
1955
Feb. 28
May 27

BETWEEN:

EGBERT DOUGLAS HONEYMAN ..... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE ..... RESPONDENT.

Revenue—Income—Income tax—The Income War Tax Act, R.S.C. 1927, c. 97, as amended, s. 3(1)—The Income Tax Act, 1948, S. of C. 1948, c. 52, as amended, ss. 3, 4, 127(1)(e)—"Taxable income"—Shareholder buying material needed by his company for its operation and reselling to latter at profit—Whether transaction constitutes a trade or business —Transaction in a scheme for profit making—Appeal from Income Tax Appeal Board dismissed.

Having refused to give their personal guarantee for a bank loan to finance the purchase of a large quantity of sulphuric acid needed by their company for refining its product the shareholders including the appellant formed a syndicate with the object of purchasing the acid and selling it to the company, each member of the syndicate contributing

to the purchase price in proportion of his holding in the company. The price paid by the syndicate for the acid was $10 per ton of acid and it was sold to the company at $30 per ton. In the years 1947, 1948 and 1949 appellant received his share of the sale price from the company and the amounts so received were added by the Minister to appellant's income for those years. An appeal from the assessments to the Income Tax Appeal Board was dismissed and from the Board's decision appellant appealed to this Court.

Held: That whether the gain or profit realized by appellant is "taxable income" is not to be determined solely by whether the transaction here constitutes a trade or business. All the facts and circumstances of the deal ought to be considered in relation to the general definition of "income" in s. 3 of the *Income War Tax Act*, R.S.C. 1927, c. 97, as amended, and of the *Income Tax Act*, S. of C. 1948, c. 52, as amended. *The Atlantic Sugar Refineries* v. *The Minister of National Revenue* [1948] Ex. C.R. 622; *McDonough* v. *The Minister of National Revenue* [1949] Ex. C.R. 300 referred to and followed.

2. That having the necessary funds to do so the shareholders of the company could have themselves readily loaned the required amount to the company. Instead, they preferred purchasing the acid and selling it at a profit. The whole operation was the carrying of a scheme for profit making. It was not a mere enhancement of value of an investment realized.

3. That the profits made as a result of the transaction by the appellant fall within the definition of "income" in both Acts and the amounts of these profits were properly added to appellant's income.

APPEAL from a decision of the Income Tax Appeal Board.

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

Allan Scarth for appellant.

F. J. Cross for respondent.

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

FOURNIER J. now (May 27, 1955) delivered the following judgment:

This is an appeal from a decision of the Income Tax Appeal Board dated May 12, 1953, dismissing the appellant's appeal from income tax assessments levied against him for the years 1947, 1948 and 1949, whereby it was sought to hold him liable to tax on the profit made by him in those years from the purchase and sale of a certain quantity of sulphuric acid and oleum.

I will first state the facts as briefly as possible.

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The appellant is a shareholder and director of a company known as Pembina Mountain Clays Limited, hereinafter called the company. The company was incorporated under the laws of the Province of Manitoba and carries on the business of refining and processing bleaching-clay in the city of Winnipeg. It commenced the refining and processing of Bentonite bleaching-clay during the last war. In processing its product it uses large quantities of sulphuric acid. The company is the sole producer of such clay in Canada and its only competitor is a large scale producer in the United States. During the war, this product was declared a strategic material and the company's only customer paid it a bonus for its production.

The price paid to the company was the equivalent of the laid down cost of the American product in Sarnia. During the war the price of the American product was increased as the result of a 10% war tax on United States products, a 7% surcharge in freight rates and a 10% or 11% discount on Canadian currency in terms of the United States dollar. With these advantages and the bonuses received from its customer, the company was able to operate successfully. But some time after the war these taxes were removed and the Canadian dollar eventually was at parity, or close to parity, with the United States dollar and the American firm lowered its price. The company had to meet the decreased price of its competitor to hold its market.

During the war years, most of the earnings of the company had been reinvested in capital equipment and in 1946 its working capital was less than satisfactory and the company's future was uncertain. To meet the requirements of its purchaser, it bought from week to week, through the ordinary trade channels, the sulphuric acid needed for the refining of its product. The above described situation had forced it to operate practically on a day-to-day basis.

Some time in the spring of 1946 the appellant, who was secretary-treasurer of the company, heard that the War Assets Corporation had for sale 2,000 tons of sulphuric acid and 200 tons of oleum. This sulphuric acid was on hand at the Defence Industries' plant at Transcona, five or six miles out of Winnipeg. He suggested to the directors of the company that it should purchase this acid, seeing that it was

at a short distance from its plant and that there would be added to its cost very little in the way of transportation charges. The company had always purchased the acid from a firm in Sudbury and the freight charges were the equivalent of the price of the sulphuric acid itself.

On March 19, 1946, the company received a letter (Exhibit A) from the War Assets Corporation stating in part:

> If your company has a definite use for 3,774,979 lbs. of sulphuric acid 92%, . . . we would be prepared to accept a reasonable offer.

On March 29, 1946, the company answered that it was making inquiries to ascertain whether the acid would meet its requirements. Before May 1, the company through the appellant, had made an offer of $17 a ton for the acid. to be delivered at the rate of two cars per month. It would appear that this offer was not acceptable. The War Assets Corporation wished to make a bulk sale of the sulphuric acid. On May 3, 1946, the company made another offer to purchase the acid at the price of $10 a ton, the acid and tanks to remain where they were at the buyers' risk and responsibility, but to be removed in two years. It would seem that this offer was agreeable to the War Assets Corporation.

The company then tried to finance the purchase through the medium of its Bank but without success. The Bank would not extend the necessary credit without collateral security or the personal guarantee of the directors of the company. The directors felt unable to guarantee the loan but discussed the matter of financing the purchase with the shareholders (only two shareholders of the company were not directors). The shareholders refused to give their personal guarantee for the loan but they agreed to form a group or syndicate of which they would all be members with the object of purchasing the acid and selling it to the company. The syndicate appointed one of the shareholders to act as its agent and to attend to the transactions with the War Assets Corporation and the company.

On June 27, 1946, the general manager and director of the company, who was also the agent for the syndicate, wrote to the War Assets Corporation that the company would accept delivery of the acid which was to be sold to

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the syndicate's agent at $10 per ton (Exhibit 8). On July 1, 1946, an agreement was entered into between the company on the one part and the syndicate's agent as vendor on the other part. The terms of this agreement read as follows:

(1) The Vendor hereby agrees to sell to the Company such of the acid and oleum purchased by the Vendor from War Assets Limited as the Company may from time to time require for the price of Thirty Dollars ($30) per ton.

(2) The Company agrees to transfer the said acid from its present site at Defence Industries'—(at a location named)—"to premises at or near the Factory of the Company at"—(location named)—"such transference to be at the company's own expense."

(3) *IT IS UNDERSTOOD AND AGREED,* however, that no title shall pass from the Vendor to the Company for the said sulphuric acid or oleum until the same has been transferred from the tanks of the Vendor to the tank of the Company.

(4) *IT IS MUTUALLY AGREED* that an inventory shall be taken by the Vendor of the amount remaining in its tanks at the end of every month to ascertain the amount of acid and oleum which has been transferred to the Company's tank during the preceding month, and the amount so transferred shall be paid for by the Company to the Vendor within thirty days thereafter.

A statement filed as Exhibit 6 shows that the purchase price of the acid was paid by instalments by the syndicate during the period of June 3 to October 22, 1946, and that the acid and oleum were delivered in varying quantities and on different dates from September 13, 1946, to January 7, 1947. The tanks were also delivered in varying numbers and on different dates.

All the shareholders of the company were members of the syndicate and contributed to the purchase price of the acid in proportion to their holdings in the company. In the years 1947, 1948 and 1949, they received their share of the sale price from the company. The syndicate had paid the acid at $10 per ton and had sold it at $30 per ton to the company. It is the excess of the price received over the amount paid that the respondent considered as income and to be assessable in the hands of the individual members of the group over the three years in question. When the assessments were made, the profits of the appellant from the transaction or transactions in sulphuric acid, oleum and tanks—the amounts of which are not disputed—were added to the amounts of the income shown on the appellant's income tax returns.

From such assessments an objection was made to the Minister on the ground that the profits were not income but capital gains. The Minister having reconsidered the assessments confirmed them on the ground that the amounts received by the taxpayer as his share of the profits from transactions in sulphuric acid and oleum were income within the meaning of section 3 of the Income War Tax Act, 1927 and sections 3, 4 and 127 (1) (*e*) of the Income Tax Act, 1948.

The issue on the appeal is whether the profits of the appellant on the transaction or transactions in sulphuric acid and oleum, as a member of the syndicate above described, were taxable income within the meaning of the Acts and sections referred to in the Minister's notification confirming the assessments.

Section 3 of the Income War Tax Act, R.S.C. 1927, c. 97, as amended defines taxable income as follows:

Sec. 3. "Income."—1. For the purposes of this Act, "income" means the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary, or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be whether derived from sources within Canada or elsewhere; and shall include the interest, dividends or profits directly or indirectly received from money at interest upon any security or without security, or from stocks, or from any other investment, and, whether such gains or profits are divided or distributed or not, and also the annual profit or gain from any other source. . . .

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

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.

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 trade but does not include an office or employment;

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Counsel for the appellant based his argument on these sections of the law and submitted that the ultimate gain by the appellant to be taxable income would have to be the result of transactions amounting to a trade or business. The transaction considered in this case was an isolated operation which was in no way related to the appellant's ordinary occupation and had none of the characteristics of a business or trade. The deal was not a series of transactions, the subject matter had not been modified, altered or processed to make it saleable and the appellant had neither before nor after been engaged in a business or trade. When the appellant, together with others, made a bulk purchase and sale of the sulphuric acid, his motive was to assure the company of a continuous supply of acid to maintain its operations on such terms of credit as would enable it to pay for the acid as funds became available in the hands of the company. He was ready to lose his investment if the company was unable to pay. The charateristics of this transaction were contrary to normal and ordinary business.

In support of his contention, the best known decision he cited was that of *Jones* v. *Leeming* (1) where it was held:

> That having regard to the finding of the Commissioners that the transaction was not a concern in the nature of trade, and to its being an isolated transaction of purchase and resale of property, the profits arising therefrom were not in the nature of income but were an accretion to capital, and were therefore not subject to tax. . . .

In the last-mentioned case the Commissioners, masters of the facts, after considering the facts and arguments, found that the transaction was not a concern in the nature of trade.

Counsel quoted other decisions to which I shall refer later.

To his first proposition that a single transaction does not constitute a trade or business, I may agree that he is right; but I would not conclude, solely on that ground, that a profit resulting from such a transaction, meeting the necessary test or tests, would not be taxable income. He contended all through his submission that the gain realized by the appellant had to be the result of a transaction which could fall only within the ambit of the words of section 3 of the Act "as being profits from a trade or commercial or financial or other business."

(1) [1930] A.C. 415.

In my opinion I believe this is a too restrictive interpretation of the definition of the word "income" for the purposes of the Act. Such an interpretation was not admitted in many decisions.

In *Morrison* v. *Minister of Customs and Excise* (1) Audette J. says (page 81, in fine):

> Now the controlling and paramount enactment of sec. 3 defining the income is "the annual net profit or gain or gratuity". Having said so much the statute proceeding by way of illustration, but not by way of limiting the foregoing words, mentions seven different classes of subjects which cannot be taken as exhaustive since it provides, by what has been called the omnibus clause, a very material addition reading "and also the annual profit or gain from any other sources." The words "and also" and "other sources" make the above illustration absolutely refractory to any possibility of applying the doctrine of *ejusdem generis*. . . .

In *Shaw* v. *Minister of National Revenue* (2) Kerwin J. made the following comment (page 348, in fine): "In view of the evident intention to tax the annual profit or gain from any source, . . ."

And in *Blackwell* v. *Minister of National Revenue* (3) Cartwright J. says (page 425):

> It is suggested that the words in section 3 of the *Income War Tax Act* "profits from a trade, or commercial or financial or other business or calling" also show that the word "business" is used in contradistinction from the word "calling". It seems to me from reading the last mentioned section as a whole that the purpose of Parliament was not to subdivide earned income into classes according to its source but rather to use the words which would embrace earned income from every source. I do not think that the words "business" or "calling" are used in the section as terms of art intended to define mutually exclusive categories of sources of income but in the popular and ordinary sense and, so used, I think that the words "profits derived from a commercial or financial or other business" are wide enough to include the earnings of a commercial traveller.

It seems to me that in determining whether the gain is considered in this instance as "taxable income" one should not be limited to the question—does the transaction above described constitute a trade or business? I rather believe that all the facts and circumstances of the deal 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".

(1) [1928] Ex. C.R. 75. (2) [1939] S.C.R. 338.
(3) [1951] S.C.R. 419.

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This rule was clearly expounded by the President of this Court in *The Atlantic Sugar Refineries* v. *The Minister of National Revenue* (1). The headnote reads in part thus:

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.

This decision was affirmed by the Supreme Court of Canada (2).

The same view was expressed by Cameron J. in *McDonough* v. *The Minister of National Revenue* (3); it is worded as follows:

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 set forth in the foregoing decisions, in the case of a single transaction the test to be applied is that which is laid down in *Californian Copper Syndicate* v. *Harris* (4) by Clerk, L.J. (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?

The transaction as explained by the appellant in his testimony would appear to be of the nature of transactions put through every day in the world of business or finance or commerce. Somebody lacks the necessary funds to purchase a necessary supply of material for his trade or business; he negotiates a loan; gets a line of credit; failing these, he finds a person to purchase the goods who will, for a consideration, sell him the goods on terms he can meet. This description in my mind covers "trading and business transactions" as understood in the ordinary sense.

(1) [1948] Ex. C.R. 622.
(2) [1949] S.C.R. 706.
(3) [1949] Ex. C.R. 300.
(4) (1904) 5 T.C. 159.

The appellant—shareholder, director and secretary-treasurer of the company—knew, as all the members of the syndicate, the financial position and the needs of the company. When the occasion presented itself that it could purchase sulphuric acid at a low price, it lacked the necessary funds. Through its board of directors, it tried to negotiate a loan from the Bank. The Bank required collateral securities or the personal guarantee of the directors. This was not forthcoming and the loan was refused. All the shareholders joined in a syndicate to finance the purchase of the acid and sell the same to the company as required by the company from time to time. The company did not undertake to purchase part or all the acid. It agreed to take delivery and pay on terms and conditions for the acid needed in its operations. Title remained with the syndicate up to the time the company took physical possession of the acid for its needs. Payment was made later on. The price paid for the acid was $10 per ton. It was sold in varying quantities and on different dates to the company at $30 per ton, the price having been agreed upon on or before the purchase of the acid by the syndicate. The members of the syndicate received payment for the acid at the agreed price and realized a gain on the transaction.

This transaction in my opinion has all the earmarks of a business or trading transaction, which, if it had been undertaken by any businessman, would have been considered as such. Why if undertaken by the shareholders of the company would it be considered otherwise, I do not know. Any person who would have made this transaction would have had uppermost in his mind the profit or loss which could have resulted from such a deal. To believe that the shareholders had no such thought in mind does not appeal to me. If they were motivated by altruistic sentiments, they could have readily themselves loaned the required amount to the company, with or without interest. They had the necessary funds to do so. Instead, they preferred purchasing the acid and selling it at a profit to their company.

I am of the opinion the the whole operation as described above was the carrying of a scheme for profit making. It certainly was not a mere enhancement of value of an investment realized.

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For these reasons I find that the profits made as a result of this business transaction by the appellant fall within the definition of "income" in the Acts applicable to the issue and that the amounts of these profits were properly added to the appellant's income tax returns for the years 1947, 1948 and 1949.

The appeal is dismissed with costs.

Judgment accordingly.