
April 1967

The Queen in the Right of the Province of Ontario v. Jennings (1966), 57 D.L.R. (2d) 644 Supreme Court of Canada

Ronald Appleby

Follow this and additional works at: <https://digitalcommons.osgoode.yorku.ca/ohlj>

Commentary

Citation Information

Appleby, Ronald. "The Queen in the Right of the Province of Ontario v. Jennings (1966), 57 D.L.R. (2d) 644 Supreme Court of Canada." *Osgoode Hall Law Journal* 5.1 (1967) : 44-54.

DOI: <https://doi.org/10.60082/2817-5069.2405>

<https://digitalcommons.osgoode.yorku.ca/ohlj/vol5/iss1/4>

This Commentary is brought to you for free and open access by the Journals at Osgoode Digital Commons. It has been accepted for inclusion in Osgoode Hall Law Journal by an authorized editor of Osgoode Digital Commons.

The Queen in the Right of the Province of Ontario v. Jennings (1966), 57 D.L.R.
(2d) 644 Supreme Court of Canada

It seems to me that in the stage of industrial development now existing it must be accepted that legislation to achieve industrial peace and to provide a forum for the quick determination of labour-management disputes is legislation in the public interest, beneficial to employee and employer.¹⁸

Surely there must be a case where, because of judicial review by certiorari, the courts and the prosecutor are in contempt of the legislature.

D. E. FRANKS.*

TAXATION

The Queen in the Right of the Province of Ontario v. Jennings (1966), 57 D.L.R. (2d) 644. Supreme Court of Canada.

DAMAGES—PERSONAL INJURIES—LOSS OF EARNINGS—DEDUCTION OF INCOME TAXES IN MEASURING COMPENSATION FOR PERSONAL INJURIES.

Claims for damages for personal injuries are a common occurrence in modern litigation and often part of the claim is for loss of earnings, past and prospective. Assessing the damages is a difficult task, both for the court deciding the matter, and for counsel attempting to negotiate a settlement. One of the most contentious issues involved in calculating the award for loss of future earnings is whether the fact that the plaintiff would have been liable for income tax, had he received the income normally, should be taken into account to reduce the damages. Because of its importance for everyday practice, the recent decision in *The Queen in the Right of the Province of Ontario v. Jennings*,¹ in which the Supreme Court of Canada finally decided the issue, is extremely significant. The decision is noteworthy for another reason as well. In deciding to ignore the incidence of tax, the court rejected the decision of the House of Lords in *British Transportation Commission v. Gourley*² where the damages awarded were an amount reduced by the plaintiff's tax liability.³

The plaintiff, Jennings, fifty years of age, was a successful vice-president of a large manufacturing concern. He was so severely injured in an automobile accident caused by the defendants' negligence that from the time of the accident he remained unconscious. His life expectancy was reduced from twenty-two to five years and those remaining years would likely be spent in hospital. The trial judge, Ferguson,

¹⁸ [1966] S.C.R. at 292, 56 D.L.R. (2d) at 201. (Italics mine.)

* D. E. Franks, B.A. (McMaster) is a member of the 1967 graduating class at Osgoode Hall Law School.

¹ (1966), 57 D.L.R. (2d) 644, (affirming) [1965] 2 O.R. 285; (1965), 50 D.L.R. (2d) 385.

² [1956] A.C. 185.

³ The express rejection of the House of Lords decision by the Supreme Court of Canada may indicate the beginning of an important trend in Canadian jurisprudence. For a comment on this aspect of the *Jennings* case see Bale, G., (1966), 44 CAN. BAR REV. 724, 726.

J., awarded the plaintiff \$146,000 in damages, and in assessing the portion of the damages for loss of future earnings he followed the *Gourley* decision and deducted a sum for the income tax that Jennings would have had to pay had he earned the income. The majority of the Ontario Court of Appeal allowed the plaintiff's appeal and increased the total award to \$180,000.⁴ Their decision was based, not on a rejection of the *Gourley* principle, but on the fact that a proper foundation had not been laid for its application in this case.⁵

The Crown appealed this decision and the Supreme Court of Canada unanimously dismissed the appeal. The important comments with respect to the tax issue are to be found in the judgment of Judson, J.⁶ He felt that since the non-taxability of damages had not yet been established in Canada in litigation involving revenue authorities, there was no basis on which to apply *Gourley*. However, he bases his decision on much broader grounds and expressly rejects the principle in the *Gourley* case. In effect, he holds that whether or not the award for loss of future earnings is taxable in the recipient's hands, the plaintiff's tax liability should not be taken into account in assessing the damages. His reasons can be divided into three categories.

The plaintiff is being compensated not for loss of future earnings, but for loss of earning capacity, i.e. a capital asset is being replaced and in Canada capital is not taxed. The value of this capital asset is the present value of the future income that it would have generated, and this income is less all expenses which would be incurred to earn it. However, income tax is not a cost of earning income but merely a compulsory disposition of part of the funds and should no more be considered than any other use which the plaintiff would have made of his funds. This argument is in agreement with one of the minority views in the Seventh Report of the Law Reform Committee in England.⁷ It has a great deal of merit and will be discussed in greater detail below.

The second reason contains two related points. The first is an answer to the submission that if tax is ignored, the plaintiff will be overcompensated. Judson, J. says that the computation of the lump sum involves so many contingencies and uncertainties that mathematical precision is impossible. A seriously disabled plaintiff would usually prefer his earning capacity unimpaired, or the effect of impairment

⁴ [1965] 2 O.R. 285; (1965) 50 D.L.R. (2d) 385. Only part of the increase was because of the tax issue.

⁵ The *Gourley* case was decided on the basis of an agreement by counsel that the damages would not be taxable in the hands of the plaintiff. However, in *Jennings* there was no such agreement and therefore Kelly, J.A. at p. 419, put the onus on the defendant to show that the non-taxability of damages has been authoritatively decided in proceedings involving the Minister of National Revenue. He also put the onus on the defendant to adduce satisfactory evidence as to the plaintiff's taxable income and other financial circumstances which might be relevant. Since the defendant had not satisfactorily discharged these burdens there was no basis for applying the rule in *Gourley's* case.

⁶ (1966) 57 D.L.R. (2d) 644, 654.

⁷ The 7th Report of the Law Reform Committee, Cmnd. 501 in England with respect to the issue in *Gourley's* case. The report was made to Parliament in August 1958.

periodically reassessed, than the receipt of the lump sum, so that the amount of the award is a guess that is nearly always to the plaintiff's detriment. It would be grossly unfair to add another uncertainty, the future incidence of tax on the plaintiff's income, and thereby increase the detriment.

Also, if no tax is levied on the plaintiff's award by the Department of Revenue, it would not be fair to allow the defendant to complain about this aspect of tax policy and reap the benefit for himself or his insurance company.

Finally, it was held that the application of the *Gourley* principle leads to many difficulties in practice. In litigation, the evidence with respect to the damages claimed usually involves a trial within the main trial establishing liability. Evidence with respect to the incidence of tax will, in effect, be a third trial and make the litigation even more cumbersome and costly. Further, Judson, J. notes many problems in determining the base on which the tax will be computed, e.g. possibilities of marriage, children, or tax planning to reduce future tax; effect of outside investment income; foreign plaintiffs and tax systems.⁸

Development of Law

Today we have a situation in which the House of Lords in England and the Supreme Court of Canada have taken diametrically opposite positions on the same issue. Before we discuss the merits of each viewpoint and compare and contrast their effects, let us note the development of the relevant law on the problem.

Before *Gourley*, the law in England was the same as it now is in Canada following the *Jennings* decision; that is, tax liability was ignored in assessing damages for loss of future earnings.⁹ These decisions were based on two Latin maxims: *restitutio in integrum*—the plaintiff should be put in the same position that he would have been in but for the wrong, i.e. receipt of his fees in full; and *res inter alios acta*, any tax liability would be a matter between the plaintiff

⁸ For a comprehensive analysis of these practical difficulties of the *Gourley* decision, see KEMP AND KEMP, *THE QUANTUM OF DAMAGES IN PERSONAL INJURY CASES*, (2nd edition), (London: Sweet & Maxwell Ltd. 1961), Vol. 1, Appendix E at p. 717.

⁹ The question of including liability for income tax in assessing damages for loss of future earnings first arose in England in *Fairholme v. Firth and Brown Ltd.*, (1933) 49 T.L.R. 470, which involved a breach of contract. Parcq, J., held that the damages could not be reduced by the income tax the plaintiff would have paid had he earned the income. Lord Sorn, in a Scottish personal injury case, *M'Daid v. Clyde Navigation Trustees*, [1946] S.C. 462; [1946] S.L.T. 127, reached the opposite conclusion and assessed damages on the basis of net income after tax. However, this conclusion was challenged by Lord Keith in another Scottish case, *Blackwood v. Andre*, [1947] S.C. 333. *Jordan v. The Limmer and Trinidad Lake Asphalt Co. Ltd.*, [1946] K.B. 356; [1946] 1 All E.R. 527, an English case decided shortly after *M'Daid*, did not follow nor even mention it but followed the principle in *Fairholme v. Firth and Brown Ltd.* The problem was first presented to the English Court of Appeal in *Billingham v. Hughes*, [1949] 1 K.B. 643, [1949] 1 All E.R. 684, (personal injuries case) and the court, after reviewing the authorities, unanimously decided to ignore the incidence of income tax.

and the Crown.¹⁰ In Ontario prior to 1956, there were only three reported cases¹¹ which dealt with this issue and all of them excluded tax consideration on the basis of the *res inter alios acta* arguments of the English cases.

British Transportation Commission v. Gourley was the cause of all the problems in this area of the law and the decision in this case established an entirely new principle. In assessing damages for loss of taxable income, if the lump sum is not taxable in the hands of the plaintiff then the award should take into account the tax that the plaintiff would have had to pay had he received the income in the ordinary course of events. This decision has been the subject of much comment, some favourable, but most critical.¹² It has been applied in England in many cases since 1956, and the scope of its application has been extended to cover many situations other than personal injury cases.

The rule in *Gourley* has been applied in cases of damages for wrongful dismissal;¹³ in a libel case;¹⁴ and to a claim for loss of profit due to an expropriation under a statute;¹⁵ among others.¹⁶ In *Hall & Co. Ltd. v. Pearlberg*,¹⁷ it was held that damages for lost rent which would be taxable in the plaintiff's hands as profits, ought not to be diminished on the *Gourley* principle. A similar result was reached in *Diamond v. Campbell-Jones*,¹⁸ where the lost profit was due to a breach of a contract to sell a leasehold interest. Generally, in situations where there are damages for lost profit due to breaches of commercial contracts (other than for employment), since the damages must be included as profits for tax purposes, the full amount is awarded to the plaintiff.¹⁹

¹⁰ See *Billingham v. Hughes*, [1949] 1 K.B. 643; [1949] 1 All E.R. 684.

¹¹ *Fine v. Toronto Transportation Commission*, [1945] O.W.N. 901, (personal injuries). *Bowers v. J. Hollinger & Co. Ltd.*, [1946] O.R. 526; [1946] 4 D.L.R. 186, (personal injuries). *Anderson v. International Waves Ltd.*, [1951] O.W.N. 113, (loss of profit due to breach of contract for sale of goods).

¹² See KEMP AND KEMP, *op. cit.*, ch. 3; Vineberg, P. F., 34 CAN. BAR REV. 940; Jolowicz J.A., DAMAGES AND INCOME TAX, [1959] C.A.M.B. L.J. 86; Stewart, LAW SOCIETY OF UPPER CANADA, SPECIAL LECTURES, 1958, Part I, 120; Fyfe, *ibid.* p. 7—all of which criticize *Gourley*. Baxter, 19 Mod. L.R. 365 (accountant's viewpoint); For a note supporting the principle see Tucker, [1959] C.A.M.B. L.J. 185.

¹³ *Beach v. Reed Corrugated Cases Ltd.*, [1956] 1 W.L.R. 807; *Phipps v. Orthodox Unit Trusts Ltd.* [1958] 1 Q.B. 314; [1957] 3 All E.R. 305; *Parsons v. B.N.W. Laboratories Ltd.*, [1963] 2 All E.R. 658. In the last case Sellers, L.J., has a very persuasive dissent at p. 660. He wishes to restrict *Gourley* to tort cases only.

¹⁴ *Lewis v. Daily Telegraph*, [1964] A.C. 234.

¹⁵ *West Suffolk County Council v. W. Rought Ltd.*, [1957] A.C. 403.

¹⁶ See also: Northern Ireland—*Morahan v. Archer and Belfast Corporation*, [1957] N.I. 61. Scotland—*Spencer v. McMillan's Trustees*, [1958] S.C. 300. England—*Thomas McGhie & Sons, Ltd. v. British Transportation Commission*, [1963] 1 Q.B. 125; [1962] 2 All E.R. 646.

¹⁷ [1956] 1 W.L.R. 244.

¹⁸ [1961] Ch. 22; [1960] 1 All E.R. 583.

¹⁹ However, an attempt was made by Lord Hunter in *Stewart v. Glentagart Ltd.*, [1963] S.L.T. 119, to extend the rule in *Gourley* to cover even cases where the award of damages was to be subject to tax. As elaborated by the appellant in *Parsons v. B.N.W. Laboratories Ltd.*, [1963] 2 All E.R. 658,

[Footnote continued on next page]

In other common law countries the *Gourley* decision has been for the most part unfavourably received although it was followed in a personal injury case in New Zealand.²⁰ As yet the *Gourley* principle has not been applied in Australia and has received no support in the U.S.²¹

The *Gourley* decision has been given a varied reception by Canadian Courts. It has been applied, without comment, in personal injury cases by courts in Newfoundland²² and Saskatchewan.²³ The Alberta Court of Appeal mentioned that tax liability should be considered in assessing damages for loss of earnings caused by breach of a contract to sell shares in a business.²⁴ In two recent cases in British Columbia,²⁵ the court, although agreeing with the decision in *Gourley*, felt it could not apply the principle in the personal injury cases before it, since in

this argument sets up an equation in which tax is taken into account on both sides. First, damages are assessed on the basis of net income after taxes and then, if the award is taxable, a sum must be added to it so that the plaintiff eventually will receive the correct sum after the tax on his damages has been met. This was a completely unanticipated and unjustified extension of the *Gourley* case (which was decided specifically on the basis that the award was not taxable) and was rejected by the Court of Appeal in the *Parsons* case. It is interesting to note that, although in the *Parsons* case this approach would have been to the defendant's advantage, generally, where the award is subject to tax, an assessment on the above basis would be to the plaintiff's benefit because of our progressive taxation. This can easily be shown:

Let t_1 represent the average rate of tax on the income if earned annually.

Let t_2 represent the average rate of tax on the lump sum award.

Let $a_{\overline{n}}$ represent the discounting factor.

Let X represent the annual income before taxes.

Therefore $(1 - t_1) X$ would be the annual income after taxes and $(1 - t_1) X a_{\overline{n}}$ would be the net lump sum award that the plaintiff should receive on the above basis.

For the plaintiff to receive this the award of damages would have to be $(1 - t_1)$

————— $X a_{\overline{n}}$ since the award would be taxed at the rate of t_2 .

$(1 - t_2)$

On the strict *Gourley* basis where the award is taxable the damages would be $X a_{\overline{n}}$ and the plaintiff's net receipts after paying taxes would be $(1 - t_2) X a_{\overline{n}}$. Thus, in the first case the plaintiff is left with $(1 - t_1) X a_{\overline{n}}$ whereas when the assessment itself isn't concerned with income tax liability he receives $(1 - t_2) X a_{\overline{n}}$. Since $t_1 \leq t_2$ and $0 \leq t_1 < 1$

$$0 \leq t_2 < 1$$

Therefore $(1 - t_1) X a_{\overline{n}} \geq (1 - t_2) X a_{\overline{n}}$.

That is with the former approach (that rejected in the *Parsons* case) the plaintiff is left with a larger net award (or at least as great where t_1 equals t_2).

²⁰ *Smith v. Wellington Manufacturing Co.*, [1956] N.Z.L.R. 491.

²¹ Under American federal law damages for loss of earnings in personal injury cases are exempted from tax by the Internal Revenue Code 1954, S. 104 (a) (2), and the award itself cannot be diminished because of income tax considerations. See *Pfister v. City of Cleveland*, 113 N.E. 2d 366 (1953).

²² *Power v. Stoyles*, (1959) 17 D.L.R. (2d) 239.

²³ *Smith v. C.P.R. Co.*, (1963) 45 W.W.R. 170; (1964) 41 D.L.R. (2d) 249.

²⁴ *Widrig v. Strazer*, (1963) 41 W.W.R. 257; 37 D.L.R. (2d) 629, decision of Alberta C.A. reversed by Supreme Court of Canada, [1964] S.C.R. 376; (1964) 47 W.W.R. 268; 44 D.L.R. (2d) 1, but without particular reference to the income tax problem.

²⁵ *Buck v. Rostill*, (1965) 51 W.W.R. 319. *Curbello v. Thompson*, (1966) 58 D.L.R. (2d) 48.

Canada the damages award might be taxable. The Ontario courts have applied *Gourley* in cases of breach of contract of employment.²⁶ These cases present a prime example of some of the undesirable consequences of the British approach. The employer is actually better off financially by breaching the contract than he is by performing. The only decision prior to the *Jennings* case which rejected the *Gourley* approach in principle was the judgment of Nitikman, J. of the Manitoba Queens Bench in *Soltys and Soltys v. Middup Moving & Storage Ltd.*²⁷

Comparison of the Approaches

The *Jennings* decision is most satisfactory in respect of its treatment of the tax issue and the rejection of the rule in *Gourley's* case. The divergence may be explained, in part, by an apparent tendency of the British courts to be overly receptive to an appeal from the defendant to be spared from ruin, and the Canadian and American courts' sympathy for the plight of the plaintiff. More important than this, however, is the fact that the rule in *Jennings's* case has a superior theoretical foundation, leads to more equitable results and, administratively, is more feasible. The question of whether the result in *Gourley* was satisfactory was referred to the Law Reform Committee in England.²⁸ The majority of the members (nine) agreed with the result in *Gourley*; three members thought the law should be as before *Gourley's* case; and three members felt the law should be as before *Gourley* except that the damages should be taxable in the plaintiff's hands.

Those who subscribe to the last opinion maintain that the damages represent income in the hands of the recipient and base their reasoning on a general principle of revenue law that damages retain the characteristics of the assets they replace.²⁹ Damages for loss of profit are taxable, but damages for loss of capital will be no more taxable than would the capital asset which the plaintiff has lost.³⁰ The damages are income because, according to this viewpoint, they are replacing, not the earning capacity (the capital asset), but the future earnings themselves. From a purely fiscal point of view this approach might be the fairest since the Crown gets its portion and yet the plaintiff's financial position has not really suffered. Since the lump sum would be taxable, then, according to the reasoning in *Gourley*, taxes could not be considered in assessing damages. The effect would be that the Crown is reshifting the benefit of the tax back from the defendant to itself. This approach is still open in Britain and awaits a decision in a case involving revenue authorities. It may well be the solution

²⁶ *Gourley* was applied in *Walker v. Copp Clark Publishing Co.*, [1962] O.R. 622; 33 D.L.R. (2d) 338. In *Postums v. Toronto Stock Exchange and Gardiner*, [1964] 2 O.R. 547; 46 D.L.R. (2d) 210, Gale, J., as he then was, indicated that had damages been awarded, he would have made a deduction for tax in the assessment.

²⁷ (1963) 44 W.W.R. 522; (1964) 41 D.L.R. (2d) 576.

²⁸ *Supra*, footnote 7.

²⁹ *Burma Steamship Co. v. Inland Revenue Commissioners*, [1931] S.C. 156.

³⁰ *Ibid.* at p. 159.

to many of the problems caused by the *Gourley* case. Of course, the new problem of selecting the proper basis on which to assess this tax would then arise. To tax the entire lump sum as income earned in the year received, at the going rates, would be grossly unfair. Some type of spreading mechanism would have to be worked out.³¹ In Canada, whether a court, in a binding decision, ultimately decides that damages for loss of future earnings in personal injury cases are taxable or not is irrelevant to the assessment of these damages. It is purely of interest in tax law because the Supreme Court held that in no case would tax liability reduce the assessment.

Even if we accept the award as not taxable, as the House of Lords did in *Gourley*, the Canadian decision is superior. The basic principle for the measure of damages, in tort as well as in contract, is that there should be *restitutio in integrum*, i.e. "that sum of money which will put the party who has been injured or who has suffered, in the same position as he would have been if he had not sustained the wrong for which he is now getting his compensation or reparation."³²

The maxim was employed in *Billingham v. Hughes* in refusing to deduct tax, but in *Gourley* it was interpreted to provide a basis for the new rule. Earl Jowitt, who delivered the leading judgment, said:³³

. . . for what damages is he liable? and if we apply the dominant rule, we should answer: 'He is liable for such damages as by reason of his wrongdoing, the plaintiff has sustained' . . . to ignore the tax element at the present day would be to act in a manner out of touch with reality. Nor can I regard the tax element as so remote that it should be disregarded in assessing damages. The obligation to pay tax . . . is almost universal in its application . . . no sensible person any longer regards the net earnings from his trade or profession as the equivalent of his available income. . . . I see no reason why in this case we should depart from the rule or why respondent should not have his damages assessed upon the basis of what he has really lost, and I consider that in determining what he has really lost the judge ought to have considered the tax liability of the respondent.

Thus, in restoring the plaintiff's position and evaluating the lost capital asset, the court finds that tax is a relevant factor. There are two major criticisms of this analysis both of which are corrected by the approach of the Supreme Court of Canada.

First, the idea that taxes are not too remote and, therefore, should be considered, is a novel and unjustified use of the concept of remoteness. This concept, as applied in tort and breach of contract cases, is only used to test whether the damages claimed flowed immediately and necessarily from the injury.

³¹ But see *Supra*, footnote 19, where a model is used to show a possible approach when the award of damages is taxable in the plaintiff's hands. If the Crown in Britain were to decide to tax damage awards for loss of earnings in personal injury cases, it may be possible to resort to the reasoning submitted by the appellant in the *Parsons* case *supra*. Although the defendant would then be paying higher damages, the result for the plaintiff would be, in effect, a spreading mechanism for the tax, since he would be left with the present value of his future yearly income after taxes.

³² Per Lord Blackburn in *Livingstone v. Rawyards Coal Co.*, (1880) 5 A.C. 25, 29. See also *McNeil v. Fingard*, [1945] O.R. 396 (Ont. C.A.).

³³ *Supra*, footnote 2 at 202, 203.

Secondly, the court in *Gourley* created what one commentator has termed a "miracle of alchemy."³⁴ That is, for the purposes of tax law, the damages are capital awarded in respect of a capital loss (and therefore not taxable); but, for the purposes of assessing damages his loss is income, for how else does his liability for income tax become relevant? This has been answered by the submission that although the award is capital, in valuing that asset the basis should be income, and for this purpose tax can be considered.³⁵ The error in this argument (and in the non-remoteness argument) is in considering income tax an element of the cost of earning income. As has been mentioned above³⁶ Judson, J., in *Jennings* case realizes that income tax is not a cost but a compulsory disposition of income. It is a disbursement of the funds after they have been earned, an incident of earning income and not an expense incurred to earn it. No matter how certain the disbursement may be the court is not justified in reducing the value of the capital asset because of it.

There is another unsatisfactory result of *Gourley* which Judson, J. highlights. It is the defendant who is getting the benefit from the Crown not taxing the damages. If the plaintiff had earned the income he would have paid taxes to the Crown, but if *Gourley* is applied the plaintiff is now paying those taxes to the defendant and, often in modern litigation, that means to a wealthy insurance company. It is inconceivable that the Crown should wish to subsidize in this way the sole person who is responsible for the damage—he who is the author of the tragedy. As Lord Keith said in *Blackwood v. Andre*,³⁷

Further the argument seems to ignore the fact that the only person who is going to benefit is the person who is liable in damages. There is no suggestion that he will account to the Revenue for the capitalized income tax which *ex hypothesi* has been taken into account in assessing the damages.

A Hypothetical Situation

As persuasive as these theoretical arguments may be, it is in the actual practical application that the superiority of the *Jennings* principle is really demonstrated. This can be best illustrated by an example. Let us begin with a very simple hypothetical situation which we will gradually complicate.

P, our plaintiff, is permanently disabled in an accident caused by the defendant's negligence and he can never work again. At the time of the accident he was fifty years old, earning \$10,000.00 per year, in good health, married to a thirty-year old woman and had no children. He had no income other than his salary and his wife had no income. His net income after taxes based on present rates would be \$8,408.00.³⁸ Let us assume he had fifteen more working years and that while he

³⁴ Jolowicz, [1959] *CAMB. L.J.* 86.

³⁵ Tucker, [1959] *CAMB. L.J.* 185.

³⁶ *Supra*, footnote 6, at 656.

³⁷ [1947] *S.C.* 333.

³⁸ *Income Tax Act R.S.C. 1952, c. 148, s. 32* (as amended to 1966, *C.C.H. Canadian Ltd.*).

cannot work any longer, his life expectancy has not been reduced.³⁹ If the courts were to apply the principle of *restitutio in integrum* strictly, the lump sum damages awarded for loss of future earnings should be sufficient to buy P an annuity to last either as long as he lives or fifteen years, whichever is less.⁴⁰ On the basis of the *Gourley* case, the annuity should provide P with a sum equal to his after-tax income annually. However, when he receives that annuity he will have to pay tax on the interest portion of each payment⁴¹ and, therefore, will be left with a sum less than his after-tax earnings. Thus the award should be increased to provide an annuity which will equal, after tax has been paid on it, his original after-tax income. Therefore, in applying *Gourley*, a court should have to set off against the taxes reducing the award, any taxes which P might have to pay from the disposition of his lump sum. This problem has not been considered in the courts and in practice they do not determine the award on such an actuarially precise basis, but if they do not, why should the court suddenly become precision and dollar-conscious with respect to one element—income taxes?

In computing the tax to be deducted, what rate should be used? Lord Goddard said⁴² the present rate should be used, but this might be unfair in Canada where the rates have a habit of fluctuating from year to year, and where the provinces also impose income tax, so that by moving from Ontario to Quebec P would have been subject to different rates.

Now, let us complicate the problem. If P has dependent children they increase his exempt income, but can be included only as long as they remain dependents. However, if he has none what is the likelihood of his having children? His wife is young. Is this not a factor which should be considered?

What if P has substantial investment income? This leads to a multitude of problems. If the taxes deducted are computed at the marginal rate based on his total income, then the damages awarded will be greatly reduced. This was exactly the situation in *Gourley* where the effect of the income tax liability on a plaintiff with a large

³⁹ If his life expectancy had been shortened, the position apparently is that the award would be based on his years now remaining and not on his life expectancy prior to the accident. See *Oliver v. Ashman*, [1962] 2 Q.B. 210; *Wise v. Kay*, [1962] 1 Q.B. 638. In Canada, although the damages in *Jennings* were computed on the basis of the shortened life expectancy, the issue has not been decided by the Supreme Court. The point was not argued in the *Jennings* case before the Supreme Court, however Cartwright, J., at 653, 654 indicates that he does not express agreement with this approach and leaves it open to future litigation. For a criticism of the present position see Fleming, *The Lost Years*, 50 CAL. L. REV. 598.

⁴⁰ This would be provided by a 15 year temporary immediate life annuity (12) which expressed in actuarial symbols for a 50 year old plaintiff is a $50 \cdot \dot{\cdot} 15$. To provide \$3,408 per year, payable in a monthly basis (as his income was probably payable), based on Manufacturers Life Insurance Co. A66 Manual, a sum of \$81,290 would be necessary.

⁴¹ Income Tax Act, R.S.C. 1952, c. 148 (as amended to 1966—C.C.H. Canadian Limited) ss. 6(1)(aa), 7(5), 11(1)(k).

⁴² *Supra*, footnote 2, at 209.

fixed investment income was to reduce the award of damages from £37,720 to £6,695. Further, what is the probability that this investment income will remain at the present level? The court must consider the different possibilities here. It is very likely that a man in this position will obtain legal and accounting advice to minimize his tax liability by means of tax planning schemes, or reduce his investment income through gift programs.

What if P were from France? Would the court not have to inquire into French tax law,⁴³ and how would this affect the application of the rule in *Gourley's* case?

If the court must consider all these matters then evidence must be adduced pertaining to the plaintiff's financial situation and the relevant tax law. This leads to problems of onus of proof. Kelly, J.A. in the Ontario Court of Appeal⁴⁴ put the burden on the defendant, whereas English cases have put the burden on the plaintiff to present such evidence.⁴⁵ The court will have to decide if the lump sum will be taxable or not, and also, if the lost income was taxable income, before *Gourley* can be applied. The civil courts will be turned into bodies of fiscal inquiry. There will be discovery on tax matters and the plaintiff may be required to disclose confidential tax and financial information. Certainly, this intrusion is undesirably oppressive to a plaintiff who has been wronged already. Can it be said that the result of applying the rule in *Gourley* is so logically and equitably satisfying that it justifies the extra cost, time and complexity of litigation?

All these problems and difficulties inherent in the House of Lords approach disappear in Canada following the *Jennings* case. P's damages would be assessed on the basis of his loss of \$10,000.00 per annum (taking into account the proper contingencies) and that is that. No consideration is necessary of all the other extraneous matters required by the *Gourley* case. Of course, if the Department of Revenue wishes to tax P on the proceeds, then that is a matter between them, and does not affect the damages which the defendant must pay to the plaintiff.

Conclusion

The Supreme Court of Canada, in the *Jennings* case, has given substantial cause for greater confidence in the maturity and independence of the Canadian judiciary.⁴⁶ It has rejected an unhappy position of the House of Lords in favour of a common sense and legally sound approach. After ten years, Canadian lawyers are finally able to advise their clients confidently with respect to the effect of income tax on damage awards.

RONALD APPLEBY.*

⁴³ See *Praet (Julien) et al, S/A v. H. G. Poland Ltd.*, [1962] 1 Lloyd's Rep. 566 (Belgian law involved).

⁴⁴ *Supra*, footnote 5.

⁴⁵ See *Hall & Co. Ltd. v. Pearlberg*, [1956] 1 W.L.R. 244; *West Suffolk County Council v. W. Rought Ltd.*, [1957] A.C. 403; *Phipps v. Orthodox Unit Trusts Ltd.*, [1958] 1 Q.B. 314, [1957] 3 All E.R. 305.

⁴⁶ *Supra*, footnote 3.

* Ronald Appleby, B.Com. (Toronto), is a second year student at Osgoode Hall Law School.