
1958
April 21
1959
Mar. 9

BETWEEN:

BAYRIDGE ESTATES LIMITED } APPELLANT,

AND

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

Revenue—Income—Income tax—Company purchased land to construct motel and service station as investment—Sold land at profit when unable to finance scheme—Capital or income—The Income Tax Act, R.S.C. 1952, ss. 3, 4 and 139 (1)(e).

The appellant was incorporated as a private company under the Quebec *Companies Act* in November 1951 with powers wide enough to include dealing in real estate. In December it acquired from one of its three shareholders a parcel of undeveloped land for which it issued fully paid shares of its capital stock. It planned on subdividing

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the land into building lots and erecting buildings for rent and for sale but abandoned the project when it was unable to finance the construction costs and in August 1952 accepted an offer of $63,200 for half the property. (It was admitted in these proceedings that the profit realized on such sale was income). A few weeks later the appellant purchased for $50,000 another parcel of undeveloped land on which it proposed erecting a service station and motel but again was unable to finance the scheme and in June 1953 sold the property at a net profit of $24,912.78. The Minister included this amount in his assessment of the appellant's 1953 income. In an appeal from a judgment of the Income Tax Appeal Board upholding the assessment the appellant contended that the land in question was not purchased by it in the course of dealing in real estate but for the sole purpose of constructing and operating thereon a motel and service station. That it was only when such purpose failed because it was unable to borrow the money required to carry out that purpose that it accepted an offer for the property and, that in these circumstances, the profit realized was a capital gain and not income.

Held: That the sale of the propery for profit was one of the several alternative purposes for which the property was acquired, and it was in the carrying out of that alternative purpose, when it became clear that the preferred purpose was unattainable, that the profit in question was made. It was, accordingly, a profit made in an operation of business in carrying out a scheme for profit-making and was properly assessable.

APPEAL from a decision of the Income Tax Appeal Board.

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

Philip Vineberg for appellant.

Raymond Décary and *J. M. Poulin* for respondent.

THURLOW J. now (March 9, 1959) delivered the following judgment:

This is an appeal from a judgment of the Income Tax Appeal Board,[1] dismissing an appeal by the appellant against an assessment of income tax for the year 1953. In making the assessment, the Minister brought into the computation of the appellant's income a net profit of $24,912.78 which the appellant had realized in that year on the sale of a parcel of real estate, and the question in the appeal is whether or not this sum was income or a capital gain.

The appellant was incorporated in November, 1951 under the *Quebec Companies Act* by letters patent, in which the purposes of the corporation are expressed in terms wide

[1] 56 D.T.C. 581.

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enough to include dealing in real estate. On December 31, 1951, the appellant acquired from one of its three shareholders a parcel of undeveloped land at Baie d'Urfé, some miles west of Montreal, for which it issued to the three shareholders as fully paid up 102 common shares of $100 each par value and 402 preferred shares of $100 each par value of its capital stock. The appellant's plan, in purchasing this property, and the purpose for which the company was incorporated were described as follows by Mr. Bercovitch, one of its three shareholders and directors:

> A. The land—or if I may and if the Court would permit, sir—the whole object of the company being formed was to develop an investment situation wherein the two professional men would participate and I, as a business man, would do the chasing and do the dog spotting work, if we may say so. That was the intent of the three gentlemen when we joined hands. To implement that policy, and this line of attack, we decided that we would buy land; we would build houses; we would hope or we hoped we would be able to build a shopping center and generally go into two types of real estate, income-producing real estate, through building and renting; then to build and sell houses in this area at Baie d'Urfe. That was our broad interpretation and we started on that basis. So the land, to answer the question, was purchased to implement the policy of the three members of the corporation.

The appellant obtained the approval of the local authorities at Baie d'Urfé for a subdivision of a part of the land into 12 building lots but was unable to obtain mortgage moneys to finance the construction of so much as one dwelling house thereon. Accordingly, it abandoned this scheme and, on August 18, 1952, accepted an offer of $63,200 for about half, though no doubt the more valuable half, of the property. The purchase price was payable as to $15,000 in cash and as to $48,200 in one year with interest. It is admitted that the profit realized on this sale was income. The appellant continued to hold the remaining portion of the land, presumably for sale, if not for development and sale, and ultimately sold it in 1956.

On August 29, 1952, the appellant purchased for $50,000 another parcel of undeveloped land, this one being located in Lachine about a mile east of Dorval airport. Of the purchase price, $1,000 was paid on the making of the agreement, $24,000 was paid on the transfer of the property to the appellant on October 27, 1952, and the balance was payable with interest on April 27, 1953. On June 3, 1953,

the appellant sold this property to the Shell Oil Company of Canada Limited for $80,000 in cash, and it is the profit realized in this transaction that is in issue in this appeal. These were the only purchases and sales of real estate made by the appellant up to that time, and none save the sale of the remaining land at Baie d'Urfé have been made since then, the appellant having in the meantime invested its funds in bonds and other securities.

The case put forward on behalf of the appellant is that the land at Lachine was not purchased in the course of any business of dealing in real estate but was acquired for the sole purpose of constructing and operating a motel and service station thereon, that it was only when such purpose failed because of the appellant's inability to borrow the moneys required to carry out that purpose that the appellant accepted an offer for the property and realized the profit in question, and that, in these circumstances, the profit was a capital gain and not income.

There is ample evidence that the appellant had such a scheme for the property in mind both before and at the time when the property was purchased and for some time thereafter, and I think it is also clear that the location was selected as one suitable for such a project. After making the contract to purchase, Mr. Bercovitch made a tour of motels in the New England States and collected information as to their operation and costs. Another director, Mr. Greenspoon, an architect, had some time earlier made a study of motels and had prepared a report on them, and in September, 1952, he prepared an artist's sketch and a floor plan of the proposed building. On the plan part of the property was indicated as the site of a proposed service station. Besides the service station and motel, the plan included a proposed restaurant and cocktail lounge. The appellant proposed to lease the service station to an oil company for a term of 20 years or thereabouts but had not decided whether it would take a sub-lease from the oil company and operate the station. It contemplated operating the motel but had no settled plan for operating the restaurant or cocktail lounge on its own. Shortly after purchasing the property, the appellant negotiated with the British American Oil Company for a loan of $100,000 to finance the building of the motel and service station, but after a time

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these negotiations ended abruptly with the refusal of that company to make the loan. The appellant thereupon applied to the McColl-Frontenac Oil Company for a loan of similar amount to finance the project. The application was strongly recommended by Montreal officials of that company but was turned down by their superiors in New York. When this occurred, the appellant made further efforts to obtain the loan from the Shell Oil Company, an insurance company, and private investors in turn but did not succeed in getting the money. In May or June the appellant abandoned the scheme and put the property up for sale.

The property in question was an area of 3.86 arpents, with a frontage of 425.5 feet on Cote de Liesse Road and 511 feet on 55th Avenue, Lachine. Both roads were heavily travelled, one carrying Montreal-New York traffic and the other Montreal-Toronto and Montreal-Ottawa traffic. The land was situated in a rapidly developing area, and the value of the portion at the corner formed by the intersection of the roads as a service station location was obvious. When acquiring the property, the directors knew that oil companies were interested in it and anxious to get it. At the same time, the amount of the purchase price paid for it represented the bulk of the appellant's resources, both of invested capital and debenture borrowings, and the appellant could not finance the motel and service station project without a loan of $100,000 or thereabouts. So long as the land remained undeveloped, however, it would produce no revenue for the appellant. That the whole motel and service station project was conditional upon the appellant's being able to secure such a loan is apparent as an inference from the circumstances, and it appears as well in the evidence of Mr. Bercovitch and Mr. Greenspoon. On that point, Mr. Bercovitch said:

Q. And you felt—did you feel that you could?

A. Providing we could get a first mortgage loan, there was no reason why we couldn't.

Q. But you needed outside help?

A. Definitely.

Mr. Greenspoon said:

Q. Well, the main reason you did not go ahead with this building of the motel then was that the efforts to raise one hundred thousand dollars ($100,000.00) failed?

A. Our first mortgage did not succeed, that is right. That was the cardinal sort of pivot on which the whole thing depended.

* * *

Q. Now, this whole plan hinged on the obtaining of a first mortgage loan?
A. Yes, sir.
Q. Of sufficient size to finance the construction of the motel?
A. Yes.

The same witness, when asked as to what the appellant intended to do with the property in the event of failure to obtain the loan, gave the following evidence:

Q. What plan did your company have for the property if it could not get the loan?
A. Frankly, sir, I do not think we considered it in that light. We were practically so sure from all the glowing reports and all the encouragement we got and from the enthusiasm that we never even gave it a serious thought that we would not be successful, only actually when we were turned down by the head offices of Texaco Company.
Q. Was that possibility not discussed amongst the Directors?
A. Well, if it was discussed, we did not put too much emphasis on it, sir, because we thought we were almost sure to succeed with that. You can usually tell by negotiations whether a thing is going to work or is not going to work out; and that seemed to click right from the beginning.
Q. You say the optimism was such that you did not seriously consider what would become of this property?
A. No sir.
Q. If the financing could not be arranged?
A. No, sir, I don't think in our records, if you look through the records, there was too much emphasis put on that aspect of the operation.
Q. You say not too much emphasis. I am anxious to find out how much?
A. Well, it is a number of years now and I don't recall us discussing that at any great length.
Q. But can you conceive of you having purchased a property at fifty thousand dollars ($50,000.00) for a particular purpose for which the money was not yet available and not having given some consideration to what would happen if you did not get the money?
A. As I say, sir, we did not discuss it in very great details. Probably in the back of our minds we thought, well, perhaps, when the time came we could put another type of building on the property. I was in the building business, the architectural end of it; and we felt that property could be put to some use by somebody sometime. We did not spell it out.

In my opinion, the substance of this is that, when purchasing the property, the directors gave some little consideration to what course was to be followed in the event of the motel scheme failing and that they intended, in that event.

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to turn the property to account for profit in some way but that the course that might be taken was not settled. It appears, however, from the evidence of Mr. Bercovitch that the only course actually considered when it became obvious that the loan could not be obtained was that of sale. Speaking of this decision, he said:

> A. It was agreed, after considerable time had elapsed, I would say, right through to the spring of the following year, if I am not mistaken—sometime in May or June. The land lay dormant, of course, throughout the entire winter. My co-partners and associates felt that I just was not able to find the financing. Within our own orbit, we did not have it, so they said *the only thing left to do was put the land up for sale.*

By s. 3 of the *Income Tax Act*, R. S. C. 1952, c. 148, the income of a taxpayer is declared to be his income from all sources, including income from all businesses, and by s. 4 it is provided that, subject to the other provisions of Part I of the Act, income from a business or property is the profit therefrom for the year. "Business" is defined in s. 139(1) (*e*) as including "a trade, manufacture or undertaking of any kind whatsoever and an adventure or concern in the nature of trade." The question whether or not the profit in question was income or capital turns on whether or not the profit was profit from a business as so defined. The Minister, in making the assessment, has proceeded on the assumption that the profit in question arose from such a business, and in this appeal the onus is upon the appellant to satisfy the Court that this assumption is wrong. *Johnson v. Minister of National Revenue.*[1]

The test to be applied in determining whether the profit in question was income from a business is that stated by the Lord Justice Clerk in *Californian Copper Syndicate v. Harris*[2]. Referring to that test, Lord Buckmaster, in *Ducker v. Rees Roturbo Development Syndicate*,[3] said:

> My Lords, I think it is undesirable in these cases to attempt to repeat in different words a rule or principle which has already been found applicable and has received judicial approval, and I find that in the case of the *Californian Copper Syndicate v. Harris*, 5 Tax Cas. 159, it is declared that in considering a matter similar to the present the test to be applied is whether the amount in dispute was "a gain made in an operation of business in carrying out a scheme for profit-making." That principle was approved in a judgment of the Privy Council in the case of *Commissioner of Taxes v. Melbourne Trust*, [1914] A. C. 1001, and it is, I think, the right principle to apply.

[1] [1948] S.C.R. 486.

[2] (1904) 5 T.C. 159 at 165. [3] [1928] A.C. 122 at 140.

In applying the test to the case before the House, Lord Buckmaster continued at p. 141:

> These reports show that the directors were contemplating from the beginning the possibility of the sale of some of these patents. It is quite true that they preferred not to sell them if a sale could be avoided, but the statement in para. 11 of the case is quite plain, that "the possibility of the sale of the foreign patents or rights has always been contemplated by the appellant company in respect of such interest as it possessed in the foreign patents." It is one of the foreign patents with which this appeal has to do, and the agreements, which are set out, showing the way in which the foreign patents in the case of France and of Canada have also been dealt with, show that that statement was not a statement of a mere accidental dealing with a particular class of property, but that it was part of their business which, though not of necessity the line on which they desired their business most extensively to develop, was one which they were prepared to undertake.

In the present case, the evidence, in my opinion, points to the conclusion that the property was acquired with the overall intention of turning it to account for profit. The method favoured by the directors by which this intention was to be carried out was that of developing the property as the site of a motel and service station if the moneys necessary to carry out that purpose could conveniently be borrowed, and for that reason they turned down the early offers received for the property. They intended, however, if such moneys could not conveniently be borrowed, to turn the property to account for profit in any way that might present itself, and in my opinion such ways included sale of the property. In purchasing the property, the directors relied on their own knowledge of real estate and acted without any independent appraisal of the property, and in the transaction they committed the bulk of their company's financial resources for an unproductive, but saleable, property. I am far from satisfied that men of their ability and experience would have done this for the purpose of building a motel and service station without having arranged for the funds to finance this construction and without, at the same time, having in mind the most obvious alternative course open to them for turning the property to account for profit. Despite their optimism the possibility, if not the probability, of their not being able to obtain the necessary loan must, in my opinion, have been present in their minds, and the experience of the appellant's first project alone would have suggested both the necessity for an alternative course and the availability of the alternative course which

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was in fact followed less than a year after the property was purchased. To my mind, it is not without significance that that course was the only alternative course considered and that it was decided upon as *the only thing left to do*. In my opinion, the sale of the property for profit was one of the several alternative purposes for which the property was acquired, and it was in the carrying out of that alternative purpose, when it became clear that the preferred purpose, was unattainable, that the profit in question was made. It was, accordingly, a profit made in an operation of business in carrying out a scheme for profit-making and was properly assessed.

The appeal will be dismissed with costs.

Judgment accordingly.