1957
Oct. 24
1958
May 2

BETWEEN:

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

AND

BEN CONSTANT ..... RESPONDENT.

Revenue—Income Tax—Income Tax Act, S. of C. 1948, c. 52, ss. 3, 4 and 127(1)(e)—Income or capital—Profits on erection and sale of apartment building constitute income—Appeal allowed.

Respondent and another formed a partnership to build and sell houses which they did and profited thereby. They then incorporated a company and transferred to it all assets of the partnership except one piece of land, ownership to which they kept for the purpose of putting up an apartment building for themselves to hold as an income producing asset of their own. By a verbal agreement the company undertook to erect the apartment on a cost basis plus a supervision fee of $6,000. Money was borrowed by the partners for the purpose of construction and offered to the company as part payment. When the building was completed the partners found themselves indebted to the company for a sum they could not finance. Consequently the apartment was sold at a price which netted each partner a profit of $8,760.48. The respondent and his partner were assessed income tax on this amount. An appeal to the Income Tax Appeal Board was allowed. The Minister of National Revenue appealed to this Court.

Held: That the whole transaction has all the earmarks of a business or trading transaction carried on as a profit making scheme and follows the same pattern as that followed by the partnership and the company in similar operations, and the profit made did not result from the enhancement of any investment but rather from the operation of an adventure in the nature of a business in carrying out a scheme for profit making.

2. That the profits made from the apartment building constitute income in the hands of the taxpayer and the appeal is allowed.

APPEAL from a decision of the Income Tax Appeal Board.

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

Paul Ollivier and *Claude Couture* for appellant.

P. F. Vineberg for the respondent.

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

FOURNIER J. now (May 2, 1958) delivered the following judgment:

This is an appeal from a decision of the Income Tax Appeal Board dated November 22, 1955, whereby it was held that the one-half share of the net gain, amounting to

$8,760.48, from the sale of an apartment building owned by the respondent and another party was a capital gain and not income taxable under the Income Tax Act, 1948. Also that the Minister's assessment including the above amount as taxable income be vacated and the matter referred to the Minister to deduct the said sum from the respondent's income for the taxation year 1950 and reassess accordingly.

The appellant contends that in computing the respondent's income for 1950 he included the amount of $8,760.48 because it was his share of the profits arising upon the sale of a property of which he was, with another person, a co-investor. On the other hand, the respondent submits that the property in question was built for him and a co-owner for investment purposes; therefore, the sale of the property constituted the realization of a capital asset.

I will summarize the relevant facts.

The respondent was an electrical contractor when in 1944 he entered into a partnership with Morris Shindel to build and sell houses, mostly of the duplex type. The partnership proceeded to construct duplexes, sold them and made profits in the operation of the business. In 1948 the partners organized and incorporated a company under the name of Shindel and Constant, Incorporated, to continue the construction business of the partnership which was dissolved. Its assets were transferred to the company with the exception of a piece of land on Côte Ste-Catherine Road, Outremont. The respondent and Morris Shindel kept the ownership of this land for the purpose of putting up an apartment building for themselves. It would not be for sale but held as an income producing asset of their own. They would lease the apartments, collect the rents, meet their obligations and have the residue as personal income. They were equal partners in this business venture as they were equal owners of the shares of the company.

In accordance with a verbal agreement, the company undertook to put up the apartment building on a cost basis plus a supervision fee of $6,000. The partners borrowed $105,000 from a company dealing with mortgages and offered it to the company as part payment of the project. When the building was completed they were indebted to the company in an amount of $38,000. This amount included $8,000 which the company had borrowed from the bank; $6,000 from other parties; $21,000 owed to the trade, arising

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out of the construction; $3,000, balance of the supervision fee. As the partners could not finance the payment of this debt and the company was pressed for the payment of these moneys, they decided to sell the apartment and did so at a price of $168,000. By this transaction they realized a net gain of $17,520.80 to be divided equally between themselves. They paid the $38,000 and loaned the balance to the company to continue its construction business, which at that time was the building of apartments for sale.

The issue on the appeal is whether the profit or gain of the respondent arising from the sale of a property known as No. 4865 Côte Ste-Catherine Road, Outremont, Que., is taxable income within the meaning of sections 3, 4 and 127(1)(*e*) of the *Income Tax Act,* 1948, and amendments or a capital gain.

In the *Income Tax Act,* Statutes of Canada, 1948, c. 52, effective January 1, 1949, sections 3, 4 and 127(1)(*e*) 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 of 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.

127. (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 a trade but does not include an office or employment.

Before determining if the provisions of the above sections of the Act are applicable to the present case, it is necessary to keep in mind certain facts which establish the relationship of the parties involved: the respondent, his partner, the partnership and the company.

When the partnership was formed, Morris Shindel, one of the partners, owned land which he turned over to the partnership as his share in the association. When this land was used up as site for the buildings put up, the partnership purchased other sites. On two of these sites, the partnership built two houses of two flats for the partners them-

selves. Each partner became the owner of one of these houses. They live in one of their flats and rent the other, thereby deriving income from same.

When the partnership was dissolved and the company incorporated in 1948, the business of constructing houses and duplexes had become more or less profitable, so the company decided to build apartments. Though the partnership had been dissolved for building purposes, it seems that it continued as to the ownership of a piece of land. As this building site was situated in a district known as an apartment district, the owners decided to use this land as a site for an apartment.

Their company undertook to construct the apartment. I am led to believe, if I understood the evidence, that their only asset was a building lot, valued at approximately $7,500, which they contributed to the undertaking. The apartment building was sold for $168,000 and the partners realized a gain or profit of $17,520.80. It follows that the building cost $150,480 less the value of the land, which would mean that the cost of the construction itself was about $143,000. To meet this obligation, the partners borrowed $105,000, leaving a balance of $38,000 which was financed by the company. This justifies the statement that all the respondent and Morris Shindel invested in the venture was a piece of land of a value of $7,500.

Counsel for the appellant based his argument on sections 3 and 127 of the Act and submitted that the *income of a taxpayer* is his income from all sources including income from *businesses* and that business includes an adventure or concern in the nature of a trade. The respondent's undertaking being an adventure in the nature of a trade, any gain or profit therefrom was taxable income.

Counsel for the respondent countered by contending that the ultimate gain by the respondent was the result of an isolated operation and that to be taxable income the gain or profit had to be derived from a series of transactions amounting to a trade or business. Personally, the respondent had never been in the business of constructing buildings for sale. His motive in this instance was to create an asset which would assure him of an income for his old age.

I am of the opinion that in determining whether the gain in this case should be considered as *taxable income* or a capital gain one should not be limited to the question—Does

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the transaction above described constitute a trade or business? I rather believe that all the facts and circumstances of the undertaking should be considered in relation to the general definition of "Income" in section 3, to see if the transaction fits into the framework of the definition. In the affirmative, the gain derived therefrom would be *taxable income.*

Even before the coming into force of the Income Tax Act (1948), wherein section 127(1)(*e*) extends the meaning of the word "business" to include an adventure or concern in the nature of trade, the above rule was expressed in clear terms in *Californian Copper Syndicate v. Harris*[1] by Clerk, L.J., at pp. 165 *et seq.*:

> It is quite a well settled principle in dealing with questions of assessment of Income Tax, that where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income Tax Act of 1842 assessable to Income Tax. But it is equally well established that enhanced values obtained from realisation or conversion of securities may be so assessable, where what is done is not merely a realisation or change of investment, but an act done in what is truly the carrying on, or carrying out, of a business. . . .
>
> What is the line which separates the two classes of cases may be difficult to define, and each case must be considered according to its facts; the question to be determined being—Is the sum of gain that has been made a mere enhancement of value by realising a security, or is it a gain made in an operation of business in carrying out a scheme for profit-making?

In *The Atlantic Sugar Refineries v. The Minister of National Revenue*[2] the same rule was expressed in the following words:

> 2. That whether the gain or profit from a particular transaction is an item of taxable income cannot be determined solely by whether the transaction was an isolated one or not. The character or nature of the transaction must be viewed in the light of the circumstances under which it was embarked upon and its surrounding facts.

The decision was affirmed by the Supreme Court of Canada.

The same view was expressed in *McDonough v. The Minister of National Revenue*[3]:

> 2. That the mere fact that a transaction is an isolated one does not exclude it from the category of trading or business transactions of such a nature as to attract income tax to the profit therefrom.

As to the respondent's intention of putting up an apartment building for investment purposes or keeping the building as an income producing asset, it is a feature which

[1] [1904] 5 T.C. 159. [2] [1948] Ex. C.R. 622.

[3] [1949] Ex. C.R. 300.

should be considered. But all the circumstances of the undertaking must be kept in mind in determining whether the gain arose from an adventure or concern in the nature of a trade, or the result of a profit making scheme. If it is established that the sum assessed has been found as profits of a business, the intention or motive is immaterial. In the case of *Mersey Docks and Harbour Board v. Lucas*[1] it was held that

> It is also well established that once the sum assessed has been ascertained to be profits of a trade or business, neither the motive which brought these profits into existence nor their application when made is material.

This rule was followed in *Minister of National Revenue v. Saskatchewan Co-operative Wheat Producers*[2].

So it may be said that an isolated transaction and the intention or motive which brought about this transaction cannot be considered as a conclusive test that the gain derived therefrom is or is not income subject to tax without looking into all the facts and circumstances of the operation.

The question now to be answered is—Was the sum of gain that was made in this case, in view of the evidence adduced, a mere enhancement of value by realizing the investment?

What was the investment? The only possible answer to this question is—A piece of land to be used as a site for building purposes, land which was taken out of the assets of a partnership which were transferred to a company incorporated to continue the business or trade of the partnership, to wit, the construction of buildings to be sold. The fact is that the respondent and his associate were both tradesmen interested in the building field. The partnership was formed to join their knowledge, skill and assets in that line of endeavour. The company, the shares of which were held by the same two persons, continued in the same business but changed over from the construction of houses, duplexes and triplexes to the construction of apartment buildings. The company's first undertaking was the building of an apartment house as above related. Afterwards, it continued to operate in the same line of construction with its assets and the moneys it borrowed from the respondent and his associate, moneys realized from the sale of the above apartment house.

[1] (1883) 8 App. Cas. 891. [2] [1928-34] C.T.C. 47 at 54.

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After hearing the witnesses and later reading the evidence, I found it difficult at times to understand if they were speaking of the project as their personal affair or the business of the company. As to that matter, they themselves were somewhat confused.

One thing I am convinced of is that the partners did not have the means to build such an apartment without the assets of their company and were in no position to finance the sums owing to the creditors after the completion of the work. The sale of the building was their only solution. They knew very well their personal financial position, as they knew that of their company, when they embarked on this project, and I am sure they knew they would be in no position to keep the building for income purposes. Those being the facts, it is impossible to think that the undertaking was an operation in the nature of an investment to create an income producing asset. I cannot agree with the argument that the leasing of the apartments before the sale of the building establishes that the associates intended to keep the building as a personal investment. At the time of the leasing they already knew they could not meet their obligations and would sell to pay their debts. I rather believe that by leasing the apartments they were in a strong position to obtain a more favourable price for the building.

The Minister, in assessing the respondent's taxable income, having fully disclosed to the taxpayer why, in fact and in law, he had added to his return for the taxation year 1950 the amount of the profit made on the sale of the building, the burden of proof that he had erred either in fact or in law fell on the taxpayer though he was respondent in the appeal.

There is no doubt in my mind, in view of the evidence as a whole, that the respondent failed to discharge the onus of proving the allegations of his reply to the appellant's notice of appeal.

The whole transaction has all the earmarks of a business or trading transaction carried on as a profit making scheme. It follows the same pattern as that followed by the partnership and the company in similar operations. I find that the profit made did not result from the enhancement of any investment but rather from the operation of an adventure in the nature of a business in carrying out a scheme for profit making.

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For these reasons, in my judgment the profits made as a result of the putting up of an apartment building on a property known as No. 4865 Côte Ste-Catherine Road, Outremont, and the sale of same by the respondent and his associate fall within the ambit of "taxpayer income" as provided for in section 3 of the Income Tax Act, 1948, and the amounts of these profits were properly added to the respondent's income tax return for the taxation year 1950.

Therefore, the appeal is allowed with costs.

Judgment accordingly.