1962
Oct. 19
1963
Dec. 31

BETWEEN:

THE MINISTER OF NATIONAL REVENUE ..... APPELLANT;

AND

VALCLAIR INVESTMENT COMPANY LIMITED ..... RESPONDENT.

Revenue—Income tax—Income Tax Act, R S C. 1952, c. 148, ss. 3, 4 and 139(1)(e)—Investment Company—Sale of real estate—Income or capital gain—Trading transaction—Meaning of "Investment", "Undertaking", "Enterprise", and "Adventure"—Capital accretion on an investment.

The respondent, an investment company incorporated by Dominion Letters Patent in 1939, had about $2,000,000 invested in Canadian revenue producing shares, when, in 1951, allegedly to create some diversification of investment, it purchased a farm property in Côte St-Luc, Parish of Notre Dame de Grâce, near Montreal for $135,000, this being the sole purchase of real estate in its 20 years of operation. When the land was purchased it was completely surrounded by other farms and no development in the area had taken place except for a small one near the City Hall of Côte St-Luc A few months after the purchase, the company leased the property for one year to the man who had been operating it as a farm for over ten years, at a rental of $250 per annum, the lessee to pay the taxes. The lease was terminable by the lessor on short notice in the event of a sale. The tenant continued to occupy the property under lease until it was sold in March, 1954. No effort to sell the property had been made by the company by way of listing or advertising it and the offer to purchase it accepted by the company was unsolicited It resulted in the sale of the property for $300,500. The appellant added the profit of $169,533 50 realized on the sale to the company's declared income for the 1954 taxation year.

Held: That in order for a purchase to qualify as an investment, the object purchased must at least be susceptible of yielding an annual return such as rental, dividends or interest, but the amount of the return is not important.

2. That whether the transaction falls within the meaning of the words "undertaking" or "adventure" depends on the degree of risk and speculation which it entails, and what could amount to a great risk for one person might be, depending on the circumstances, negligible to another.

3. That this was not an undertaking or an adventure in the nature of trade since the elements of speculation and risk were negligible, the only risk facing the company being the duration of the waiting period before development reached the locality of its property, and its financial position was such that it could easily afford to bide its time.

4. That even if the transaction could be called "an adventure" it would not attract income tax unless it also bears the badges of trade.

5. That in the present case there is an absence of evidence of "commercial animus" and it cannot be said that the company carried out the trans-

action in issue in a manner characteristic of those who are trading in real estate.

6. That the gain in question was the realization by the company of a capital accretion on an investment which is not subject to tax.

7. That the appeal is dismissed.

APPEAL from a decision of the Tax Appeal Board.

The appeal was heard before the Honourable Mr. Justice Kearney at Montreal.

Paul Boivin, Q.C. and *Paul Ollivier* for appellant.

P. N. Thorsteinsson and *Philippe Guay* for respondent.

The facts and questions of law raised are stated in the reasons for judgment.

KEARNEY J. now (December 31, 1963) delivered the following judgment:

This is an appeal from a decision of the Tax Appeal Board dated November 28, 1961[1], wherein an appeal by the respondent from a reassessment made by the Minister, which added $169,533.50 to the taxpayer's previously declared income for its taxation year 1954, was maintained.

The appellant submits that the said decision was unfounded in fact and in law and that the aforesaid sum was not a capital gain on an investment but a profit made by the respondent on a sale of real estate under circumstances later described which stamped it as a trading transaction subject to tax within the meaning of ss. 3, 4 and 139(1)(*e*). The provisions of these sections read as follows:

3 The income of a taxpayer for a taxation year for the purposes of this Part is his income for the year from all sources inside or outside Canada and, without restricting the generality of the foregoing, includes income for the year from all

(*a*) businesses,

(*b*) property, and

(*c*) offices and employments.

4. Subject to the other provisions of this Part, income for a taxation year from a business or property is the profit therefrom for the year.

139. (1) In this Act,

(*e*) "business" includes a profession, calling, trade, manufacture or undertaking of any kind whatsoever and includes an adventure or concern in the nature of trade but does not include an office or employment;

[1] 28 Tax A.B.C. 193.

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The respondent, *per contra,* contends that the proceeds from the sale in question did not constitute taxable income but was a capital gain realized on an investment and it adopted as its own the reasons given in the said decision.

Another similar appeal, *post* p. 478 *The Minister of National Revenue v. Cosmos Inc.,* was the next case on the roll for hearing and was one in which the respective parties were represented by the same counsel engaged in the present case. Counsel agreed that the evidence to be placed before this Court would be identical to that filed before the Board, consisting in each case of a transcript of the evidence, all exhibits, the documents furnished to the said Appeal Board by the Minister, as required by s. 89(4), all of which were duly filed.

Counsel furthermore declared that they proposed to make only one argument which would apply to both cases, since the legal principles involved were the same although factually the cases are quite separate and distinct and the shareholders were not the same in both instances.

The main facts of the case are as follows.

The respondent (hereinafter sometimes referred to as "the Company" or "the taxpayer") was incorporated by Dominion Letters Patent in 1939 and has been admittedly an investment company and treated as such by the Department of National Revenue, except in respect of the one transaction in issue.

The Company is and has been, at all material times, owned and controlled by La Société des Aéroplanes H. Potez, which was incorporated under the laws of France, where its head office is located.

The authorized capital of the Company consists of 12,000 common shares having a par value of $100 each, all of which were issued for cash shortly after its incorporation. Thus, as appears by its 1939 financial statement (which is the earliest of the financial statements filed as Exhibit A-1), the Company began business with cash available for investment amounting to $1,200,000.

When the land in question was purchased in 1951 the Company had a net equity of about 2-million dollars invested almost exclusively in Canadian revenue producing shares and a cash balance of over $130,000, as appears by its annual financial statement for the year ending Decem-

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ber 31, 1951. Mr. Joseph Blain, Q.C., had been retained to incorporate the Company but a Mr. Archibald was organizer and manager of it until 1949 when Mr. Blain, whose only stock interest in the Company was one qualifying share, replaced him and became its president and general manager.

According to the evidence of Mr. Blain, who was the only witness called, he considered that a better diversification of investments was required so that, in the event of a stock market crisis, the Company would have an interest in another sphere of investment, such as real estate. When it came to Mr. Blain's knowledge that a farm property, owned by Le Trust Général du Canada, which was located in the Municipality of the Parish of Montreal, was for sale, he engaged a surveyor engineer named J. A. Papineau to examine and report on the property. He also consulted The Sun Trust Company and after due consideration came to the conclusion that the property would make a sound long-term investment and recommended its purchase to the Administrative Committee of the Company. His recommendation was accepted, but, because the Company was incorporated by Dominion Letters Patent, in order to hold lands in the province of Quebec it became necessary for it to obtain a provincial licence in mortmain. The Company did not procure a general licence but one for a single acquisition in a single year.

The Company took title to the property on December 21, 1951, which, as more fully appears by Exhibit A-2, consisted of farmland situated in Côte St-Luc, Parish of Notre-Dame de Grâce, measuring $2\frac{1}{2}$ arpents in width by 20 arpents deep, more or less, together with a stone house, a barn and other buildings erected thereon. The purchase price amounted to $135,000, payable in cash.

On March 31, 1952 the Company leased the property for a period of one year commencing November 1, 1952, to Ange-Emile Jasmin, who had been operating it as a farm for over ten years. The rental was $250 per annum and the lessee assumed liability for all municipal, ordinary and special taxes, as well as any school taxes which he might be required to pay. In the event that the lessor wished to sell the whole or part of the said property it could terminate the lease on giving the lessee prior notice of 30 or 60 days, depending upon the season in which the said notice was

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given, the whole as more fully appears on reference to Exhibit A-6.

The evidence shows that the above-mentioned lease was extended in 1953 for another year and that the tenant continued to occupy the property until it was sold on March 25, 1954.

Mr. Blain's evidence discloses that the Company had no intention of subdividing the property or otherwise developing it in order to make it marketable or to secure additional revenue from it. It was not listed for sale with any real estate broker or elsewhere. No sale sign was placed on it nor did any of the Company's officers make any effort to bring about its sale.

On November 19, 1953, the Company received an unsolicited offer to purchase the property from Messrs. Dubrovsky and Chaimberg for the price of $300,000 payable $50,000 down and the balance upon the signing of the deed of sale, which was to take place not later than March 31, 1954. A second offer was subsequently received from Notary I. R. Hart, of whose existence Mr. Blain was unaware. Except that the second offer was $500 higher, namely, $300,500, it was in the same terms as the previous one.

As appears by the minutes of a meeting of the directors of the Company, held on November 25, 1953 (Ex. A-4), the last-mentioned offer was accepted and on March 25, 1954 the president was authorized to sign the deed (Ex. 5).

Why the respondent purchased the property and why it disposed of it were subjects to which considerable evidence was devoted.

In respect of the purpose or intent of the Company in purchasing the property, Mr. Blain stated that the Company had a superabundance of cash surplus and they were looking to diversify their investments, which were almost entirely in stocks and bonds, "pour que, advenant une crise sur le marché ou quelque chose, nous puissions avoir des mises solides dans d'autres secteurs de l'économie". After making a study of the property, he thought it was a reasonable and sound investment and was of the opinion that, if held for a long period, it would yield a capital appreciation (Transcript, pp. 10, 12, 13).

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On cross-examination the witness confirmed the above testimony (Transcript, p. 25 and particularly p. 27), where, being pressed on the question of re-sale, he stated:

Q Lorsque vous dites que vous vouliez obtenir une appréciation du capital, de quelle façon vouliez-vous obtenir cette appréciation au moment de l'achat de la terre?

R. Une revente éventuelle. Je ne peux pas concevoir autrement.

Q. Comme cela, quand vous avez acheté vous aviez l'intention de revendre?

R. Je ne peux pas acheter une chose pour la garder perpétuellement.

Q Au point de vue placement, on peut garder pour cultiver ou autre chose?

R Ce n'était pas pour cultiver, ni pour lotir non plus. On n'avait jamais eu cette intention-là. On n'y a jamais pensé un seul instant.

In answer to the undermentioned question as to why the Company sold the property, the president replied as follows (Transcript, p. 16):

Q Maintenant, pourquoi, en votre fonction de président de cette compagnie, pourquoi est-ce que la compagnie a vendu le terrain?

R Parce que à ce moment-là nous étions entourés de spéculateurs qui faisaient des lotissements tout autour de nous autres. Et, cela provoquait des travaux publics considérables, cela amenait évidemment une augmentation de taxes. Et, en plus de cela, le statut provincial qui avait, depuis un très grand nombre d'années, constitué la base d'imposition pour les terrains en culture alentour de Montréal, qui limitait la valeur imposable à $300, cessait d'être en vigueur Alors, on ne pouvait plus juger la situation comme charge fixe à apporter en rapport avec le placement Et, en plus de cela, il y avait des tentatives de changement de zonage dans tout le coin.

Alors, quand l'offre nous est venue, nous avons vendu parce que nous n'avions pas l'intention de lotir ou de subdiviser et de nous laisser entraîner dans un mouvement de spéculation qui se faisait autour de chez nous à ce moment-là. Et qui s'est développé brusquement dans l'espace de quelques mois.

Further, at page 25 of the Transcript, the witness in cross-examination testified as follows:

Q Lorsque vous avez acheté le terrain en question, votre intention était de faire le plus de profit que vous pouviez faire. Advienne que pourra, en prévoyant l'avenir un petit peu?

R Ce n'était pas là notre intention. Notre intention c'était de diversifier nos placements et d'escompter une appréciation sur un placement immobilier.

Q Mais, vous aviez le but, lors de l'achat, vous aviez l'intention de revendre dans une période de temps?

R. Lors de l'achat, nous avions l'intention de faire un placement immobilier, et nous n'avions pas l'espoir de perdre. Cela aurait été ridicule n'est-ce pas? Et je peux avoir la prétention de viser à

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d'autres choses qu'à poser des actes qui n'auraient pas de sens. Je n'ai pas acheté dans le dessein de perdre.

Speaking of the risk in effecting the said purchase, the witness testified that, although one expert whom he consulted thought that the price which the Company was ready to pay was too high, nevertheless, after careful consideration, he felt at ease in recommending its purchase (Transcript, pp. 26 and 29).

The taxpayer procured its working capital from the cash subscriptions made by the original subscribers amounting to $1,200,000. The Company never paid any dividend and any surplus which it accumulated was undistributed and used to increase the Company's investments.

At the time of the purchase no development in the area had taken place but for a small one near the City Hall of Côte St-Luc, and the land in question was completely surrounded by other farms (Transcript, p. 29).

It is proved beyond peradventure that the transaction in question was an isolated one and that in the twenty years of the Company's activities it was the only instance in which the Company had purchased and sold real estate.

Counsel for the Minister conceded that the taxpayer functioned as an investment company during the period of 1939 to 1959, except with respect to its purchase in 1951 for $135,951 of the farmland in question and its subsequent sale thereof in 1954 for $300,500, and that the issue in the case is restricted to this operation alone and the gain of $170,000 (approximately) which resulted therefrom.

As a consequence, the issues in this case can be reduced to very narrow dimensions. First, was the purchase of the instant land a transaction of such a nature that it could be properly termed an investment? Secondly, if, as submitted by counsel for the appellant, even assuming that the aforementioned query is answered in the affirmative, was the transaction in issue carried out in such a manner as to constitute an undertaking or an adventure in the nature of trade, as set out in s. 139(1)(*e*).

With respect to the first query, in the absence in the Act of any definition of "investment" I think recourse must be had to dictionaries and jurisprudence; the following defini-

tion of the word "investment" is found in The Shorter Oxford English Dictionary, 3rd ed., p. 1040:

> 5. Comm. The investing of money or capital; an amount of money invested in some species of property. b A form of property viewed as a vehicle in which money may be invested.

In respect of jurisprudence I think it indicates that when a purchase is made—such as in the instant case—in order for it to qualify as an investment, the object purchased must be at least susceptible of yielding an annual return such as rental, dividends or interest.

In the case of *Commissioners of Inland Revenue v. Reinhold*[1], Lord Carmont at page 392, referring to the observations of Lord Dunedin in the case of *Leeming v. Jones*[2], sets out, in the following terms, the requirements necessary to constitute an investment:

> . . . Lord Dunedin says, in the case I have already cited, at page 423:
> . . . The fact that a man does not mean to hold an investment may be an item of evidence tending to show whether he is carrying on a trade or concern in the nature of trade in respect of his investments, but *per se* it leads to no conclusion whatever. (15 T.C. 360)
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> * * *
>
> I draw attention to Lord Dunedin's language being used with reference to "an investment", meaning thereby, as I think, the purchase of something normally used to produce an annual return such as lands, houses, or stocks and shares. The language would, of course, cover the purchase of houses as in the present case, but would not cover a situation in which a purchaser bought a commodity which from its nature can give no annual return. . . .

Shares sometimes called growth stocks which, at the date of their purchase, are not on a dividend-paying basis, often form part of an investment company's portfolio and are considered, for tax purposes, as investments, since they are susceptible not only of capital growth but also of producing income. I think the same can be said of the purchase of the instant property.

Counsel for the appellant contended that because the taxpayer was concerned with the gain to be derived from the long-term prospect of selling the property rather than the meagre return which it yielded, the money expended in acquiring it was not an investment.

I do not think that the amount of return is important; it may vary with the circumstances. Thus, a vacant prop-

[1] 34 T.C. 389.

[2] [1930] A.C. 415, 420, 423.

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erty in the centre of the city, when used for automobile parking space, sometimes commands high rentals. True, the return was a very modest sum; nevertheless, I think the farmland in issue falls well within the definition previously described.

Now, with respect to the second question, admitting it would otherwise rank as an investment, did the transaction, due to the manner in which it was carried out, constitute an undertaking or adventure in the nature of trade?

Counsel for the appellant relied upon and directed his argument to the words "undertaking" and "adventure in the nature of trade", which was a less onerous task than the attempting to establish that the Company was engaged in a trade or the real estate business.

I do not think that the instant transaction warrants the appellation "undertaking". The Shorter Oxford English Dictionary, 3rd ed., p. 2294, defines "undertaking" as

1. Energy, enterprise.
2. Something undertaken or attempted; an enterprise.

The same dictionary at p. 616 defines "enterprise" thus:

1. A design of which the execution is attempted; a piece of work taken in hand; *now only,* a bold, arduous, or dangerous undertaking.
2. Disposition to engage in undertakings of difficulty, risk, or danger; daring spirit.

I believe I might as well here also consider the word "adventure", which, in my opinion, is akin to "undertaking". At pages 27 and 28 of the above-mentioned Oxford dictionary the following definitions are given:

1. That which happens without design; chance, hap, luck.
2. A chance occurrence.
3. A trial of one's chance; a venture, or experiment.
4. Chance of danger or loss; risk, jeopardy.
5. A hazardous enterprise or performance; hence, a novel or exciting incident.
6. A pecuniary venture, a speculation.
7. Adventurous activity, enterprise.

The element of uncertainty attends innumerable transactions in everyday life, but whether, for taxation purposes, the instant transaction falls within the aforesaid meaning of the words "undertaking" or "adventure" depends, I think, on the degree of risk and speculation which it entails.

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Counsel for the appellant placed great reliance on Mr. Blain's statement that a superintendent of the real estate department of The Sun Trust Co., whom he consulted, was of the opinion that it was risky for the Company to pay as high a price as $135,000 for the property, which, according to my calculations, amounts to 7¢ per square foot. In my opinion, what could amount to a great risk for one person might be, depending on the circumstances, negligible to another—it has sometimes been observed that there is one law for the rich and another for the poor. The respondent was in the privileged position of having an abundance of liquid assets in the form of cash and it could afford to (figuratively) fold its arms and adopt a safe and passive attitude in respect of the instant property while allowing the impact of an expanding city population to make its presence felt. In the instant case, development, because of a sudden rise in real estate values near the city limits of Montreal, was more rapid than anticipated, but the waiting period was more than two years and there is no suggestion in the evidence that the retention of the property during the interval adversely affected the financial position of the Company or that it ran any perceptible risk in doing so. I am not surprised that Mr. Blain's judgment was not affected by the adverse comments of one of the persons whom he consulted, because judging the state of the market is a matter of opinion—and whether a stock (or stocks) is selling too high is a very open question and the same may be said of real estate.

In the present instance the purchaser anticipated that it would be some years before development would take place in the locality of the property and its financial position was such that it could easily afford to bide its time.

The purchase of land is one of the oldest types of long-term investment, and, since diversification of investments was one of the Company's main objects insofar as the facts are concerned, in my opinion practically the only risk that it ran was the duration of such waiting period. I am of the opinion that the elements of speculation and risk were negligible in the transaction in issue and did not amount to nor can it be regarded as an undertaking or an adventure in the nature of trade within the meaning of the Act.

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Even if the transaction in question may be appropriately called "an adventure", this does not mean that it will attract income tax—unless it is also established that it bears the badges of trade. I think that it is particularly in this latter respect that the weakness of the appellant's case is revealed.

It has been consistently held that each case should be judged on its own facts. However, there has been a wealth of jurisprudence dealing with the question of what constitutes an adventure *in the nature of trade,* but by no means are all of them pertinent to the instant case and they should be carefully distinguished.

Counsel for the appellant cited as clearly applicable to the case at bar *Rutledge v. The Commissioners of Inland Revenue*[1], wherein profits realized on the sale of a quantity of toilet paper was held to be a deal in the nature of trade.

I think that those cases which concern the sale of commodities, such as toilet paper or the like, which are consumed by use and by their nature not susceptible of producing income are distinguishable from and inapplicable in the instant case, where the farm was not only susceptible of producing income but actually did so at all material times.

Much more apposite is the case of *Irrigation Industries v. The Minister of National Revenue*[2] which was invoked by counsel for the respondent together with many of the authorities therein referred to. This well-known case concerned a purchase by the Irrigation Co. of 4,000 common shares of a public offering of 500,000 shares of treasury stock of Brunswick Mining and Smelting Co. Ltd. with money borrowed from the Bank for another purpose. The shares were of a highly speculative character and although the purchaser was forced to sell practically all of them within a few months after their purchase, in order to repay the Bank, it was, nevertheless, able to realize a considerable profit in doing so.

The Brunswick Company did not own an operating mine but was trying to revive one which was defunct and the likelihood of it paying a dividend was remote. It was under circumstances as above described that Martland J., who rendered the judgment for the majority of the Court, found

[1] (1929) 14 T.C. 419.

[2] [1962] S.C.R. 346.

that the transaction was not subject to tax and at page 350 he stated:

> However, assuming that the conclusion was correct that this purchase was speculative in that it was made, not with the intention of holding the securities indefinitely, with a view to dividends, but made with the intention of disposing of the shares at a profit as soon as reasonably possible, does this, in itself, lead to the conclusion that it was an adventure in the nature of trade?
>
> It is difficult to conceive of any case, in which securities are purchased, in which the purchaser does not have at least some intention of disposing of them if their value appreciates to the point where their sale appears to be financially desirable.
>
> * * *

Again, at page 355, the learned Judge said:

> The only test which was applied in the present case was whether the appellant entered into the transaction with the intention of disposing of the shares at a profit so soon as there was a reasonable opportunity of so doing Is that a sufficient test for determining whether or not this transaction constitutes an adventure in the nature of trade? I do not think that, standing alone, it is sufficient.

I think that in the present case there is a marked absence of evidence of what Fournier J., in *Sterling Paper Mills Inc. v. The Minister of National Revenue*[1] called *commercial animus,* and it cannot be said that in the present case the respondent carried out the transaction in issue in a manner characteristic of those who are trading in real estate. Indeed the passive role played by the respondent was the antithesis of what one would expect from a trader under like circumstances.

In my view the evidence establishes that the gain in question was the realization by the respondent of a capital accretion on an investment which is not subject to tax.

For the foregoing reasons, I am of the opinion that the appeal must fail.

The respondent will be entitled to its taxable costs.

Judgment accordingly.

[1] [1960] Ex. C.R. 401.