Minister is entitled to his costs in the Exchequer Court and in this Court.

The judgment of Taschereau, Locke and Judson JJ. was delivered by

JUDSON J.:—This is an appeal from a judgment of the Exchequer Court[1] which allowed the appeal of the respondent company from its 1951 income tax assessment with costs. The company claimed that it was entitled under Regulation 1201 of the Regulations passed pursuant to s. 11(1)(*b*) of the *Income Tax Act* to an allowance of $13,023,666.59 for the year 1951. The Minister, in a notice of re-assessment, allowed only $790,067.36, and the company appealed. The same issues are also involved in appeals from the assessments for the 1952 and 1953 taxation years but, by agreement, the trial in the Exchequer Court was limited to the appeal for the year 1951. The company's contention is that for the purpose of computing its profits to establish the base on which the allowance under s. 11(1)(*b*) is to be calculated, the profits from each well should be treated individually. On two out of three issues in this appeal, the company's submissions are the same as those of the appellant company in *Home Oil Limited v. Minister of National Revenue*[2].

In that case, however, the Court had to consider Regulation 1201 as it applied to the taxation years 1949 and 1950, but by Order-in-Council P.C. 4443, dated August 29, 1951, Regulation 1201 in force in 1949 and 1950 was revoked and a new Regulation 1201 in the precise form set out below was substituted for it and made applicable to the 1951 taxation year. Consequently, the main problem is to determine to what extent the decision in the *Home Oil* case is affected by the change in the regulation.

[1] [1959] C.T.C. 29, 59 D.T.C. 1034.
[2] [1955] S.C.R. 733, [1955] 4 D.L.R. 796.

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Judson J.

I set out now s. 11(1)(*b*) of the Act and the old and new Regulation 1201, the old one applicable to the taxation years 1949 and 1950 and the new one to the year 1951:

11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year

(*b*) such amount as an allowance in respect of an oil or gas well, mine or timber limit, if any, as is allowed to the taxpayer by regulation.

For 1949 and 1950	*For 1951*
1201. (1) Where the taxpayer operates an oil or gas well or where the taxpayer is a person described as the trustee in subsection (1) of section 73 of the Act, the deduction allowed for a taxation year is 33⅓ per cent of the profits of the taxpayer for the year reasonably attributable to the production of oil or gas from the well.	1201. (1) Where the taxpayer operates an oil or gas well the deduction allowed for a taxation year is 33⅓ per cent of the profits of the taxpayer for the year reasonably attributable to the production of oil or gas from the well.
(2) Where a person, other than the operator of an oil or gas well and the person described as the trustee in section 73 of the Act, has an interest in the proceeds from the sale of the products of the well or an interest in income from the operation of the well, the deduction allowed for a taxation year is 25 per cent of the amount in respect of such interest included in computing his income for the year.	(2) Where a person, other than the operator has an interest in the proceeds from the sale of the products of an oil or gas well or an interest in income from the operation of the well, the deduction allowed for a taxation year is 25 per cent of the amount in respect of such interest included in computing his income for the year.
For 1949 and 1950	*For 1951*
(3) Where an amount received in respect of an interest in the income from the operation of a well is a dividend or is deemed by section 73 of the Act to be a dividend, no deduction shall be allowed under subsection (2) of this section.	(3) Where an amount received in respect of an interest in the income from the operation of a well is a dividend or is deemed by the Act to be a dividend, no deduction shall be allowed under this section.
	(4) Where the taxpayer operates more than one oil or gas well, the profits referred to in subsection one shall be the aggregate of the profits minus the aggregate of the losses of the taxpayer for the year reasonably attributable to the production of oil or gas from all wells operated by the taxpayer.

For 1949 and 1950	*For 1951*
(4) In computing the profits reasonably attributable to the production of oil or gas for the purpose of this section a deduction shall be made equal to the amounts, if any, deducted from income under the provisions of section 53 of chapter 25 of the Statutes of 1949, Second Session, in respect of the well.	(5) In computing the profits reasonably attributable to the production of oil or gas for the purpose of this section a deduction shall be made equal to the amounts, if any, deducted in computing the taxpayer's income for the taxation year under the provisions of section 53 of Chapter 25 of the Statutes of 1949, Second Session.

There are two differences between the old and the new regulation of importance in this appeal: First, subs. (4) is entirely new; second, subs. (5) of the new regulation is subs. (4) of the old with the words "in respect of the well" omitted at the end of the paragraph.

Subsection (4) of the old and subs. (5) of the new regulation both refer to a deduction under s. 53 of c. 25, Statutes of 1949, Second Session. Section 53, so far as relevant, is as follows:

53. (1) A corporation whose principal business is the production, refining or marketing of petroleum or petroleum products or the exploring and drilling for oil or natural gas, may deduct, in computing its income for the purposes of *The Income Tax Act*, the lesser of

(*a*) the aggregate of the drilling and exploration costs, including all general geological and geophysical expenses, incurred by it, directly or indirectly, on or in respect of exploring or drilling for oil and natural gas in Canada

(i) during the taxation year, and.....

The following table shows the claims of the company, the allowance made by the Minister, and the disposition of the case made in the Exchequer Court:

1. *CLAIMED BY COMPANY*

Profits of profitable wells	$39,070,999.79
Allowance claimed by company—33⅓% of above	13,023,666.59

2. *ALLOWED BY MINISTER*

Profits of profitable wells as computed by company	$39,070,999.79
Losses of loss wells as computed by company	8,066,012.55
	$31,004,987.24
Unrelated drilling, exploration and other costs	19,992,588.33
	$11,012,398.91

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Judson J.

Increase in unrealized profit in supply, manufacturing and marketing inventories	8,642,196.84
	$ 2,370,202.07
Allowance 33⅓% of last item	$ 790,067.36

3. *AS HELD BY THORSON P.*

Profits of profitable wells	$39,070,999.79
Losses of loss wells	8,066,012.55
	$31,004,987.24
Allowance 33⅓% of last item	$10,334,995.74

The company arrived at the figure of $39,070,999.79 by computing its profits from the production of oil or gas from its producing wells operated at a profit in 1951 on a well by well basis. It did make a deduction in arriving at this figure for drilling, exploration and other costs related to the particular wells but, as may be expected, these costs were of minor significance for these producing wells in the taxation year 1951.

As is apparent from the table set out above, the Minister made three further deductions from the figure of $39,070,-999.79:

(1) He deducted losses from loss wells, claiming that Regulation 1201(4) required this. The profits were not to be calculated having regard only to the profitable wells. On this point, and on this point alone, the judgment of the Exchequer Court sustains the Minister's assessment.

(2) The Minister deducted, in addition to the related drilling, exploration and other costs, unrelated costs of this character, claiming that this was required by Regulation 1201(5). The judgment of the Exchequer Court rejected this deduction on the ground that these expenditures were not reasonably attributable to the production of oil or gas in 1951 from any of the company's producing wells.

(3) The Minister deducted $8,642,196.84 because this amount represented unrealized profits of the company which had been regarded by the company as actual profits for the purpose of making the calculation of profits under Regulation 1201. This figure relates only to oil delivered by the producing department of the company to other departments and still unsold

by the company at the end of the year 1951. The company included this amount in its calculation for corporate purposes of the "profits" of the producing department, but did not include this amount in its calculation of the company's profits or of the company's taxable income. The judgment of the Exchequer Court rejects the Minister's deduction and allows this purely notional computation of profits for the purpose of the allowance under Regulation 1201.

The Minister, in this appeal, seeks to have his assessment confirmed in full. The company cross-appeals, claiming that a deduction should not have been allowed in the Exchequer Court of the losses on loss wells. These are the three issues before this Court. I would allow the appeal and confirm the assessment in full and dismiss the cross-appeal.

I will deal with the deductions made by the Minister under Regulation 1201 in the same order as they appear in the statement: (a) losses of loss wells; (b) unrelated drilling, exploration and other costs; (c) the unrealized inventory profit. The first two deductions were also considered in the *Home Oil* case. The third is new.

(a) *Losses of Loss Wells, $8,066,012.55.*

The question now is whether the company, notwithstanding the addition of subs. (4) to Regulation 1201, is still entitled to have its allowance computed on the basis solely of the profits from its profitable producing wells without deduction of its losses of its loss producing wells. This question was decided in the company's favour in the *Home Oil* case, in the absence of anything in the regulation corresponding to subs. (4). The judgment under appeal holds that this deduction must now be made. With this decision I agree. When subss. (1) and (4) are read together, words could not be plainer. However, the company still contends that the *Home Oil* judgment and the statute limit the scope of any regulation that may be made and compel the making of the allowance, if one is to be made, on the basis of the individual well. Consequently, it is argued, subs. (4) of the 1951 regulation, in purporting to require the deduction of the aggregate of losses reasonably attributable to the production of oil or gas from all wells operated by the taxpayer from the profits referred to in subs. (1), is not authorized

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Judson J.

by the Statute and is ineffective. This argument was rejected in the following passage of the reasons for judgment of the learned President[1]:

> The power to enact a regulation determining the amount of the deductible allowance permitted by Section 11(1)(*b*) of the Act and the base for its computation was granted in the broadest terms and I cannot see any limitation of it such as counsel suggests. The section of the Act does not specify what the base for the computation of the allowance should be or its amount. Thus, it was permissible to fix the profits reasonably attributable to the production of oil or gas as the base for the computation of the allowance and 33⅓ per cent of such base as its amount, as subsection (1) did. But it was also permissible to define such profits for application in cases where a taxpayer operated more than one well and some of the wells were loss producing, even if such definition altered the base fixed by subsection (1), as subsection (4) did. It contains a statutory definition of the profits referred to in subsection (1) for use in the cases stated in it. I see no objection to such a definition for use in the circumstances specified. In my opinion, subsection (4) is within the authority of Section 11(1)(*b*) of the Act. That being so, it is unnecessary to consider the question of its severability.

I agree with this in full and have nothing to add. It completely disposes of the cross-appeal, which fails and must be dismissed with costs.

(b) *Unrelated drilling, exploration and other costs, $19,992,588.33.*

These costs, in this amount, were not related to the production of oil or gas from any of the company's wells during the year 1951. The *Home Oil* case, on the old wording of the regulation, had decided that these costs were not to be deducted from the "reasonably attributable" profits under subs. (1). The basis of the decision in the *Home Oil* case is that unless s. 53 items are related to a profit producing well, they are not to be taken into account in determining the allowance under the regulation because wells are to be dealt with on an individual basis. Subsection (1) required a well by well treatment and the old subs. (4) required only the deduction of s. 53 items "in respect of the well". Therefore, unrelated s. 53 items disappeared from the computation. The judgment under appeal holds that this is still the law and that this is so notwithstanding the new subs. (4) and the deletion of the words "in respect of the well". In my respectful opinion, there is error in this conclusion, for I think that Regulation 1201 now requires

[1] [1959] C.T.C. at p. 50, 59 D.T.C. at p. 1046.

the following procedure in determining the base for the allowance to be granted to a taxpayer who operates more than one oil or gas well:

(1) Determine the profits or losses of each producing well in the normal manner by ascertaining the difference between the receipts reasonably attributable to the production of oil or gas from the well and the expenses of earning those receipts. At this point no s. 53 items are deductible for these are of a capital nature.

(2) Determine the aggregate of the profits of the profitable wells and the aggregate of the losses of the loss wells and deduct the aggregate of the latter from the aggregate of the former.

(3) Deduct from the amount of profits remaining, the exploration and drilling costs deducted under s. 53 in computing the taxpayer's income.

The judgment under appeal took the first and second steps but not the third. In spite of the scope of subs. (5), widened, in my opinion, by the deletion of the words "in respect of the well", and the addition of the new subs. (4), the Exchequer Court held, as did this Court in the *Home Oil* case, that s. 53 items were to be applied on a well by well basis and only in so far as they related to the profitable wells dealt with in subs. (1). To me, this is reading into the new regulation a limitation which I cannot find. To arrive at this result the assessor must first assume that subss. (1) and (5) are to be read together to the exclusion of subs. (4). If this is done, the problem is indeed one of well by well. But this is not an adequate statement of the problem because it ignores the presence of the new subs. (4). Where the taxpayer operates more than one well, the profits referred to in subs. (1) (i.e. the reasonably attributable profits) are to be computed in a new way—the aggregate of profits from the profitable wells minus the aggregate of the losses from the loss wells. Then subs. (5) comes into play.

It is this computation, made under the combined operation of subss. (1) and (4), which gives the profits reasonably attributable to the production of oil or gas for the purpose of subs. (5). Subsection (5) says, in computing the

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Judson J.

"reasonably attributable profits for the purpose of this section", not for the purpose of subs. (1) of this section. For the purpose of this section has already required the application of subss. (1) and (4) before we get to subs. (5). The reasonably attributable profits mentioned in subs. (5) are not on a well by well basis, taking only profitable wells, but on the composite basis as required by subs. (4). Then all s. 53 items must be deducted—not, as formerly, only those "in respect of the well".

Therefore, what the new 1951 regulation did was to legislate away not only the well by well basis for the determination of profits, as the learned President has already found, but also the limitation on the application of the old subs. (4), now subs. (5), to the deduction of s. 53 items in relation only to the profitable wells. The error in the judgment under appeal may be stated also in a slightly different way. Under the new formula supplied by the new regulation, the s. 53 items are not required to be reasonably attributable to the production of oil or gas from the wells mentioned in subs. (1). It is only the profits which have to be "reasonably attributable" and these "reasonably attributable" profits are to be computed in a defined way and from them a defined deduction must be made. It is, therefore, in my opinion, fundamental error in the judgment under appeal to arrive at "reasonably attributable" profits for the purpose of applying subs. (5) by considering only subss. (1) and (5) to the exclusion of subs. (4).

Section 53 items, required to be deducted from reasonably attributable profits, newly defined, are not now required to be related items. If they have been deducted in computing the taxpayer's taxable income—and there is no compulsion to do this—then they must be deducted in computing the allowance under Regulation 1201, whether related or unrelated to profitable wells mentioned in subs. (1).

That, I think, is all that is meant when subs. (5) speaks of "the amounts, if any" deducted under s. 53 of the Act. It simply means that whatever amounts the taxpayer deducts for determining taxable income must be deducted under Regulation 1201. The presence of these words in subs. (5), far from reinforcing the company's submission on the construction of the new regulation, seems to me to be entirely consistent with the Minister's submission and to support the assessment. A taxpayer who deducts these s. 53 items in one place for the purpose of determining taxable income, must do so in another for the purpose of determining the allowance under Regulation 1201.

The company also appeals to s. 11(3) of the Act in support of its submission that Regulation 1201 still requires the application of the *Home Oil* judgment on unrelated costs. This point was not dealt with in the reasons delivered in the Exchequer Court. Section 11(3) provides:

> (3) Where a deduction is allowed under paragraph (*b*) of subsection (1) in respect of an oil or gas well, mine or timber limit operated by a lessee, the lessor and lessee may agree as to what portion of the allowance each may deduct and, in the event that they cannot agree, the Minister may fix the portions.

The argument is that the subsection authorizes only one allowance, which must be divided between lessor and lessee. Regulation 1201, in fact, grants what appear to be separate allowances to the lessor and lessee and there is no occasion, therefore, for the allowance to be divided under s. 11(3) of the Act. If the regulation made under s. 11(1) (b) had granted an allowance to a lessee in such terms that the drilling and exploration costs incurred by the lessee on other lands in which the lessor had no interest were permitted to reduce the allowances in respect of the well on the lessor's lands, the regulation would have operated unfairly.

As the regulation stands, if the operator of a well is a lessee, he is granted an allowance under subss. (1), (4) and (5). The lessor of the land on which the well is operated is granted a quite different allowance under subs. (2). Under the latter subsection the lessor is entitled to an allowance equal to 25 per cent of the amount in respect of his interest in the proceeds from the sale of the products of the well on his land included in computing his income for the year.

In my opinion, the separate allowances given by Regulation 1201, first, to the operator, and then to a person other than the operator, are authorized by the wide scope of s. 11(1)(b).

With the making of this regulation, the need for the application of s. 11(3) of the Act to oil or gas wells disappears. If, on the other hand, there is no statutory authorization for dealing with the allowance between operator

1960 MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD. Judson J.

and non-operator, as both the old and the new regulation do, there is no allowance at all given to anybody and that is the end of the litigation.

(c) Increase in unrealized profit in supply, manufacturing and marketing inventories. . . $8,642,196.84

This question is new and did not arise in the *Home Oil* litigation. The Minister claimed that the amount of $8,-642,196.84 was not part of the profits of the taxpayer for the year reasonably attributable to the production of oil or gas from all wells of the company operated within the meaning of subs. (4) of Regulation 1201 and that the company was not entitled to include it in determining the base for its allowance. The appellant's submission is that although it may have been convenient for the company for its own corporate purposes to treat the producing department as a separate entity and to include this unrealized profit as part of the profits of the producing department, in fact, the producing department was not a separate entity and for tax purposes the company was not entitled to treat the producing department as a separate entity. The judgment of the Exchequer Court correctly, of course, drew a distinction between the company's taxable income, which was not under consideration in the case, and the profits from the production of oil or gas "reasonably attributable to the well". However, on a well by well basis of accounting, which the Exchequer Court adopted as the proper one, the inventory "had all moved out from the well to some other department as if it had been sold and was no longer in its hands. This was the opinion of the accountancy witnesses based on the assessment made. What happened to the inventory in the hands of other departments and how it affected the computation of the appellant's taxable income as a whole is outside the scope of the present inquiry". It is apparent that the judgment of the Exchequer Court did treat the producing department as a separate entity for the purpose of Regulation 1201.

In my opinion, this was error. It may have been convenient for the company for its own corporate purposes to treat the producing department as a separate entity and to include this "unrealized profit" as part of the "profits" of the producing department. In fact, the producing department was not a separate entity for tax purposes and, therefore, the company was not entitled to treat the producing department in this way. If it makes any difference, and I do not think that it does, all the accountancy witnesses based their opinion in resisting the claim for deduction on the assumption that the producing department could be treated as a separate entity. No such assumption could be made in law. No company makes an actual profit merely by producing oil. There is no profit until the oil is sold. *International Harvester Co. of Canada v. Provincial Tax Commission*[1]. *Laycock v. Freeman, Hardy & Willis Ltd.*[2].

The judgment of the Exchequer Court should be set aside, the appeal of the Minister allowed, the cross-appeal of the company dismissed and the Minister's notice of reassessment affirmed. The Minister is entitled to his costs in the Exchequer Court and in this Court.

The judgment of Cartwright and Ritchie JJ. was delivered by

RITCHIE J. (*dissenting in part*):—This appeal involves the construction to be placed on s. 1201 of the Income Tax Regulations in its amended form as passed by Order-in-Council P.C. 4443 dated August 29, 1951, but before embarking on any close analysis of the provisions of this section it is important to determine under what authority and for what purpose it was enacted.

This Order-in-Council was expressed as being passed "by virtue of the powers conferred by section 106 of The Income Tax Act", the relevant part of which reads as follows:

> 106. (1) The Governor-in-Council may make regulations
>
> (*a*) prescribing anything that, by this Act, is to be prescribed or is to be determined or regulated by regulation,

By s. 11(1)(b) of *The Income Tax Act*, 1948, it is provided:

> 11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year
>
> * * *
>
> (*b*) such amount as an allowance in respect of an oil or gas well, mine or timber limit, if any, as is allowed to the taxpayer by regulation;

[1] [1949] A.C. 36 at 49.
[2] [1939] 2 K.B. 1 at 6 and 11, [1938] 4 All E.R. 609.

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Ritchie J.

The Governor-in-Council expressly confined the relevant sections of the Regulations by which it exercised this authority to the requirements of the enabling legislation by enacting s. 1200 which reads:

> For the purposes of paragraph (*b*) of subsection (1) of section 11 of the Act there may be deducted in computing the income of a taxpayer for a taxation year amounts to be determined as hereinafter set forth in this Part.

Pursuant to this authority and in furtherance of these purposes, s. 1201 of the Regulations was originally passed by P.C. 6471 of December 22, 1949, and subsequently amended by P.C. 4443 hereinbefore referred to in which latter form it was in force during the taxation period in question. Subsection (1) of s. 1201 reads as follows:

> 1201. (1) Where the taxpayer operates an oil or gas well the deduction allowed for a taxation year is 33⅓ per cent of the profits of the taxpayer for the year reasonably attributable to the production of oil or gas from the well.

This subsection, taken alone, is clearly effective to fulfil the purposes of s. 11(1)(b) in the case of a taxpayer who operates a single oil or gas well and it not only establishes once and for all the percentage to be allowed by way of deduction under s. 1201 but also fixes "profits . . . reasonably attributable to the production of oil or gas from the well" as the primary ingredient in the computing of the base amount upon which such percentage is to be calculated.

Under ss. 11(1)(b) and 106(1) the method of calculating the allowance to be allowed is left to be dealt with entirely by regulation, and in my opinion it is within the ambit of the authority created by these sections for the Governor-in-Council to provide that when a number of wells are operated by one taxpayer he shall be required, in calculating the amount of his allowance, to make a deduction from the aggregate of the aforesaid profits from each well, equal to the aggregate of the losses from loss wells, provided always that in computing the reasonably attributable profits from the aggregate of which the deduction is to be made, the producing wells are dealt with individually.

In my view this is the effect of subs. (4) of s. 1201 which was first introduced by the amendment to the Regulations (P.C. 4443) and which was inserted between subs. (3) and the present subs. (5) which, in its old form, was subs. (4). Section 1201(4) reads as follows:

> (4) Where the taxpayer operates more than one oil or gas well, the profits referred to in subsection one shall be the aggregate of the profits minus the aggregate of the losses of the taxpayer for the year reasonably attributable to the production of oil or gas from all wells operated by the taxpayer.

It is to be observed that the word "profits" occurs twice in this subsection, and in my opinion it must bear the same meaning in both places so that the words "aggregate of the profits" must mean "aggregate of the profits referred to in subsection one" (i.e., the profits of the taxpayer for the year reasonably attributable to the well).

The word "aggregate" is defined in the Oxford English Dictionary as meaning "Collected into one body; formed by the collection of many units into one, association." Other dictionary definitions are in slightly different language but all indicate that in its primary sense and meaning the word implies a plurality of units whose total amount it represents.

It is upon "the profits reasonably attributable to the production of oil or gas from the well" that a taxpayer operating a single well is entitled to a deduction of 33⅓ per cent in computing his income tax, and it appears to follow from the above that in the case of a taxpayer operating more than one well it is these same profits which must be computed and then aggregated to find the profits reasonably attributable to all the wells which he operates from which he is required to deduct the aggregate of the losses from loss wells in order to determine the amount on which he is entitled to the 33⅓ per cent deduction.

It seems to me, therefore, that the first question facing the operator of one or more oil or gas wells who seeks a deduction under this section must be how he is to compute the profits reasonably attributable to the production of oil or gas from each well, and in this regard he is at once faced with the mandatory provisions of s. 1201(5) which read as follows:

> (5) In computing the profits reasonably attributable to the production of oil or gas for the purpose of this section a deduction shall be made equal to the amounts, if any, deducted in computing the taxpayer's income for the taxation year under the provisions of section 53 of Chapter 25 of the Statutes of 1949, Second Session.

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Ritchie J.

The relevant deduction is specified by the said s. 53 to be

> . . . the aggregate of the drilling and exploration costs, including all general and geological and geophysical expenses incurred by it (the corporate taxpayer) directly or indirectly on or in respect of exploring or drilling for oil or natural gas in Canada.

It is noteworthy that provision is made under s. 1201 for two different kinds of deduction, both of which are to be made in respect of "profits reasonably attributable to the production of oil or gas". The one under subs. (4) (i.e., losses of loss wells) is to be made *after* the profits from all wells operated by the taxpayer have been computed and aggregated, whereas the other under subs. (5) is to be made *"in computing"* these same profits for the purpose of the section.

As I take the view that the aggregate of these profits from all wells cannot be determined for the purpose of subs. (4) until the profits of each have been computed and as subs. (5) requires a deduction to be made "in computing" these profits, it follows that I am of opinion that the s. 53 costs specified in subs. (5) must be deducted in respect of each well.

It was strongly urged on behalf of the appellant that the procedure to be followed in determining the base for the allowance granted by the Regulation to a taxpayer that operates more than one oil or gas well is as follows:

> 1. Determine the profits or losses of each producing well in the normal manner by ascertaining the difference between the receipts reasonably attributable to the production of oil or gas from the well and the expenses of earning those receipts.
> 2. Determine the aggregate of the profits of the profitable wells and the aggregate of the losses of the loss wells and deduct the aggregate of the latter from the aggregate of the former.
> 3. Deduct from the amount of profits remaining, the exploration and drilling costs deducted under s. 53 in computing the taxpayer's income.

The difficulty which this reasoning presents to me is that, as I understand the provisions of subs. (5), a taxpayer is *not permitted* "to determine (i.e. compute) . . . . the profits of each producing well in the *normal manner*" for the purpose of this section (1201) if he has deducted under s. 53, in computing his income tax, any sums which are reasonably attributable to the production of oil or gas from such well.

On the contrary he is expressly required by subs. (5) to make the deduction of s. 53 costs "*in computing the profits* reasonably attributable to the production of oil or gas for the purpose of this section" and in my opinion these words carry the deduction there referred to back to the very first step which the taxpayer is required to take in making his calculation under subss. (1) and (4), namely, the computation of the reasonably attributable profits of each well.

The reasoning advanced on behalf of the appellant would require the taxpayer to compute the "profits reasonably attributable to the production of oil or gas from each well" without reference to the deduction for which provision is made in subs. (5) and would require him to deduct the s. 53 costs from the aggregate of such profits minus losses from loss wells without regard to whether or not such costs are reasonably attributable to the production of oil or gas from a well. I am of opinion, on the other hand, that whenever it is necessary for the purposes of s. 1201 for a taxpayer to compute the profits reasonably attributable to the production of oil or gas from a well, he is required to work out the amount, if any, of his s. 53 costs which is reasonably attributable to the production of oil or gas from that well, and if there is no such amount he is not required to make any such deduction. Although the calculating of the amount of such a deduction in reference to each well may appear at first glance to present difficulties, it is nonetheless apparent that the respondent's auditors have not found such difficulties insurmountable because they have made the appropriate deduction in compiling the "profits of profitable wells" for the purpose of presenting this claim.

The terms of s. 1201 have been hereinbefore considered without reference to the case of *Home Oil Company Limited v. Minister of National Revenue*[1], because that case was decided under Regulation 1201 before the enactment of subs. (4) and before the concluding words "in respect of the well" had been deleted from subs. (5).

The *Home Oil* case was thus decided when s. 53 costs were the only deduction authorized by the Regulation and before subs. (4) had made provision for the deduction of losses of producing wells from the aggregate of "the profits reasonably attributable to the production of oil or gas from the

[1] [1955] S.C.R. 733, [1955] 4 D.L.R. 796.

1960
MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.
Ritchie J.

well". The Court was, therefore, only directly concerned with the question of whether the s. 53 costs could be deducted as a lump sum in computing "the *profits* of the well" or whether the latter expression required a separate ascertainment for each profitable well. The decision of this Court, that the section then before it did not authorize such a deduction and that such profits should be separately ascertained, in my opinion applies with equal force to the amended Regulation, and the following observation of Rand J., speaking on behalf of the Court at p. 736, applies directly to the question at issue:

> The allowance under s. 53 is an overall allowance related to total income for a specific purpose; the ascertainment of profits for the purpose of Regulation No. 1201 is on the basis of reasonable relation to the source of income and for a different purpose; and I am unable to agree that the total allowance under s. 53 can be said to be made "in respect of" the profitable wells.

As has been observed, in the original Regulation 1201 as passed by P.C. 6471 of December 22, 1949, there was no provision equivalent to the present subs. (4), and the only express language used in that Regulation requiring that s. 53 costs were to be deducted on a well-to-well basis consisted of the last four words of the then subs. (4) (now subs. (5)), namely, the words "in respect of the well".

As the terms of the new subs. (4) in my view require the profits reasonably attributable to each well to be computed separately before they can be aggregated, and as under subs. (5) the s. 53 deductions must be made in computing those profits, it seems to me to follow that "the purpose of this section" as a whole (s. 1201) cannot be fulfilled unless the deductions for which provision is made in subs. (5) are made "in respect of the well", and it is, therefore, no longer necessary to employ those words in that subsection in order to convey the meaning that the deduction is to be made on a well-to-well basis.

It would make the provisions of subs. (4) quite purposeless if *all* the s. 53 costs were required to be deducted in computing the profits of *each* of a number of wells and as subs. (5) requires the deduction to be made both "in computing the profits..." and "for the purpose of this section" it seems to me that it can only be complied with by deducting, in computing the profits of each well, such of the s. 53 costs as can be related thereto.

To deduct all the s. 53 costs from the aggregate of the profits of *all* the wells is to leave this deduction out of account "in computing the profits" which have been aggregated and to deduct *all* the same costs from *each* well is to defeat "the purpose of this section", but if these costs are related to the individual wells and deducted in computing the profits of each, then it appears to me that the language of subs. (5) has been applied in such manner as to comply with the overall purpose of the Regulation and of the statute as interpreted by the *Home Oil* case.

My opinion as to the applicability of the above quotation from the decision of Rand J. in the *Home Oil* case to the present circumstances is based in some degree on the reasons last recited, but it is to be remembered also that there has been no material change in s. 11(1)(b) of the *Income Tax Act* since that decision was rendered, and that what was there said concerning the meaning and purpose of that subsection has lost none of its force by reason of the change in the Regulation.

In the present case the respondent claimed its allowance under s. 1201 for the year 1951 on the basis, first, that the aggregate losses from loss wells could not properly be deducted from the aggregate profits because subs. (4) was *ultra vires* the authority conferred by s. 11(1)(b), secondly, that the s. 53 deduction could only be made to the extent that the costs therein specified were reasonably attributable to the production of oil or gas from each well, and lastly, that there should be added to the profits reasonably attributable to each well an amount of unrealized profits based on notional sales, from the respondent's producing department to other of its departments, of oil not actually sold by the company during the taxation year.

The learned President of the Exchequer Court, in the course of the decision from which this appeal is asserted, held that subs. (4) of s. 1201 made valid and effective provision for the deduction of the aggregate of reasonably attributable losses from the aggregate of reasonably attributable profits in computing the allowance authorized by s. 11(1)(b). From this finding the Imperial Oil Company

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Ritchie J.

has entered a cross-appeal. I am of opinion that this cross-appeal should be dismissed and I agree with the views expressed by the learned President of the Exchequer Court when he said:

> The power to enact a regulation determining the amount of the deductible allowance permitted by section 11(1)(*b*) of the Act and the base for its computation was granted in the broadest terms and I cannot see any limitation of it such as counsel suggests.

As I have indicated, the provisions of subs. (4) do not appear to me to run contrary to the purposes of the section as a whole or of s. 11(1)(b) of the Income Tax Act because in my view subs. (4) requires the profits of each producing well to be separately computed. As the identity of each well is thus preserved as a unit in the aggregate amount which constitutes the basic ingredient of the calculation required by the subsection, I am of opinion that the allowance for which it provides is made "in respect of an oil well" and therefore *intra vires*.

As to the deduction under subs. (5) of s. 1201, the learned President has held that this is required to be made on a well-to-well basis. From this finding the Minister has appealed. For the reasons hereinbefore stated as well as those stated by the learned President, I am of opinion that the appeal from this finding should be dismissed.

The learned President further held that the unrealized profits reasonably attributable to each well should be taken into account for the purposes of s. 1201 and the Minister has appealed from this finding also. To agree with this finding requires the acceptance of the proposition that "the producing department" of the respondent is a separate entity and involves the recognition of the existence of a profit where there has been no actual sale. As I am unable to view the existence of "the producing department" as a separate entity in a realistic light, and as I feel that no profit exists for the purpose of this section until the oil is sold, I am unable to agree with the finding of the learned President in this regard and to this extent would allow the appeal.

In the result, I am of opinion that the amount of the deductible allowance to which the respondent was entitled in 1951 under s. 11(1)(b) of the Act and s. 1201 of the Regulations is $7,454,263.47 being 33⅓ per cent. of the base of $22,362,790.40 which has been calculated by deducting the unrealized profits and the losses of loss wells from the profits of profitable oil wells as claimed by the company.

I would, therefore, allow the appeal in part and dismiss the counterclaim with costs to follow the event in both cases.

MARTLAND J. (*dissenting in part*):—The relevant facts are set out in the reasons of my brother Judson and do not require repetition. I am in agreement with his conclusions in respect of the cross-appeal and in respect of the contention by the appellant that the amount of $8,642,196.84, respecting increase in unrealized profits in supply, manufacturing and marketing inventories, was not part of the respondent's profits reasonably attributable to the production of oil or gas from all the wells of the company, so as to entitle the respondent to include it in determining the base for its allowance.

I have, however, reached a different conclusion in respect of the item of unrelated drilling, exploration and other costs in the amount of $19,992,588.33.

Regulation 1201 must be read in the light of ss. 12(1) (b) and 11 of the *Income Tax Act*. The former provides:

* * *

12. (1) In computing income, no deduction shall be made in respect of

* * *

(*b*) an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part,

The relevant portions of s. 11 are:

11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year

* * *

(*b*) such amount as an allowance in respect of an oil or gas well, mine or timber limit, if any, as is allowed to the taxpayer by regulation,

* * *

(3) Where a deduction is allowed under paragraph (*b*) of subsection (1) in respect of an oil or gas well, mine or timber limit operated by a lessee, the lessor and lessee may agree as to what portion of the allowance each may deduct and, in the event that they cannot agree, the Minister may fix the portions.

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Martland J.

The deduction in computing income permitted by Regulation 1201 is clearly a depletion allowance, as was stated by Rand J., who delivered the unanimous judgment of this Court in *Home Oil Company Limited v. Minister of National Revenue*[1]:

> That this allowance is made to offset the wasting capital resource is clear from the language of s. 12(*b*) which speaks of "depreciation, obsolescence or depletion", and if its purpose is not to be defeated, the producing wells must be dealt with individually.

Section 11(1)(b) refers to an allowance in respect of an oil or gas well. Section 11(3) makes provision for the portions of the allowance permitted which a lessor and a lessee may respectively deduct where an oil or gas well is operated by a lessee. This, to my mind, contemplates the determination of the depletion allowance on a well by well basis and this was the conclusion reached by this Court in the *Home Oil* case.

Subsection (1) of Regulation 1201 now under consideration reads as follows:

> 1201. (1) Where the taxpayer operates an oil or gas well the deduction allowed for a taxation year is 33⅓ per cent of the profits of the taxpayer for the year reasonably attributable to the production of oil or gas from the well.

It is similar in effect to the subsection which was under consideration in the *Home Oil* case and speaks of "profits of the taxpayer for the year reasonably attributable to the production of oil or gas from the well", which contemplates the determination of profits for each individual well of the taxpayer.

Subsection (4) of Regulation 1201 did not apply in the taxation years under consideration in the *Home Oil* case. It reads as follows:

> (4) Where the taxpayer operates more than one oil or gas well, the profits referred to in subsection one shall be the aggregate of the profits minus the aggregate of the losses of the taxpayer for the year reasonably attributable to the production of oil or gas from all wells operated by the taxpayer.

When this subsection refers to the "aggregate" of profits and the "aggregate" of losses reasonably attributable to the production of oil or gas from all wells operated by the taxpayer it must mean the aggregate of the profits and the

[1] [1955] S.C.R. 733 at 737, [1955] 4 D.L.R. 796.

aggregate of the losses attributable to the individual oil or gas wells from which oil or gas production was obtained. It is speaking of an aggregate of individual items. Consequently the computation must still be made on a well by well basis, but subs. (4) added a new feature to the Regulation in that losses on a per well basis in respect of wells operated at a loss had also to be computed and the aggregate of those losses had to be deducted from the aggregate of the profits earned by the individual profitable wells.

Subsection (5) reads as follows:

> (5) In computing the profits reasonably attributable to the production of oil or gas for the purpose of this section a deduction shall be made equal to the amounts, if any, deducted in computing the taxpayer's income for the taxation year under the provisions of section 53 of Chapter 25 of the Statutes of 1949, Second Session.

It commences with the words "In computing the profits reasonably attributable to the production of oil or gas for the purpose of this section . . . " As above indicated, the computation of profits for the purpose of the section has to be made on an individual well basis. Subsection (1) refers to the profits from the well. Subsection (4) contemplates the obtaining of an aggregate of the profits resulting from the operation of the profitable wells and an aggregate of the losses resulting from the operation of the loss producing wells. When, therefore, subs. (5) refers to the computation of profits reasonably attributable to the production of oil or gas, it is speaking of a computation which has to be made on an individual basis for each well operated by the taxpayer. It calls for "a deduction of the *amounts,* if any, deducted in computing the taxpayer's income for the taxation year under the provisions of s. 53 of c. 25 of the Statutes of 1949, Second Session." In my view this is a requirement that the taxpayer, in respect of each individual well which he operated to produce oil or gas, must make a deduction of the amount, if any, in relation to that well which he had deducted in computing his income for the taxation year under s. 53 of c. 25 of the Statutes of 1949, Second Session.

The relevant portion of s. 53 provides as follows:

> 53. (1) A corporation whose principal business is production, refining or marketing of petroleum, petroleum products or natural gas or exploring or drilling for petroleum or natural gas may deduct in computing its income, for the purposes of *The Income Tax Act,* . . .

1960

MINISTER OF NATIONAL REVENUE v. IMPERIAL OIL LTD.

Martland J.

(a) the aggregate of the drilling and exploration costs, including all general geological and geophysical expenses, incurred by it, directly or indirectly, on or in respect of exploring or drilling for oil or natural gas in Canada

(i) during the taxation year, and

(ii) during previous taxation years, to the extent that they were not deductible in computing income for a previous taxation year,

The deduction which may be made by a corporation which comes within the provisions of this subsection is an aggregate of costs incurred by it for drilling and exploring for oil or natural gas in Canada. The purpose of the subsection is clearly to provide an incentive for oil and gas exploration and for the drilling of wells for the production of those substances. Exploration costs may be incurred without wells necessarily being drilled in the area explored. Drilling costs may be incurred which result only in dry holes.

The purpose of s. 11(1)(b) of the Act is to provide a depletion allowance in respect of a wasting asset, one such asset being oil or gas produced from an operating well. Under Regulation 1201, in the case of an oil or gas well, such allowance is determined on the basis of a percentage of the profits reasonably attributable to the production of oil or gas from such a well.

As I see it, the purpose of subs. (5) of Regulation 1201 is to require that, in computing the profits attributable to the production of oil or gas from operating wells, account must be taken of any amounts expended for exploration and drilling in relation to such wells, which have been included in the aggregate of costs deducted by a taxpayer in computing income under the authority of s. 53.

Considerable stress was laid in argument on behalf of the appellant upon the fact that, when the new subs. (5) of Regulation 1201 was enacted to replace the former subs. (4), the words "in respect of the well", which appeared at the end of subs. (4), were eliminated. It was contended that the meaning of this subsection was thereby altered substantially so as to require the deduction of all drilling and exploration costs which had been claimed by a corporation under s. 53, whether such costs related to wells which it operated or not. I do not agree that the deletion of those words has that result. It is my view that the words were omitted from the new subs. (5) so as to make it conform with the provisions introduced into Regulation 1201 by the new subs. (4). That subsection for the first time introduced the element of a deduction of losses from loss producing wells where a taxpayer operated more than one well. It involved aggregating profits from profitable wells and losses from loss producing wells. Consequently, where subs. (4) has application, consideration now has to be given to s. 53 expenditures in relation to all wells operated by the taxpayer, whether profitable or loss producing, and the words "in respect of the well" were no longer apt for that purpose.

I agree with the disposition of this appeal proposed by my brother Ritchie.

Appeal allowed and cross-appeal dismissed with costs, CARTWRIGHT, MARTLAND *and* RITCHIE JJ. *dissenting in part.*

Solicitor for the appellant: A. A. McGrory, Ottawa.

Solicitors for the respondent: Blake, Cassels & Graydon, Toronto.